

EESTI ENERGIA ANNUAL REPORT 2016

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Hando Sutter

Dear reader

For energy companies, the beginning of 2016 was challenging because energy prices dropped to a new low. In January, the world market price of Brent crude oil fell below 30 USD/bbl, its lowest point in 12 years. During the year the oil price recovered, reaching 53 USD/bbl in December. In 2016, the average oil price was 43 USD/bbl, 17% weaker than a year earlier.

In the first half-year, the market price of electricity was not attractive for electricity producers either. With the exception of January and June, average monthly electricity prices in the Estonian price area were consistently below 30 €/MWh. However, we were able to align the operation of our power plants to market conditions and target the hours where market prices were higher in order to maximise output and earn a profit. This allowed us to set a record in power production – on 15 January our production capacity surged to 2,109 MW, the highest in the time Estonia has been independent. In January there was also another noteworthy event which reflects the volatility of the electricity market – Estonia exported to Finland an exceptional quantity of electricity, around 50 GWh per month, a twofold increase on the full-year figure for 2015.

In the second half-year, market prices increased and softened the situation for electricity producers. Lower availability of Scandinavian hydro energy, cooler than usual weather, and maintenance downtime of interconnectors and major power plants pushed up the price. Thus, in 2016 the market price of electricity in the Estonian price area of the Nord Pool power exchange was 33.1 €/MWh, 6% up on the year before.

A crucial change for the Estonian oil shale energy industry took place in the summer of 2016 when the government

linked the oil shale resource charges, which used to be fixed, to the world market price of fuel oil. The government took swift action to respond to the difficulties which had hit the oil shale industry at the beginning of the year due to low energy prices. Flexible taxation helps the oil shale sector retain production capacities and jobs when prices are low and enables the state to earn more tax revenue when prices rise. This has already happened – in the last quarter of 2016 the world market price of heavy fuel oil was around 260 €/t, triggering a rise in companies' tax burden in the first quarter of 2017.

The Paris Climate Conference held at the end of 2015 did not put an end to the oil shale industry as was predicted in the media. However, the climate goals agreed by the heads of the EU members states in 2014 also apply to Eesti Energia. Moreover, the harsh operating environment at the beginning of 2016 made energy producers seek efficiencies wherever possible. Hence, we put a lot of effort into continuing the development of our unique, clean and highly efficient oil, gas and electricity co-production technology. In addition, in 2016 we signed a contract with Amec Foster Wheeler for rebuilding generating unit 8 of our Eesti power plant to increase its capacity for using oil shale gas. The reconstructed unit, which will begin operating in 2018, will reduce the environmental impacts of oil shale-based electricity production. The planned cost of the project is 15 million euros.

Oil shale processing continues to have global prospects. This is reflected in the strong interest in the International Oil Shale Symposium held in Tallinn and Ida-Viru county in September 2016. The event which was dedicated to 100 years of oil shale mining in Estonia attracted around 300 experts, scientists and business leaders from 21 countries across the world.

In the past decade, technology has been advancing at a rapid pace and our production operations must also become consistently smarter. We can already adjust the loads of the power plants of Enefit Energiatootmine, our power production subsidiary, which were designed to operate at base load, to market conditions but we need to go further. For example, in a pilot project at the Eesti power plant we are using equipment that measures the humidity and calorific value of oil shale in real time. This allows us to improve the management and efficiency of the production process. We are planning to implement similar equipment in oil production and mining. Developing effective digital production planning tools is among our priorities because this allows achieving the best results in the oil shale value chain.

In 2016, our network operation subsidiary Elektrilevi completed a far-reaching and unique project: replacement of the customers' previous-generation electricity meters with

new hourly smart meters that can be read remotely. This has made Estonia a country with one of the world's smartest distribution networks. In addition to releasing people from the obligation to submit the reading, the new metering system is a platform for many smart and energy-saving solutions. The project of installing new smart meters lasted for four years and cost 93 million euros.

Last year we began selling natural gas to residential customers in Estonia. We have been selling gas to companies since 2013 and by the end of 2016 our market share of the Estonian gas market was roughly 25% already. In 2016 we established a subsidiary in Poland to enter the Polish energy sales market. We are planning to launch electricity and gas sales in Poland in 2017. We are also analysing the opportunities for entering the energy sales markets of other countries of the Baltic Sea area.

In 2016, we developed Eesti Energia's strategy for the next five years. The purpose of strategy renewal was to improve our competitiveness in a situation where the market prices of energy do not increase considerably. In June the strategy was approved by Eesti Energia's supervisory board and we began implementing it. The new strategy, which has also been well received by the staff, foresees among other things that by 2020 electricity produced from alternative

including renewable sources must increase to 40% of our power production. In addition, we are working to achieve a more efficient management structure. We established a new renewable energy company, Enefit Taastuenergia, which is going to comprise all our renewable energy production units. We merged the Narva power plants and the oil industry into a single company, Enefit Energiatootmine, and combined Eesti Energia Tehnoloogiatööstus, Hoolduskeskus and Testimiskeskus, the entities involved in equipment production, maintenance, and testing, into a single company, Enefit Solutions. The new streamlined structure is clearer, more efficient and supports achievement of our strategic objectives.

An important event, which had a strong impact on Eesti Energia's financial performance, occurred in November when we signed an interim agreement on the delivery of the Auvere power plant with General Electric (GE). According to the agreement, by July 2017 GE will equip the power plant with new fabric filters which will ensure that the plant meets stringent particle emission standards also when operating at full capacity. Although the plant has been producing electricity since 2 May 2015, at high loads it does not meet applicable particle emission standards. Until the new filters have been installed, the plant will operate at loads where particle emissions do not exceed established limits. Under

the interim agreement, GE will pay Eesti Energia liquidated damages of 66 million euros for the delay in the delivery of the plant. We also agreed how subsequent liquidated damages will be calculated. GE is planning to deliver the plant to us in October 2017.

The Group ended 2016 with sales revenue of 742 million euros, 4.5% down from the year before. Despite this, we earned our highest-ever EBITDA: 327 million euros, a 23% increase on 2015. Net profit grew more than fourfold to 171 million euros. In 2016, we did not have to make any significant adjustments to the values of our assets.

In 2016, we produced 9.1 TWh of electricity, 18% up on 2015. The figure includes the output of renewable energy which grew by 5% to 380 GWh. Shale oil production totalled 318 thousand tonnes, 6% down from the year before. Oil production decreased because at the beginning of the year the market prices of oil were exceptionally low and in the summer our oil, gas and electricity co-production plant Enefit280 was closed for extended maintenance. The work done was productive – in the second half-year the plant operated steadily at close to designed capacity and at the end of the year yielded its best-ever 90-day output: 51 thousand tonnes. We expect strong output from Enefit280 also in 2017.

Eesti Energia's capital expenditures of 2016 totalled 140.5 million euros, a 43% decrease from 2015. Most of the capital outlay (88.5 million euros) was spent on improving the quality of the electricity network. According to Eesti Energia's strategy, the largest development projects of the next five years are the construction of the Tootsi wind farm, the Narva underground mine and a plant for extracting gasoline from oil shale gas and the reconstruction of generating unit 8 of the Eesti power plant.

We are optimistic about 2017. Eesti Energia has a new strategy and a clear action plan for moving forward. Furthermore, the market outlook for energy producers is better than in 2016. We are also going to pass an important milestone – the owner has announced that it would like to list a minority interest in our renewable energy subsidiary on the stock exchange. This will be the first time for one of Eesti Energia's entities to become a publicly-traded company.



HANDO SUTTER
Chairman of the
Management Board



EESTI ENERGIA AT A GLANCE

Eesti Energia operates in the electricity market of the Baltic Sea area as well as in the Estonian gas market and the international fuel market. The company's sole shareholder is the Republic of Estonia.

We mine oil shale and produce electricity, heat, liquid fuels (shale oil), and power engineering and industrial equipment. We sell electricity in the Baltic retail market and the Nord Pool wholesale market, natural gas in the Estonian retail and wholesale market, and liquid fuels in the international wholesale

market. We intend to launch electricity sales in the Polish market soon. In addition, we offer contemporary energy solutions and energy services to both residential customers and companies. Our Group's subsidiary Elektrilevi provides the distribution network service in the Estonian market.

We have divided our operations into four key areas: oil shale energy, renewables, network services, and retail sale of energy and other services.

We have around 5,700 employees.

SALES REVENUE

742.1 million euros

▼ -34.7 million euros, -4.5%

EBITDA

327.3 million euros

▲ +61.6 million euros, +23.2%

NET PROFIT

171.0 million euros

▲ +130.5 million euros, +322.4%

CAPITAL EXPENDITURES

140.7 million euros

▼ -105.0 million euros, -42.7%

CREDIT RATINGS

BBB/Baa3

ELECTRICITY
sales volume

9.0 TWh

▲ +1.3 TWh, +16.3%

DISTRIBUTION
sales volume

6.6 TWh

▲ +0.3 TWh, +4.4%

SHALE OIL
sales volume

301.8 thousand tonnes

▼ -13.3 thousand tonnes, -4.2%

Main business functions



Oil shale mining.



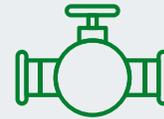
Organising complete logistics: oil shale, biomass, shale oil.



Repair, maintenance, technological solutions. Services both inside and outside the Group including exports.



Producing shale oil from oil shale. Efficient electricity production from oil shale, biomass and shale oil.



Retail sale of energy - both electricity and gas.



Energy production from alternative fuels.



Electricity distribution services in both the regulated and open market.



Wholesale of electricity and sale of shale oil.



Key Events of the Year

Despite a challenging environment
Eesti Energia sustained rapid development

IN JANUARY WE SET THE RECENT DECADES' ELECTRICITY PRODUCTION RECORD.

On 15 January, our production units' maximum capacity rose to 2,109 MW. The last time our production units operated at such capacity was more than 25 years ago.

WE DESIGNED A NEW GROWTH STRATEGY FOR EESTI ENERGIA.

In June 2016, the supervisory board approved Eesti Energia's new strategic action plan. The strategy foresees achieving gradual EBITDA growth in the next five years. For this, we will invest in increasing the competitiveness of our existing production capacities and creating new ones.

WE MOVED ON WITH OUR PROJECT IN JORDAN BY SIGNING THE DOCUMENTS REQUIRED FOR FINANCING THE ELECTRICITY PROJECT AND DIVESTING OUR MAJORITY INTEREST.

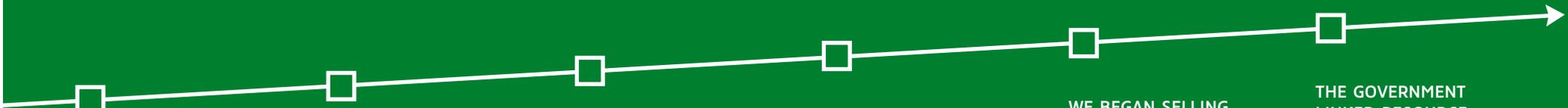
In the first quarter Attarat Power Company, which is partly owned by Eesti Energia, and major Chinese banks signed an agreement for financing the oil shale power plant and quarry to be built in Jordan. In the second quarter, Eesti Energia signed an agreement by which it is going to sell its majority stake in the Jordanian oil shale power plant and quarry project and retain a 10% minority interest in it.

WE CONTINUED ORGANISATIONAL STREAMLINING IN LINE WITH THE NEW STRATEGY.

We merged Eesti Energia Testimiskeskus, Eesti Energia Hoolduskeskus and Eesti Energia Tehnoloogiatööstus into one company, Enefit Solutions. We acquired full ownership of our Latvian energy company, Enefit Power and Heat Valka. We incorporated our power plants and oil industry into one company, Enefit Energiatootmine. We established a new renewable energy company, Enefit Taastuenergia, which is going to comprise all our renewable energy units and will be one of the largest renewable energy producers in the Baltic region. In addition, we are preparing for listing a minority interest in Enefit Taastuenergia on the stock exchange.

WE DECIDED TO INVEST IN INCREASING THE USE OF OIL SHALE GAS.

In the third quarter, we signed a contract for increasing our capacity to use oil shale gas, which is a by-product of oil production. Amec Foster Wheeler is going to reconstruct part of the electricity production equipment of the Eesti power plant to increase its capacity to use oil shale gas. This will increase electricity production efficiency and reduce its environmental impacts.



WE ENTERED THE POLISH ELECTRICITY MARKET.

In the third quarter, we established a subsidiary in Poland with a view to launching electricity and gas sales in the Polish market in 2017.

IN SEPTEMBER WE SET AN OIL PRODUCTION RECORD.

In September, Eesti Energia produced 38.4 thousand tonnes of shale oil, most of it at the Enefit280 oil plant. This is the largest-ever monthly quantity for us.

OUR NEW MINING TECHNOLOGY REACHED THE DESIGNED CAPACITY.

Longwall mining at our Estonia mine reached its designed production capacity. Under the new technology, oil shale extraction costs are considerably smaller than under the usual room-and-pillar technology. Our total investment in the project was 19.5 million euros.

WE SIGNED AN AGREEMENT BY WHICH THE BUILDER WILL DELIVER THE AUVERE POWER PLANT IN 2017 AND WILL PAY LIQUIDATED DAMAGES FOR THE DELAY.

In the fourth quarter, we signed an agreement with the builder of the Auvere power plant, General Electric, by which the builder will deliver the power plant by October 2017 and will pay liquidated damages of 66 million euros for the delay. The damages cover a period of one year up to November 2016.

WE BEGAN SELLING GAS TO RESIDENTIAL CUSTOMERS AND THANKS TO GOOD WORK SEIZED 23.5% OF THE ESTONIAN GAS MARKET BY THE YEAR-END.

In the fourth quarter, Eesti Energia also began selling natural gas to residential customers. In 2016, we supplied a record quantity of natural gas to all our Estonian gas customers.

THE GOVERNMENT LINKED RESOURCE CHARGES TO THE SHALE OIL MARKET PRICE.

In 2016, the Estonian government made a decision which had a strong impact on Eesti Energia's competitiveness and financial performance: from July 2016 the resource charges paid by the oil shale industry were linked to the world market price of shale oil. This helped us come through the period of low market prices.

Key Figures and Ratios (m€)

Definitions of ratios and terms are provided in the Glossary on page 190.

* Due to a change in the policy for reporting of sales volume, from 2015 sales volume includes the total sales volume of the Auvere power plant (the Group's sales revenue does not include the variable costs of electricity production and electricity sales revenue to the extent those items have been capitalised).

		2012	2013	2014	2015	2016
Total electricity sales*, of which	GWh	10,022	11,368	9,137	7,698	8,956
wholesale sales*	GWh	2,490	4,271	3,125	1,823	2,760
retail sales	GWh	7,532	7,097	6,012	5,875	6,196
Electricity distributed	GWh	6,365	6,280	6,294	6,337	6,616
Shale oil sales	th t	189	208	231	315	302
Heat sales	GWh	919	1,021	1,063	1,018	1,148
Average number of employees	No.	7,573	7,314	6,792	6,289	5,696

Sales revenues	m€	822.1	966.4	880.0	776.7	742.1
EBITDA	m€	278.4	310.5	312.3	265.8	327.3
Operating profit	m€	100.1	175.5	186.1	57.2	183.9
Net profit	m€	76.9	159.5	159.3	40.5	171.0

Investments	m€	513.5	418.9	275.9	245.6	140.7
Cash flow from operating activities	m€	185.2	244.6	228.2	307.7	200.3
FFO	m€	220.6	263.4	203.2	239.6	278.1
Non-current assets	m€	2,101.9	2,368.3	2,509.7	2,552.5	2,550.6
Equity	m€	1,409.2	1,574.7	1,619.5	1,571.9	1,698.0
Net debt	m€	581.0	744.3	834.7	792.0	716.6

Net debt / EBITDA	times	2.1	2.4	2.7	3.0	2.2
FFO/ net debt	times	0.38	0.35	0.24	0.30	0.39
FFO/ interest cover	times	7.2	7.9	5.5	6.4	7.7
EBITDA/ interest cover	times	9.1	9.3	8.5	7.1	9.0
Leverage	%	29.2	32.5	34.0	33.5	29.7
ROIC	%	5.6	8.6	8.1	2.4	7.8
EBITDA margin	%	33.9	32.1	35.5	34.2	44.1
Operating profit margin	%	12.2	18.2	21.1	7.4	24.8



OPERATING ENVIRONMENT

Eesti Energia's operations and performance are influenced by various global and regional factors including oil, electricity and emission allowance prices, the euro exchange rate, and changes in the legal environment. According to the estimates of the International Monetary Fund, in 2016 the global economy grew by 3.1% and the Estonian economy by 1.0%.

In 2016, the following events had a strong impact on our performance:

- The world market prices of oil products were very low at the beginning of the year but during the year they grew.
- Emission allowance prices decreased compared to 2015 and were volatile throughout the year.
- Average electricity prices in the Baltic countries became more similar.
- The state linked the oil shale resource charges to the world market price of fuel oil, making the tax burden flexible.

Liquid Fuels Prices

In the first half of 2016, the price of Brent crude oil rose even though production exceeded supply and the outlook of the Chinese economy and the United Kingdom's decision to leave the European Union caused uncertainty in the markets. In September, the price of Brent crude was lifted by OPEC's decision to cut production by 750 thousand barrels per day. In December, when non-OPEC producers also decided to make production cuts, the oil price strengthened even further.

In 2016 the average price of Brent crude oil was 43.3 USD/bbl, i.e. 16.8% (-8.8 USD/bbl) weaker than in 2015. However, during the year the price increased considerably – from 30.8 USD/bbl in January to 53.0 USD/bbl in December, i.e. by 72%.

In 2016, the euro/USD exchange rate was 1.107 US dollars to the euro. Compared to 2015, the euro weakened by 0.3%. The euro/USD exchange rate is relevant for Eesti Energia because shale oil sales are predominantly priced in US dollars and the base currency of a loan we have provided to an associate is the US dollar.

A widely-traded oil product, which is closest to the oil produced by Eesti Energia, is fuel oil with 1% sulphur content. Compared to the year before, in 2016 the European fuel oil market was influenced by stronger local demand and increased arbitrage opportunities* in Asia.

Liquid Fuels Prices

AVERAGE PRICE		2016	2015	CHANGE
Brent crude oil	USD/bbl	43.3	52.1	▼ -16.8%
Fuel oil (1% sulphur content)	€/t	195.0	235.5	▼ -17.2%
<i>Fuel oil 1% crack spread</i>	€/bbl	-9.9	-11.3	▼ -12.2%
Euro exchange rate	EUR/USD	1.1070	1.1103	▼ -0.3%

* Term explained in the Glossary section of the report, page 190.

Liquid Fuels Prices

Source: Thomson Reuters



Fuel oil Crack Spread

Source: Thomson Reuters



Although the average price of Fuel oil with 1% sulphur content remained 17.2% (40.5 €/t) lower than the year before, it showed strong growth similarly to the oil price, rising from 115.1 €/t in January to 288.7 €/t at the year-end.

In 2016, the crack spread was -9.9 €/bbl, i.e. 1.4 €/bbl narrower than the year earlier.

The crack spread, which measures the difference between the prices of fuel oil with 1% sulphur content and Brent crude oil, reflects the relative value of fuel oil compared to

the general price level in the oil market (Brent). The main factors which influence the crack spread are the relationship between demand and supply in the Baltic Sea area and the world. Lower demand for fuel oil widens the negative crack spread and lowers the value of Eesti Energia's oil compared to the general price level in the oil market.

Rises in crude oil and fuel oil prices have a positive impact on Eesti Energia because they raise the price of our shale oil and thus increase our revenue.

Emission Allowance Prices

In the first quarter of 2016, the average price of CO₂ futures plummeted by 35.6% (compared with the beginning of the year) because low energy prices at the beginning of the year reduced demand for emission allowances and the European Union granted the member states free emission allowances on 535 million tonnes to improve the competitiveness of its manufacturing sector. In mid-year, allowance prices were weakened by Brexit – the United Kingdom’s decision to leave the European Union. However, in the second half-year, the low price of coal increased its use in energy production. This increased demand for CO₂ emission allowances and drove up the price of CO₂ futures.

In 2016, the average price of CO₂ emission allowance futures maturing in December was 31.6% lower than the year before and highly volatile: 6.9 €/t in January, 4.3 €/t in September and 4.7 €/t in December.

The lower the price of emission allowances, the lower our electricity production costs. Therefore, a rise in emission allowance prices has a negative impact on our results. The impact of fluctuations in market prices is mitigated by free emission allowances received as investment support and use of hedging transactions for closing our CO₂ emission allowance positions.

CO₂ Emission Allowance Prices

AVERAGE PRICE (€/t)	2016	2015	CHANGE
CO ₂ December 2016	5.3	7.8	▼ -31.6%
CO ₂ December 2017	5.4	7.9	▼ -31.8%

Prices of CO₂ Emission Allowances



Electricity Prices

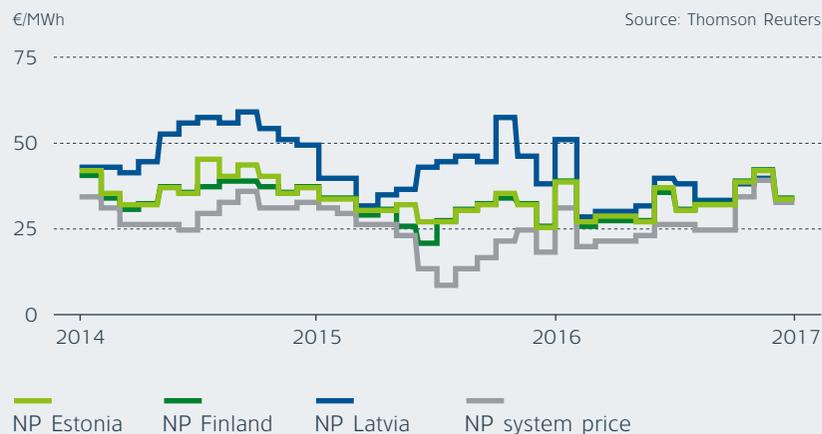
In 2016, electricity prices in the Nordic countries and Estonia fluctuated. From February until mid-year, the prices were lower than the year before because the air temperature was higher and there were good conditions for producing hydropower. In the second half-year, the prices were higher because the air temperature was lower than usual, the supply of hydropower decreased and several power plants and inter-connectors underwent maintenance.

In the reporting period, the average level of the Nordic water reservoirs was 0.1 percentage points higher than in 2015.

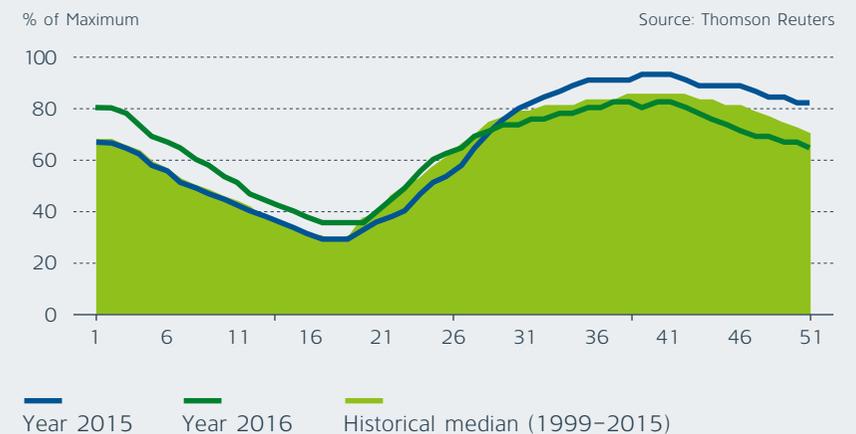
Until the middle of the year, abundant rainfall kept the water level in the reservoirs above the historical median. However, from August the level of the water reservoirs began declining and the production of hydro energy decreased compared to both 2015 and the historical median.

In 2016, the Estonian and Nordic electricity prices increased whereas the Latvian and Lithuanian electricity prices decreased. Compared to 2015, electricity prices in the Baltic countries became more even. In 2016, the average electricity price in Estonia was 33.1 €/MWh, i.e. 6.3% higher than in 2015.

Monthly Average Electricity Prices



Week Levels of Nordic Water Reservoirs



Electricity Prices on Nord Pool Power Exchange

In 2016, the average electricity price in Estonia was 0.7 €/MWh higher than in Finland; compared to 2015 the price gap decreased by 0.7 €/MWh. The volume of electricity exported from Estonia to Finland grew, driven by Finland's higher electricity prices in January and September. In January, Estonia exported to Finland 49.7 GWh of electricity, which is twice the full-year figure for 2015 (24.5 GWh). This resulted mainly from maintenance operations on the interconnection between Sweden and Finland, transmission restrictions on the interconnection between Estonia and Finland, and maintenance of unit 1 of the Loviisa power plant. In January, we set a record in electricity production: on 15 January the maximum capacity of our production units was 2,109 MW.

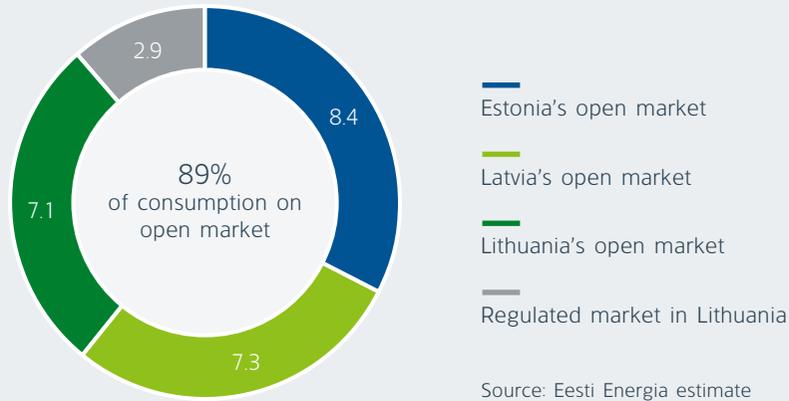
In 2016, the launch of the NordBalt power link narrowed differences in the Baltic electricity prices because cheaper hydro and nuclear energy, transmitted from Sweden to Lithuania, lowered the Latvian and Lithuanian electricity prices. In January 2016 when the NordBalt interconnector was not yet operational, the average electricity prices were 50.0 €/MWh in Latvia and 50.3 €/MWh in Lithuania.

At the same time, the average electricity price in Estonia was 37.6 €/MWh. Prices began to even out at the beginning of the second half-year when the testing and commissioning of NordBalt, which had been launched in February, ended. In 2016, the average electricity price in Latvia was 3.0 €/MWh higher than in Estonia. Compared to 2015, the gap between Estonia's and Latvia's average electricity prices narrowed by 71% (7.7 €/MWh). In 2016, the average electricity price in Lithuania was 3.5 €/MWh higher than in Estonia. Compared to the year before, the gap between Estonia's and Lithuania's average electricity prices narrowed by 68% (7.3 €/MWh).

Electricity Prices on Nord Pool Power Exchange

AVERAGE PRICE (€/MWh)	2016	2015	CHANGE
System price	27.0	21.0	▲ +28.5%
Finland	32.4	29.7	▲ +9.4%
Estonia	33.1	31.1	▲ +6.3%
Latvia	36.1	41.8	▼ -13.7%
Lithuania	36.6	41.9	▼ -12.8%

Electricity Consumption in the Baltic Market in 2016 (TWh)



The Estonian and Latvian retail electricity markets have been deregulated since 2013 and 2015 respectively. In 2016, the Lithuanian electricity market was partly deregulated. All companies in Lithuania purchased electricity from the open market but residential consumers were not obliged to do so. According to estimates, in 2016 around 71% of the Lithuanian electricity market (in terms of consumption volume) was open to competition.

In 2016, Eesti Energia's clean dark spread (CDS¹) in the electricity price of Nord Pool's Estonian price area (NP Estonia) was 8.7 €/MWh (+6.1 €/MWh, +239.8% compared to 2015).

Eesti Energia Clean Dark Spread (CDS) in NP Estonia Electricity Price



The electricity price increased by 2.0 €/MWh year on year and the impact of the change in CO₂ and oil shale costs was +4.2 €/MWh.

Clean dark spread reflects an electricity producer's estimated profit margin, which remains after fuel and CO₂ emission allowance costs have been deducted from the average market price of electricity.

As Eesti Energia earns most of its revenue from electricity sales, the rise in Estonian and Finnish electricity prices was positive for us.

¹ Compared to *Annual report 2015*, the CDS methodology has been specified by taking into account the oil shale costs included in making electricity wholesale bids.

Changes in the Legal Environment

In June 2016, legislators adopted amendments to Estonian legislation which lowered oil shale resource charges retrospectively from July 2015 from the previous 1.58 euros to 0.275 euros per oil shale tonne. The amendments took effect from July 2016. The state made the taxation of extraction rights flexible by linking the resource charge rates to the world market price of heavy fuel oil. The following diagram reflects the oil shale resource charge rates which apply at different market prices of fuel oil.

The change in resource charge rates has a positive impact on Eesti Energia's financial performance. It makes our cost base flexible because it links the cost base to the market price of the end-products and thus helps us withstand market downturns.

Oil Shale Resource Charges (€/t)





STRATEGY

Foundations for new success

In 2016, we developed Eesti Energia's strategic action plan for the period 2016-2020, which was approved in June the same year. The goal of the five-year strategy is to gradually increase Eesti Energia's EBITDA and create a basis for long-term competitiveness, profitability and ability to pay the owner dividends in a situation where market prices are low.

Our key objectives until 2020:

- To increase liquid fuel production to 500 thousand tonnes per year.
- To increase the share of electricity produced from sources alternative to oil shale to 40% of the Group's electricity output.
- To export renewable energy to countries which do not yet meet the European Union's renewable energy targets.
- To sell electricity and gas in the Baltic Sea area using a uniform e-solution.

The new strategy comprises five key activities.

Increasing the Competitiveness of Production Assets Which Use Oil Shale

Increasing the Burning of Oil Shale Gas

We are going to rebuild generating unit 8 of the Eesti power plant by 2018 so that in the future up to 50% of the plant's oil shale fuel can be replaced by oil shale gas which arises on oil production. This will reduce the environmental impacts of electricity production and make it easier to compete with Nordic electricity producers.

Extracting Gasoline from Oil Shale Gas

We intend to supplement our oil plants with a plant which will extract gasoline from oil shale gas. This will increase the production volume of liquid fuels by 10%, double the output of the most valuable shale oil product – oil shale gasoline, and increase the profitability of oil production. The investment decision will be made in 2017 and if it is positive, the plant will start operating in 2019.

Bringing Consumption to Production

For higher and more stable loading of our production capacities, we will offer large consumers an opportunity to connect to the power plant via a direct line. This solution would allow us to minimise transmission costs and enable large consumers save around a third of their electricity costs. The direct line concept should be attractive for entities such as data centres where electricity costs account for more than half of the service price. Making investment in Estonia attractive for large, energy-intensive industry and data centres assumes implementation of the tax changes suggested in the green paper on industrial policy.

Participating in Statistical Transfers

We would like to sell statistical units of renewable energy in the European Union's renewable energy market where countries that exceed their renewable energy target for 2020 can transfer statistical units of renewable energy to countries that have not been able to meet the target. Estonia exceeds the target. Eesti Energia could participate in the transfers with generating unit 11 of the Balti power plant and the Auvere power plant which can use biomass to the extent of 50%. The plan can be realised if amendments are made to the Electricity Act which will create a basis for statistical transfers.

Opening the Narva Underground Mine

To produce more competitive oil and electricity, we are planning to implement the harvester technology at the new Narva underground mine. The technology, which can reduce oil shale losses to 5-10%, is more efficient than the room-and-pillar technology whereby 22-35% of oil shale is left underground to support the overlying strata. The investment decision will be made in 2017 and if it is positive, the mine will be opened in 2019.

Streamlining the Management Structure

In 2016, we merged our power plants and oil industry into one company – Enefit Energiatootmine. We established a new renewable energy company, Enefit Taastuvenergia, which is going to incorporate all our renewable energy production units and will be one of the largest renewable energy producers in the Baltics. Eesti Energia's owner has announced its intention to list a minority interest in Enefit Taastuvenergia on the stock exchange. Eesti Energia Tehnoloogiatööstus and its subsidiaries Eesti Energia Testimiskeskus and Eesti Energia Hoolduskeskus were merged into one company – Enefit Solutions.

The new management structure which has fewer levels is clearer as well as more effective and cost-efficient.

Implementing Data-based Management

In 2016, we completed phase I in our production process integration programme and began preparing for implementing the information systems required for the integration and data-based management of the business processes of the oil shale value chain. The new systems allow to measure the properties and quality of oil shale in real time and thus improve the planning of our production processes.

Ensuring the Sustainability of Oil Shale Energy

Expanding Co-production of Oil, Electricity and Gas

Estonian mineable oil shale reserve exceeds a billion tonnes. According to its owner's expectations, Eesti Energia must ensure the sustainability of oil shale energy in the next 30 years with a focus on higher-value products such as shale oil. To achieve this, we have started preparations for expanding co-production of oil, electricity and gas and building the next Enefit280 oil plant. The new oil plant can be built when the market situation improves and it is cost effective.

Creating New Renewable Energy Capacities

Building the Tootsi Wind Farm

To increase the share of renewables in our portfolio, we will develop the Baltic region's largest wind farm on the depleted Tootsi Suursoo peat extraction site which can accommodate up to 52 modern turbines. The Tootsi wind farm would meet the energy needs of an area equal to Pärnu county, boost Estonia's renewable energy production, and give value to the abandoned peat extraction site. The investment decision will be made in 2017 and if it is positive, the wind farm will start operating in 2019.

Taking Production to Consumption

We are preparing a turnkey solar solution which would allow the consumers to fix their electricity price for decades. The consumer would save on network charges and would not have to deal with equipment maintenance. A pilot project has proven the viability of the service.

In addition, we will develop a solar power solution of 250 kW on the island of Ruhnu. An off-grid power system would cover the island's energy needs and ensure stable electricity supply in combination with batteries and diesel generators.

Growing in New Electricity and Gas Markets in the Baltic Sea Area

Eesti Energia has set itself the goal of transforming from a Baltic electricity supplier into a Baltic Sea area energy supplier by the year 2020. We believe that gas sale has strong potential: if the annual volume of the Baltic electricity market is around 25 TWh, the annual volume of the Baltic gas market is almost twice as large – over 45 TWh. In 2017, when the Latvian gas market becomes deregulated, Eesti Energia will begin selling gas to Latvian business customers.

We are also analysing the opportunities for penetrating other electricity and gas markets. In 2016, we made preparations for entering the Polish market and established a subsidiary in Poland, which should start signing energy contracts with business customers in 2017.

Increasing the Competitiveness of the Distribution Network Operator Elektrilevi

The key goal of the subsidiary Elektrilevi is to ensure quality network service. To reduce power outages, Elektrilevi is planning to upgrade the weather-resistance of its distribution network through cost effective solutions.

For several years, Elektrilevi has been providing outdoor lighting control service to the city of Tallinn and, as a new project, substation maintenance services to the water utility company Tallinna Vesi. In the next few years, Elektrilevi intends

to expand its offering of network management services to owners of infrastructure similar to the electricity network. The investment focus will be on new technologies and research and development.

Implementation of the new strategic action plan assumes making capital investments. Our largest investment projects of the period 2016 – 2020 include building the Tootsi wind farm, extracting gasoline from oil shale gas, increasing the burning of oil shale gas, and building the Narva underground mine. Capital expenditures on the strategic initiatives of 2016-2020 are likely to exceed 300 million euros but should pay back around half of the original outlay already in the same period and participate in the generation of the Group's profit also in the future.



FINANCIAL RESULTS

Despite a difficult operating environment, Eesti Energia ended 2016 with results which were considerably better than we expected at the beginning of the year.

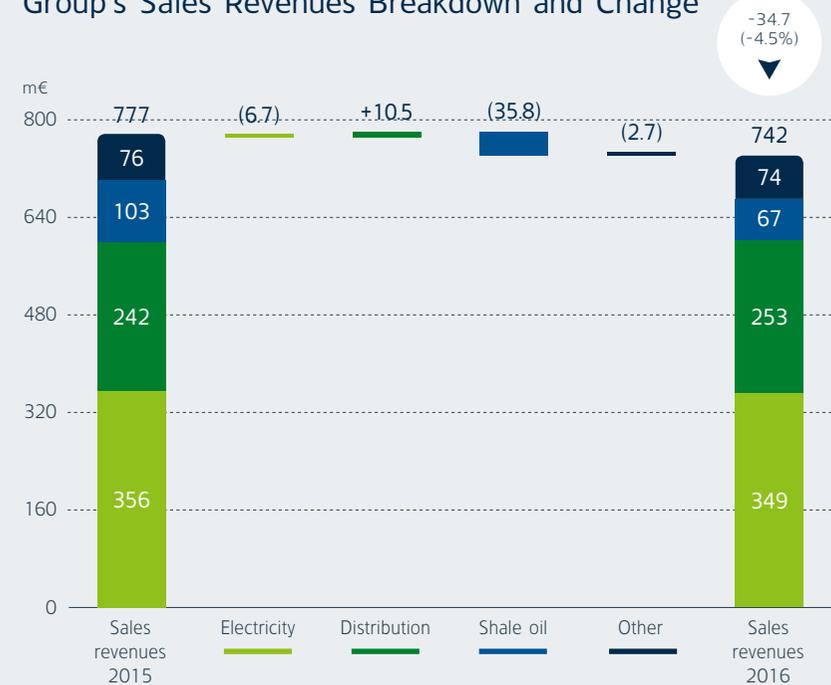
Revenue and EBITDA

Despite a difficult operating environment, Eesti Energia ended 2016 with results which were considerably better than we expected at the beginning of the year. Although sales revenue decreased slightly, EBITDA and net profit grew.

The Group's sales revenue for 2016 amounted to 742.1 million euros. Due to a negative external environment, revenue decreased by 4.5% (-34.7 million euros) year on year. EBITDA grew by 23.2%, rising to an exceptional 327.3 million euros (+61.6 million euros). Net profit grew by 322.4%, rising to 171.0 million euros (+130.5 million euros).

The decrease in sales revenue is primarily attributable to lower gain on derivative instruments. Gain declined on both electricity and liquid fuel derivatives.

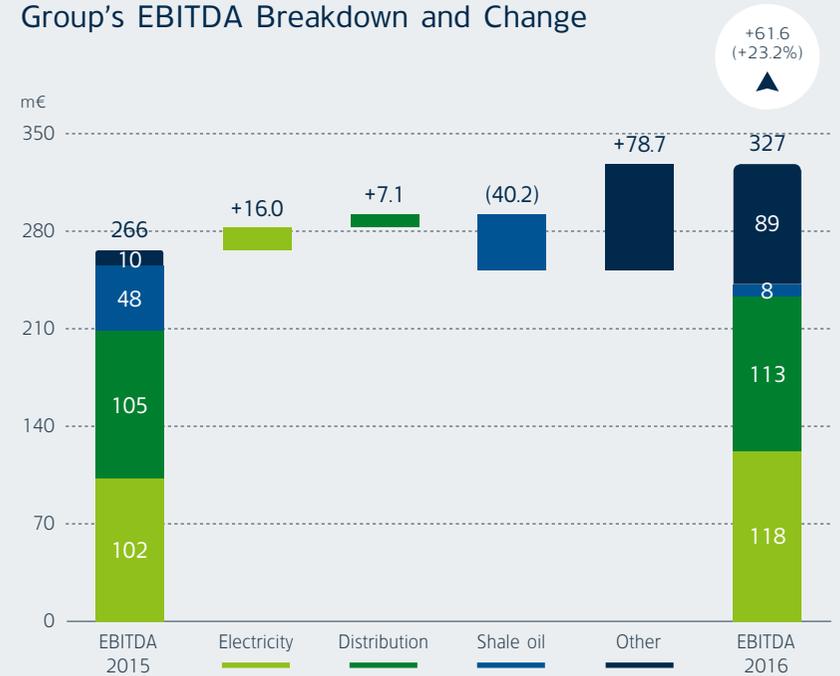
Group's Sales Revenues Breakdown and Change



Electricity and distribution EBITDA² grew significantly. The Group's EBITDA was substantially increased by an exceptional factor, which is reported in EBITDA on other products and services: the impact of liquidated damages of 68.6 million euros related to the construction of the Auvere power plant. As a result of negotiations, the builder of the Auvere power plant agreed to compensate Eesti Energia for unearned revenue caused by the delay in the works.

Exceptional net profit growth (+130.5 million euros compared to 2015) is partly attributable to the fact that in 2015 profit was weakened by a write-down of non-current assets of 65.5 million euros and income tax paid on dividends.

Group's EBITDA Breakdown and Change

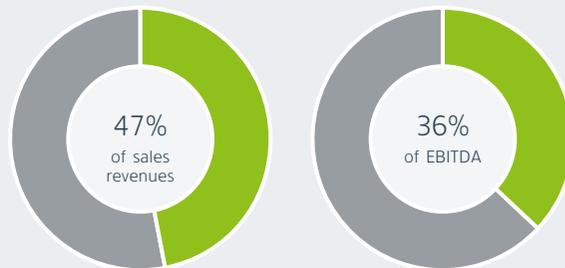


² Compared to *Annual report 2015*, segment reporting has been adjusted due to the specification of an accounting policy.

Electricity

Over the years, electricity has been one of the main sources of Eesti Energia's sales revenue and profit. Also in 2016, most of our revenue and EBITDA resulted from electricity sales.

Share of Electricity Product in Group's Sales Revenues and EBITDA



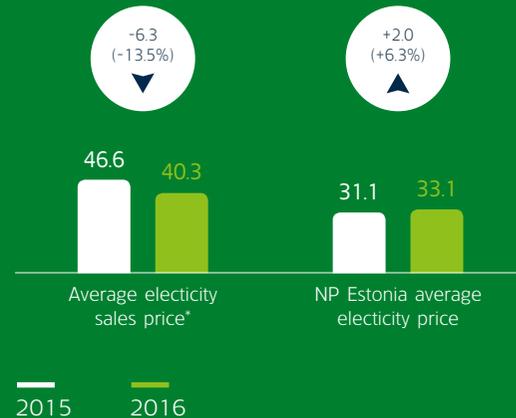
Electricity Sales Revenue

Although sales prices were more than 10% lower, we were able to keep sales revenue almost at the same level as in 2015. Electricity sales revenue amounted to 348.8 million euros, 1.9% down from 2015 (-6.7 million euros).

Average Sales Price

The average electricity sales price was 40.3 €/MWh, i.e. 13.5% lower than in 2015 (-6.3 €/MWh). The average sales price includes, among other items, the impact of derivative transactions. Excluding gain on derivative instruments, the average sales price of 2016 would have been 39.8 €/MWh, i.e. 5.1% lower (-2.1 €/MWh) than in 2015. Although gain on derivative instruments fell by 86.1%, gain on derivative transactions contributed 4.8 million euros to our revenue (-29.5 million euros).

Average Sales Price (€/MWh)



Electricity Sales Revenue (m€)



Electricity Sales Volume** (TWh)



* Total average sales price of electricity product (including retail sales, wholesale sales and gain on derivatives). Average sales price excludes subsidies for renewable energy and municipal waste gate fees.

** Sales volume includes total Auvere power plant sales volume.

Electricity Sales Volume and Eesti Energia's Market Share

In 2016, we sold 16.3% more electricity than in 2015. Retail sales grew by 5.5% and wholesale sales by 51.4%. Our electricity sales totalled 8,956 GWh (+1,257 GWh), including retail sales of 6,196 GWh (+321 GWh) and wholesale sales of 2,761 GWh (+937 GWh).

Retail sales broke down between markets as follows: Estonia 4,492 GWh (+226 GWh), Latvia 1,151 GWh (+17 GWh) and Lithuania 553 GWh (+78 GWh).

In terms of customers' electricity consumption volume, in 2016 Eesti Energia's market share in Estonia was 59% (-2.1 percentage points compared to 2015.)³. Market share decreased mainly due to changes in the large business customer segment.

Customers trust Eesti Energia: at the year-end when contracts are mostly renewed, 98.3% of our Estonian customers decided to extend their electricity contract. Most of our customers prefer packages with partly or fully fixed prices. At the beginning of 2017, Estonian customers purchased

³ According to the data of the Estonian transmission system operator Elering.

electricity from Eesti Energia at 447,408 consumption points (one customer may have several electricity consumption points). During the year, the number of consumption points decreased by around 9,600, mainly due to a decline in the number of residential customers.

In 2016, our electricity sales in Latvia and Lithuania totalled 1,704 GWh (+95 GWh). Sales grew by 5.9%, driven by successful sales and the fact that in 2016 opportunities for purchasing instruments for hedging cross-border risk between Estonia and Latvia increased. This allowed us to sell electricity in Latvia and Lithuania at a competitive fixed price. We sold fixed-price products, products indexed to the exchange price, and green energy. In 2016, Eesti Energia's market shares in Latvia and Lithuania were 16% and 5% respectively. Market shares grew year on year by +0.3 and +0.5 percentage points respectively. Eesti Energia's total market share in the Baltic countries was 26% (-0,6pp).

Electricity Production Volume

In 2016, we produced 9,071 GWh of electricity, 18.0% up on 2015 (+1,382 GWh). A significant factor that supported production growth was a decrease in production costs. The product cost of oil shale decreased and we could offer electricity on the exchange at a more competitive price.

Production growth was also underpinned by lower CO₂ emission allowance prices and more stable and larger output from the Auvere power plant.

Renewable energy output grew by 5.4%. We produced 380.3 GWh of renewable energy, most of it, i.e. 185.5 GWh, at wind farms (-16.9%, -37.7 GWh). The rise in renewable energy output is mainly attributable to growth in the quantity of biomass co-burnt in the oil-shale fired generating units where electricity produced from biomass grew to 115.1 GWh (+37.6%, +31.4 GWh). We received renewable energy and efficient co-generation support of 15.0 million euros (-1.0 million euros). The amount of support received decreased because output of renewable energy eligible to support declined.

Key Figures of Electricity Product

		2016	2015
Return on fixed assets*	%	9.8	6.2
Electricity EBITDA	€/MWh	14.4	14.2

* Excluding impairment of generation assets in December 2013 and December 2015.

Electricity EBITDA

Electricity EBITDA grew by 15.6% to 118.0 million euros (+16.0 million euros).

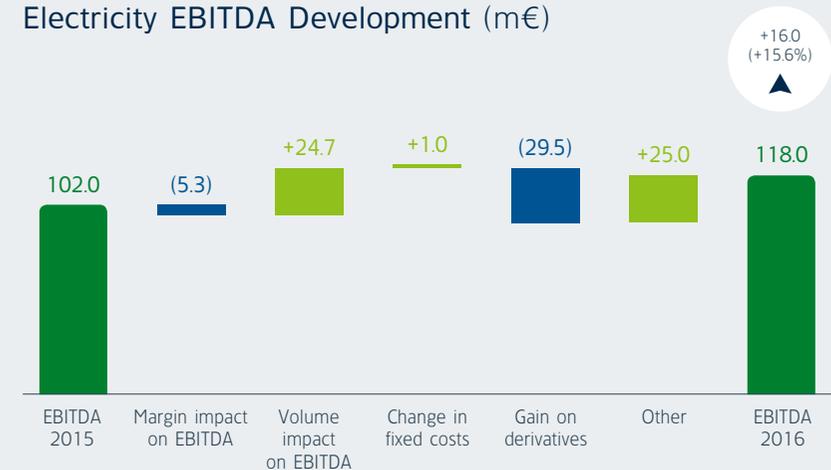
Growth in electricity sales volume increased EBITDA by 24.7 million euros.

The decrease in gain on derivative instruments reduced electricity EBITDA by 29.5 million euros.

The impact of a margin decrease was -5.3 million euros (-0.6 €/MWh). The margin decrease resulted from smaller sales revenue (impact: -21.2 million euros), which was partly offset by a decrease in variable costs (impact: +15.9 million euros). Average electricity sales revenue declined by 2.6 €/MWh, renewable energy subsidies decreased by 0.4 €/MWh and average sales price weakened by 2.1 €/MWh. Variable costs decreased mostly due to smaller border-crossing costs and environmental charges.

The impact of a change in fixed costs was +1.0 million euros. Personnel expenses and repair costs decreased (impacts: +8.1 million euros and +6.6 million euros respectively). Inventory-related fixed costs increased (impact: -13.8 million euros). Other impacts of +25.0 million euros comprise a change in the value of derivative instruments (impact: +23.9 million euros) and recognition of smaller environmental provisions (impact: +1.6 million euros).

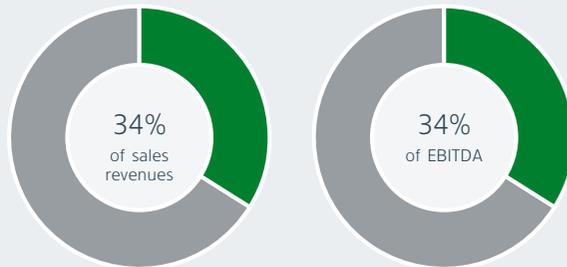
Electricity EBITDA Development (m€)



Distribution

Distribution service is Eesti Energia's second-largest source of revenue and profit.

Share of Distribution Product in Group's Sales Revenues and EBITDA



Distribution Sales Revenue, Sales Volume and Average Price

In 2016, distribution sales revenue and sales volume grew by 4.3% and 4.4% respectively. Sales revenue amounted to 252.7 million euros (+10.5 million euros) and sales volume to 6,616 GWh (+279.2 GWh).

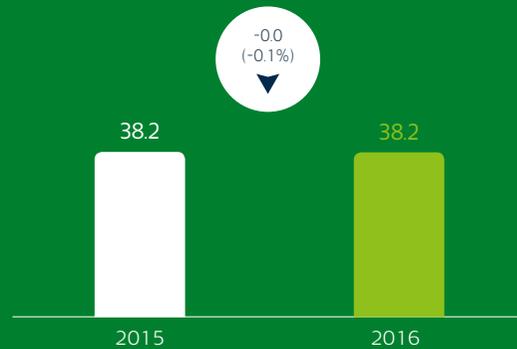
The growth in sales volume was underpinned by a favourable economic environment and weather conditions.

The average distribution price was 38.2 €/MWh (-0.02 €/MWh). The price level did not change compared to 2015 (-0.1%).

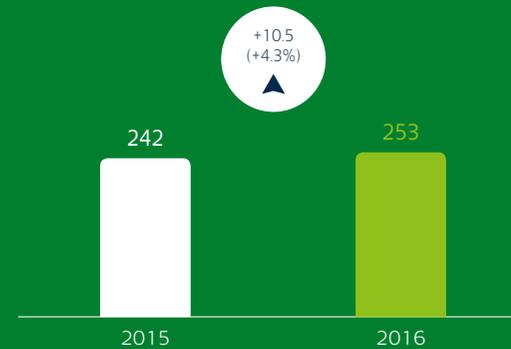
Network Losses

Network losses totalled 293.4 GWh, i.e. 4.1% of electricity entering the network (2015: 326.2 GWh, i.e. 4.8%). Losses decreased because new smart meters and balance meters measure quantities more accurately and help detect illegal and unmetered consumption more effectively.

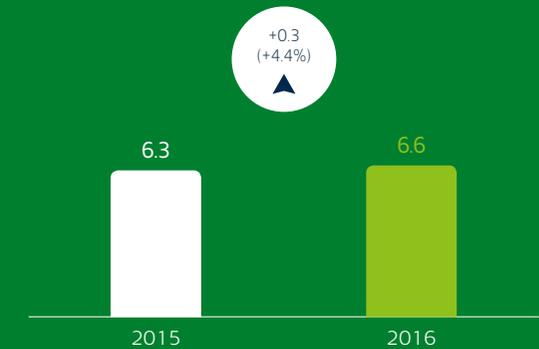
Distribution
Average Sales Price (€/TWh)



Distribution
Sales Revenue (m€)



Distribution
Volume (TWh)



Supply Interruptions

In 2016, the average duration of unplanned interruptions was 163 minutes (187 minutes in 2015), including the impact of the June and July storms of 52 minutes. The average duration of planned interruptions was 78 minutes (74 minutes in 2015). The rise in the figure for planned interruptions results from growth in network renewal.

The main factor that influences the number of interruptions is the weather. Power outages can be reduced by the replacement of regular overhead lines with weather-proof cables. At the end of 2016, 79% of Elektrilevi's low-voltage network and 37% of its high-voltage network was weather-proof.

Key Figures of Distribution Product

		2016	2015
Return on fixed assets	%	6.8	6.7
Distribution losses	GWh	293.4	326.2
SAIFI	Index	1.6	1.9
SAIDI (unplanned)	Index	163.0	186.6
SAIDI (planned)	Index	78.3	74.0
Adjusted RAB	m€	757.0	725.4

Distribution EBITDA

In 2016, distribution EBITDA grew by 6.7% to 112.6 million euros (+7.1 million euros).

Growth in distribution EBITDA was supported by growth in distribution sales volume, which increased EBITDA by 6.8 million euros, and a decrease in fixed costs, which increased EBITDA by 0.8 million euros.

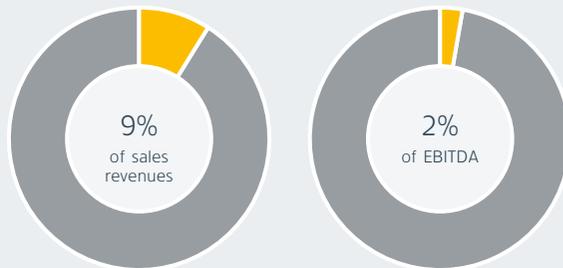
Margin change lowered distribution EBITDA by 0.5 million euros. Margin change comprises the decrease in the average sales price of the distribution service (impact: -0.1 million euros) and growth in variable costs (impact: -0.4 million euros).

Distribution EBITDA Development (m€)



Shale Oil

Share of Shale Oil Product in Group's Sales Revenues and EBITDA



Production of shale oil has strong potential but due to a negative external environment in 2016 the contribution of shale oil to the Group's sales revenue and EBITDA decreased considerably.

Shale Oil Sales Revenue and Sales Volume

In 2016, shale oil sales revenue amounted to 67.0 million euros and sales volume was 301.8 thousand tonnes. Sales volume declined by 4.2% (-13.3 thousand tonnes) but owing to the price decrease sales revenue fell by 34.8% (-35.8 million euros). Sales volume decreased because in the first half-year we reduced oil production due to low prices and carried out maintenance operations at the oil plants.

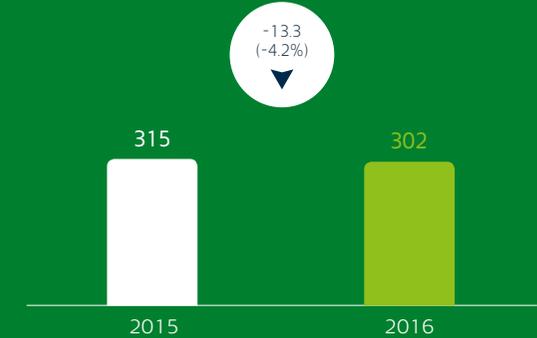
Average Shale Oil Sales Price (€/t)



Shale Oil Sales Revenue (m€)



Shale Oil Sales Volume ('000 tonnes)



Average Sales Price

In 2016, the average sales price of shale oil fell by 32.0% to 221.9 €/t (104.2 €/t). The price decrease is mainly attributable to a decline in gain on derivative instruments. Gain on derivative instruments fell by 89.4% to 12.7 €/t (-107.1 €/t). Excluding the impact of derivative transactions, the average sales price of shale oil was 209.2 €/t (206.4 €/t in 2015). In 2016, the world market price of the reference product, heavy fuel oil, declined by 17%.

The fall in the average sales price of shale oil was held back by the fact that we were able to sell middle oil for a market price closer to that of the reference product (heavy fuel oil).

Key Figures of Shale Oil Product

		2016	2015
Return on fixed assets*	%	-4.3	10.4
Shale oil EBITDA	€/t	25.9	152.4

* Excluding the impairment of assets in December 2015 in relation to Utah project.

Shale Oil Production Volume

In 2016, we produced 317.7 thousand tonnes of shale oil. Production volume decreased by 5.6% (-18,7 thousand tonnes). Output was reduced by cutbacks in production as well as repair and renovation work carried out in the period in which the market prices of shale oil were the lowest.

Shale Oil EBITDA

In 2016, shale oil EBITDA decreased by 83.7% to 7.8 million euros (-40.2 million euros).

The decline in gain on derivative instruments reduced shale oil EBITDA by 33.9 million euros.

The impact of a decrease in shale oil sales volume was -1.3 million euros.

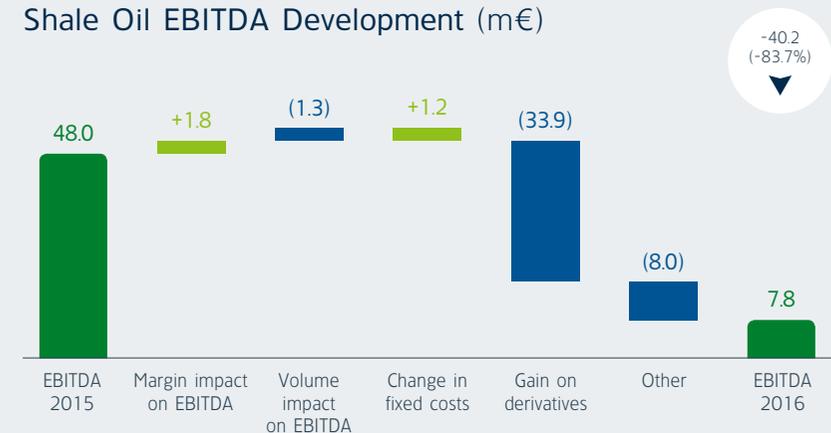
The impact of margin growth was +1.8 million euros (+6.1 €/t).

The average sales price increased (excluding gain on derivative instruments) and lower variable costs increased shale oil EBITDA by 1.0 million euros. Variable costs decreased mostly due to a decline in resource charges, which resulted from a lower market price of fuel oil.

The impact of a change in fixed costs was +1.2 million euros. The largest items within the figure are a decrease in personnel expenses (impact: +3.3 million euros), growth in inventory-related fixed costs (impact: -3.6 million euros) and a decline in repair expenses (impact: +0.9 million euros).

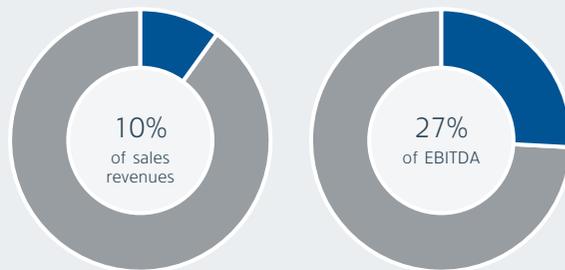
The impact of other factors was -8.0 million euros. The main other factors were a decrease in the value of derivative instruments (impact: -8.9 million euros) and recognition of smaller environmental provisions (impact: +0.8 million euros).

Shale Oil EBITDA Development (m€)



Other Products and Services

Share of Other Products and Services Product in Group's Sales Revenues and EBITDA



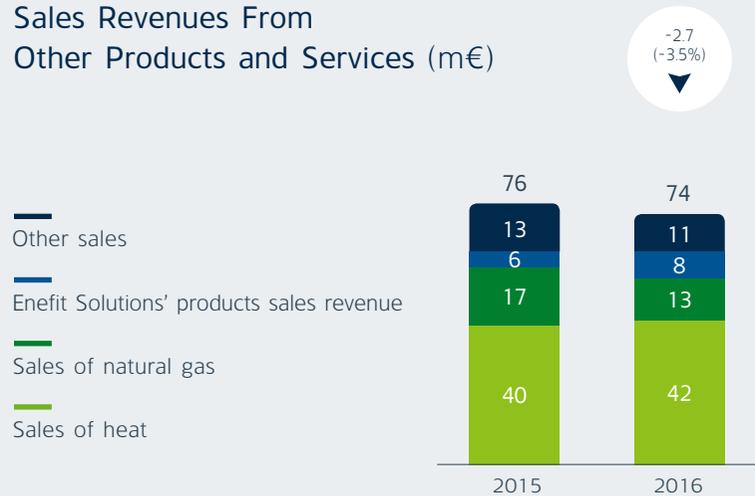
Sale of heat, natural gas and industrial equipment supplements Eesti Energia's product portfolio and generates additional revenue. In addition to the sale of heat, we see potential in the sale of natural gas: in 2016 we increased our market share in the Estonian gas market to 23.5%.

Other Products and Services Sales Revenue

In 2016, our other products and services generated sales revenue of 73.5 million euros. Sales revenue decreased by 3.5% (-2.7 million euros).

Sales revenue on the products of Enefit Solutions which produces industrial equipment grew by 1.9 million euros (+32.0%) and heat sales revenue increased by 1.2 million euros (+2.9%). Revenue from the sales of natural gas decreased by 3.7 million euros (-22.2%) due to a lower average sales price, which resulted from weaker fuel prices in the global market.

Sales Revenues From Other Products and Services (m€)

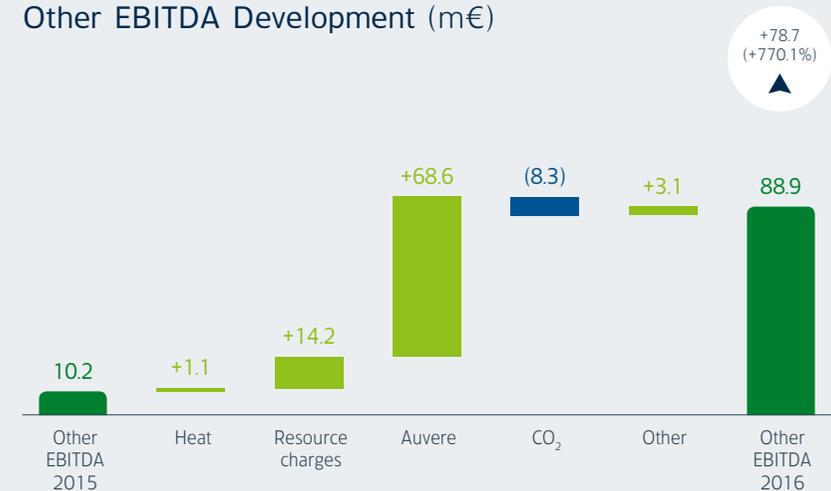


Other Products and Services EBITDA

In connection with exceptional factors, EBITDA on other products and services grew by 770.1% to 88.9 million euros (+78.7 million euros).

The total impact of liquidated damages related to the delay in the delivery of the Auvere power plant was +68.6 million euros. The figure comprises liquidated damages agreed with the builder of 66 million euros which will be settled by July 2017 and additional monthly liquidated damages which will accrue until the delivery of the power plant.

Other EBITDA Development (m€)



Retrospective reduction of resource charge rates had an impact of +14.2 million euros.

The impact of CO₂ emission allowances of -8.3 million euros results from the fact that in 2015 the Group earned 8.3 million euros from the sale of surplus emission allowances but in 2016 emission allowances were not sold.

Heat EBITDA grew by 1.1 million euros.

EBITDA for the comparative period was influenced, among other things, by the adjustment of a loan provided to a subsidiary (impact: +11.0 million euros).



CASH FLOWS

The Group's net operating cash flow for 2016 amounted to 200.3 million euros. Compared to EBITDA (327.3 million euros), net operating cash flow was 38.8%, i.e. 127.0 million euros, smaller.

The key item that caused net operating cash flow to be smaller than EBITDA (327.3 million euros) was recognition of a receivable for liquidated damages of 60.6 million euros related to the Auvere power plant (the damages are settled in instalments).

The impact of settlements related to CO₂ emission allowances was +5.2 million euros.

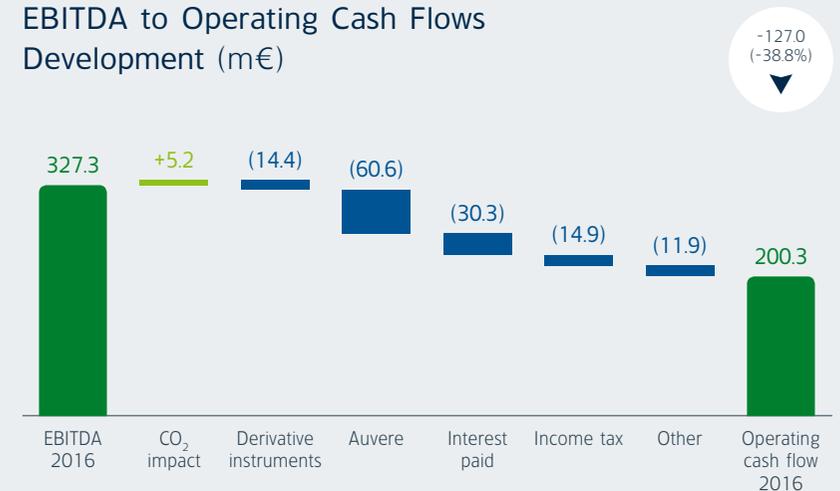
The impact of derivative instruments (excluding CO₂ instruments) was -14.4 million euros, comprising the impacts of electricity derivatives of -28.7 million euros and oil derivatives of +14.3 million euros. The impacts of derivative instruments comprise both monetary and non-monetary impacts on EBITDA and operating cash flows.

Loan interest payments lowered net operating cash flow compared to EBITDA by 30.3 million euros.

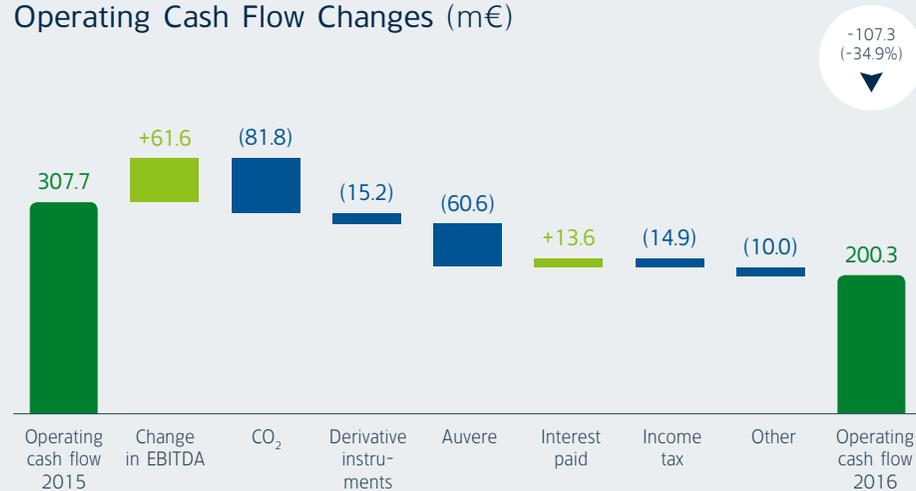
The impact of income tax recognised in 2015 and paid at the beginning of 2016 was 14.9 million euros.

Other impacts totalled -11.9 million euros. The impact of an inventory decrease of +6.7 million euros resulted mostly from the consumption of oil shale and shale oil stocks. The impact of a change in other working capital components of -10.1 million euros consists mainly of growth in oil industry receivables, which results from sales transactions concluded at the year-end which are to be settled in the next financial year. The impact of regular recognition of network connection fees was -7.0 million euros.

EBITDA to Operating Cash Flows Development (m€)



Operating Cash Flow Changes (m€)



Compared with 2015, operating cash flow decreased by 34.9% (-107.3 million euros).

The impact of settlements related to CO₂ emission allowances was -81.8 million euros. Above all, this resulted from the fact that in 2015 cash was received for allowances sold and in 2016 cash was paid for allowances purchased.

The impact of derivative instruments (excluding CO₂ instruments) was -15.2 million euros, comprising the impacts of

electricity derivatives of -38.7 million euros and oil derivatives of +23.5 million euros.

The impact of the recognition of liquidated damages receivable from the builder of the Auvere power plant was -60.6 million euros (mainly a non-cash impact on EBITDA).

In 2016, loan interest payments were 13.6 million euros smaller than the year before.

The impact of income tax recognised in 2015 and paid in 2016 was -14.9 million euros.

Other impacts totalled -10.0 million euros. The impact of an inventory change was +37.8 million euros, resulting mostly from a change in oil shale inventories (in 2015, oil shale inventories grew by 28.2 million euros, in 2016 they decreased by 13.6 million euros). The impact of other changes in working capital was -38.3 million euros, resulting mainly from a change in receivables (in 2015 receivables decreased by 15.5 million euros, in 2016 receivables increased by 9.4 million euros) and a change in prepaid taxes of 3.2 million euros.

EBITDA for the comparative period was influenced, among other things, by the adjustment of a loan provided to a subsidiary by 11.0 million euros.

INVESTMENT

Investment in new growth

In 2016 our capital expenditures totalled 140.7 million euros (-42.7%, -105.0 million euros). Expenditures on the distribution network totalled 88.5 million euros (-5.2%, -4.8 million euros) and maintenance and repair expenditures (excluding the distribution network) amounted to 21,6 million euros (-47.5%, -19.6 million euros). Maintenance and repair expenditures on

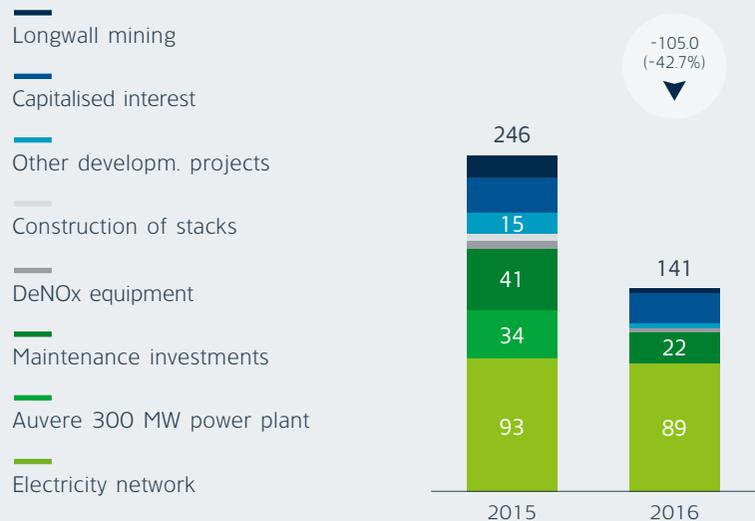
the Narva power plants decreased by 12.0 million euros (-74.2%). Expenditures on Eesti Energia's recent years' largest investment project, the Auvere power plant, totalled 1.2 million euros (-96.4%, -32.8 million euros). The decrease in the capital expenditures of 2016 results mainly from the deferral of the last payment for the Auvere power plant.

New Strategic Development Projects

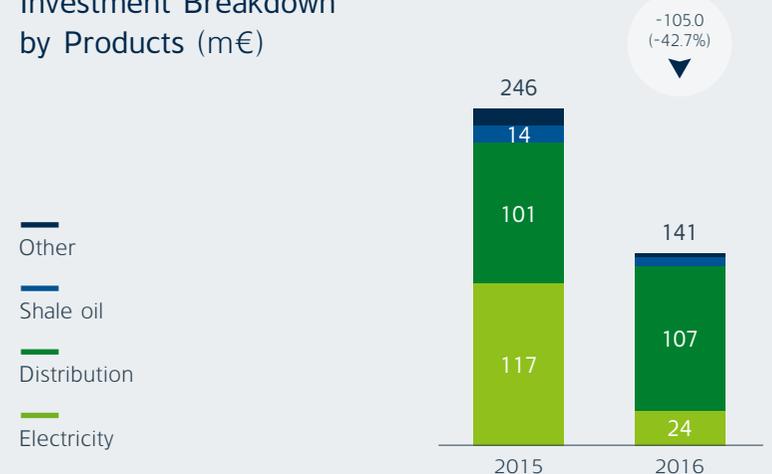
In the period 2016-2020 we are going to carry out a number of projects outlined in our strategic action plan, which are aimed at increasing Eesti Energia's competitiveness. A more detailed overview of the projects is provided in the strategy chapter. In 2016, we incurred mostly development expenses in connection with those projects and not yet expenditures to be recognised as assets.

Capital expenditures on increasing the share of oil shale gas burnt by generating unit 8 of the Eesti power plant amounted to 1.5 million euros in 2016. The total cost of the project is 15.1 million euros.

Capex Breakdown by Projects (m€)



Investment Breakdown by Products (m€)



Auvere Power Plant

The Auvere power plant whose construction started in 2011 began operating in 2015 but delivery of the plant has been delayed because during the testing and commissioning period it appeared that under certain circumstances the particle emissions of the plant exceed the regulatory limit. The builder, General Electric, is going to install additional fabric filters. General Electric has signed an interim agreement with Eesti Energia according to which it will pay for the delay in the delivery of the power plant liquidated damages of 66 million euros by July 2017. The parties have also agreed the methodology by which calculation of liquidated damages will continue until the delivery of the plant. According to the agreement, the plant which meets all contractual parameters will be delivered to Eesti Energia in October 2017. Until then the Auvere power plant will operate at modes and loads where its emissions meet requirements.

The Auvere power plant is a modern 300 MW circulating fluidised bed (CFB) power plant where oil shale fuel can be supplemented with wood chips (to the extent of 50%), peat (to the extent of 20%) and oil shale gas (to the extent of 10%). This allows reducing its emissions to the level of a modern gas-fired plant. The maximum annual net generation of the power plant is around 2.2 TWh, i.e. the plant can cover around one fourth of Estonia's annual electricity consumption.

In support of the construction of the Auvere power plant, the European Commission allowed Estonia to allocate to Eesti Energia 17.7 million tonnes of free CO₂ emission allowances for the period 2013–2020. Of this amount, 5 million tonnes was received in April 2014, 4.3 million tonnes in April 2015, and 3.6 million tonnes in April 2016.

The planned cost of the project is 638 million euros. By the end of 2016, 567 million euros (89%) of this had been invested.

Improvement of Network Quality

In 2016, capital expenditures on maintaining and improving the quality of the distribution network totalled 88.5 million euros (2015: 93.3 million euros). During the year, 253 substations and 2,699 kilometres of network were built (2015: 336 substations and 1,906 kilometres of network).

In 2016, distribution network operator Elektrilevi successfully completed a four-year project in the course of which smart meters were installed at all consumption points in the network. The project released Elektrilevi's customers from the obligation to submit the reading. In the future, the remote reading system can also be used to determine network quality and profile loads more accurately. In addition, the project has helped reduce network losses noticeably.

In 2016, 96 thousand new smart meters were installed and 192 thousand meters were switched over to the remote

reading system. Altogether, in the course of the project 596 thousand new smart meters were installed. The total cost of the project was 92.9 million euros.

Implementation of Longwall Mining

Eesti Energia successfully implemented longwall mining at its Estonia mine. Under the longwall technology, the costs of oil shale mining are lower than under the previously applied room-and-pillar technology because road way construction volumes are smaller. The method is similar to conventional room-and-pillar mining where pillars support the overlying strata but mining takes place along a long work face that may extend to 700 metres in place of the conventional 200 metres. Preparations for the project began in 2014. The planned cost of the project was 21 million euros. By the end of 2016, 19.5 million (93%) of this had been invested.

Electricity and Oil Production Projects in Jordan

Eesti Energia has electricity and oil production development projects in Jordan which were launched in 2006 with a view to building an oil shale power plant and an oil industry in Jordan. Jordan's first oil shale power plant with a gross capacity of 554 MW and net capacity of 470 MW should be completed by 2020.

In 2016, Eesti Energia's interest in both projects was 65%. The projects' co-investors are YTL Power International Berhad from Malaysia with a 30% interest and Near East Investment from Jordan with a 5% interest.

In 2016, the investors and Chinese banks signed financing agreements for the Jordanian electricity project of 1.6 billion US dollars (approx. 1.5 billion euros) and agreements required for obtaining a credit guarantee. The guarantee needed the approval of the government of China. In January 2017, China's

export credit agency Sinosure notified Eesti Energia of the fact that the government of China had approved the credit guarantee.

In May 2016, we signed a share sale agreement with Guangdong Yudean Group Co by which Eesti Energia's interest in the electricity project will decrease to 10%. The transaction will be finalised when the official guarantee policy has been issued and the preliminary terms of the financing agreements have been fulfilled.

In 2016, the investors in the electricity project focused on meeting the preliminary terms of the financing agreements. In addition, the project agreements concluded with the government of Jordan in 2014 were amended and electricity production and mining permits were obtained.

The next steps in the oil project will be decided when the financing activities of the electricity project have been completed.



FINANCING

At the year-end, the nominal value of the Group's borrowings was 999.2 million euros (1,018.5 million euros at the end of 2015) and the amortised cost of the Group's borrowings was 939.8 million euros (951.8 million euros at the end of 2015). Borrowings comprised Eurobonds listed on the London Stock Exchange with a nominal value of 758.3 million euros and loans from the European Investment Bank (EIB) with a nominal value of 240.9 million euros.

Debt Maturity (m€)



In contrast to 2015 when the Group refinanced bonds issued and extended their average maturity, in 2016 borrowings did not change significantly. The only change resulted from regular repayments to EIB of 19.3 million euros.

At the end of 2016, the Group had liquid assets of 223.3 million euros. Liquid assets grew more than expected because some payments for the Auvere power plant which were sched-

Liquidity Development in 2016 (m€)



uled to be made in 2016 were deferred and the owner decided not to take dividends. In addition to liquid assets, at the year-end the Group had undrawn credit facilities of 220 million euros including revolving credit facilities of 150 million euros maturing in July 2020 from two regional banks (SEB and OP Corporate Bank) and a long-term loan agreement of 70 million euros with EIB. In 2016, the term for drawing the loan was extended to October 2017.

At the reporting date, the Group's credit ratings were BBB (Standard & Poor's) and Baa3 (Moody's). Due to the price decrease in electricity and shale oil markets, in April 2016 Moody's downgraded Eesti Energia's rating by one notch to Baa3. At the year-end the outlook of the rating was stable. In June, Standard & Poor's confirmed Eesti Energia's previous BBB rating. The outlook of the rating is negative.

Interest is paid on borrowings at the weighted average interest rate, which was 2.65% at the end of 2016 (2.92% at the end of 2015). The Group has predominantly hedged the risk resulting from fluctuations in the base interest rate (for 95% of borrowings the base interest rate is fixed until maturity and 5% of borrowings have floating rates). All borrowings are denominated in euros.

At the end of 2016, the Group's equity amounted to 1,699.0 million euros. Eesti Energia's sole shareholder is the Republic of Estonia. During the year, no dividends were distributed. In 2017, the owner expects from Eesti Energia a dividend of 47.0 million euros.

At the year-end, the Group's net debt amounted to 716.6 million euros (792.0 million euros at the end of 2015) and net debt to EBITDA ratio was 2.2 (3.0 at the end of 2015). The objective of Eesti Energia's financing policy is to maintain the net debt to EBITDA ratio below 3.5. Under its loan agreements, Eesti Energia has undertaken to comply with certain financial covenants. At the end of 2016, the Group's financial indicators complied with all contractual covenants.

Net Debt/EBITDA Ratio and Financial Leverage





OUTLOOK FOR 2017

We expect that in 2017 our sales revenue and capital expenditures will increase and EBITDA will decrease compared with 2016. Excluding the positive impact of the liquidated damages related to the Auvere power plant (68.6 million euros) and the retrospective reduction of the resource charge rates (14.2 million euros) on 2016, EBITDA for 2017 will remain at the same level as in 2016.

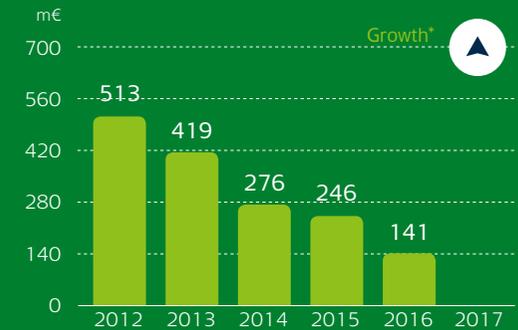
Sales Revenues



EBITDA



Investments



* Slight growth/slight decline until 5%, growth/decline >5%.

The factor which will have a positive impact on electricity sales revenue is the expected rise in the average sales price of electricity, which will also have an impact on electricity EBITDA. We expect that our electricity output will increase in 2017.

Shale oil sales revenue and EBITDA will probably increase because the market price of shale oil will be higher.

Capital expenditures will increase compared to 2016, mainly in connection with growth in the volume of development projects. According to plan, the largest capital investments of 2017 are the final payment for the Auvere power plant and the Tootsi wind farm.

We are planning to pay the owner for 2016 a dividend of 47.0 million euros, which will give rise to income tax expense of 11.8 million euros. Final approval of the dividend distribution is at the discretion of the owner.

Hedging Transactions

Eesti Energia's revenues from electricity and liquid fuel sales depend on global market prices. The key factors which influence our performance indicators are electricity price on the Nord Pool power exchange and the world market price of fuel oil with 1% sulphur content, which is the reference product for shale oil.

Our forward sales for delivery in 2017 comprise 4.7 TWh of electricity (including forward sales in the retail market) at an average price of 35.4 €/MWh and 286.8 thousand tonnes of shale oil at an average price of 237.0 €/t. Forward sales

for delivery in 2018 comprise 0.9 TWh of electricity at an average price of 33.6 €/MWh and 179.6 thousand tonnes of shale oil at an average price of 252.5 €/t.

Our CO₂ emission allowance position for 2017 amounts to 9.1 million tonnes at an average price of 5.6 €/t (comprises futures, free emission allowances transferred as investment support and the surplus of previous periods). The position for 2018 amounts to 2.2 million tonnes (comprises free emission allowances transferred as investment support.)



CORPORATE GOVERNANCE

Eesti Energia's sole shareholder is the Republic of Estonia that holds an interest in Eesti Energia to:

- add value to Estonia's primary natural resource, oil shale, and related expertise;
- grow the company's value and earn stable dividend income;
- ensure the security of power supply in Estonia;
- employ regional labour resources;
- reduce adverse environmental impacts.

The owner's expectations consist of the principles the Group should follow in designing its strategy and action plan, and strategic and financial objectives.

Strategic objectives set by the owner:

- to maintain a significant share of the regional electricity market;
- to reduce CO₂ emissions in power production;

- to develop oil production and other ways of adding value to oil shale;
- to increase international recognition of Estonia's competence in oil shale energy;
- to improve the quality of network service;
- to minimise the environmental impacts of the company's operations.

Financial objectives set by the owner:

- to organise operations so that the Group earns a sufficient return on equity;
- to improve operating efficiency;
- to ensure stable and increasing dividend income;
- to organise operations so that the Group has an optimal capital structure and the industry's average risk level;
- to finance investments predominantly with the Group's operating cash flow and debt capital;
- to ensure that each of the Group's business lines generates independent and measurable return on invested capital.

Management Principles

The ambition of Eesti Energia's supervisory board and management board is to develop and manage Eesti Energia so that it would be a positive example for all other Estonian companies in terms of clarity of strategy, good corporate governance practices, operating efficiency, and financial performance

as well as collaboration with all stakeholders. The management board and the supervisory board manage Eesti Energia in accordance with the owner's expectations, the Group's vision, strategy and values, and applicable laws and regulations.

Organisational Structure

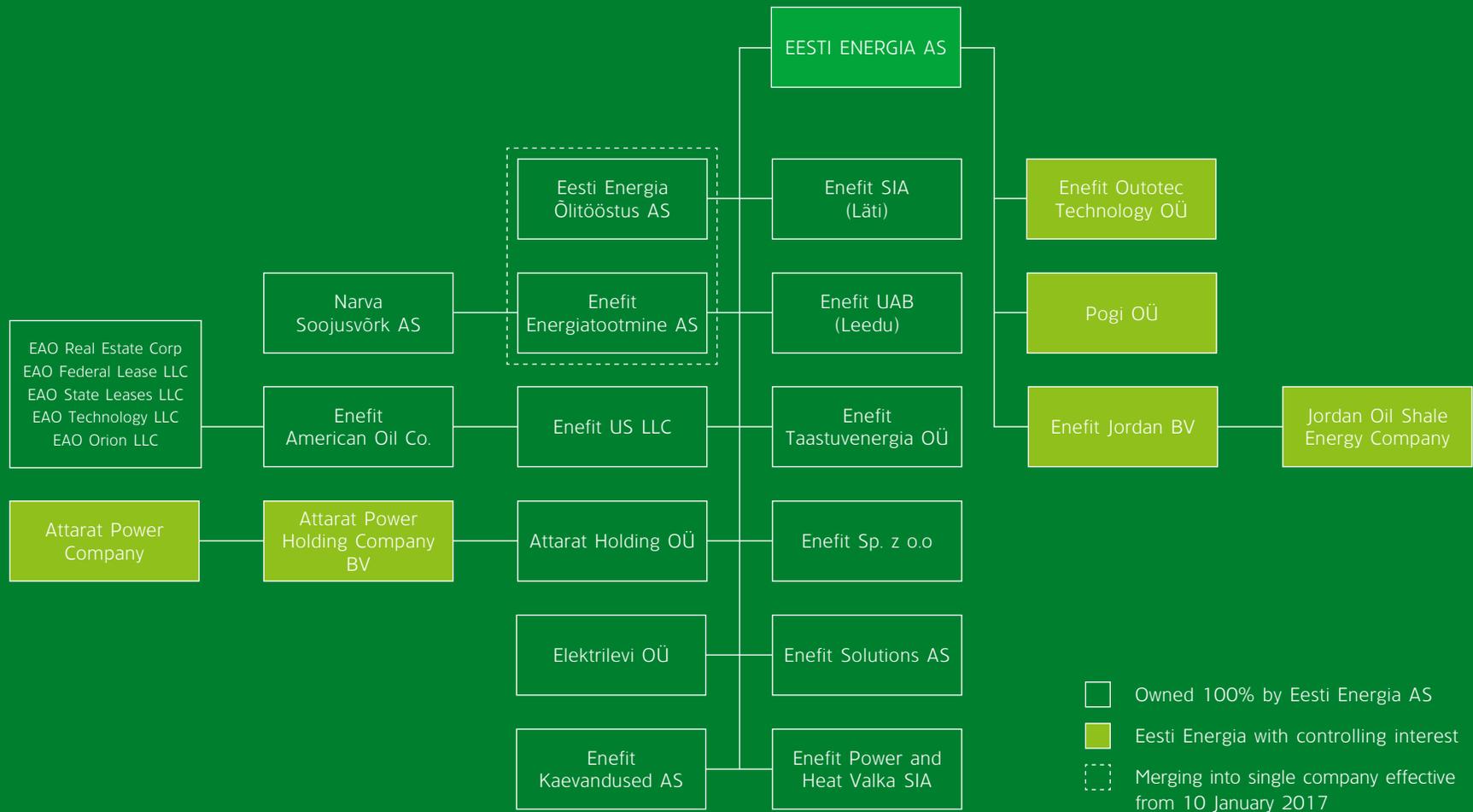
Eesti Energia strives to keep the Group's structure simple and aligned with the organisation's goals and needs. In 2016, several changes were made to streamline the management structure.

- AS Narva Elektriijaamad and Eesti Energia Õlitööstus AS were merged into a single company – Enefit Energiatootmine AS.
- Eesti Energia Tehnoloogiatööstuse AS and its two subsidiaries, Eesti Energia Hoolduskeskuse AS and Eesti Energia Testimiskeskuse AS, were merged into a single company – Enefit Solutions AS.
- Renewable energy units (Iru power plant and other renewable energy and co-production units) were incorporated into a new company – Enefit Taastuenergia OÜ.

In 2016, Eesti Energia established a subsidiary in Poland – Enefit Sp. z o.o. – which is going to engage in energy sales. The subsidiary was established to implement the strategy of expanding to new markets.

Group structure as at 31 December 2016*

* Comprises entities in which the interest of Eesti Energia AS equals or exceeds 51%.



Eesti Energia's Governing Bodies

The governing bodies of the Group's parent, Eesti Energia AS, are the general meeting, the supervisory board and the management board.

General Meeting

The general meeting is Eesti Energia's highest governing body, which decides, among other things, the establishment and acquisition of new and the liquidation of existing companies, the appointment and removal of the members of the supervisory board, major investments, the appointment of the auditor, and the approval of the results for the financial year.

Eesti Energia's sole shareholder is the Republic of Estonia which is represented at the general meeting by the minister of finance.

The annual general meeting is convened once a year, within six months after the end of the Group's financial year, at the time and in the place determined by the management board.

Supervisory Board

Eesti Energia's supervisory board is a governing body that plans the Group's activities, organises the Group's management and supervises the activities of the management board. Eesti Energia's supervisory board has eight members who are appointed by the resolution of the minister of finance who represents the sole shareholder. The supervisory board is headed by the chairman.

The requirements and expectations for the members of Eesti Energia's supervisory board are set forth in the Commercial Code and the State Assets Act. In addition, the supervisory board is guided by the articles of association of Eesti Energia AS and the rules of procedure of the supervisory board. The primary functions of the supervisory board are as follows:

- supervising the implementation of the Group's strategy;
- planning the Group's activities, adopting major strategic decisions, organising management, and supervising the activities of the management board.

The supervisory board communicates the results of its supervision activities to the sole shareholder.

In 2016, the legal adviser of the supervisory board was Attorney at Law Sven Papp from law firm Raidla Ellex.

At the end of 2016, the supervisory board of Eesti Energia comprised the chairman of the supervisory board Erkki Raasuke and the members of the supervisory board Meelis Virkebau, Danel Tuusis, Märt Vooglaid, Rannar Vassiljev, Väino Kaldoja, Ants Pauls and Veiko Tali. Based on a resolution adopted by the owner in January 2017, Erkki Raasuke and Märt Vooglaid were removed from the supervisory board and Kaie Karniol was appointed as a new member of the supervisory board. In addition, based on a resolution adopted by the sole shareholder, Meelis Virkebau was removed from the supervisory board effective from 28 February 2017.

Remuneration of the members of Eesti Energia's supervisory board is regulated by the State Assets Act according to which the amount of the remuneration and its payment procedure are at the discretion of the sole shareholder. The limits for the remuneration are provided in a regulation issued by the minister of finance. Additional remuneration may be provided for participation in the work of a committee formed by the supervisory board (e.g. the audit committee). The members of the supervisory board are not entitled to termination benefits or other additional remuneration. As a rule, the supervisory board meets once a month, except during the summer season. In 2016, the supervisory board held 12 meetings and 3 resolutions were passed without calling a meeting.

Supervisory Boards of Subsidiaries and Associates

The powers and responsibilities of the members of the supervisory boards of Eesti Energia's subsidiaries and associates are determined by their articles of association. Their supervisory boards consist mostly of the members of Eesti Energia's management board.

The meetings of the supervisory boards of subsidiaries and associates take place according to need and are called in accordance with the Group's rules, the subsidiary's or associate's articles of association, the law and agreements with co-shareholders.

Supervisory Board Members' Participation in Meetings and Total Remuneration Paid

	PARTICIPATION IN MEETINGS 2016	TOTAL REMUNERATION IN 2016 (€)	TOTAL REMUNERATION IN 2015 (€)
ERKKI RAASUKE	12	5,675	5,675
VÄINO KALDOJA	12	4,257	1,064
ANTS PAULS	12	4,257	1,016
VEIKO TALI	11	3,902	1,016
TANEL TUUSIS	10	3,547	4,257
RANNAR VASSILJEV	12	4,257	145
MEELIS VIRKEBAU	12	4,257	4,257
MÄRT VOGLAID	10	3,547	3,902

Supervisory Board

(as at 31 December 2016)



ERKKI RAASUKE / 45
Chairman

Term of office:
31.08.2014 – 24.01.2017
(Chairman of the Supervisory Board since 01.09.2014)



VÄINO KALDOJA / 60
Member

Term of office:
09.09.2015 – 09.09.2018



VEIKO TALI / 56
Member

Term of office:
06.10.2015 – 06.10.2018



MEELIS VIRKEBAU / 59
Member

Term of office:
28.08.2014 – 28.02.2017



ANTS PAULS / 76
Member

Term of office:
06.10.2015 – 06.10.2018



DANEL TUUSIS / 46
Member

Term of office:
12.06.2014 – 11.06.2017



RANNAR VASSILJEV / 35
Member

Term of office:
17.12.2015 – 17.12.2018



MÄRT VOOGLAID / 48
Member

Term of office:
21.09.2011 – 24.01.2017

Management Board

The Group's executive management is the responsibility of Eesti Energia's management board which follows the lawful instructions of the supervisory board. The chairman of the management board is appointed by the supervisory board. The members of the management board are approved by the supervisory board based on proposals made by the chairman of the management board.

In 2016, the composition of Eesti Energia's management board did not change. At the year-end, the management board of Eesti Energia comprised the chairman of the management board Hando Sutter and the members of the management board Andri Avila, Raine Pajo, Margus Vals and Andres Vainola. The areas of responsibility of the members of the management board are outlined in the following overview.

Remuneration of the members of Eesti Energia's management board is regulated by the State Assets Act. The amount of their remuneration is at the discretion of the supervisory board. The members of the management board are remunerated for

fulfilling their responsibilities as members of the management board. The remuneration is set out in the contracts signed with the members of the management board and it can be altered subject to mutual agreement. The members of the management board may be paid additional remuneration. The total amount of additional remuneration paid during the financial year may not exceed fourfold average monthly remuneration received by the member of the management board in the previous financial year. Assignment of additional remuneration must be justified and consistent with the Group's performance, value added and market position. Termination benefits may only be paid if the supervisory board removes a member of the management board on its initiative before the term of office of the member of the management board expires and the amount may not exceed threefold monthly remuneration of the member of the management board

As a rule, the management board meets once a week. Where necessary, meetings are held electronically. In 2016, 57 meetings were held, five of which were conducted electronically.

Total Remuneration Paid to the Management Board

	PARTICIPATION IN MEETINGS 2016	TOTAL REMUNERATION IN 2016 (€)	TOTAL REMUNERATION IN 2015 (€)
HANDO SUTTER	51	163,850	135,600
ANDRI AVILA	54	105,850	73,000
RAINE PAJO	57	105,850	116,460
ANDRES VAINOLA	49	134,850	105,600
MARGUS VALS	51	105,850	87,600

Management Board (as at 31 December 2016)



HANDO SUTTER / 46

Chairman of the Management Board and Chief Executive Officer

Term of office:

1 December 2014 -
30 November 2017

PREVIOUS CAREER

- Nord Pool Spot AS: Regional Market Manager, Estonia, Latvia, Lithuania and Russia
- US Invest AS: Development Adviser
- Olympic Entertainment Group AS: Chief Operating Officer

EDUCATION

- Estonian Business School, MBA Course
- Tallinn University of Technology, Mechanical Engineer



ANDRI AVILA / 41

Member of the Management Board and Chief Financial Officer

Term of office:

1 March 2015 -
30 November 2017

PREVIOUS CAREER

- Premia Foods AS: Member of the Management Board/Chief Financial Officer
- Olympic Entertainment Group AS: Chairman of the Management Board
- Olympic Entertainment Group AS: Member of the Management Board/Chief Financial Officer/ Chief Operating Officer

EDUCATION

- Concordia International University Estonia, International Business Administration *cum laude*



RAINE PAJO / 40

Member of the Management Board
Area of responsibility: energy production

Term of office:

1 December 2006 -
30 November 2017

PREVIOUS CAREER

- Eesti Energia: Member of the Management Board, Technical Director, environment, electricity and heat production, energy trading, technology industry, oil production
- OÜ Põhivõrk (current name Elering): Chairman of the Supervisory Board, Member of the Management Board, Head of Development Department, Director of Electrical Grid Planning Division, Client Account Manager
- Finnish Transmission System Operator Fingrid Oy: Network Planner
- AS Ecomatic: Product Manager

EDUCATION

- Tallinn University of Technology, MA in Business Administration
- Tallinn University of Technology, MSc and Doctor of Engineering
- Tallinn University of Technology, Electrical Engineer



MARGUS VALS / 37

Member of the Management Board
Area of responsibility: projects, technology and new business

Term of office:

1 December 2014 -
30 November 2017

PREVIOUS CAREER

- Eesti Energia AS: Director of Strategy
- Eesti Energia AS: Director of Energy Trading

EDUCATION

- London Business School, Master of Research
- Tallinn University of Technology, BA in Economics



ANDRES VAINOLA / 50

Member of the Management Board
Area of responsibility: mining and maintenance

Term of office:

1 December 2014 -
30 November 2017

PREVIOUS CAREER

- Empower Group Oy: Member of Management, CEO of Baltic Division
- Empower EEE AS: Chairman of the Management Board
- Eesti Elektrivõrkude Ehituse AS: Chairman of the Management Board
- Eesti Liinirongid AS (ELRON): Member of the Supervisory Board and Chairman of the Audit Committee

EDUCATION

- Leadership Academy Helsinki, Executive Training Programme
- Tallinn University of Technology, Business Administration

Differences Applying to Management of the Distribution Network Operator Elektrilevi OÜ

Under the Electricity Market Act, Elektrilevi as the distribution network operator has to ensure, among other things, that all market participants are treated equally and that the information of the network operator is protected.

In accordance with legislation and best practice, Eesti Energia has put in place differences applying to the management of Elektrilevi, which ensure the network operator's independence in adopting investment decisions, conducting procurements and maintaining the confidentiality of information pertaining to market participants and customer contracts.

Agreed Reporting Principles

The Group has implemented reporting processes for monitoring the key performance indicators and other significant indicators on a weekly, monthly, quarterly and annual basis. Once a month, results are compared with the budget and the latest forecast. Once a quarter, the Group reviews its action plan for the rest of the year and, where necessary, adjusts its business operations so that they are appropriate in the current market situation. Once a year, the Group updates its five-year strategic action plan.

Information on the company's operations and information that may affect the price of the Eurobond is released in accordance with the rules of the London Stock Exchange and, in the first place, via the information system of the London Stock Exchange. Information which is not expected to affect the price of the Eurobond is released via domestic media channels. In both cases, information is disseminated in line with the Group's rules for handling inside information, which are designed to protect the interests of bondholders and ensure fair and orderly trade of the bonds. All relevant information on Eesti Energia and its subsidiaries must be available to all bondholders and potential investors in a timely, consistent and equitable manner (to the same extent, at the same time, and in the same manner).

Effective Supervision

Eesti Energia Group has a multi-level and balanced chain of supervision, which ensures effective risk management. Supervision is carried out by the Group's supervisory board and management board, the audit committee, the supervisory boards and management boards of Group entities, risk management and internal audit departments and other departments and units entrusted with supervision.

Audit Committee and External Auditor

Eesti Energia's supervisory board has set up an audit committee which is responsible for advising the supervisory board in risk management, internal audit and audit, compliance and similar matters.

The audit committee has four members. The composition and the chairman of the audit committee are determined by the supervisory board of Eesti Energia. The audit committee meets as per the agreed schedule at least once a quarter. In 2016, the committee had 11 ordinary meetings. The audit committee submits its report to the supervisory board once a year, before the supervisory board approves the annual report of Eesti Energia. In 2016, the audit committee fulfilled its responsibilities. The audit committee statement is on page 73. Eesti Energia's financial statements are audited in accordance with International Standards on Auditing. Under Eesti Energia's articles of association, appointment of the auditor of the financial statements is the responsibility of the general

meeting. Based on the tender results, the general meeting has appointed audit firm PricewaterhouseCoopers (PwC) as the auditor of the financial statements for financial years 2014–2016. The person authorised to sign the auditor's report depends on the country of incorporation of the Group entity. The auditor responsible for the audit of the consolidated financial statements is Certified Public Accountant Tiit Raimla. Eesti Energia does not disclose the fee paid to the external auditor because the Group believes that this could undermine the outcomes of future tenders.

PwC presented the results of the work related to the reporting period in two stages:

- 1) the results of the interim audit were presented at the meeting of the audit committee held in December 2016;
- 2) the results of the year-end audit were presented at the meeting of the audit committee held in February 2017.

The independent auditor's report is on page 181.

Eesti Energia supports the independence of the external auditor and avoids conflicts of interest. For this, the audit committee has established a set of principles to be followed when the auditor wishes to provide additional services to Group entities. In 2016, PwC did not provide any services to Eesti Energia that could have compromised the auditor's independence.

Audit Committee

(as at 31 December 2016)



KAIE KARNIOL / 46
Chairwoman

Term of office:
23.05.2013 – 16.06.2019



DANEL TUUSIS / 46
Member

Term of office:
01.11.2015 – 15.10.2018



MEELIS VIRKEBAU / 59
Member

Term of office:
17.12.2009 – 24.01.2019



MÄRT VOOGLAID / 48
Member

Term of office:
01.09.2014 – 31.08.2017

Audit Committee Members' Participation in Meetings and Total Remuneration Paid

	PARTICIPATION IN MEETINGS 2016	TOTAL REMUNERATION IN 2016 (€)	TOTAL REMUNERATION IN 2015 (€)
KAIE KARNIOL	12	2,400	2,200
DANEL TUUSIS	8	710	177
MEELIS VIRKEBAU	12	1,065	976
MÄRT VOOGLAID	11	976	710

Internal Audit

The work of the internal audit function is organised in accordance with the Auditors Activities Act and related regulations and the International Professional Practices Framework which sets out international standards for internal auditing. The work of the internal audit function covers the activities of the whole Group.

Ensuring effective operation of the internal audit function is the responsibility of the internal audit department. The department is accountable to the audit committee and the supervisory board. The action plans and reports of the internal audit department are evaluated and approved by the audit committee. The role of the internal auditors is to contribute to improving the internal control environment, risk management, and busi-

ness management culture. The internal audit report for 2016 was submitted to the audit committee in February 2017.

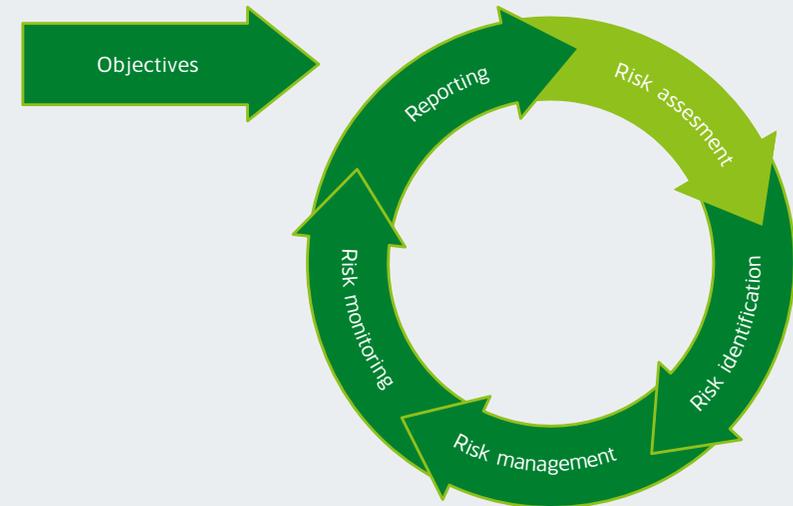
The Group has established a system for declaration of economic interests by which employees who may encounter conflicts of interest in fulfilling their responsibilities declare their economic interests and confirm their independence through regular self-assessment. To the knowledge of Eesti Energia, the members of the Group's management board and the management boards of the subsidiaries did not have conflicts of interest in 2016 and they did not conduct any related party transactions on terms different from market terms. An overview of related party transactions conducted in 2016 is presented in the financial statements.



RISK MANAGEMENT

The purpose of risk management is to support the Group in implementing its strategy, achieving its financial and operating targets, identifying potential risk factors and preventing undesirable events.

Risk management is underpinned by Eesti Energia's objectives and comprises the following activities:



Risk Profile and Risk Management Framework

We have identified and described the risks which may have an impact on the Group and its entities and have assigned responsibility for the management of those risks. The risks described in Eesti Energia's risk profile include financial risk (including market, credit and liquidity risks), legal and compliance risk, technological and technical risk, environmental risk, work safety and work environment risk, IT risk, and other

operational risks (including personnel and procurement risks). To create a risk management framework, we have adopted both general and specific risk management policies and prepared risk management rules which our staff must observe. In developing risk management policies, we rely, among other things, on laws, recognised international standards, and best practice (e.g. OHSAS, ISO 14001, HAZOP).

Risk Management System

Management of the Group's risks is the responsibility of the Group's management board.

Due to the Group's operating principles and practicality, the day-to-day management of many risks such as the environmental, financial, IT, legal and compliance, security, and fire risk has been assigned to the Group's central services. Central services monitor, analyse, handle, and respond to risks and coordinate relevant activities at Group entities.

Developing specific risk management policies and techniques, notifying stakeholders, and supporting the application of adopted policies is the responsibility of each entity or unit manager tasked with risk management. Risk-related information exchange, reporting, decision-making and similar activities take place at the meetings of relevant levels of management or separate committees (e.g. financial risk committee).

Oversight of the proper functioning of risk management activities and processes is the responsibility of the Group's supervisory board, audit committee, and internal audit department.

Key Risks and Risk Mitigation

The key risks which influence the achievement of Eesti Energia's objectives include market risk, which is part of financial risk, environmental risk, legal risk, and various operational risks.

Market risk influences the sale of our goods and services and the purchase of the resources we need. The most significant market risk is the price risk related to the sale of electricity and shale oil and the purchase of emission allowances. We hedge financial risks, among other things, with derivative financial instruments on which further information can be found in the financial statements. We have also set up a separate department for financial risk management.

Legal risk, which arises from regulators' activities and political decisions, influences both our day-to-day business and long-term objectives as well as development projects. The key measures for mitigating legal risk include monitoring the changes and trends in the legal environment, participating in the development of new legislation, monitoring our compliance and preventing potential non-compliance.

Operational risks result from inadequate or ineffective processes, people, equipment, systems, or external events. Operational risks are managed through relevant policies, standards, management principles and performance indicators.

Because of the nature of our business, we pay special attention to work safety and environment risks. Our production entities have implemented occupational health and safety assessment system OHSAS 18001. Our goal is to work without accidents and occupational diseases. To achieve this, we analyse our risks, make appropriate changes, and increase employee awareness and involvement in the solution of work environment issues. We provide regular occupational health and safety training. Every quarter our production units organise safety at work days. In addition to applying recognised safety standards, we have created incident and near miss reporting channels. According to a survey conducted in 2016, 88% of our people uphold our core value Safety First.

We notify our partners of our ethics, occupational health, safety at work, and fire safety requirements and demand that they observe those requirements at Eesti Energia's entities, sites and projects.

As a production company, we pay a lot of attention to the operation and maintenance of our assets. To ensure efficient and economical operation of our assets, we have created asset management units.

In addition to applying risk management policies, we pay a lot of attention to training and informing activities aimed at preventing the realisation of risks. Besides regular employee development activities, we pay separate attention to providing information about the work environment and our anti-corruption standards. This is done through relevant training programmes. In 2016, over 500 employees received corruption risk training delivered in cooperation with external experts. We also carry out regular fraud risk analyses. In 2016 we updated our Code of Ethics and distributed its printed version to all employees.

Risk Analysis Methodology

For risk analysis we use, among other techniques, quantitative assessments and simulation methods by which we analyse the indeterminacy of various factors on achieving our objectives, the cash flows planned for funding our investments, compliance with the financial covenants of our loan agreements, and the ability to maintain our financial ratios at an optimal level.

Risk Reporting

Eesti Energia's reporting and information exchange processes ensure that risk-related information reaches all stakeholders. Risk-related data is also included in our general reporting and analysis of performance indicators and results.

The risks which may have a significant impact on the achievement of the Group's targets are regularly reported to the Group's management board and audit committee. Management and all other stakeholders are notified without delay of any significant events and changes in the Group's risk profile.

AUDIT COMMITTEE STATEMENT

In 2016, the audit committee carried out its responsibilities in accordance with its approved statutes and action plan. No restrictions were imposed on our activities and the Group's representatives made all the necessary information available to us. Well-defined reporting lines ensured a fluent flow of relevant information to us. We informed the Group's supervisory board and the representatives of the Group's management board of the opinions we formed based on our work and related suggestions.

We formed our opinion on the following activities of the Group in fiscal 2016:

- adherence to established accounting policies;
- operation of processes for the preparation and approval of budgets and financial statements;
- arrangement of a sufficient and effective external audit and assurance of its independence;
- development and operation of the internal control system;
- monitoring of the legal and regulatory compliance of the company; and
- organisation of the internal audit function.

The audit committee finds that the activities of Eesti Energia Group do not involve any deficiencies of which the management is unaware and/or which could have a material impact on the Group's annual report for 2016.

We submitted our activity report and assessments along with this statement to the supervisory board of Eesti Energia in February 2017.



KAIE KARNIOL
Chairwoman
of the Audit Committee



ENVIRONMENT

In 2016 our key environmental goals were meeting the new environmental requirements which took effect at the beginning of the year and observing them at highly changeable operating capacities. The year also marked an end of a major and intensive investment period, which was aimed at bringing our operations in compliance with the EU environmental regulations which entered into force at the beginning of the year.

The reporting period was also a milestone in expanding the use of one of our by-products – oil shale ash. We completed, in collaboration with partners, the OSAMAT project, which was conducted for four years to test the use of oil shale ash in road construction, and launched Enefix – a new oil shale ash-based agricultural product, which can be used for neutralising acidic soils in place of the traditionally used lime.

Implementing Cleaner and More Efficient Technologies

Reducing the environmental impacts and increasing the efficiency of its oil shale industry are among the Group's key priorities. Hence, we work hard to implement cleaner and more efficient technologies.

Previously we used oil shale mostly for power production. Now we strive to use it for co-producing shale oil and electricity. In 2016, a major share of our oil output came from our new liquid fuel and electricity co-production plant Enefit280, which was launched in 2013. Results reflect that the emissions of Enefit280, which is based on a new technology, are substantially smaller than those of previous-generation plants. Enefit280 is also more efficient as it uses semi-coke for electricity production.

Efficiency growth is also supported by our strategic initiatives. Reconstructing generating unit 8 of the Eesti power plant

will allow us to use the gas produced by our oil plants more efficiently and operate our power plants more flexibly. The project of extracting gasoline from oil shale gas will allow us to further widen the use of oil shale gas and produce a product with higher added value – oil shale gasoline.

Monitoring Air Quality

At the end of 2016 we installed an air quality monitoring station in Vaivara parish to improve the monitoring of air quality. The modern station allows us to monitor the impacts of our production activities on the air quality of the surrounding areas in different weather conditions and to adjust our operations based on data received. In 2017, the station will be included in a monitoring system which covers the whole country and its data will become publicly available. Besides providing information about the environmental impacts of our production facilities, the station makes the results of our activities more accessible for the communities and improves information exchange.

Increasing Renewable Energy Output

One of the goals of Eesti Energia's new strategy is to increase the share of renewables in our electricity production portfolio.

In addition to biomass, a major source of renewable energy in Estonia is wind. We have wind farms in Narva, Aulepa, Paldiski and Virtsu already but we have also started preparations for developing a wind farm with up to 52 generators and a capacity of over 150 MW at Tootsi. If the project is realised, our renewable energy output will increase significantly. We are also analysing other opportunities for increasing the share of renewables in our portfolio.

Reducing Mining Impacts and Losses

Eesti Energia works every day to reduce the environmental impacts of its mining operations. Rehabilitation of mining sites and mining with minimal environmental disturbance are among our priorities. At the same time, it is important that mining waste should be minimal.

Previously we have used the room-and-pillar mining technology which ensures the stability of the ground surface and minimal disturbance of above-ground activity but leaves a relatively large portion of the resource underground in the form of pillars left to support the overlying strata. The deeper the oil shale layer extends, the larger the pillars need to be and, thus, the larger the waste.

An alternative technology is harvester mining by which no pillars are left underground and the surface above the mined-out area is allowed to collapse in a controlled manner.

Our specialists developed the historical harvester mining technology further by implementing a longer work area (long work face) which ensures even collapse of the surface so that the landscape is less affected. The year 2016 was a milestone for us because after a thorough environmental impact assessment we obtained a permit for using the enhanced technology at the Narva opencast mine and made extensive preparations for starting the work.

In addition, we built an additional sediment pool in the Estonia mine where suspended solids are removed from the water pumped out from the mining area before the water is released back to the environment. The underground solution allows us to remove solid matter from mine water more effectively.

Minimising the Environmental Impacts of Load Changes

In 2016 market conditions were volatile. Therefore, we were flexible in our production operations and constantly increased and reduced the loads of our production assets. As operation at different modes hinders the work of the flue gas treatment systems, we adjusted their work to minimise the environmental impacts of load increases and decreases (e.g. on changing the mode, we changed the quantity of reagent and made technical changes).

Recycling Tyres

In 2016, the list of fuels used by Eesti Energia was supplemented with scrap tyres. In summer 2016 we tested burning of tyres in our Iru waste-to-energy unit to check the environmental safety of the incineration technology. Results reflect that a certain quantity of crushed tyres may be added to other waste burnt at the Iru power plant. Altogether, we could burn up to 5,000 tonnes of scrap tyres at Iru.

Scrap tyres which do not contain hazardous substances are also a good raw material for liquid fuel production. Use of tyres as a raw material of Enefit140 and Enefit280 would reduce oil shale consumption and help solve Estonia's scrap tyre recycling problem, which is acute. Industrial testing of the use of scrap tyres will begin in 2017. We will use the test results to supplement our environmental permits and, if necessary, also the technology.

Reusing Production Waste

In 2016 we completed the OSAMAT project, which lasted for several years and was aimed at testing the suitability of oil shale ash for road construction. The project, carried out in partnership with the National Road Administration and construction company Nordecon, showed that oil shale ash can be used for mass-stabilisation in road construction as well as other large-scale infrastructure projects such as port construction. As a result of the project, in the future oil shale ash should be a significant alternative road construction material in Estonia as well as the neighbouring countries.

We revived the use of oil shale ash in agriculture – in 2016 we launched a new oil shale ash-based product called Enefix, which can be used for neutralising acidic soils. Current experience shows that farmers are highly interested in the product because in addition to its neutralising qualities oil shale ash contains various microelements which improve plant growth.

Improving Older Technologies

Besides implementing new technologies, we put a lot of effort into reducing the environmental impacts of our older plant and equipment.

The most perceptible environmental impact of the Enefit140 oil plant is odour nuisance. To improve the community's quality of life, we made system improvements which reduced emissions that cause a strong odour. We also launched a development project aimed at reducing emissions into air which may arise on the storage and loading of shale oil, particularly the lighter fractions. The purpose of the project which will be completed in 2017 is to make sure that all of the oil shale gas is burnt before it reaches the atmosphere. This should ensure that components with a strong odour will not reach the environment.

Key Environment Figures ►

		2012	2013	2014	2015	2016
PRODUCTION						
Electricity	GWh	9,378	10,560	9,687	7,689	9,071
Renewable electricity	GWh	534	263	297	361	380
Heat	GWh	1,137	1,242	1,309	1,288	1,358
Produced using biofuels and waste	GWh	155	223	337	357	412
Liquid fuels	thousand t	209	214	265	337	318
Retort gas	million m ³	65	61	72	95	91
RESOURCES USED						
Oil shale	million t	14.8	17.2	17.0	13.7	15.2
Natural gas	million m ³	61.1	47.3	43.8	47.1	60.7
Biofuels	million t	0.5	0.1	0.1	0.1	0.2
Municipal waste	thousand t	0.0	183.6	221.4	244.6	247.9
Cooling water	million m ³	1,302.2	1,475.0	1,454.5	1,365.1	1,481.9
Pumped mining water	million m ³	203.0	138.2	117.3	103.6	139.5
water from open cast mines	million m ³	112.2	61.6	57.0	49.0	71.2
water from underground mines	million m ³	90.8	76.5	60.3	54.7	68.3

► Key Environment Figures

		2012	2013	2014	2015	2016
EMISSIONS						
SO ₂	thousand t	23.2	20.9	24.2	17.5	20.7
incl. Narva Power Plants	thousand t	23.1	20.8	24.1	17.2	20.4
NO _x	thousand t	9.7	8.8	8.5	5.9	6.4
Fly ash	thousand t	5.7	9.1	8.5	3.5	2.3
CO ₂	million t	11.0	13.4	12.8	10.0	11.5
SOLID WASTE						
Oil shale ash	million t	6.9	8.1	7.9	6.3	7.0
incl. recycled	million t	0.1	0.1	0.1	0.1	0.1
Waste rock	million t	8.1	6.3	6.4	6.6	5.0
incl. recycled	million t	7.6	4.4	1.8	2.0	1.5
WATER POLLUTANTS						
Suspended matter	thousand t	1.1	0.8	0.8	0.6	1.0
Sulphates	thousand t	76.0	64.8	51.7	60.1	71.1
ENVIRONMENTAL CHARGES						
Resource charges*	m€	30.4	28.3	28.5	28.1	1.3
Pollution charges	m€	17.8	24.5	31.8	30.4	30.3

* Resource charges for 2016 are impacted by a retrospective reduction of resource charge rates. Excluding the impact of the retrospective reduction of resource charge rates, resource charges for 2016 would have amounted to 17.3 million euros.



TAX FOOTPRINT

In disclosing and paying taxes, Eesti Energia is responsible, open and transparent. All our entities comply with the tax laws of their jurisdictions.

In calculating our tax footprint, we distinguish between taxes borne and taxes collected. Taxes borne are taxes directly borne by Eesti Energia. Taxes collected are taxes for which

Eesti Energia acts as an intermediary, i.e. we collect the taxes from consumers and employees and transmit them to the tax authority. In 2016, taxes borne by Eesti Energia totalled 98.8 million euros and taxes collected by Eesti Energia totalled 96.5 million euros. Therefore, the Group's tax footprint amounted to 195.3 million euros.

With 57.8 million euros Eesti Energia is the largest payroll tax payer in Estonia. Compared to the year before, the amount of taxes paid was strongly influenced by growth in VAT paid, which resulted from a decrease in capital investment, and income tax

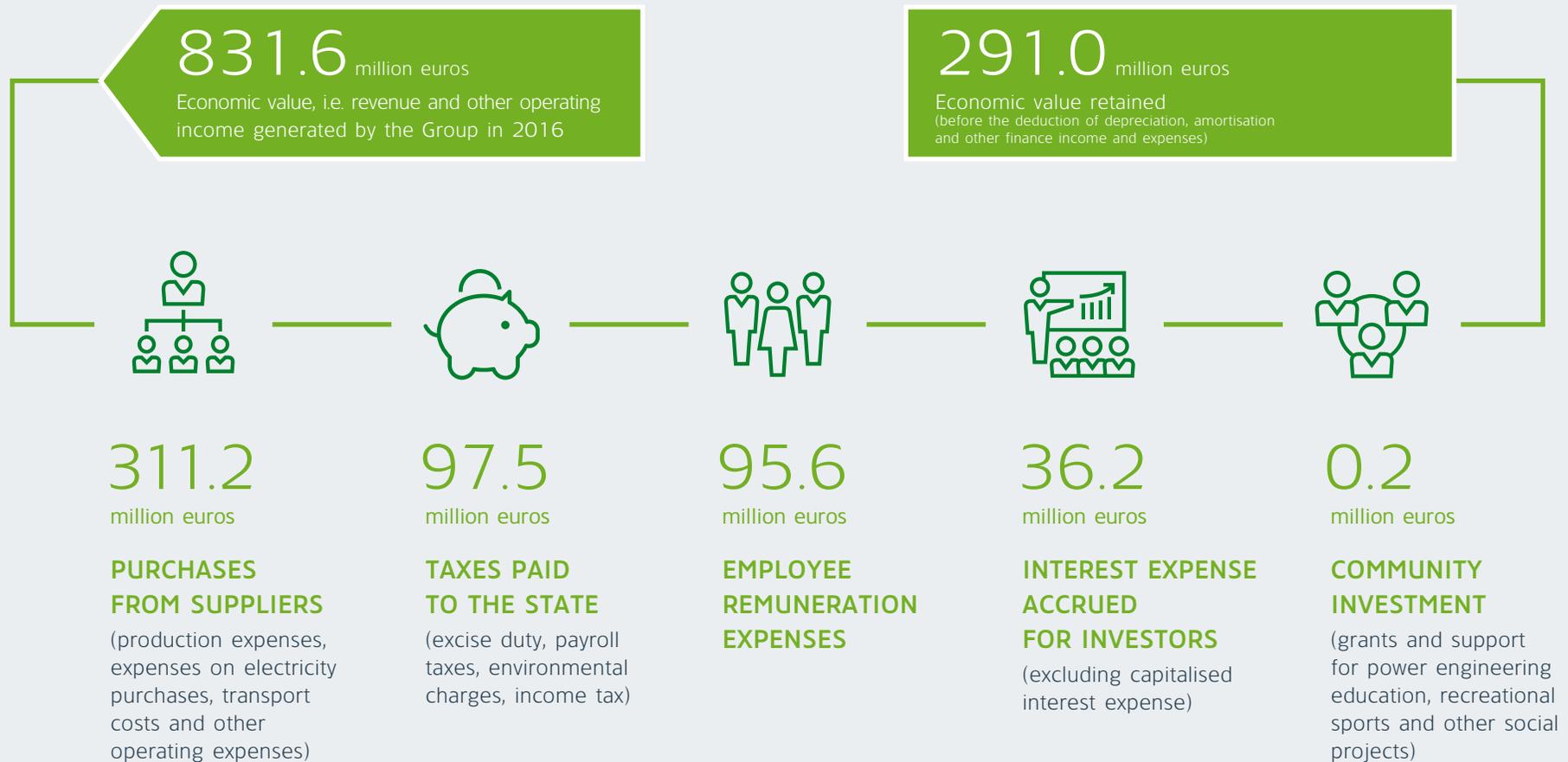
paid on dividends distributed in December 2015. The main item which reduced taxes paid was the decrease in resource charges paid, which resulted from the linking of the oil shale resource charge rate to the world market price of the end product.

Tax Footprint: Tax Payments in Estonia by Eesti Energia Group* (m€)

	IN ESTONIA 2016	IN ESTONIA 2015	CHANGE 2016 vs 2015	
TAXES BORNE				
Payroll taxes (social security tax, employer's unemployment insurance)	36.1	39.5	-3.4	-9%
Environmental charges: resource charges	15.1	28.6	-13.5	-47%
Environmental charges: pollution charges	31.6	28.9	2.7	9%
Corporate income tax	15.3	0.4	14.9	3,713%
Customs VAT	0.4	0.4	0.0	-10%
Land tax	0.3	0.3	0.0	3%
TOTAL TAXES BORNE	98.8	98.1	0.7	1%
TAXES COLLECTED				
Excise taxes	33.3	30.1	3.2	11%
Payroll taxes (income tax, employees' unemployment insurance, mandatory pension insurance)	21.7	23.8	-2.1	-9%
VAT (balance)	41.5	19.0	22.5	118%
TOTAL TAXES COLLECTED	96.5	72.9	23.6	32%
TOTAL TAXES	195.3	171.0	24.3	14%

* Reported on a cash basis – i.e. when money is paid or received.

The value Eesti Energia delivers to society and its breakdown





EESTI ENERGIA AS AN EMPLOYER

An inclusive organisation
that values its employees

Our Values and Vision

We value our employees because we know that Eesti Energia's success depends on talented and motivated employees who have the necessary skills and knowledge.

We wish to be an organisation where:

- there is a high work ethic and a safe working environment;
- people are remunerated and recognised fairly;
- there is effective cooperation and responsible management;
- development is supported and employee health and wellbeing is taken seriously;
- employees know that their work is important and necessary.

To support achievement of business strategic goals, in 2016 we developed the personnel strategy People 4.0. The purpose of the strategy is to help the organisation increase its productivity through better management quality, develop the required competencies and internal cooperation. According to the vision of our personnel strategy, by the year 2020 Eesti Energia will be recognised as an innovative, environment friendly and value-based company which values its employees' commitment, development, outstanding results, individual accountability, cooperation and initiative. The Group will have a consistently high management quality, good internal collaboration and experience-sharing, and dedicated and competent employees.



Our people

On 31 December 2016 we had 5,840 employees (31 December 2015: 6,015). At the end of 2016, 56% of our employees were workers, 32% were specialists, and 12% were managers.

During the year, the number of staff decreased mainly because we streamlined our work arrangement and, due to the deterioration of the external environment, were forced to reduce the headcount in some areas.

We have made sure that Eesti Energia's employees can exercise all human rights and fundamental freedoms without discrimination.

Employee Satisfaction and Commitment

For successful implementation of our business strategy, we need a dedicated team. To obtain the feedback required for maintaining and increasing employee motivation, we carry out satisfaction and engagement surveys.

In 2016, we carried out a thorough engagement survey in partnership with TNS Emor among all employees who had been working for us for at least four months at the start

of the survey. The participation rate was very high – 77%, reflecting the employees' trust in the company. Compared to the results of a survey conducted in 2012 using the same methodology, the participation rate rose significantly at almost all Group entities. The survey mapped our employees':

- TRI*M index which measures the level of commitment;
- satisfaction with the nature of the work, development opportunities, work arrangement, cooperation, leadership quality, salary, and other motivators; and
- opinion of Eesti Energia's reputation as an employer, the organisation's values, and internal communication channels.

The survey showed that in the past four years our employees' commitment has increased at the same pace as Estonia's average indicator and continues to be at the average level for the manufacturing sector. Every sixth employee feels that he or she is a truly dedicated contributor to Eesti Energia's success.

Based on feedback received, both the units and the Group drew up an action plan for further improvement of the working environment.

Employee Development

We believe that employee development and engagement is vital, as it helps to maintain and increase our competitive advantage.

In employee development, we follow Eesti Energia's strategic action plan, governance principles, values, personnel strategy, people management policy and code of ethics.

To create an environment that fosters development, we:

- encourage employees to take responsibility for their development;
- support employees' development through our performance and development management system;
- appreciate the creation and implementation of new ideas, knowledge and solutions;
- offer learning opportunities based on the 70/20/10 model according to which 70% of skills and knowledge is obtained through on-the-job practice, 20% is obtained through feedback from colleagues and 10% is obtained through traditional training;
- recognise the work of internal trainers and participation in internal training events;
- improve our internal training system so that it would develop into a complete knowledge management system: e.g. in 2016 we launched a development

programme for new and less experienced trainers and started to prepare training tools.

In 2016, our employees had 98,000 hours of training. We invested 974,590 euros in employee development.

Development of Management Competencies

Contemporary industry requires skilful people management. Therefore, we pay a lot of attention to developing our current and future managers.

In 2016 we organised various events and training courses aimed at enhancing our managers' competencies, including Eesti Energia's management conference, and introduced a new tradition – managers' summer academy.

The purpose of the summer academy is to support the development of a uniform management style and effective achievement of the company's objectives. At the summer academy of 2016 our managers obtained new knowledge about setting, monitoring and achieving goals and inspiring employees and shared their experience. 248 managers of various levels took part in the two-day event.

In 2016, we also prepared a leadership development programme for current and future managers which will be launched in 2017. Within three years, around 300 employees should benefit from it.

Support and Recognition

Eesti Energia cares about its employees. We pay a competitive salary and offer career and development opportunities. We notice those who need help and support the staff during medical incapacity or when they contract an occupational disease. We recognise good employees, thank our people on their work anniversaries, celebrate our staff's accomplishments, and are there for their personal life events.

We recognise employees who achieve the best results with gold and silver badges which are awarded at our New Year party. In 2016, we awarded gold and silver badges in four categories: lifetime service at Eesti Energia, a successful start, a good mentor, and a considerate colleague. Altogether, we awarded 4 gold and 40 silver badges.

In addition, we recognise the staff for the engineering solution of the year and the deed of the year. This time, the engineering solution of the year was the re-launch of longwall mining at the Estonia mine and the deed of the year was Elektrilevi's remote reading (smart meter installation) project.

Joint Activities

We value the time we spend together, as joint activities increase the sense of unity and facilitate cooperation.

In addition to activities arranged at the level of departments and business units, every year we organise some events which bring together all our staff such as Eesti Energia's New Year party, children's Christmas parties, and Energy Day with the running event Narva Energiajooks.

During the period we again organised the traditional Miners' Day for miners, their families and the entire Ida-Viru county. This time we organised it together with the chemicals group Viru Keemia Grupp.

To support the health and wellbeing of our people, we have set up Eesti Energia sports club, which has around 1,500 members. In addition to weekly workout options, the club supports our employees' participation in public sport events as well as internal and inter-company competitions. In 2016, our companies invested approximately 300,000 euros in our employees' recreational sports activities.

Future Employees

For sustainable operation of the business and consistent development of the energy sector, we need young people who would help create innovative and effective solutions. We wish to be the preferred employer for young people who excel in sciences and we do our best to make an increasing number of young engineers find an opportunity to apply their knowledge and skills at Eesti Energia.

Similarly to previous years, in 2016 we offered internship opportunities for future information technologists, analysts, mining engineers and other specialists. During the year, we had around 160 interns: 117 of them did their internship at our Ida-Viru entities, 23 at our head office in Tallinn, and the rest mostly at Elektrilevi's units across Estonia.

To support initiatives promoting engineering education, in 2016 we established Insenergia Fund through which we supported eight projects with a total of 21,159 euros. In addition, we supported the science club of Tallinn University of Technology Virumaa College where young people could conduct experiments with oil shale under the guidance of professional engineers.

We support future engineering specialists through scholarship programs. In 2016, we awarded scholarships to three

mining and mineral processing students of Ida-Viru Vocational Education Centre and one geo-technology student of Tallinn University of Technology.

To improve young people's knowledge about Eesti Energia, we invite students who study subjects related to our activity to visit our companies. In 2016, we organised 42 tours for a total of 92 secondary school and university students.

In partnership with other large companies of Ida-Viru county (Viru Keemia Grupp and Eastman Specialities) we launched at Jõhvi secondary school an elective STEM (Science, Technology, Engineering and Mathematics) course in order to promote engineering studies. Visiting lecturers of the programme include companies' specialists and course work includes trips to industrial enterprises.

In connection with the 100th anniversary of oil shale mining in Estonia, in 2016 our employees delivered more than 100 lessons at Estonian schools in the framework of the Back to School project. By speaking about energy and sharing their personal experience with more than 2,000 students, our staff increased young people's knowledge about contemporary, innovative, efficient and environment friendly power engineering and inspired them to find their future in it.



CUSTOMER RELATIONS

The highest customer satisfaction indicators of the past seven years

Eesti Energia is the largest energy seller in Estonia. A large-scale customer base involves great responsibility which sets high customer service targets. In making business decisions, preparing action plans, setting objectives and measuring results, we take into account the annual customer satisfaction survey carried out by TNS EMOR. According to the survey conducted in 2016, in the residential category our customer relationship strength remained almost at the same level as before whereas in the business and large business category our customer relationship strength improved.

Customer Relationship Index (Tri*M)

	2012	2013	2014	2015	2016
Household customer relationship index (or Tri*M)	45	42	61	64	62
Corporate customer relationship index (or Tri*M)	36	38	53	57	67
Large corporate customer relationship index (or Tri*M)	50	42	64	66	73

Key Conclusions from Survey 2016

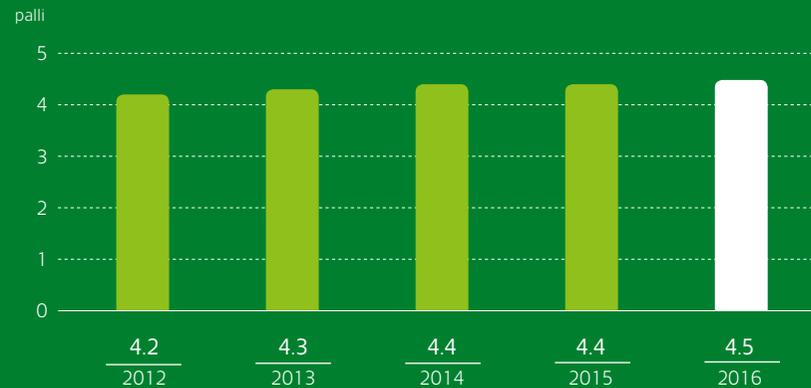
We succeeded in maintaining residential and business customers' general satisfaction with our services and customer care at the same level as the year before.

Residential customers' overall ratings remained stable but the ratings given to some service processes improved. Business customers' ratings of several important service and price aspects weakened but the ratings given to the competitive advantage improved and thus the customer relationship strengthened. According to residential, business, and large business customers, Eesti Energia's main competitive

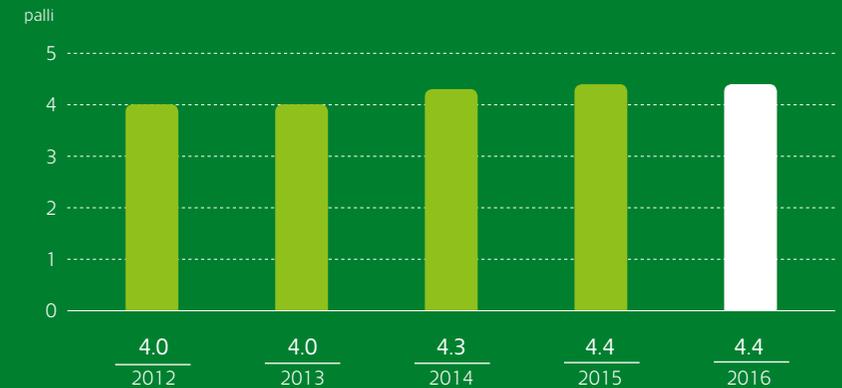
edge is its size and the sense of security that this provides. Our strengths which both residential and business customers value the most are smooth invoicing and contract conclusion and amendment processes and friendly and helpful staff. According to both residential and business customers, energy efficiency consulting and related smart solutions will allow us to differentiate ourselves from the competition also in the future.

Large business customers appreciate our customer managers' communication skills, business culture, initiative and energy competence.

Customer Assessment of our Customer Hotline Number (in 5 Point Rating Scale^{*})



Assessment of teenindus@energia.ee (in 5 Point Rating Scale^{*})



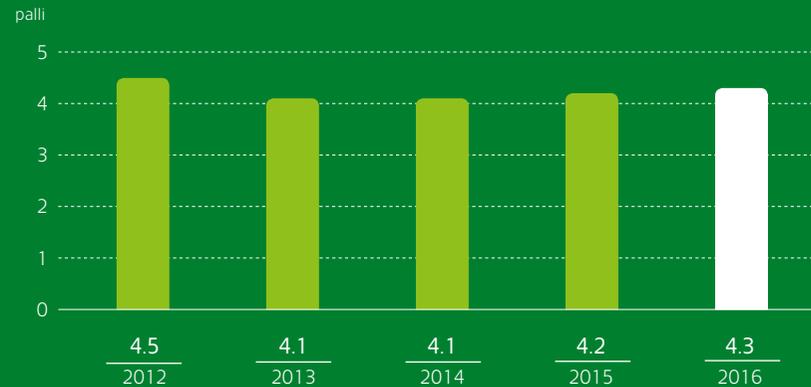
Phone Service

We have set ourselves the target to respond to 70-80% of calls within 25 seconds. In 2016, the percentage of calls answered within 25 seconds was 57% for the customer service number and 75% for the fault reporting number.

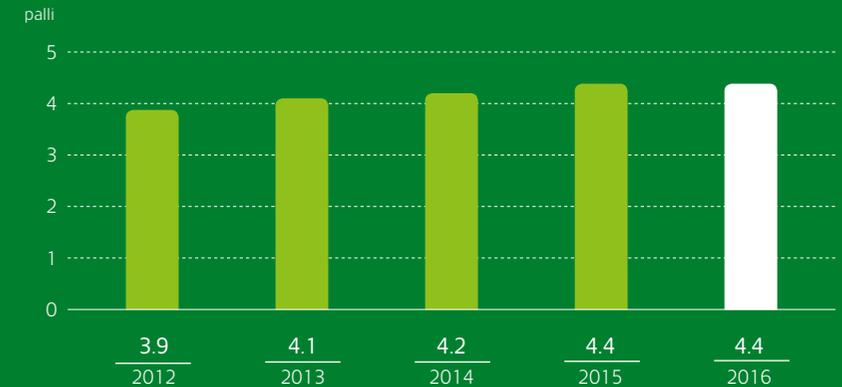
In 2015, Eesti Energia was contacted by phone 460,692 times. In 2016, the figure dropped to 431,181. The number of calls decreased thanks to process improvements and a more personal and proactive approach: on responding to a call our service staff discussed with the customer not only the matter raised by the customer but also other matters which could make the customer contact us again in the near future.

^{*} Assessment is based on Eesti Energia's monthly feedback survey from customers who had contacted us in previous month.

Customer Satisfaction with E-service, channel
(in 5 Point Rating Scale')



Customer Satisfaction with E-service, process
(in 5 Point Rating Scale')



E-Service

Our online e-service has become our customers' most preferred communication channel. Over 150,000 customers visit Eesti Energia's e-service every month and every fifth visit is via a smart device. Every second customer uses our e-service. Our e-service is a convenient option for signing electricity and gas contracts, checking electricity and gas prices, changing the package, submitting readings, viewing and paying bills, giving authorisations, and tracking consumption. Customers can also view special offers and request further information about Eesti Energia.

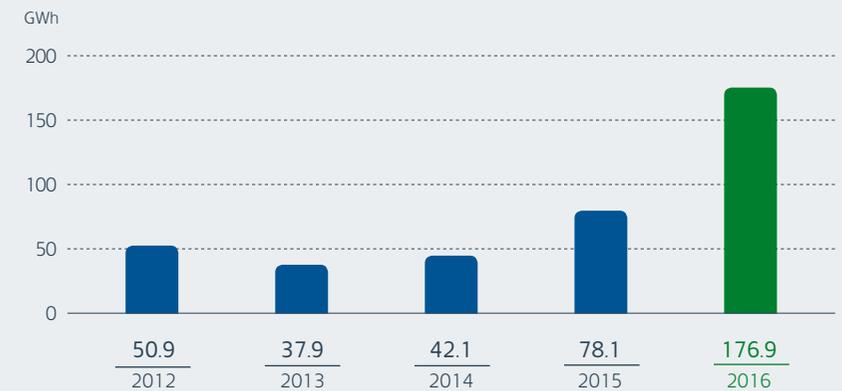
Simple Mobile App

Eesti Energia has created a user-friendly mobile app which enables our customers, among other things, to see and pay energy bills, view contract details, obtain price information, manage electricity consumption and request gas price offers on the go. Customers can also view our partners' special offers, which change regularly.

Renewable or green energy gains popularity among customers

By the end of 2016, 3,497 of our residential customers and 168 of our business customers preferred renewable energy. In 2016, our Estonian customers consumed 176.9 GWh of renewable electricity. We produced a total of 380 GWh of renewable energy of which 186 GWh from wind, 189 GWh from biomass and waste, and 6 GWh from water.

Consumption of Green Energy





GIVING BACK TO SOCIETY

We understand that our operations have a significant impact and this requires us to be responsible. For us, being responsible means caring about our employees, our customers and other members of society, and contributing to the development of society and the communities where we operate.

We prefer to support initiatives and projects which involve large target groups and lead to positive long-term changes in society. Thus, our priorities include:

- supporting education in the field of energy and power engineering and related innovation;
- promoting recreational sports;
- supporting the development of Ida-Viru county and the life of the local community;
- protecting the environment.

In 2016, we supported the projects and initiatives of the above areas with 195,557 euros.

A decision on allocating support is first made by a Group-wide sponsorship committee and then by the management board. We have set up a separate sponsorship committee for allocating support to the development of Ida-Viru county, which adopts decisions on projects aimed at Ida-Viru communities.

For an overview of the areas and projects we support, see: <https://www.energia.ee/en/uhiskondlik-tegevus>.

Supporting Education and Innovation

Among Estonian energy companies, we have the longest history and the most extensive experience. Thus, we are committed to supporting education in the field of energy and power engineering. We invest in making sure that there would be good and motivated specialists both now and in the future. We have initiated many projects aimed at inspiring, increasing and maintaining interest in sciences and seeing career opportunities in the energy sector, several of them in cooperation with educational establishments.

In 2016, we offered a lot of young people internship and field trip opportunities at our entities. We supported Europe's largest robotics competition Robotex and a research competition for students, published study aids for science studies in cooperation with a recipient of a Noored Kooli scholarship, and delivered more than 100 lessons in energy and power engineering at Estonian schools.

Promoting Healthy Lifestyles

Eesti Energia cares about the health of its employees and all Estonians. Thus, we create opportunities for doing sports and encourage people to exercise daily.

In partnership with Swedbank and Merko Ehitus, we have set up a foundation, Eesti Terviserajad, for building and improving health trails in Estonia. We have used it for over 10 years to fix up more than 100 health trails across Estonia. The mission of the foundation is to provide everyone, regardless of the time of day and location, with an opportunity to enjoy exercising in fresh air. On the foundation's website people can find informative videos which give useful tips to both beginners and experienced recreational athletes. We also invite our employees to participate in the development of health trails.

Besides outdoor activities, we support exercising on our indoor health trail set up on the stairs between the 16 floors of Eesti Energia's head office. Once a year we organise a competition which promotes using stairs and outdoor health trails. The number of floors and kilometres covered in a month is recorded and at the end of the month the most active exercisers are announced. In 2016, over 300 people participated. They climbed 54,182 floors and ran or walked 15,186 kilometres on outdoor trails. The staff of NetGroup, Súdameapteek and Tere who work in the same building also took part in the event.

The most important outcome is that many employees use the indoor health trail even when the competition is not on.

Supporting Life in Ida-Viru County

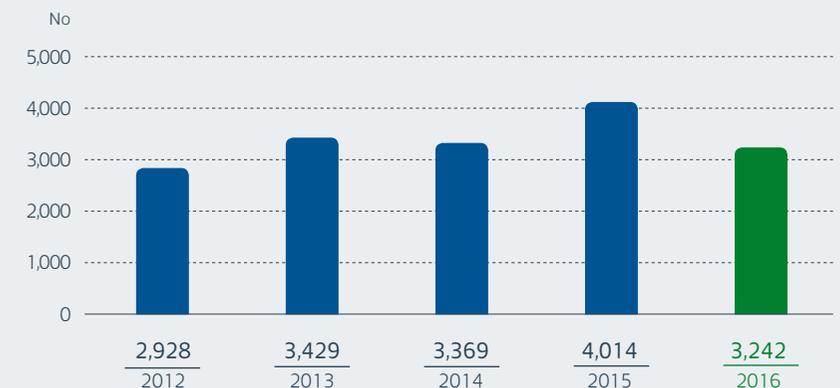
We pay great attention to Ida-Viru county as this is the region where most of our employees live and where the Estonian oil shale energy industry develops. We invest in the area's development to maintain important local traditions, make the living environment more attractive, and create more diverse development opportunities for young people.

In 2016, we supported 53 schoolchildren through the Ida-Viru Talented Young People's Energy Fund. The fund was established by Eesti Energia and the Association of Ida-Viru Local Governments in 2013 to support the recreational activities of the area's young people. Most grants are awarded to young people who are interested in sciences or sports but we have also supported development in the field of music, culture and arts. Since 2013 the fund has awarded grants to more than 170 young people.

To promote health and wellbeing, we initiated a recreational sports tradition in Ida-Viru county. In 2016, the running event

Narva Energiajooks was held for the sixth time already. It has become the area's largest sport event – in 2016 it attracted 3,242 small and big sports fans. In addition to organising Narva Energiajooks, we help develop an exercise station on the Pähklimäe health trails in Narva to provide local people with a convenient year-round opportunity to enjoy exercising outdoors.

No of Participants of Running Event Narva Energiajooks



Protecting the Environment

As an energy company, Eesti Energia is in contact with nature every day. Protecting the environment requires a sense of responsibility and knowledge. We consume natural resources responsibly and as efficiently as possible, we make consistent efforts to reduce the environmental impacts of our activities and promote caring for the environment.

Once a year we organise an Environment Day on which we organise environmental discussions with various groups of stakeholders. In 2016, the day addressed the future of renewable energy and the environmental impacts of Estonia's energy production and different ways of producing renewable energy. The event was attended by 120 stakeholders including state and local government officials, environmental specialists, scientists, and business executives.

The year 2016 was the sixth in the partnership of Eesti Energia and Looduse Omnibuss. We work together to educate people about nature by organising trips and evenings in nature for large numbers of people. Looduse Omnibuss has become a strong movement that helps preserve Estonian nature and culture.

Donating Time for Charity

In 2016, Eesti Energia joined the initiative Let's Donate Time which was started by the Employers' Confederation and Swedbank to give employees an opportunity to use one working day per year to volunteer for charity. This allows us to support our employees' desire to do good in areas that matter to them and to us.

Charity Instead of Christmas Gifts

For years, we used to thank our partners with symbolic Christmas gifts. In 2016, we decided to introduce a new tradition and donate relevant funds for charity.

In 2016, the recipient of our Christmas donation was Avatud Värav MTÜ Kiiikla Children's Home in Ida-Viru county whom we have supported before. Our donation helped make the Christmas wishes of the children's home children come true.



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Consolidated Income Statement

in million EUR	1 JANUARY - 31 DECEMBER		Note
	2016	2015	
Revenue	742.1	776.7	5, 25
Other operating income	89.6	16.7	26
Change in inventories of finished goods and work-in-progress	(14.5)	28.0	11
Raw materials and consumables used	(290.0)	(326.7)	27
Payroll expenses	(130.2)	(139.6)	28
Depreciation and amortisation	(143.4)	(144.1)	5, 6, 8, 32
Impairment	-	(64.5)	5, 6, 8, 32
Other operating expenses	(69.7)	(89.3)	29
OPERATING PROFIT	183.9	57.2	
Financial income	0.3	6.3	30
Financial expenses	(14.1)	(10.6)	30
Net financial income (expense)	(13.8)	(4.3)	5, 30
Profit (loss) from associates using equity method	1.0	2.5	5, 9, 32
PROFIT BEFORE TAX	171.1	55.4	5
Corporate income tax expense	(0.1)	(14.9)	31
PROFIT FOR THE YEAR ATTRIBUTABLE TO:	171.0	40.5	
Equity holder of the Parent Company	170.9	40.5	
Non-controlling interest	0.1	-	
<i>Basic earnings per share (euros)</i>	<i>0.27</i>	<i>0.07</i>	34
<i>Diluted earnings per share (euros)</i>	<i>0.27</i>	<i>0.07</i>	34

Consolidated Statement of Comprehensive Income

in million EUR	1 JANUARY - 31 DECEMBER		Note
	2016	2015	
PROFIT FOR THE YEAR	171.0	40.5	
Other comprehensive income			
Items that may be reclassified subsequently to profit or loss:			
Revaluation of hedging instruments	(45.3)	(30.2)	20
Currency translation differences attributable to foreign subsidiaries	0.9	5.3	
Other comprehensive income for the year	(44.4)	(24.9)	
TOTAL COMPREHENSIVE INCOME FOR THE YEAR ATTRIBUTABLE TO:	126.6	15.6	
Equity holder of the Parent Company	126.5	15.6	
Non-controlling interest	0.1	-	

Consolidated Statement of Financial Position

in million EUR	31 DECEMBER		Lisa
	2016	2015	
ASSETS			
Non-current assets			
Property, plant and equipment	2,469.3	2,473.9	6
Intangible assets	40.2	41.1	8
Investments in associates	2.0	4.6	5, 9
Long-term receivables	39.1	32.9	13
Total non-current assets	2,550.6	2,552.5	
Current assets			
Inventories	65.2	71.9	11
Greenhouse gas allowances	47.3	33.5	16
Trade and other receivables	199.4	99.8	13
Derivative financial instruments	1.4	40.3	12, 14, 15
Cash and cash equivalents	223.3	159.8	12, 15, 17
Total current assets	536.6	405.3	
Total assets	3,087.2	2,957.8	5

in million EUR	31 DECEMBER		Lisa
	2016	2015	
EQUITY			
Capital and reserves attributable to equity holder of the Parent Company			
Share capital	621.6	621.6	18
Share premium	259.8	259.8	
Statutory reserve capital	62.1	62.1	18
Hedge reserve	(28.5)	16.8	20
Unrealised exchange rate differences	11.9	11.0	20
Retained earnings	770.2	599.5	18
Total equity and reserves attributable to equity holder of the Parent Company	1,697.1	1,570.8	
Non-controlling interest	0.9	1.1	
Total equity	1,698.0	1,571.9	
LIABILITIES			
Non-current liabilities			
Borrowings	920.6	932.5	12, 21
Other payables	1.8	1.2	22
Derivate financial instruments	6.1	-	12, 14
Deferred income	181.0	171.4	23
Provisions	30.7	31.0	24
Total non-current liabilities	1,140.2	1,136.1	
Current liabilities			
Borrowings	19.3	19.3	12, 21
Trade and other payables	155.4	179.0	22
Derivative financial instruments	16.5	11.8	12, 14
Provisions	57.8	39.7	24
Total current liabilities	249.0	249.8	
Total liabilities	1,389.2	1,385.9	
Total liabilities and equity	3,087.2	2,957.8	

Consolidated Statement of Cash Flows

in million EUR	1 JANUARY - 31 DECEMBER		Lisa
	2016	2015	
Cash flows from operating activities			
Cash generated from operations	245.3	351.1	32
Interest and loan fees paid	(30.3)	(43.9)	
Interest received	0.2	0.5	
Corporate income tax paid	(14.9)	-	
Net cash generated from operating activities	200.3	307.7	
Cash flows from investing activities			
Purchase of property, plant and equipment and intangible assets	(126.7)	(224.9)	
Proceeds from connection and other fees	15.2	14.0	23
Proceeds from sale of property, plant and equipment	4.9	3.0	6, 26
Dividends received from associates	2.0	1.9	
Net change in deposits not recognised as cash equivalents	-	40.0	12
Net change in restricted cash	(6.9)	0.6	13
Loans granted	(4.3)	(2.9)	37
Net cash used in investing activities	(115.8)	(168.3)	
Cash flows from financing activities			
Loans received	-	30.4	21
Repayments of bank loans	(19.3)	(6.9)	21
Repayments of other loans	(0.7)	(0.2)	
Dividends paid	(0.1)	(61.9)	19, 31
Acquisition of non-controlling interest in a subsidiary	(0.9)	(1.2)	10
Net cash used in financing activities	(21.0)	(39.8)	
Net cash flows	63.5	99.6	
Cash and cash equivalents at the beginning of the period	159.8	60.2	12, 15, 17
Cash and cash equivalents at the end of the period	223.3	159.8	12, 15, 17
Net increase/(-)decrease in cash and cash equivalents	63.5	99.6	

The notes on pages 107-180 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

in million EUR	ATTRIBUTABLE TO EQUITY HOLDER OF THE COMPANY						Non-controlling interest	Total equity	Note
	Share capital (Note 18)	Share premium	Statutory reserve capital (Note 18)	Other reserves	Retained earnings (Note 18)	Total			
Equity as at 31 December 2014	621.6	259.8	59.0	52.7	624.0	1,617.1	2.3	1,619.4	
Profit for the year	-	-	-	-	40.5	40.5	-	40.5	
Other comprehensive income for the year	-	-	-	(24.9)	-	(24.9)	-	(24.9)	
Total comprehensive income for the year	-	-	-	(24.9)	40.5	15.6	-	15.6	
Acquisition of non-controlling interest of subsidiary	-	-	-	-	-	-	(1.2)	(1.2)	
Dividends paid	-	-	-	-	(61.9)	(61.9)	-	(61.9)	19, 31
Transfer of retained earnings to statutory reserve capital	-	-	3.1	-	(3.1)	-	-	-	
Total contributions by and distributions to owners of the company, recognised directly in equity	-	-	3.1	-	(65.0)	(61.9)	(1.2)	(63.1)	
Equity as at 31 December 2015	621.6	259.8	62.1	27.8	599.5	1,570.8	1.1	1,571.9	
Profit for the year	-	-	-	-	170.9	170.9	0.1	171.0	
Other comprehensive income for the year	-	-	-	(44.4)	-	(44.4)	-	(44.4)	
Total comprehensive income for the year	-	-	-	(44.4)	170.9	126.5	0.1	126.6	
Increase of non-controlling interest due to the conversion of subsidiary's debt into equity	-	-	-	-	-	-	0.6	0.6	
Acquisition of non-controlling interest of subsidiary	-	-	-	-	(0.2)	(0.2)	(0.9)	(1.1)	10
Total contributions by and distributions to owners of the company, recognised directly in equity	-	-	-	-	(0.1)	(0.1)	(0.3)	(0.4)	
Equity as at 31 December 2016	621.6	259.8	62.1	(16.6)	770.2	1,697.1	0.9	1,698.0	

The notes on pages 107-180 are an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

1. General Information

The consolidated financial statements of Eesti Energia Group for the year ended 31 December 2016 include the financial information concerning Eesti Energia AS (parent company, legal form: public limited company) and its subsidiaries (the Group) and the Group's participation in associated entities.

Eesti Energia is an international energy company operating in the Baltic Sea region's energy market and the global oil market. Eesti Energia is engaged in mining oil shale, production of power, heat and oil, development of oil shale refining know-how and technologies as well as provision of services and products to customers. The company's objective is to enhance Estonia's primary natural resource in the most efficient manner possible and to reduce the ecological footprint of the oil shale-based energy sector. Besides oil shale, electricity is also generated from wind, water, mixed household waste and biomass. Outside Estonia, Eesti Energia operates under the Enefit trademark. The Group has investments in associates which operate in Jordan.

The registered address of the Parent Company is Lelle 22, Tallinn 11318, Republic of Estonia.

The sole shareholder of Eesti Energia AS is the Republic of Estonia.

The bonds of Eesti Energia AS are listed on London Stock Exchange.

These consolidated financial statements of the Group were authorised for issue by the Management Board on 20 February 2017. Under the Commercial Code of the Republic of Estonia, the annual report must additionally be approved by the Supervisory Board of the Parent Company and authorised for issue by the General Meeting of Shareholders.

2. Summary of significant accounting policies

The principal accounting policies used in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently used for all reporting periods presented, unless otherwise stated.

2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with the **International Financial Reporting Standards (IFRS) and IFRIC Interpretations**, as adopted by the European Union.

The consolidated financial statements have been prepared under the historical cost convention, except financial assets and liabilities (including derivative financial instruments) at fair value through profit and loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates.

It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement and where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

2.2 Changes in accounting policy and disclosures

(a) Adoption of New or Revised Standards and Interpretations

There were no new or revised standards or interpretations that were effective for the first time for the financial year beginning on or after 1 January 2016 that had a material impact to the Group.

(b) New standards and interpretations not yet adopted

Certain new or revised standards and interpretations have been issued that are mandatory for the Group's annual periods beginning on or after 1 January 2017, and which the Group has not early adopted:

- *IFRS 9, Financial Instruments: Classification and Measurement*. The standard will be mandatory for the Group from 1 January 2018. Key features of the new standard are:
 1. Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
 2. Classification for debt instruments is driven by the entity's business model for managing the financial assets

and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets' cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.

3. Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.
4. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
5. IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a 'three stage' approach which is based

on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.

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

The standard may have an effect on the classification of Group's financial instruments and value measurement.

- *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture - Amendments to IFRS 10 and IAS 28.* The effective date will be determined by the IASB, the amendments are not yet adopted by the EU. These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when

a transaction involves a business. A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are held by a subsidiary and the shares of the subsidiary are transferred during the transaction. The amendments may have an effect on the recognition of the Group's transactions with the associates.

- *IFRS 16, Leases.* The standard will be effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU. The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The standard will have an effect on recognising the expenses, assets and liabilities arising from operating lease contracts in the financial statements.

- *Disclosure Initiative - Amendments to IAS 7*. The standard will be effective for annual periods beginning on or after 1 January 2017; not yet adopted by the EU. The amended IAS 7 will require disclosure of a reconciliation of movements in liabilities arising from financing activities. The standard may impact the disclosure of information in the financial statements.
- *IFRS 15, Revenue from Contracts with Customers*. The standard will be effective for annual periods beginning on or after 1 January 2018. The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed. The Group is currently assessing the impact of the standard on its financial statements.

There are no other new or revised standards or interpretations that are not yet effective that would be expected to have a material impact on the Group.

2.3 Consolidation

(a) Subsidiaries

Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are de-consolidated from the date that control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis, either at fair value or at the non-controlling interest's proportionate share of the recognised amounts of acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at

the acquisition date; any gains or losses arising from such re-measurement are recognised in profit or loss.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

Goodwill is initially measured as the excess of the aggregate of the consideration transferred and the fair value of non-controlling interest over the net identifiable assets acquired and liabilities assumed. If the consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss.

In preparation of consolidated financial statements, the financial statements of the Parent Company and its subsidiaries are consolidated on a line-by-line basis. In preparation of consolidated financial statements, inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

In the Parent Company's separate financial statements the investments in subsidiaries are accounted for at cost less impairment.

(b) Changes in ownership interests in subsidiaries without change of control

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions – that is, as transactions with the owners in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains and losses on disposals to non-controlling interests are also recorded in equity.

(c) Disposal of subsidiaries

When the Group ceases to have control any retained interest in the entity is remeasured to its fair value at the date when the control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets and liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

(d) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity

method of accounting and are initially recognised at cost, and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. The Group's investment in associates includes goodwill identified on acquisition.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income is reclassified to profit or loss where appropriate.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in the associates' other comprehensive income is recognised directly in other comprehensive income with a corresponding adjustment to the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise any further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount adjacent to "Share of other profit/loss of the associates" in the income statement.

Profits and losses resulting from upstream and downstream transactions between the Group and its associate are recognised in the Group's financial statements only to the extent of unrelated investor's interests in the associates. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

2.4 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, is the Management Board of the Parent Company.

2.5 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in euros, which is the functional currency of the parent company and presentation currency of the Group. The financial statements have been rounded to the nearest million, unless stated otherwise.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the official exchange rates of the European Central Bank prevailing at the dates of the transactions or valuation where items are re-measured. When the European Central Bank does not quote a particular currency, the official exchange rate against the Euro of the central bank issuing the currency is used as the basis. Foreign exchange gains and losses resulting from the settlement of such transactions are recognised in the income statement. Monetary assets and liabilities denominated in foreign currencies are translated using the official exchange rate of the European Central Bank prevailing at the balance sheet date or on the basis of the official exchange rate of the central bank of the country issuing the foreign currency when the European Central Bank does not quote the particular currency. Foreign exchange gains and losses from translation are recognised in the income statement, except for gains and losses from the revaluation of cash flow hedging instruments recognised as effective hedges, which are recognised in other comprehensive income. Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented as finance income and costs; other foreign exchange gains and losses are presented as other operating income or other operating expenses.

(c) Group companies

The results and financial position of the subsidiaries that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities are translated at the closing rate of the European Central Bank at the date of that balance sheet;
- income and expenses are translated at average exchange rates of the period (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
- all resulting exchange differences are recognised in other comprehensive income.

Goodwill and fair value adjustments arising on the acquisition of a foreign subsidiary are treated as assets and liabilities of the foreign subsidiary and translated at the closing rate. Exchange differences arising are recognised in other comprehensive income.

None of the subsidiaries in the Group operates in a hyper-inflationary economy.

2.6 Classification of assets and liabilities as current or non-current

Assets and liabilities are classified in the statement of financial position as current or non-current. Assets expected to be disposed of during the next financial year or during the normal operating cycle of the Group are considered as current. Liabilities whose due date is during the next financial year or that are expected to be settled during the next financial year or during the normal operating cycle of the Group are considered as current. All other assets and liabilities are classified as non-current.

2.7 Property, plant and equipment

Property, plant and equipment (PPE) are tangible items that are used in the operating activities of the Group with an expected useful life of over one year. Property, plant and equipment are presented in the statement of financial position at historical cost less any accumulated depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. The cost of purchased non-current assets comprises the purchase price, transportation costs, installation, and other direct expenses related to the acquisition or implementation of the asset. The cost of the self-constructed items of property, plant and equipment includes the cost of materials, services and payroll expenses.

If an item of property, plant and equipment consists of components with significantly different useful lives, these components are depreciated as separate items of property, plant and equipment.

When the construction of an item of property, plant and equipment lasts for a substantial period of time and is funded with a loan or other debt instrument, the related borrowing costs (interest) are capitalised in the cost of the item being constructed. Borrowing costs are capitalised if the borrowing costs and expenditures for the asset have been incurred and the construction of the asset has commenced. Capitalisation of borrowing costs is ceased when the construction of the asset is completed or when the construction has been suspended for an extended period of time.

Subsequent expenditures incurred for items of property, plant and equipment are included in the carrying amount of the item of property, plant and equipment or are recognised as a separate asset only when it is probable that future economic benefits associated with the assets will flow to the Group and the cost of the asset can be measured reliably. The replaced component or proportion of the replaced item of PPE is de-recognised. Costs related to ongoing maintenance and repairs are charged to the income statement.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

Buildings	30–40 years
Facilities, including	
electricity lines	12.5–50 years
other facilities	10–60 years
Machinery and equipment, including	
transmission equipment	5–45 years
power plant equipment	7–32 years
other machinery and equipment	3–30 years
Other property, plant and equipment	3–10 years

The expected useful lives of items of property, plant and equipment are reviewed during the annual stocktaking, when subsequent expenditures are recognised and in the case of significant changes in development plans. When the estimated useful life of an asset differs significantly from the previous estimate, it is treated as a change in the accounting estimate, and the remaining useful life of the asset is changed, as a result

of which the depreciation charge of the following periods also changes.

An asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.9).

To determine the gains and losses from the sale of property, plant and equipment, the carrying amount of the assets sold is subtracted from the proceeds. The resulting gains and losses are recognised in the income statement items under "Other operating income" or "Other operating expenses" respectively.

2.8 Intangible assets

Intangible assets are recognised in the statement of financial position only if the following conditions are met:

- the asset is controlled by the Group;
- it is probable that the future economic benefits that are attributable to the asset will flow to the Group;
- the cost of the asset can be measured reliably.

Intangible assets (except for goodwill) are amortised using the straight-line method over the useful life of the asset.

Intangible assets are tested for impairment if there are any impairment indicators, similarly to the testing of impairment for items of property, plant and equipment (except for goodwill). Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually by comparing their carrying amount with their recoverable amount.

(a) Goodwill

Goodwill acquired in a business combination is not subject to amortisation. Instead, for the purpose of impairment testing, goodwill is allocated to cash-generating units and an impairment test is performed at the end of each reporting period (or more frequently if an event or change in circumstances demands it). The allocation is made to those cash-generating units that are expected to benefit from the synergies of the business combination in which the goodwill arose. Goodwill is allocated to a cash generating unit or a group of units, not larger than an operating segment. Goodwill is written down to its recoverable amount when this is lower than the carrying amount. Impairment losses on goodwill are not subsequently reversed. Goodwill is reported in the statement of financial position at the carrying amount (cost less any impairment losses) (Note 2.9). When determining gains and losses on the disposal of a subsidiary, the carrying amount of goodwill relating to the entity sold is regarded as part of the carrying amount of the subsidiary.

(b) 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 starting up a new business unity, research carried out for collecting new scientific or technical information and training costs are not capitalised.

(c) Contractual rights

Contractual rights acquired in a business combination are recognised at fair value on acquisition and are subsequently carried at cost less any accumulated amortisation. Contractual rights are amortised using the straight-line basis over the expected duration of the contractual right.

(d) Computer software

Costs associated with the ongoing maintenance of computer software programs are recognised as an expense as incurred.

Acquired computer software which is not an integral part of the related hardware is recognised as an intangible asset. Development costs that are directly attributable to the design and testing of identifiable software products controlled by the Group are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use it;
- there is an ability to use the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources for completing the development and using the software product are available;
- the expenditure attributable to the software product during its development can be reliably measured.

Capitalised software development costs include payroll expenses and an appropriate portion of related overheads. Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Computer software development costs are amortised over their estimated useful lives (not exceeding 15 years) using the straight-line method.

(e) Right of use of land

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 99 years.

(f) Greenhouse gas emission allowances

Greenhouse gas emission allowances controllable by the Group are accounted for as current asset. Greenhouse gas emission allowances received from the state free of charge are recognised at zero cost. Any additionally purchased allowances are recognised at purchase cost or based on the revaluation method, if the Group has acquired the greenhouse gas emission allowances more than presumably needed and the Group has a plan to sell the allowances. The provision for greenhouse gas emissions is set up in the average price of the greenhouse gas emission allowances that are owned by the Group or that will be allocated to the Group free of charge (Note 2.24).

(g) Exploration and evaluation assets of mineral resources

Expenditures that are included in the initial measurement of exploration and evaluation assets include the acquisition of rights to explore; topographical, geological, geochemical and geophysical studies; exploratory drilling; sampling and activities related to evaluation of the technical feasibility and economic viability of extracting a mineral resource.

Exploration and evaluation assets are initially recognised at cost. Depending on the nature of the asset, the exploration and evaluation assets are classified as intangible assets or items of property, plant and equipment. Expenditure on the construction, installation and completion of infrastructure facilities is capitalised within items of property, plant and equipment, other exploration and evaluation assets are recognised as intangible assets. After initial recognition, exploration and evaluation assets are measured using the cost model.

Exploration and evaluation assets are tested for impairment (Note 2.9) when one or more of the following circumstances are present:

- the period for which the Group has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on future exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned;
- exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources and the Group has

- decided to discontinue such activities in the specific area;
- sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

(h) Mining rights

Mining rights controllable by the Group are accounted for as current or non-current intangible assets depending on the expected realisation period. Mining rights received from the state free of charge are recognised at zero cost. The fee for extracted natural resources that is paid according to the volume of natural resources extracted is recognised in expenses as incurred (Note 2.22).

2.9 Impairment of non-financial assets

Assets that have indefinite useful lives (for example goodwill or intangible assets not ready to use) are not subject to amortisation but are tested annually for impairment. Assets that are subject to amortisation/depreciation and land are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the asset's:

- fair value less costs of disposal; and
- value in use.

If the fair value of the asset less costs to sell cannot be determined reliably, the recoverable amount of the asset is its value in

use. The value in use is calculated by discounting the expected future cash flows generated by the asset to their present value.

An impairment test is carried out if any of the following indicators of impairment exist:

- the market value of similar assets has decreased;
- the general economic environment and the market situation have worsened, and therefore it is likely that the future cash flows generated by assets will decrease;
- market interest rates have increased;
- the physical condition of the assets has considerably deteriorated;
- revenue generated by assets is lower than expected;
- results of some operating areas are worse than expected;
- the activities of a certain cash generating unit are planned to be terminated.

If the Group identifies any other evidence of impairment, an impairment test is performed.

Impairment tests are performed either for an individual asset or group of assets (cash-generating unit). A cash-generating unit is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows generated by other assets or groups of assets. An impairment loss is recognised immediately as an expense in the income statement.

At the end of each reporting period, it is assessed whether there is any indication that the impairment loss recognised in the prior periods for an asset other than goodwill may no

longer exist or may have decreased. If any such indication exists, the recoverable amount is estimated. According to the results of the estimate, the impairment loss can be partially or wholly reversed. An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

2.10 Non-current assets (or disposal groups) held-for-sale

Non-current assets (or disposal groups) are classified as assets held for sale when their carrying amount is to be recovered principally through a sale transaction rather than through continuing use, and a sale is considered highly probable. They are stated at the lower of carrying amount and fair value less costs to sell.

2.11 Financial assets

2.11.1 Classification

The Group classifies its financial assets in the following categories: at fair value through profit or loss and loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading, acquired for the purpose of selling in the short term. Derivatives are also recognised at fair value through profit or loss unless they are designated and effective hedging instruments. Assets in this category are classified as current assets.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. The Group's loans and receivables are included in the statement of financial position lines "Cash and cash equivalents", "Deposits at banks with maturities of more than three months", "Trade and other receivables".

2.11.2 Recognition and measurement

Regular purchases and sales of financial assets are recognised or de-recognised using the trade-date accounting method. Investments which are not carried at fair value through profit or loss are initially recognised at fair value plus transaction costs. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are de-recognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards incidental to ownership. Financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss are presented in the income statement line "Net financial income

(-expense)" in the period in which they arise or are incurred (Note 30). Interest income on available-for-sale financial assets and on loans and receivables is reported in the income statement line "Financial income" (Note 30). The Group has not received any interest income or dividend income on financial assets recognised at fair value through profit or loss in the current and comparative reporting period.

The fair values of quoted investments are based on the bid prices prevailing at the end of the reporting period. To find the fair value of unquoted financial assets, various valuation techniques are used. Depending on the type of financial asset, these include the listed market prices of instruments that are substantially the same, quotes by intermediaries and estimated cash flow analysis. The Group uses several different measures and makes assumptions which are based on the market conditions at the end of each reporting period. The fair value of derivatives is based on the quotes of exchange as far as possible

2.12 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the company or the counterparty.

2.13 Impairment of financial assets

Assets carried at amortised cost

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets 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.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation, and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

For loans and receivables category the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated income statement.

If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in the consolidated income statement.

2.14 Derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The method for recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if it is, the nature of the item being hedged. The Group uses cash flow hedging instruments in order to hedge the risk of changes of the prices of shale oil and electricity.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, and also its risk management objectives and strategy for undertaking various hedge transactions. The Group also documents its assessment and tests, both at hedge inception

and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in the cash flows of the hedged items.

The fair values of derivative financial instruments used for hedging purposes are disclosed in Note 14. Movements on the hedge reserve in other comprehensive income are disclosed in Note 21. The full fair value of hedging derivatives is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Derivatives held for trading are classified as current assets or liabilities.

(a) Cash flow hedge

The effective portion of changes in the fair value of derivatives (for options only the intrinsic value) that are designated and qualify as cash flow hedges is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the income statement as a net amount within other operating income or operating expenses.

Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss (for instance, when the forecast sale that is hedged takes place).

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately

recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately recognised as other operating income or operating expenses in the income statement.

Hedging instruments, which are combined from various components of derivative instruments, are recognised at fair value with changes through profit or loss until the acquisition of all components.

(b) Derivatives at fair value through profit or loss

Derivatives which are not designated as hedging instruments are carried at fair value through profit or loss. The gains and losses arising from changes in the fair value of such derivatives are included within other operating income or operating expenses in the income statement.

(c) Derivatives at own use

Derivative contracts that are entered into use and continue to be held for the purpose of the receipt of the underlying commodity in accordance with the Group's expected purchase requirements are accounted for as regular purchases of underlying commodities. For example, any futures contracts for buying greenhouse gas emissions allowances that are necessary for the Group's electricity production purposes are not recognised as derivatives on the balance sheet; the emissions allowances purchased are recognised as intangible assets when settlement of future contract occurs and emissions allowances are transferred to the Group. Any payments made

to the counterparty before the settlement date are recognised as prepayments for intangible assets.

If the terms of the contracts permit either party to settle it net in cash or another financial instrument or the commodity that is the subject of the contracts is readily convertible to cash, the contracts are evaluated to see if they qualify for own use treatment. Contracts that do not qualify for own use treatment, are accounted for as derivatives as described above

2.15 Inventories

Inventories are stated in the statement of financial position at the lower of cost or net realisable value. The weighted average method is used to expense inventories. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity), but it excludes borrowing costs. The cost of raw and other materials consists of the purchase price, expenditure on transportation and other costs directly related to the purchase.

Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

2.16 Trade receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business.

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective

interest rate method, less provision for impairment. A provision for the impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, the probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 90 days overdue) are considered indicators that the trade receivable is impaired. Material receivables are assessed individually. The rest of the receivables are collectively assessed for impairment, using previous years' experience of impairment which is adjusted to take account of current conditions. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within other operating expenses. When a receivable is classified as uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited in the income statement against other operating expenses.

If collection is expected within one year or less, the receivables are classified as current assets. If not, they are presented as non-current assets. Long-term receivables from customers are recognised at the present value of the collectible amount. The difference between the nominal value and the present value of the collectible receivable is recognised as interest

income during the period remaining until the maturity date using the effective interest rate.

2.17 Cash and cash equivalents

Cash and cash equivalents include bank account balances and cash in transit as well as short-term highly liquid investments in banks.

2.18 Share capital and statutory reserve capital

Ordinary shares are classified as equity. No preference shares have been issued. Unavoidable incremental costs directly attributable to the issue of new ordinary shares are shown in equity as a deduction from the proceeds. Shares approved at the General Meeting but not yet registered in the Commercial Registry are recognised in the equity line "Unregistered share capital".

The Commercial Code requires the Parent Company to set up statutory reserve capital from annual net profit allocations, the minimum amount of which is 1/10 of share capital. The amount of allocation to annual statutory reserve capital is 1/20 of the net profit of the financial year until the reserve reaches the limit set for reserve capital. Reserve capital may be used to cover a loss that cannot be covered from distributable equity, or to increase share capital.

2.19 Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payables are classified as current

liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities. Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

2.20 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred, and are subsequently carried at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowing using the effective interest method.

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.

Borrowings are recognised as current liabilities unless the Group has an unconditional right to defer the settlement of the liability for at least 12 months after the end of reporting period.

2.21 Borrowing costs

General and specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

The capitalised borrowing costs are recognised in the statement of cash flows under item "Interest and loan fees paid".

2.22 Taxation

(a) Corporate income tax on dividends in Estonia

Under the Income Tax Act, the annual profit earned by entities is not taxed in Estonia. Corporate income tax is paid on dividends, fringe benefits, gifts, donations, costs of entertaining guests, non-business related disbursements and adjustments of the transfer price. From 1 January 2015, the tax rate on the net dividends paid out of retained earnings is 20/80. In certain

circumstances, it is possible to distribute dividends without any additional income tax expense. The corporate income tax arising from the payment of dividends is accounted for as a liability and expense in the period in which dividends are declared, regardless of the actual payment date or the period for which the dividends are paid. The 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 entities 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 retained earnings is disclosed in the notes to the financial statement.

(b) Other taxes in Estonia

The following taxes had an effect on the Group's expenses:

Tax	Tax rate
Social security tax	33% of the payroll paid to employees and of fringe benefits
Unemployment insurance tax	0,8% of the payroll paid to employees
Fringe benefit income tax	20/80 of fringe benefits paid to employees
Pollution charges	Paid for contamination of the air, water, ground water, soil and waste storage, and based on tonnage and type of waste
Fee for extraction right for oil shale	0,275 euros per tonne of oil shale extracted (in 2015 1.53 euros per tonne of oil shale extracted)
Water utilisation charges	1.61-170.08 euros per 1000 m ³ of pond or ground water used (in 2015 1.59-168.4 euros per 1000 m ³ of pond or ground water used).
Land tax	0.1-2.5% on taxable value of land per annum
Tax on heavy trucks	3.50 – 232.60 euros per truck per quarter
Excise tax on electricity	4.47 euros per MWh of electricity
Excise tax on natural gas	33.77 euros per 1000 m ³ of natural gas (in 2015 28.14 euros per 1000 m ³ of natural gas)
Excise tax on shale oil	57.0 euros per 1000 kg of shale oil (In 2015 15.01 euros per 1000 kg of shale oil)
Excise tax on oil shale	0.93 euros per giga-joule (in 2015 0.30 euros per giga-joule)
Corporate income tax on non-business related expenses	20/80 on non-business related expenses (in 2014 21/79 on non-business related expenses)

(c) Income tax rates in foreign countries in which the Group operates

Latvia	Income earned by resident legal persons is taxed at an income tax rate of 15%
Lithuania	Income earned by resident legal persons is taxed at an income tax rate of 15%
Germany	Income earned by resident legal persons is taxed at an income tax rate of 28.425% (corporate and trade tax combined)
the USA	Income earned by resident legal persons is taxed at an income tax rate of 35%
Jordan	Income earned by resident legal persons is taxed at an income tax rate of 24%. Jordan Oil Shale Energy is fully and Attarat Power company in the 75% extent exempted from income tax according to the contracts concluded with the Hashemite Kingdom of Jordan.
the Netherlands	Income earned by resident legal persons is taxed at an income tax rate of 25%

(d) Deferred income tax

Deferred income tax is recognised in foreign subsidiaries on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax assets and liabilities are recognised under the liability method. Deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill; deferred income tax is not accounted for if it arises from initial recognition of an asset and liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised on deductible temporary differences arising from investments in subsidiaries and associates only to the extent that it is probable the temporary difference will reverse in the future and there is sufficient taxable profit available against which the temporary difference can be utilised.

As at 31 December 2016 and 31 December 2015, the Group had neither any deferred income tax assets nor deferred income tax liabilities.

2.23 Employee benefits

Short-term employee benefits

Short-term employee benefits include wages and salaries as well as social security taxes, benefits related to the temporary halting of the employment contract (holiday pay or other similar pay) when it is assumed that the temporary halting of the employment contract will occur within 12 months from the end of the period in which the employee worked, and other benefits payable after the end of the period during which the employee worked.

If during the reporting period the employee has provided services in return for which benefits are expected to be paid, the Group will set up a liability (accrued expense) for the amount of the forecast benefit, from which all paid amounts are deducted.

Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits at the earlier of the following dates: (a) when the Group can no longer withdraw the offer of those benefits; and (b) when the Group recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of termination benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end

of the reporting period are discounted to their present value. Redundancy provisions are set up for redundancies occurring in the course of restructuring (Note 2.24).

Other employee benefits

Provisions have been set up to cover the benefits arising from collective agreements and other agreements and the compensation for work-related injuries (Note 2.24).

2.24 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using an interest rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

Provisions are recognised based on management's estimates. If required, independent experts may be involved. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Although the likelihood of an outflow of resources may be small for any individual item, it may be probable that some outflow of

resources will be needed to settle the class of obligations as a whole. If that is the case, the provision is recognised (if the other recognition criteria are met).

Provisions are reviewed at the end of each reporting period and adjusted to reflect current best estimates. The costs related to setting up provisions are charged to operating expenses or are included within the acquisition cost of an item of PPE when the provision is related to the dismantlement, removal or restoration or other obligation, incurred either when the item is acquired or as a consequence of use of the item during a particular period.

Provisions are used only to cover the expenses for which they were set up.

Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognised when, and only when, it is virtually certain that reimbursement will be received if the Group settles the obligation. The reimbursement shall be treated as a separate asset. The amount of the reimbursement may not exceed the amount of the provision.

(a) Provisions for post-employment benefits and work-related injury compensation

If the Group has the obligation to pay post-employment benefits to their former employees, a provision is set up to cover these costs. The provision is based on the terms of the obligation and the estimated number of people eligible for the compensation.

Provisions for work-related injuries are recognised to cover expenditure related to future payments to former employees according to court orders over the estimated period of such an obligation.

(b) Environmental protection provisions

Environmental protection provisions are recognised to cover environmental damages that have occurred before the end of the reporting period when this is required by law or when the Group's past environmental policies have demonstrated that the Group has a constructive present obligation to liquidate this environmental damage. Experts' opinions and prior experience in performing environmental work are used to set up the provisions.

(c) Provisions for the termination of mining operations

Provisions for the termination of mining operations are set up to cover the costs related to the closing of mines and quarries, if it is required by law. Experts' opinion and prior experience gained from the termination of mining operations is used to set up the provisions.

(d) Provision for termination benefits

Provisions for termination benefits have been recognised to cover the costs related to employee redundancy if the Group has announced a restructuring plan, identifying the expenditure, the business or part of a business concerned, the principal locations affected, the location, function and approximate number of employees who will be compensated for termination of their services, the timing of the implementation of the

plan; and if the Group has raised a valid expectation among those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

(e) Provision for the dismantling cost of assets

The provisions for the dismantling of assets are set up to cover the estimated costs relating to the future dismantling of assets if the dismantling of assets is required by law or if the Group's past practice has demonstrated that the Group has a present constructive obligation to incur these costs. The present value of the dismantling costs of assets is included within the cost of property, plant and equipment.

(f) Provisions for greenhouse gas emissions

A provision for greenhouse gas emissions is set up in the average price of the greenhouse gas emission allowances that are owned by the Group or that will be allocated to the Group free of charge to meet the obligations arising from legislation relating to greenhouse gas emissions. When the Group surrenders the greenhouse gas emission allowances to the state for the greenhouse gases emitted, both the provision and the intangible assets are reduced by equal quantities and amounts (Note 2.8).

(g) Provisions for onerous contracts

A provision for onerous contract is set up if the Group has concluded a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The provision is set up in

the amount which is the lower of the cost of fulfilling it (revenues received less expenses occurred of fulfilling the contract) and any compensation or penalties arising from failure to fulfill it.

(h) Provision for obligations arising from treaties

Provision for obligations arising from treaties is set up to meet the obligations arising from treaties, in which realization of timing or amount is uncertain.

2.25 Contingent liabilities

Possible obligations where it is not probable that an outflow of resources will be required to settle the obligation, or where the amount of the obligation cannot be measured with sufficient reliability, but which may become in certain circumstances liabilities, are disclosed in the notes to the financial statements as contingent liabilities.

2.26 Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable for the sale of goods and provision of services in the ordinary course of business. Revenue is shown net of value-added tax and discounts after the elimination of intra-group transactions. Revenue is recognised only when the amount of revenue can be reliably measured and it is probable that future economic benefits will flow to the Group, all significant risks and rewards incidental to ownership have been transferred from the seller to the buyer, and the additional criteria presented below have been met. The amount of revenue can be measured reliably only when all the conditions related to the transaction are evident.

(a) Sale of electricity and grid services

Revenue is recognised on the basis of meter readings of customers. Meter readings are reported by customers, read by remote counter reading systems based on actual consumption, or estimated based on past consumption patterns. Additionally, estimates are made of the potential impact of readings either not reported or incorrectly reported by the end of the reporting period, resulting in a more precise estimation of the actual consumption and sale of electricity.

(b) 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 them to the network. The revenue from connection fees is deferred and recognised as income over the estimated average useful lives of assets acquired for the connections. The average amortisation period of connection fees is 32 years. Deferred connection fees are carried in the statement of financial position as long-term deferred income.

(c) Revenue recognition under the stage of completion method

Revenue from unfinished and finished but undelivered services is recognised using the stage of completion method. Under this method, contract revenue and profit is recognised in the proportion and in the accounting periods in which the contract costs associated with the service contract were incurred. Unbilled but recognised revenue is recorded as accrued income in the statement of financial position. Where progress billings at the end of the reporting period exceed costs incurred plus

recognised profits, the balance is shown as due to customers on construction contracts, under accrued expenses.

(d) Interest income

Interest income is recognised when it is probable that the economic benefits associated with the transaction will flow to the Group and the amount of revenue can be measured reliably. Interest income is recognised using the effective interest rate, unless the receipt of interest is uncertain. In such cases the interest income is accounted for on a cash basis.

(e) Dividend income

Dividend income is recognised when the Group has established the right to receive payment.

2.27 Government grants

Government grants are recognised at fair value, when there is reasonable assurance that the grant will be received and the Group will comply with all attached conditions. Grants are recognised as income over the periods necessary to match them with the costs which they are intended to compensate.

Assets acquired through government grants are initially recognised in the statement of financial position at cost. The amount received as a government grant is recognised as deferred income related to the government grant. Related assets are depreciated and the grant is recognised as income over the estimated useful life of the depreciable asset.

2.28 Leases

A lease is an agreement whereby the lessor conveys to the

lessee the right to use an asset for an agreed period of time in return for a payment or series of payments. Leases which transfer all significant risks and rewards incidental to ownership to the lessee are classified as finance leases. Other leases are classified as operating leases.

(a) The Group as the lessee

Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

(b) The Group as the lessor

The accounting policies for items of property, plant and equipment are applied to assets leased out under operating lease terms. Rental income is recognised in the income statement on a straight-line basis over the lease term.

2.29 Dividend distribution

Dividends are recognised as a reduction of retained earnings and a payable to shareholders at the moment the dividends are announced.

2.30 Related party transactions

For the purposes of preparing the consolidated financial statements, the related parties include the associates of the Group, the members of the Supervisory and Management Boards of Eesti Energia AS and other individuals and entities who can control or significantly influence the Group's financial and operating decisions. As the shares of Eesti Energia AS belong 100% to the Republic of Estonia, the related parties also include entities under the control or significant influence of the state.

3. Financial risk management

3.1 Financial risks

The Group's activities are accompanied by a variety of financial risks: market risk (which includes currency risk, cash flow and fair value interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

The purpose of financial risk management is to mitigate financial risks and minimise the volatility of financial results. The risk and internal audit department under the Chairman of the Management Board and auditing committee is engaged in risk management and is responsible for the development, implementation and maintenance of the Group's risk management system. The Group's financial risks are managed in accordance with the principles established by the Management Board at the Group level. The Group's liquidity, interest rate and currency risks are managed in the finance department of the Parent Company.

3.1.1 Market risks

3.1.1.1 Currency risk

Currency risk is the risk that the fair value of financial instruments or cash flows will fluctuate in the future due to exchange rate changes. The financial assets and liabilities denominated in euros are considered to be free of currency risk. All long-term

borrowings and electricity export contracts are also concluded in euros to avoid currency risk.

The Group's main currency risk arises in connection with the part of the sales transactions of shale oil denominated in US dollars that is not hedged with future transactions (Note 14). In addition, a few other procurement and other contracts have been concluded in a currency other than the functional currency of the Group companies. The majority of these transactions included the transactions concluded in US dollars.

At the end of reporting period, the Group had the following balances of financial assets and liabilities denominated in US dollars.

in million EUR	31 DECEMBER	
	2016	2015
Cash and cash equivalents (Note 17)	0.3	0.1
Trade and other receivables	48.5	36.3
Trade and other payables	0.3	0.1

Had the US dollar's exchange rate at 31 December 2016 been 10% (31 December 2015: 12%) higher or lower (with other factors remaining constant), the Group's profit for the financial year would have been EUR 4.6 million higher/lower (2015: EUR 4.5 million higher/lower) as a result of the revaluation of the balances of cash and cash equivalents, trade and other receivables and trade and other payables.

The cash and cash equivalents by currencies is disclosed in Note 17.

3.1.1.2 Price risk

Price risk is the risk that the fair value and cash flows of financial instruments will fluctuate in the future for reasons other than changes in the market prices resulting from interest rate risk or foreign exchange risk. The sale of goods produced and services provided by the Group under free market conditions, the purchase of resources used in production, and financial assets recognised at fair value through profit or loss are impacted by price risk.

3.1.1.2.1 The price risk of commodities

The most significant price risks of goods and services are the price risks related to the sale of electricity and shale oil, and to the purchase of greenhouse gas emission allowances. The Group uses various derivatives to hedge the price risks related to the sale of goods and services and purchase and sale of greenhouse gas emission allowances. To hedge the risk related to changes in the price of electricity, forward contracts are used which are entered into for the sale of a specific volume of electricity at each trading hour. The volume of derivative transactions for sales of electricity through the power exchange Nord Pool depends on the price difference between the market price of electricity and the price level of greenhouse gas emission allowances and the planned production capacity of electrical energy.

Swap and option transactions are used to hedge the risk in the price of shale oil. With these transactions, the Group or a transaction partner undertakes to pay the difference between the fixed price and the market price in the reporting period.

According to the risk hedging principles of the Group, the goal of hedging transactions is to ensure predefined profits after variable expenses. The volume of the underlying assets, the risks of which are being hedged, is determined separately for each period. The minimum price level is set for price risk hedge transactions, after which transactions can be concluded. The volume of transactions depends on the time horizon of the underlying period and the contract price offered.

The need to buy greenhouse gas emission allowances arises when CO₂ emissions exceed the number of greenhouse gas emission allowances allocated free of charge by the state. To lower the risk from changes in the price of the amount of greenhouse gas emissions allowed, the Group uses option and future transactions (Note 14). According to the risk management strategy concerning greenhouse gas emission allowances, the missing quantity is purchased on a dispersed basis throughout the year based on the expected price and shortage of greenhouse gas emission allowances.

3.1.1.3 Cash flow and fair value interest rate risk

Interest rate risk is the risk that the fair value of financial instruments or cash flows will fluctuate in the future due to changes in market interest rates. Cash flow interest rate risk arises to the Group from floating interest rate borrowings and lies in the danger that financial expenses increase when interest rates increase.

Sensitivity analysis is used to assess the interest rate risk. For managing the Group's interest rate risks, the principle that the

share of fixed interest rate borrowings in the portfolio should be over 50% is followed. The Group has predominantly locked the risk resulting from fluctuations in the base interest rate. As at the financial year-end, for 95% of borrowings the base interest rate is locked until maturity and 5% of borrowings have floating interest rates (31 December 2015: for 82% was locked until maturity, for 13% until July 2016 and 5% with floating interest rate). Due to that the changes in the market interest rate don't have material effect on the Group's borrowings, however they may affect the fair value of the borrowings.

Overnight deposits and term deposits have been entered into with fixed interest rates and they do not result in an interest rate risk for cash flows to the Group. Any reasonably possible change in the fair value of financial assets at fair value through profit or loss would not have had significant impact on the Group's net profit.

3.1.2 Credit risk

Credit risk is the risk that the Group will incur a monetary loss caused by the other party to a financial instrument because of that party's inability to meet its obligations. Cash in bank deposits, derivatives with a positive value and trade and other receivables are exposed to credit risk.

According to the principles of depositing of available monetary funds of the Group, the following principles are followed:

- preserving capital
- ensuring liquidity at the right moment for the needs of business;
- optimal return considering the previous two goals.

Short-term monetary funds can be deposited in the following domestic and foreign financial instruments:

- money market funds and interest rate funds in which holdings or shares can be redeemed or sell on a regular basis;
- deposits of credit institutions;
- freely negotiable bonds and other freely negotiable debt instruments.

Requirements for the level of credit risk of issuers and partners of financial instruments (including hedge transactions) and maximum positions of each partner are approved by the Group's committee of the financial risks.

The available monetary funds can be deposited only in financial instruments nominated in euros. In addition there are certain requirements for the maturities of the financial instruments and diversification.

The unpaid invoices of clients are handled on a daily basis in the departments specifically set up for this purpose. The automated reminder and warning system sends messages to customers about overdue invoices with the warning that if they are not paid, the clients will be cut off from the electricity network. After that, a collection petition is filed at the court or a collection agency. Special agreements are in the jurisdiction of special credit committees.

The maximum amount exposed to credit risk was as follows as at the end of the reporting period:

in million EUR	31 DECEMBER	
	2016	2015
Trade and other receivables (Notes 12 and 13)*	232.8	131.1
Bank accounts and deposits recognised as cash equivalents in banks (Note 12, 15 and 17)	223.3	159.8
Derivatives with positive value (Notes 3.3, 12, 14 and 15)	1.4	40.3
Total amount exposed to credit risk	457.5	331.2

Trade receivables are shown net of impairment losses. Although the collection of receivables can be impacted by economic factors, management believes that there is no significant risk of loss beyond the provisions already recorded. The types of other receivables do not contain any impaired assets.

More detailed information on credit risk is disclosed in Notes 13 and 15.

3.1.3 Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its financial obligations due to insufficient cash inflows. Liquidity risk is managed through the use of various financial instruments such as loans, bonds and commercial papers.

The Group's liquidity risk has two dimensions. Short-term liquidity risk is the risk that the Group's bank accounts do not include sufficient cash to meet the Group's financial commitments. Long-term liquidity risk is the risk that the Group does not have sufficient amount of unrestricted cash or other

sources of liquidity to meet its future liquidity needs in order to carry out its business plan and meet its commitments, or that for the above reason the Group needs to raise additional cash in a hurry and on terms, which are less than optimal. Short-term liquidity risk is mitigated so that the Group keeps certain amount of cash buffer in its bank accounts in order to have sufficient amount of cash available also in case there are deviations from the cash flow forecast. Long-term liquidity risk is mitigated by regular forecasts of liquidity needs for the next 12 months (including cash requirement for investments, loan repayments and dividends, and positive cash flow from operations) and by keeping sufficient liquidity buffer in the form of unrestricted cash, undrawn investment loans, and limits of liquidity loans. The Group's liquidity risk is managed at the Group level by the parent company's Financial Department.

As at 31 December 2016, the Group had spare monetary balances of EUR 223.3 million (31 December 2015: EUR 159.8 million). Additionally, as at the end of the financial year, the Group had undrawn loan facilities of EUR 220.0 million (31 December 2015: EUR 220.0 million) (Note 21). This included bilateral liquidity loan agreements with floating interest rate of EUR 150.0 million in aggregate, with SEB and OP Corporate bank, which will mature in five years (July 2020) and long-term investment loan agreement with EIB of EUR 70.0 million. The loan can be taken into use until October 2017.

The following liquidity analysis includes the division between the Group's current and non-current liabilities (including derivatives with net payments) by the maturity date of liabilities.

All amounts shown in the table are contractual undiscounted cash flows. The payables due within 12 months after the end of the reporting period, except for borrowings, are shown at their carrying amount.

Division of liabilities by maturity date as at 31 December 2016 (in million EUR):

in million EUR	Less than 1 year	Between 1 and 5 years	Later than 5 years	Total undiscounted cash flows	Carrying amount
Borrowings (Notes 3.2, 12 and 21)*	39.5	485.0	599.3	1,123.8	939.9
Derivatives (Notes 3.3, 12 and 14)	16.5	6.1	-	22.6	22.6
Trade and other payables (Notes 12 and 22)	95.7	1.8	-	97.5	97.5
Tax liabilities and payables to employees (Note 22)	53.1	-	-	53.1	53.1
Total	204.8	492.9	599.3	1,297.0	1,113.1

* Interest expenses have been estimated on the basis of the interest rates prevailing as at 31 December 2016.

Division of liabilities by maturity date as at 31 December 2015 (in million EUR):

in million EUR	Less than 1 year	Between 1 and 5 years	Later than 5 years	Total undiscounted cash flows	Carrying amount
Borrowings (Notes 3.2, 12 and 21)*	41.3	478.3	666.7	1,186.3	951.8
Derivatives (Notes 3.3, 12 and 14)	11.8	-	-	11.8	11.8
Trade and other payables (Notes 12 and 22)	104.3	1.2	-	105.5	105.5
Tax liabilities and payables to employees (Note 22)	68.0	-	-	68.0	68
Total	225.4	479.5	666.7	1,371.6	1,137.1

* Interest expenses have been estimated on the basis of the interest rates prevailing as at 31 December 2015.

The information about the dividends that will be declared and become payable after the end of the reporting period is disclosed in Note 19.

3.2 Management of equity

All shares of Eesti Energia AS belong to the state. Decisions concerning dividend distribution and increases or decreases of share capital are made by the Republic of Estonia through the Ministry of Finance. Each financial year, the dividends payable by Eesti Energia AS to the state budget are defined by order of the Government of the Republic of Estonia (Notes 18 and 19).

The Group follows a strategy according to which net debt should not exceed EBITDA more than 3.5 times and equity should be at least 50% of the total assets. As at 31 December 2016 and 31 December 2015, the net debt to EBITDA ratio and the equity to assets ratio were as follows (in million EUR):

in million EUR	31 DECEMBER	
	2016	2015
Debt (Notes 3.1, 12 and 21)	939.9	951.8
Less: cash and cash equivalents (Notes 3.1, 12 and 17)	(223.3)	(159.8)
Net debt	716.6	792.0
Equity	1,698.0	1,571.9
EBITDA	327.3	265.8
Assets	3,087.2	2,957.8
Net debt/EBITDA	2.2	2.98
Equity/assets	55%	53%

3.3 Fair value

The Group estimates that the fair values of assets and liabilities reported at amortised cost in the statement of financial position as at 31 December 2016 and 31 December 2015 do not materially differ from the carrying amounts reported in the consolidated financial statements, with the exception of bonds (the fair value is calculated with the inputs that are classified to Level 1 in the fair value hierarchy, Note 21). The carrying amount of current accounts receivable and payable and loan receivables less impairments is estimated to be approximately equal to their fair value. For disclosure purposes, the fair value of financial liabilities is determined by discounting the contractual cash flows at the market interest rate which is available for similar financial instruments of the Group.

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

- quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
- inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly (Level 2);
- inputs for the asset or liability that are not based on observable market data (Level 3).

The following tables present the Group's assets and liabilities that are measured at fair value by the level in the fair value hierarchy as at 31 December 2016 and 31 December 2015:

in million EUR	31 DECEMBER 2016			
	Tase 1	Tase 2	Tase 3	Kokku
Assets				
Trading derivatives (Notes 12, 14 and 15)	0.4	0.4	-	0.8
Cash flow hedges (Notes 12, 14 and 15)	-	-0.1	0.7	0.6
Total financial assets (Notes 3.1, 12, 14 and 15)	0.4	0.3	0.7	1.4
Liabilities				
Trading derivatives (Notes 12 and 14)	-	2.0	-	2.0
Cash flow hedges (Notes 12 and 14)	1.3	19.3	-	20.6
Total financial liabilities (Notes 3.1, 12 and 14)	1.3	21.3	-	22.6

in million EUR	31 DECEMBER 2015			
	Tase 1	Tase 2	Tase 3	Kokku
Assets				
Trading derivatives (Notes 12, 14 and 15)	-	1.8	-	1.8
Cash flow hedges (Notes 12, 14 and 15)	7.5	7.4	23.6	38.5
Total financial assets (Notes 3.1, 12, 14 and 15)	7.5	9.2	23.6	40.3
Liabilities				
Trading derivatives (Notes 12 and 14)	10.0	1.8	-	11.8
Total financial liabilities (Notes 3.1, 12 and 14)	10.0	1.8	-	11.8

(a) Financial instruments in level 1

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the group is the current bid price.

In level 1 are classified the Group's electricity derivatives that have been cleared in Nasdaq OMX.

(b) Financial instruments in level 2

The fair value of financial instruments that are not traded in an active market is determined using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. An instrument is included in level 2 if all the significant inputs required to establish the fair value of the instrument are observable. If one or more significant inputs are not based on observable market data, an instrument is included in level 3. The value of trading derivatives and cash flow hedges are found using notations of Nasdaq OMX, ICE, Platt's European Marcetscani and Nymex.

- The fair value of forward, swap and future contracts is determined using forward prices at the balance sheet date, with the resulting value discounted back to present value.

(c) Financial instruments in level 3

All instruments in Level 3 are options. The fair value of options is found using analytical solution of Turnbull-Wakeman Asian-type option pricing, inputs for which include the futures price,

the strike price, volatility of the underlying, the risk free interest rate, time to maturity, time to the beginning of average period, the already realised average futures price during the average period.

The following table represents the changes in Level 3 instruments for the year ended 31 December 2016

in million EUR	Cash flow hedges	Total
Opening balance	23.6	23.6
Gains (+) and losses (-) recognised in profit or loss	4.8	4.8
Gains (+) and losses (-) recognised in other comprehensive income	-7.3	-7.3
Settlements (receipts - / payments+)	-20.4	-20.4
Closing balance	0.7	0.7
Total gains(+) or losses(-) for the period included in profit or loss for assets held at the end of the reporting period under "Other operating income/expenses"	0.6	0.6
Change in unrealised gains(+) or losses(-) for the period included in profit or loss for assets held at the end of the reporting period	-0.1	-0.1

The following table represents the changes in Level 3 instruments for the year ended 31 December 2015

in million EUR	Trading derivatives at fair value through profit or loss	Cash flow hedges	Total
Opening balance	10.8	-	10.8
Transfer from trading derivatives to cash flow hedges	(10.8)	10.8	-
Option premiums received	(3.3)	-	(3.3)
Gains (+) and losses (-) recognised in profit or loss	3.3	5.5	8.8
Gains (+) and losses (-) recognised in hedge reserve	-	7.3	7.3
Closing balance	-	23.6	23.6
Total gains or losses for the period included in profit or loss for assets held at the end of the reporting period under "Other operating income/expenses"	3.3	5.5	8.8
Change in unrealised gains or losses for the period included in profit or loss for assets held at the end of the reporting period	3.3	5.5	8.8

3.4 Offsetting financial assets and financial liabilities

(a) Financial assets

The following financial assets are subject to offsetting:

As at 31. December 2016

in million EUR	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities set off in the balance sheet	Net amounts of financial assets presented in the balance sheet (Notes 3.1, 3.3, 12, 14 ja 15)	Related amounts not set off in the balance sheet	Net amount
Derivative financial instruments	22.1	(20.7)	1.4	(1.3)	0.1

Seisuga 31. detsember 2015

in million EUR	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities set off in the balance sheet	Net amounts of financial assets presented in the balance sheet (Notes 3.1, 3.3, 12, 14 ja 15)	Related amounts not set off in the balance sheet	Net amount
Derivative financial instruments	57.8	(17.5)	40.3	(7.7)	32.6

(b) Financial liabilities

The following financial liabilities are subject to offsetting:

As at 31. December 2016

in million EUR	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets set off in the balance sheet	Net amounts of financial liabilities presented in the balance sheet (Notes 3.1, 3.3, 12, 14 ja 15)	Related amounts not set off in the balance sheet	Net amount
Derivative financial instruments	43.3	(20.7)	22.6	(1.3)	21.3

Seisuga 31. detsember 2015

in million EUR	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets set off in the balance sheet	Net amounts of financial liabilities presented in the balance sheet (Notes 3.1, 3.3, 12, 14 ja 15)	Related amounts not set off in the balance sheet	Net amount
Derivative financial instruments	29.3	(17.5)	11.8	(7.7)	4.1

Agreements between the Group and the counterparties allows for offsetting in concrete single transaction when mutual

claims are in the same currency. In some agreements offsetting between two or more transactions is allowed.

4. Critical accounting estimates and assumptions

Accounting estimates and assumptions

The preparation of the financial statements requires the use of estimates and assumptions that impact the reported amounts of assets and liabilities, and the disclosure of off-balance sheet assets and contingent liabilities in the notes to the financial statements. Although these estimates are based on management's best knowledge of current events and actions, actual results may ultimately differ from these estimates. Changes in management's estimates are recognised in the income statement of the period of the change.

The estimates presented below have the most significant impact on the financial information disclosed in the financial statements.

(a) Determination of the useful lives of items of property, plant and equipment

The estimated useful lives of items of property, plant and equipment are based on management's estimate of the period during which the asset will be used. Previous experience has shown that the actual useful lives have sometimes been longer than the estimates. As at 31 December 2016, the net book amount of property, plant and equipment of the Group totalled EUR 2 469.3 million (31 December 2015: EUR 2 473.9 million), and the depreciation charge of the reporting period was EUR 143.4 million (2015: EUR 137.1 million) (Note 6).

If depreciation rates were changed by 10%, the annual depreciation charge would change by EUR 14.3 million (2015: EUR 14.0 million).

(b) Evaluation of the recoverable amount of property, plant and equipment and intangible assets

As needed, the Group performs impairment tests to determine the recoverable amount of items of property, plant and equipment and intangible assets. When carrying out impairment tests, management uses various estimates for the cash flows arising from the use of the assets, sales, maintenance, and repairs of assets, as well as estimates for inflation and growth rates and likelihood of getting grants. The estimates are based on forecasts of the general economic environment, consumption and the sales price of electricity, for estimating the fair value also the expert evaluations are used. If the situation changes in the future, either additional impairment could be recognised, or previously recognised impairment could be partially or wholly reversed. The recoverable amounts of fixed assets used for network services are impacted by the Competition Board which determines the reasonable rate of return to be earned on these assets. If the income, expenses and investments related to the sale of network services remain within the expected limits, the revenue derived from the sale of goods and services guarantees a reasonable rate of return for these assets. Information about impairment losses incurred in the comparative period is disclosed in Notes 6 and 8.

(c) Recognition and revaluation of provisions

As at 31 December 2016, the Group had set up provisions for environmental protection, termination of mining operations, dismantling of assets, employees and contracts related totalling EUR 41.5 million (31 December 2015: EUR 42.4 million) (Note 24). The amount and/or timing of the settlement of these obligations is uncertain. A number of assumptions and estimates have been used to determine the present value of provisions, including the amount of future expenditure, inflation rates, and the timing of settlement of the expenditure. The actual expenditure may also differ from the provisions recognised as a result of possible changes in legislative norms, technology available in the future to restore environmental damages, and expenditure covered by third parties.

(d) Contingent assets and liabilities

When estimating contingent assets and liabilities, the management considers historical experience, general information about the economic and social environment and the assumptions and conditions of possible events in the future based on the best knowledge of the situation. Further information is disclosed in Note 33.

(e) Effectiveness testing of hedging instruments

The Group has conducted a significant number of future transactions to hedge the risk of the changes in the prices of electricity and shale oil with regard to which hedge accounting is applied, meaning that the gains and losses from changes in the fair value of effective hedging instruments are accounted

through other comprehensive income. The evaluation of the effectiveness of hedging is based on management's estimates for future sales transactions concerning electricity and liquid fuels. When hedging instruments turn out to be ineffective, the total gain/loss from the changes in the fair value should be recognised in the income statement. As at 31 December 2016, the amount of the hedge reserve was EUR -28.5 million (31 December 2015: EUR 16.8 million) (Note 20).

(f) Recognition of liquidated damages

Enefit Energiatootmine AS (fully owned subsidiary of Eesti Energia Group) has reached on November 3, 2016 a settlement with General Electric (GE) (including Alstom Estonia AS, GE Power Sp.z o.o and Alstom Power Systems) regarding the new Auvere power plant. On the basis of previous agreements the plant was due to be handed over to Eesti Energia by GE in November 2015 but acceptance has been delayed because the plant does not fully comply with emissions standards.

As part of the agreement, GE agreed to compensate Eesti Energia unearned revenue of EUR 66.0 million caused by the delay in the works. Compensation covers unearned revenue of Eesti Energia for the period November 2015 until November 2016. GE will pay liquidated damages to Eesti Energia under agreed payment schedule. The deadline of the last installment is July 2017. As liquidated damages are related to unearned revenue for previous periods, it is reflected in 2016 income statement.

5. Segment reporting

For the purposes of monitoring the Group's performance and making management decisions, the Management Board uses product-based reporting. The Group has determined main products and services, i.e. value-creating units that generate external revenues and profit, and has built up a methodology of allocation of revenues and expenses, and assets to the products.

The Group has distinguished three main products and services, which are presented as separately reportable segments, and a number of minor products and services that are presented together as "Other segments":

1. Electrical Energy (production and sale of electricity generated from renewable and non-renewable sources, and electricity trading);
2. Network Services (sale of electricity distribution network services on regulated market);
3. Liquid Fuels (production and sale of liquid fuels);
4. Other segments (including production and sale of heat, sale of oil-shale, construction of electrical network, power engineering equipment and services, development and sale of technology for production and sale of liquid fuels, sale of old metal, ash of oil-shale, other products and services).

Other segments include co-products which individual share of the Group's revenue and EBITDA is immaterial. Non of these co-products meet the quantitative thresholds that would require reporting separate information.

Segment revenues include revenues from external customers only, generated by the sale of respective products or services.

All operating expenses of the Group are allocated to the products and services to which they relate. If a product (eg electricity) is created by several Group entities in a vertically integrated chain, then the related expenses include the production cost of each entity involved in preparation of the product (eg the cost of electricity includes the cost of oil shale used for its production). Group overheads are allocated to products and services proportionally to the services provided. The Management Board assesses the performance of the segments primarily based on EBITDA and it also monitors operating profit. Finance income and expenses, and income tax are not allocated to the segments.

The Group's assets are allocated to the segments based on the same proportion as the related expenses. Liabilities are not allocated to the segments as they are managed centrally by the Group's finance department.

As the segments are based on externally sellable products and services (as opposed to legal entities), there are no transactions between segments to be eliminated.

For Network Services segment, the sales prices need to be approved by the Estonian Competition Authority as stipulated by the Electricity Market Act of Estonia. The Estonian Competition Authority has an established methodology for approving the prices that considers the costs necessary to fulfil the legal obligations and ensures justified profitability on invested capital. Generally, the Estonian Competition Authority considers the annual average carrying amount of non-current assets plus 5% of external sales revenue as invested capital. The rate for

5. Segment reporting, continued

justified profitability is the Company's weighted average cost of capital (WACC). The sales prices for all other segments are not regulated by the law.

Revenue

The revenue from external customers reported to the management board of the parent company is measured in a manner consistent with that in the consolidated income statement.

in million EUR	1 JANUARY – 31 DECEMBER 2016	1 JANUARY – 31 DECEMBER 2015*
	Revenue from external customers	Revenue from external customers
Electrical Energy	348.8	355.6
Network Services	252.7	242.2
Liquid Fuels	67.0	102.8
Other	73.5	76.1
Total	742.1	776.7

* The comparative figures have been adjusted due to a change in cost allocation method as a result of which only the revenues and costs related to production and sale of liquid fuels are recognised in segment Liquid Fuels. Development and sale of technology for production and sale of liquid fuels are now recognised in segment Other. Also allocation of operating expenses of Enefit Solutions was renewed. As a result of which costs between intragroup and external clients made to offering a product are allocated according to proportion of specific product's direct costs between external and intra group projects.

in million EUR	changed	before	difference
Liquid Fuels	102.8	103.8	(1.0)
Other	76.1	75.1	1.0
Total	178.9	178.9	(0.0)

EBITDA

in million EUR	1 JANUARY – 31 DECEMBER 2016	1 JANUARY – 31 DECEMBER 2015*
	EBITDA	EBITDA
Electrical Energy	118.0	102.0
Network Services	112.6	105.5
Liquid Fuels	7.8	48.0
Other	88.9	10.2
Total	327.3	265.8
Depreciation and amortisation (Notes 6 and 8)	(143.4)	(143.1)
Impairment	-	(65.5)
Net financial income (-expense)	(13.8)	(4.3)
Profit (loss) from associates using equity method (Note 9)	1.0	2.5
Profit before tax	171.1	55.4

* The comparative figures have been adjusted due to a change in cost allocation method as a result of which only the revenues and costs related to production and sale of liquid fuels are recognised in segment Liquid Fuels. Development and sale of technology for production and sale of liquid fuels are now recognised in segment Other. Also allocation of operating expenses of Enefit Solutions was renewed. As a result of which costs between intragroup and external clients made to offering a product are allocated according to proportion of specific product's direct costs between external and intra group projects.

in million EUR	changed	before	difference
Electrical Energy	102.0	114.1	(12.0)
Network Services	105.5	105.2	0.3
Liquid Fuels	48.0	41.5	6.6
Other	10.2	5.1	5.1
Total	265.8	265.8	(0.0)

The EBITDA of segment „Other” also contains the revaluation of the loan granted to the associate Enefit Jordan B.V in the amount of EUR 11.0 million in 2015 and in the amount of EUR 0.9 million in 2016 (Notes 13, 29, 32 and 35).

Liquidated damages related to the Auvere power plant in a sum EUR 68.6 million is recognised under segment „Other” because it is an extraordinary revenue and is not associated with ordinary business of other segments.

5. Segment reporting, continued

Other profit and loss disclosures

in million EUR	1 JANUARY – 31 DECEMBER 2016			1 JANUARY – 31 DECEMBER 2015*		
	Depreciation and amortisation	Impairment	Recognition (-) and reversal (+) of provisions	Depreciation and amortisation	Impairment	Recognition (-) and reversal (+) of provisions
Electrical Energy	(61.7)	-	42.8	(65.2)	(35.9)	27.7
Network Services	(51.2)	-	0.9	(48.0)	-	1.2
Liquid Fuels	(18.9)	-	3.5	(19.7)	(0.8)	4.5
Other	(11.6)	-	1.2	(10.3)	(28.8)	(15.1)
Total	(143.4)	-	48.4	(143.1)	(65.5)	18.3

* The comparative figures have been adjusted due to a change in cost allocation method as a result of which only the revenues and costs related to production and sale of liquid fuels are recognised in segment Liquid Fuels. Development and sale of technology for production and sale of liquid fuels are now recognised in segment Other. Also allocation of operating expenses of Enefit Solutions was renewed. As a result of which costs between intragroup and external clients made to offering a product are allocated according to proportion of specific product's direct costs between external and intra group projects.

Depreciation and amortisation

in million EUR	changed	before	difference
Electrical Energy	(65.2)	(64.7)	(0.5)
Network Services	(48.0)	(48.0)	0.1
Liquid Fuels	(19.7)	(20.6)	1.0
Other	(10.3)	(9.7)	(0.6)
Total	(143.1)	(143.1)	(0.0)

Impairment

in million EUR	changed	before	difference
Electrical Energy	(65.2)	(64.7)	(0.5)
Network Services	-	-	-
Liquid Fuels	(0.8)	(26.8)	26.0
Other	(28.8)	(2.8)	(26.0)
Total	(65.5)	(65.5)	0.0

Recognition (-) and reversal of provisions

in million EUR	changed	before	difference
Electrical Energy	(65.2)	(64.7)	(0.5)
Network Services	1.2	1.2	-
Liquid Fuels	4.5	3.0	1.5
Other	(15.1)	(15.0)	(0.1)
Total	18.3	18.3	(0.0)

Interest income and expenses, corporate income tax expense and profit (loss) from associates using equity method are not divided between segments and the information is not provided to the management board of the parent company.

Additional information about the impairment, depreciation and amortisation is disclosed in Notes 6 and 8 and recognition and change of provisions in Note 24.

5. Segment reporting, continued

Assets

The amounts reported to the management board of the parent company with respect to total assets are measured in a manner consistent with that of the consolidated financial statements.

in million EUR	1 JANUARY – 31 DECEMBER 2016			1 JANUARY – 31 DECEMBER 2015*		
	Total assets	Investments in associates (Note 9)	Capital expenditure (Notes 6 and 8)	Total assets	Investments in associates (Note 9)	Capital expenditure (Notes 6 and 8)
Electrical Energy	1,271.2	1.5	24.4	1,239.9	3.7	117.5
Network Services	1,048.1	-	107.4	983.2	-	101.3
Liquid Fuels	305.0	0.4	6.0	305.2	0.6	14.3
Other	462.9	0.1	2.8	429.5	0.2	12.6
Total	3,087.2	2.0	140.7	2,957.8	4.6	245.6

* The comparative figures have been adjusted due to a change in cost allocation method as a result of which only the revenues and costs related to production and sale of liquid fuels are recognised in segment Liquid Fuels. Development and sale of technology for production and sale of liquid fuels are now recognised in segment Other. Also allocation of operating expenses of Enefit Solutions was renewed. As a result of which costs between intragroup and external clients made to offering a product are allocated according to proportion of specific product's direct costs between external and intra group projects.

Total assets

in million EUR	changed	before	difference
Electrical Energy	1,239.9	1,236.1	3.8
Network Services	983.2	968.8	14.4
Liquid Fuels	305.2	360.4	(55.2)
Other	429.5	392.5	37.0
Total	2,957.8	2,957.8	0.0

The Group operates mostly in Estonia, but electricity, liquid fuels and some other goods and services are also sold in other countries.

In „Other” segments there are no segments which results amounted to 10% or more of the Group's results.

5. Segment reporting, continued

Entity-wide information

External revenue by location of clients

in million EUR	1 JANUARY – 31 DECEMBER 2016	1 JANUARY – 31 DECEMBER 2015
Estonia	633.0	645.5
Latvia	54.9	57.7
Lithuania	23.4	23.9
United Kingdom	18.6	(0.1)
Nordic countries	11.3	38.8
Other countries	0.9	10.9
Total external revenue (Note 26)	742.1	776.7

Allocation of non-current assets by location*

in million EUR	1 JANUARY – 31 DECEMBER 2016	1 JANUARY – 31 DECEMBER 2015
Estonia	2,469.6	2,475.2
USA	27.7	26.6
Latvia	8.4	8.8
Other countries	3.8	4.4
Total (Notes 6 and 8)	2,509.5	2,515.0

* other than financial instruments and investments in associates

The Group did not have in the reporting period nor in the comparable period any clients whose revenues from transactions amounted to 10% or more of the Group's revenues.

6. Property, plant and equipment

in million EUR	Land	Buildings	Facilities	Machinery and equipment	Other	Construction in progress and prepayments	Total
Property, plant and equipment as at 31 December 2014							
Cost	42.6	254.3	917.2	1,885.7	5.4	615.8	3,721.0
Accumulated depreciation	-	(96.4)	(361.9)	(849.7)	(4.5)	-	(1,312).5
Net book amount		157.9	555.3	1,036.0	0.9	615.8	2,408.5
Total property, plant and equipment as at 31 December 2014	42.6	157.9	555.3	1,036.0	0.9	615.8	2,408.5
Movements, 1 January - 31 December 2015							
Purchases (Note 5)	0.7	0.1	0.5	19.0	0.2	222.8	243.3
Depreciation charge and write-downs (Notes 4, 5 and 32)	-	(7.4)	(26.6)	(102.0)	(0.5)	(0.6)	(137.1)
Impairment loss (Notes 4, 5 and 32)	-	-	(0.2)	(0.1)	-	(39.6)	(39.9)
Disposals	(0.3)	-	-	(1.0)	-	-	(1.3)
Exchange differences	0.4	-	-	-	-	-	0.4
Transfers	0.2	2.4	39.5	145.2	1.1	(188.4)	-
Total movements, 1 January - 31 December 2015	1.0	(4.9)	13.2	61.1	0.8	(5.8)	65.4
Property, plant and equipment as at 31 December 2015							
Cost	43.6	256.6	953.5	2,024.9	5.9	610.0	3,894.5
Accumulated depreciation	-	(103.6)	(385.0)	(927.8)	(4.2)	-	(1,420).6
Net book amount	43.6	153.0	568.5	1,097.1	1.7	610.0	2,473.9
Total property, plant and equipment as at 31 December 2015 (Notes 4)	43.6	153.0	568.5	1,097.1	1.7	610.0	2,473.9

6. Property, plant and equipment, continued

in million EUR	Land	Buildings	Facilities	Machinery and equipment	Other	Construction in progress and prepayments	Total
Movements, 1 January - 31 December 2016							
Purchases (Note 5)	0.2	0.1	-	8.3	0.3	129.2	138.1
Depreciation charge and write-downs (Notes 4, 5 and 32)	-	(6.0)	(26.6)	(105.2)	(0.5)	(0.2)	(138.5)
Disposals	(1.1)	(1.4)	(0.1)	(0.3)	-	(0.8)	(3.7)
Exchange differences	0.1	-	-	-	-	-	0.1
Transfers	0.2	1.2	39.4	92.5	0.1	(134.0)	(0.6)
Total movements, 1 January - 31 December 2016	(0.6)	(6.1)	12.7	(4.7)	(0.1)	(5.8)	(4.6)
Property, plant and equipment as at 31 December 2016							
Cost	43.0	249.3	989.7	2,061.7	6.2	604.2	3,954.1
Accumulated depreciation	-	(102.4)	(408.5)	(969.3)	(4.6)	-	(1,484.8)
Net book amount	43.0	146.9	581.2	1,092.4	1.6	604.2	2,469.3
Total property, plant and equipment as at 31 December 2016 (Note 4)	43.0	146.9	581.2	1,092.4	1.6	604.2	2,469.3

In 2016, the Group carried out impairment tests on its Auvere power plant and Narva power plants. The two production units are treated as separate cash generating units because the Auvere power plant is considerably more efficient than other generating units and has a different cost base. In the Group's sales strategy, the Auvere power plant could not be replaced with other production units. Therefore, any decisions on the Auvere power plant's maintenance and investment plans are made primarily based on market forecasts and separately from those of the other production units.

The carrying amount of the assets of Auvere power plant at 31 December 2016 was EUR 527.6 million (31 December 2015 EUR 526.3 million). The results of the impairment test did not reflect the need for recognising an impairment loss (in 2015 the assets of Auvere power plant were written down by EUR 39.6 million) or reversing the previously recognised impairment loss, as the value in use of the assets was comparable to carrying amount of the assets. The recoverable amount of the assets was estimated based

on their value in use. The expected future cash flows were discounted using a discount rate of 9.0% (comparable number in 2015: 7.86%). A 1% growth in the discount rate would amount to EUR 82 million effect to the recoverable amount of the assets.

The assets of the Auvere power plants are sensitive to changes in the market prices of electricity, fuel price (oil shale) and CO₂ emission allowances and the implementation of the flexible cooperation mechanism as well as its time, price and volume.

In conducting the impairment test, the near-term market price of electricity was forecast by relying on both a third party consultant's estimates and the projections made based on relevant forward prices. It was assumed that by 2020 price levels in the Estonian and the neighbouring electricity markets would equalise. If this assumption did not apply, its impact on the recoverable amount of the assets would amount to EUR 85 million (in 2015 up to EUR 128 million). It was assumed that from 2021 the prices would increase

6. Property, plant and equipment, continued

at the rate of 2.7% per year (in 2015 2.7% per year) (based on the Ministry of Finance forecast of the consumer price index dated 4 April 2016). Thanks to the Group's sales strategy according to which it strives to sell more electricity during peak hours, in 2016 the average sales price achieved by the Group on the Nord Pool Spot power exchange was 4-15% higher (in 2015 5-17%) than the Nord Pool Spot market price. The Group plans to pursue the same strategy also in subsequent years. In addition, the test took into account the impacts of the following years' hedging transactions.

The share of renewable energy revenues was forecast assuming that from 2017 it would be possible to export renewable energy to other European countries with a view to earning additional revenue (Europe-wide auctions of renewable energy units for countries whose legislation supports this in accordance with Directive 2009/28/EC, henceforth "flexible cooperation mechanism"). Accordingly, up to 50% (up to 1 TWh) of electricity generated at the Auvere power plant could be produced from biomass and the Group could earn additional revenue through flexible cooperation mechanisms. It was assumed that that the rate of additional revenue from electricity generated from biomass would fall within the range of 20-30 €/MWh (in 2015 20-30 €/MWh). If this assumption did not apply, its impact on the value of the assets would amount to EUR 64 million (in 2015 up to EUR 160 million).

The market price of CO₂ emission allowances was forecast for the near term based on relevant forward prices and thereafter assuming that from 2021 the price would increase at the rate of 2.7% per year (based on the Ministry of Finance forecast of the consumer price index dated 4 April 2016), (in 2015 1.4% per year (based on 5 years' average growth rate). As regards the oil shale price, it was assumed that it could be kept stable in the future by improving the efficiency of the production process. If this assumption did not

apply, its impact to the value of the assets would amount to EUR 50 million (in 2015 up to EUR 91 million).

The carrying amount of the assets of the Narva power plants at 31 December 2016 was EUR 222.1 million (31 December 2015: EUR 245.1 million). The results of the impairment test of the assets of Narva power plants did not reflect the need for recognising an impairment loss (in 2015 the impairment test did not reflect the need for recognising an impairment loss). The recoverable amount of the assets was estimated based on their value in use. The expected future cash flows were discounted using a discount rate of 9.0% (comparable number in 2015: 7.86%). A 1% growth in the discount rate would amount to EUR 53 million effect to the recoverable amount of the assets. If the discount rate would be 1% higher, the carrying amount of the assets would not exceed their recoverable amount.

The assets of the Narva power plants are sensitive to changes in the market prices of electricity and CO₂ emission allowances, changes in fuel prices and the implementation of flexible cooperation mechanism. The market assumptions used in the impairment test of Narva power plants are accordance with the assumptions used in the impairment test of Auvere power plant. The greatest impact to the value of the assets of the Narva power plants is the price of electricity. If the assumption of equalisation of price levels in Estonian and the neighbouring electricity markets did not apply, its impact to the value of the assets would amount to EUR 93 million. If this assumption did not apply, the carrying amount of the assets would not exceed their recoverable amount

In 2016, the assets of the Enefit280 oil plant, carrying amount at 31 December 2016: EUR 245.1 million (31 December 2015: EUR 257.0 million) were tested for impairment by estimating

6. Property, plant and equipment, continued

their recoverable amount. The results of the impairment test did not reflect the need for recognising an impairment loss. (in 2015 the impairment test did not reflect the need for recognising an impairment loss). The recoverable amount of the assets was estimated based on their fair value less cost of disposal (in 2015 it was estimated based on their value in use). As a basis of the fair value, the expected future cash flows of the assets were used. This took into account the cash flows from the device that separates petrol from the shale gasoline (in 2015 given investment was not planned). The calculation is based on Level 3 input in the fair value hierarchy. The expected future cash flows were discounted using a discount rate of 9.0% (comparable number in 2015: 10.81%). A 1% growth in the discount rate would amount to EUR 52 million effect to the recoverable amount of the assets. If the discount rate would be 1% higher, the carrying amount of the assets would not exceed their recoverable amount.

The assets of the oil plant are sensitive to changes in the market prices of oil shale and CO₂ emission allowances and the world market price of 1% sulphur content heavy fuel oil.

The market prices of the output of the oil factory were forecast based on the forward prices of the reference product, 1% sulphur content heavy fuel oil, and the hedged positions (in 2015 same assumption was used) and assuming that from 2021 the prices would increase at the rate of 2.7% per year (based on the Ministry of Finance forecast of the consumer price index dated 4 April 2016). In other respects, the impairment test was conducted by applying market price forecasts described above at impairment test of Auvere power plant.

Forecasting the output of the oil factory, it was assumed that in 2019 the plant which will extract gasoline from oil shale gas will start working, this will increase the production volume of liquid fuels by 10%. (in 2015 given investment was not planned). If this assumption did not apply, its impact on the recoverable amount of the assets would amount to EUR 67 million. If this assumption did not apply, the carrying amount of the assets would not exceed their recoverable amount.

As regards the oil shale price, it was assumed that it could be kept stable in the future by improving the efficiency of the production process. If the oil shale price increases on a long-term basis at the growth rate of the consumer price index, its impact on the recoverable amount of the assets will amount to EUR 28 million (in 2015 up to EUR 64 million). If this assumption did not apply, the carrying amount of the assets would not exceed their recoverable amount (in 2015 the carrying amount of the assets would have exceeded their recoverable amount by up to EUR 62 million).

In 2016, the assets of the Eesti Energia wind farms (Aulepa, Paldiski, Narva) were tested for impairment by estimating their recoverable amount. The results of the impairment test did not reflect the need for recognising an impairment loss (in 2015 the impairment test did not reflect the need for recognising an impairment loss). The recoverable amount of the assets was estimated based on their value in use. The expected future cash flows were discounted using a discount rate of 6.0% (comparable number in 2015: 6.32%). The impairment test was conducted by applying the above electricity market price forecasts. Above all, the assets of wind farms are sensitive to changes in the electricity market price. If the assumption of

6. Property, plant and equipment, continued

the equalisation of price levels in the Estonian and the neighbouring electricity markets in 2020 did not apply, the total impairment loss of the Aulepa and Narva wind farms would amount to EUR 1.1 million and EUR 1.3 million respectively (in 2015 the impairment loss of Aulepa wind farm would have amounted to EUR 1.1 million).

In 2016 the assets of Enefit American Oil were tested for impairment. The results of the impairment test did not reflect the need for recognising an impairment loss (in 2015 an impairment loss of EUR 0.3 million for property, plant and equipment and EUR 25.6 million for intangible assets was recognised). The recoverable amount of the assets was estimated based on same methodology as in 2015 where the assets were revalued to the value of land. For this, the average price of ten similar plots of land, which were for sale in Utah state in the vicinity of Verna area (20 miles) was found. The additional information about the impairment of assets of Enefit American Oil is disclosed in Note 8.

During the year, the Group has capitalised borrowing costs amounting to EUR 21.7 million (2015: EUR 24.7 million) on qualifying assets. The capitalisation rate of 3.8% (2015: 4.0%) was used to determine the amount of borrowing costs eligible for capitalisation (Note 30).

Buildings and facilities leased out under operating lease terms

in million EUR	31 DECEMBER	
	2016	2015
Cost	7.1	6.6
Accumulated depreciation at the beginning of the financial year	(3.8)	(3.5)
Depreciation charge	(0.2)	(0.2)
Net book amount	3.1	2.9

Leased assets are partly used in the Group's own operations and partly for earning rental income. Cost and depreciation have been calculated on the basis of the part of the asset leased out. Income from lease assets is disclosed in Note 7.

7. Operating lease

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Rental and maintenance income		
Buildings	1.3	1.5
<i>of which contingent rent</i>	<i>0.5</i>	<i>0.7</i>
Total rental and maintenance income (Note 25)	1.3	1.5
Rental expense		
Buildings	2.3	2.5
Transport vehicles	0.6	0.5
Other machinery and equipment	2.2	2.5
Total rental expense (Note 29)	5.1	5.5

Future minimum lease receivables under non-cancellable operating lease contracts by due dates

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Rental income		
< 1 year	0.5	0.7
1 - 5 years	2.0	2.6
> 5 years	5.6	8.0
Total rental income	8.1	11.3

The oil terminal has been leased out under non-cancellable lease agreement.

Operating lease agreements, where the Group is lessee, are mostly cancellable with short-term notice.

8. Intangible assets

in million EUR	Goodwill	Computer software	Right of use of land	Exploration and evaluation assets for mineral resources	Contractual rights	Development costs	Total
Intangible assets as at 31 December 2014							
Cost	3.5	32.8	2.5	10.6	32.9	-	82.3
Accumulated amortisation	-	(20.3)	(0.6)	-	-	-	(20.9)
Net book amount	3.5	12.5	1.9	10.6	32.9	-	61.4
Intangible assets not yet available for use	-	4.2	-	-	-	-	4.2
Total intangible assets as at 31 December 2014	3.5	16.7	1.9	10.6	32.9	-	65.6
Movements, 1 January - 31 December 2015							
Purchases (Note 5)	-	1.3	0.1	0.5	-	0.4	2.3
Amortisation charge and write-downs (Notes 5 and 32)	-	(5.9)	(0.1)	-	-	-	(6.0)
Impairment loss (Note 5 and 32)	-	-	-	(10.6)	(15.0)	-	(25.6)
Exchange differences	-	-	-	1.1	3.7	-	4.8
Total movements, 1 January - 31 December 2015	-	(4.6)	-	(9.0)	(11.3)	0.4	(24.5)
Intangible assets as at 31 December 2015							
Cost	3.5	36.1	2.6	1.6	21.6	0.4	65.8
Accumulated amortisation	-	(24.5)	(0.7)	-	-	-	(25.2)
Net book amount	3.5	11.6	1.9	1.6	21.6	0.4	40.6
Intangible assets not yet available for use	-	0.5	-	-	-	-	0.5
Total intangible assets as at 31 December 2015	3.5	12.1	1.9	1.6	21.6	0.4	41.1
Movements, 1 January - 31 December 2016							
Purchases (Note 5)	-	1.9	-	0.3	-	0.4	2.6
Amortisation charge and write-downs (Notes 5 and 32)	-	(4.7)	(0.1)	-	(0.1)	-	(4.9)
Exchange differences	-	-	-	-	0.8	-	0.8
Transfers	-	0.5	-	-	0.1	-	0.6
Total movements, 1 January - 31 December 2016	-	(2.3)	(0.1)	0.3	0.8	0.4	(0.9)
Intangible assets as at 31 December 2016							
Cost	3.5	37.8	2.6	1.9	22.5	0.8	69.1
Accumulated amortisation	-	(29.1)	(0.8)	-	(0.1)	-	(30.0)
Net book amount	3.5	8.7	1.8	1.9	22.4	0.8	39.1
Intangible assets not yet available for use	-	1.1	-	-	-	-	1.1
Total intangible assets as at 31 December 2016	3.5	9.8	1.8	1.9	22.4	0.8	40.2

8. Intangible assets, continued

Goodwill

Allocation of goodwill by cash-generating units

in million EUR	Mining	Valka co-generation plant	Paide co-generation plant
Carrying amount at 31 December 2016	2.5	0.6	0.4
Carrying amount at 31 December 2015	2.5	0.6	0.4

The recoverable amount of assets is determined on the basis of their value in use and using the cash flow forecast prepared up to the next 20 years. The selection of the periods is based on an investment horizon regularly used in the electricity business. The cash flow forecasts are based on historical data and the forecasts of the Estonian energy balance. The weighted average cost of capital (WACC) is used as the discount rate, which is being determined on the basis of area of operations of the Company and its risk level. No impairment was identified during these tests.

Key assumptions used in determining value in use

Discount rate	31 DECEMBER	
	2016	2015
Mining	9.0%	10.0%
Valka co-generation plant	6.0%	8.0%
Paide co-generation plant	6.0%	7.0%

Exploration and evaluation assets of mineral resources

The costs related to the exploration of an oil shale mine located in the state of Utah, USA are recognised as exploration and evaluation assets of mineral resources.

Contractual rights

The costs related to the mining rights acquired in the state of Utah are recognised as contractual rights, the estimated useful life of which is 20 years.

Determining the recoverable amount of the assets of Enefit American Oil on the basis of fair value less cost of disposal

In 2016 the assets of Enefit American Oil (EUR 30.5 million as at 31 December 2016, including exploration and evaluation assets of mineral resources EUR 3.8 million) were tested for impairment. The results of the impairment test did not reflect the need for recognising an impairment loss or reversing the previously recognised impairment loss.

In 2015 the assets of Enefit American Oil (EUR 54.6 million as at 31 December 2015, including exploration and evaluation assets of mineral resources EUR 14.2 million) were tested for impairment, according to which an impairment loss of EUR 0.3 million for property, plant and equipment (Note 6) and EUR 25.6 million for intangible assets was recognised. The recoverable amount was determined based on fair value less cost of disposal. The impairment loss was allocated to the individual assets on a pro rata basis (except for land), based on the carrying amount of each asset. As a basis of revaluation the value analysis of Enefit American Oil performed by Hard Rock Consulting LLC in 2015 was used that is a Level 3 input in the fair value hierarchy. The impairment loss resulted mostly from the low market prices of oil and fuel oil prices that is the reason for suspending the active development of the project.

9. Investments in associates

Nature of investments in associates 2016 and 2015:

Name of the company	Place of business	Ownership (%)	Nature of the relationship	Measurement method
Orica Eesti OÜ*	Estonia the Netherlands	35.0	Note 1	Equity
Enefit Jordan B.V. Group	Jordan Estonia	65.0	Note 2	Equity
Attarat Mining Co BV	the Netherlands	50.0	Note 3	Equity
Attarat Power Holding Co BV Group	the Netherlands	65.0	Note 3	Equity
Attarat Operation & Maintenance Co BV	the Netherlands	25.0	Note 3	Equity

* The financial year of Orica Eesti OÜ is from 1 October to 30 September

Note 1: Orica Eesti OÜ manufactures and sales explosives and is a strategic partner for Eesti Energia Kaevandused AS

Note 2: Enefit Jordan B.V. Group is engaged with the oil shale development project in Jordan. Enefit Jordan B.V. Group is recognised as associate as according to the Shareholders' Agreement, the Group does not have the right to make any relevant decisions regarding Enefit Jordan B.V. Group without the consent of one or, in cases, both of other shareholders who hold the remainder of the 35% shares. Based on voting quorum requirements for different decisions joint control is not established.

Note 3: As at 31 December 2016 Attarat Mining Co BV, Attarat Power Holding Co BV and Attarat Operation & Maintenance Co BV had not started their business activities.

According to the opinion of the Management Board none of the associates is material to the Group.

Reconciliation of summarised financial information of associates

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Summarised net assets of associates at the beginning of the period	(32.4)	(20.1)
Profit/loss for the period	23.4	(8.8)
Other comprehensive income	(0.4)	(3.5)
Dividends declared	(10.2)	-
Summarised net assets of associates at the end of the period	(19.6)	(32.4)
Interest in associates	(14.5)	(25.0)
Notional goodwill	12.3	12.3
Group's share in negative net assets not recognised by the Group using the equity method	4.2	17.3
Carrying amount at the end of the period (Note 5)	2.0	4.6
Group's share of associates profit/loss for the period (Notes 5 and 32)	1.1	2.5

10. Principal subsidiaries

The Group had the following subsidiaries at 31 December 2016

Name	Country of incorporation	Nature of business	Proportion of ordinary shares held by the Group (%)		Proportion of ordinary shares held by noncontrolling interests (%)	
			31 DECEMBER		31 DECEMBER	
			2016	2015	2016	2015
Eesti Energia Õlitööstus AS	Estonia	Producing liquid fuels and retort gas from oil shale	100.0	100.0	-	-
Elektrilevi OÜ	Estonia	Network operator	100.0	100.0	-	-
Enefit Kaevandused AS (until 30.6.2016 Eesti Energia Kaevandused AS)	Estonia	Oil shale mining	100.0	100.0	-	-
Enefit Energijatootmine AS (until 1.7.2016 Eesti Energia Narva Elektriijaamad AS)	Estonia	Production of electrical energy	100.0	100.0	-	-
AS Narva Soojusvõrk	Estonia	Distribution and sale of heat	100.0	100.0	-	-
Enefit Solutions AS (until 30.6.2016 Eesti Energia Tehnoloogiatööstus AS)	Estonia	Manufacture and supply of metal structures, energy industry machinery and other industrial equipment	100.0	100.0	-	-
Eesti Energia Hoolduskeskus AS	Estonia	Maintenance and repair of power engineering equipment	-	100.0	-	-
Eesti Energia Testimiskeskus OÜ	Estonia	Testing and providing expertise for metals and welded joints; certifying welders and welding procedures (WPQR)	-	100.0	-	-
Enefit Taastuenergia OÜ (until 30.6.2016 Eesti Energia Aulepa Tuuleelektriijaam OÜ)	Estonia	Establishment and operation of wind parks	100.0	100.0	-	-
Eesti Energia Tabasalu Koostootmisjaam OÜ	Estonia	Establishment of heat-and-power cogeneration station	-	55.0	-	45.0
Pogi OÜ	Estonia	Production and sale of heat and electrical energy	83.3	66.5	17.7	33.5
Attarat Holding OÜ	Estonia	Holding	100.0	100.0	-	-
Enefit Outotec Technology OÜ	Estonia and Germany	Developing and licensing the new generation of Enefit shale oil production technology	60.0	60.0	40.0	40.0
Enefit SIA	Latvia	Selling electricity to end consumers	100.0	100.0	-	-
Enefit Power & Heat Valka SIA	Latvia	Production and sale of heat and electrical energy	100.0	90.0	-	10.0
Enefit UAB	Lithuania	Selling electricity to end consumers	100.0	100.0	-	-
Enefit U.S., LLC	USA	Holding	100.0	100.0	-	-
Enefit American Oil Co.	USA	Developing of liquid fuels production	100.0	100.0	-	-
Enefit Sp. z o.o.	Poland	Selling electricity to end consumers	100.0	-	-	-

10. Principal subsidiaries, continued

On 19 August 2016 the transaction of the sale of the 55% shareholding in Eesti Energia Tabasalu Koostootmisjaam OÜ

On 18 November 2016, the Group acquired an additional 16,7% of the share capital of OÜ Pogi, after which 83,3% of OÜ Pogi shares was owned by parent company. The purchase price of shares was EUR 0.8 million.

Eesti Energia merged its renewable energy operations into a single subsidiary called Enefit Taastuenergia in autumn 2016. During the merging of the Group's renewable energy units Eesti Energia AS sold operating activities of Keila-Joa Hydro-electricity power plant, Virtsu, Narva and Paldiski Wind Farms and Iru Power Plant to Enefit Taastuenergia OÜ. Also shares of Pogi OÜ were sold to Enefit Taastuenergia OÜ. The transactions were made at the market price. Enefit Taastuenergia OÜ operates all of the Group's renewable energy production units, and is one of the biggest renewable energy producers in the Baltic States.

On 30 November 2016, the Group acquired an additional 10% of the share capital of SIA Enefit Power & Heat Valka, after which SIA Enefit Power & Heat Valka was fully owned by Eesti Energia AS. The purchase price of shares was EUR 0.1 million. In December parent company sold its shares to Enefit Taastuenergia OÜ. The transaction was made at the market price.

In 2016 Eesti Energia Hoolduskeskus AS and Eesti Energia Testimiskeskus AS were merged with Enefit Solutions AS.

All subsidiary undertakings are included in the consolidation. The proportion of the voting rights in the subsidiary undertakings held directly by the parent company do not differ from

the proportion of ordinary shares held. The parent company does not have any shareholdings in the preference shares of subsidiary undertakings included in the Group. None of the carrying amounts of the non-controlling interests as at 31 December 2016 and 31 December 2015 was material.

Significant restrictions

Until the investments of the network operator (Elektrilevi OÜ) do not exceed the limits of the approved financing plan, according to the Electricity Market Act of Estonia the parent company may not intervene in the everyday economic activities of the network operator or in the decisions concerning the construction or upgrades of the network.

11. Inventories

in million EUR	31 DECEMBER	
	2016	2015
Raw materials and materials at warehouses	33.7	25.9
Work-in-progress		
Stored oil shale	26.8	39.8
Stripping works in quarries	1.8	2.3
Other work-in-progress	0.1	1.6
Total work-in-progress	28.7	43.7
Finished goods		
Shale oil	2.4	1.9
Other finished goods	0.4	0.3
Total finished goods	2.8	2.2
Prepayments to suppliers		0.1
Total inventories (Notes 4 and 32)	65.2	71.9

In the reporting period, the Group wrote down damaged and slow-moving inventories of raw materials and materialstotaling EUR 0.2 million (2015: EUR 0.6 million).

12. Division of financial instruments by category

in million EUR	Loans and receivables	Financial assets at fair value through profit or loss	Derivatives for which hedge accounting is applied	Total
As at 31 December 2016				
Financial asset items in the statement of financial position				
Trade and other receivables excluding prepayments (Notes 3.1 and 13)	232.8	-	-	232.8
Derivative financial instruments (Notes 3.1, 3.3, 14 and 15)	-	0.8	0.6	1.4
Cash and cash equivalents (Notes 3.1, 3.2, 15 and 17)	223.3	-	-	223.3
Total financial asset items in the statement of financial position	456.1	0.8	0.6	457.5
As at 31 December 2015				
Financial asset items in the statement of financial position				
Trade and other receivables excluding prepayments (Notes 3.1 and 13)	131.1	-	-	131.1
Derivative financial instruments (Notes 3.1, 3.3, 14 and 15)	-	1.8	38.5	40.3
Cash and cash equivalents (Notes 3.1, 3.2, 15 and 17)	159.8	-	-	159.8
Total financial asset items in the statement of financial position	290.9	1.8	38.5	331.2

in million EUR	Liabilities at fair value through profit or loss	Derivatives for which hedge accounting is applied	Other financial liabilities	Total
As at 31 December 2016				
Financial liability items in the statement of financial position				
Borrowings (Notes 3.1, 3.2 and 21)	-	-	939.9	939.9
Trade and other payables (Notes 3.1 and 22)	-	-	97.5	97.5
Derivative financial instruments (Notes 3.1, 3.3 and 14)	2.0	20.6	-	22.6
Total financial liability items in the statement of financial position	2.0	20.6	1,037.4	1,060.0
As at 31 December 2015				
Financial liability items in the statement of financial position				
Borrowings (Notes 3.1, 3.2 and 21)	-	-	951.8	951.8
Trade and other payables (Notes 3.1 and 22)	-	-	105.5	105.5
Derivative financial instruments (Notes 3.1, 3.3 and 14)	11.8	-	-	11.8
Total financial liability items in the statement of financial position	11.8	-	1,057.3	1,069.1

13. Trade and other receivables

in million EUR	31 DECEMBER	
	2016	2015
Short-term trade and other receivables		
Trade receivables		
Accounts receivable (note 32)	160.6	90.6
Allowance for doubtful receivables (Note 4)	(2.1)	(2.1)
Total trade receivables	158.5	88.5
Accrued income		
Amounts due from customers under the stage of completion method	0.8	0.8
Other accrued income	0.3	0.6
Total accrued income	1.1	1.4
Prepayments	5.8	1.6
Receivables from associates (Note 35)	1.6	1.7
Cash restricted from being used	12.4	5.5
Other receivables	20.0	1.1
Total short-term trade and other receivables	199.4	99.8
Long-term receivables		
Loan receivables from associates (Note 35)	50.1	42.5
Allowance for doubtful loan receivables (Notes 5, 29, 32 and 35)	(12.2)	(11.0)
Other long-term receivables	1.3	1.4
Total long-term receivables	39.2	32.9
Total trade and other receivables (Notes 3.1 and 12)	238.6	132.7

The receivables from associates include the termless loan granted to the associate Enefit Jordan B.V. with the interest rate 15% (2015: 15%). In 2015 the loan granted to associate Enefit Jordan B.V was revalued by EUR 11.0 million and in 2016 by EUR 0.9 million (Notes 5, 29, 32 and 35). In the revaluation of the loan the value of the assets and the future plans were taken into consideration as the participation in the project is going to be decreased.

Under cash restricted from being used are recognised financial resources that are held on SEB Futures account as a guarantee for the transactions. The fair values of receivables and prepayments do not significantly differ from their carrying amounts. Collection of receivables and prepayments for services and goods is not covered by securities. Most of the Group's receivables and prepayments are in euros. The amount of receivables denominated in US dollars is disclosed in Note 3.1. Information about the credit quality of the receivables is disclosed in Note 15.

Under trade receivables is recognised receivable amount for liquidated damages related to the Auvere power plant in a sum EUR 57.8 million.

Under other receivables are recognised trading guarantees for Nasdaq due to electricity hedging transactions in a sum EUR 19.5 million.

13. Trade and other receivables, continued

Analysis of accounts receivable

in million EUR	31 DECEMBER	
	2016	2015
Accounts receivable not yet due (Notes 4 and 15)	151.1	80.8
Accounts receivable due but not classified as doubtful		
1-30 days past due	6.4	6.6
31-60 days past due	0.7	0.6
61-90 days past due	0.1	0.3
Total accounts receivable due but not classified as doubtful	7.2	7.5
Accounts receivable written down		
3-6 months past due	0.2	0.4
more than 6 months past due	2.1	1.9
Total accounts receivable that are more than 3 months past due	2.3	2.3
Total accounts receivable	160.6	90.6

Under the accounting policies of the Group, receivables 90 days past due are usually written down in full. The total amount of allowance for receivables 90 days past due is adjusted using prior experience of how many of the receivables classified as doubtful are collected in a later period and how many of the receivables not more than 90 days past due are not collected in a later period. Also other individual and extraordinary impacts like the global economic recession are taken into account during evaluation.

Changes in allowance for doubtful trade receivables

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Allowance for doubtful trade receivables at the beginning of the period	(2.1)	(2.4)
Classified as doubtful and collections during the accounting period	(0.6)	(0.3)
Classified as irrecoverable	0.6	0.6
Allowance for doubtful trade receivables at the end of the period (Note 4)	(2.1)	(2.1)

The other receivables do not contain any impaired assets.

Revenue under the stage of completion method

in million EUR	31 DECEMBER	
	2016	2015
Unfinished projects at the end of the period		
Total of revenue of unfinished projects since the beginning of the projects	15.6	8.5
Total of progress billing submitted since the beginning of the projects	(15.8)	(8.6)
Amounts due from customers under the stage of completion method	0.8	0.7
Amounts due to customers under the stage of completion method	(1.0)	(0.8)
Total expenses on unfinished projects	(15.3)	(7.8)
Profit/loss calculated on unfinished projects	0.3	0.7
Total revenue from construction projects in the financial year	8.2	6.3
Total expenses on construction projects in the financial year	(10.7)	(7.5)
Total profit calculated on construction projects	(2.5)	(1.2)

Long-term construction projects are mostly power equipment manufacturing and network equipment design and construction.

14. Derivative financial instruments

in million EUR	31 DECEMBER 2016		31 DECEMBER 2015	
	Assets	Liabilities	Assets	Liabilities
Future contracts for buying and selling electricity as cash flow hedges	(0.1)	1.3	7.5	-
Forward and future contracts for buying and selling electricity as trading derivatives	0.6	1.4	1.3	11.0
Future contracts for buying and selling greenhouse gas emissions allowances as trading derivatives	-	0.6	0.1	0.8
Swap, forward and option contracts for selling fuel oil as cash flow hedges	0.7	19.3	31.0	-
Swap and option contracts for selling fuel oil as trading derivatives	0.2	-	0.4	-
Total derivative financial instruments (Notes 3.1, 3.3, 12, 15 and 20)	1.4	22.6	40.3	11.8
including non-current portion:				
Swap, forward and option contracts for selling fuel oil as cash flow hedges	-	6.1	-	-
Total non-current portion	-	6.1	-	-
Total current portion	1.4	16.5	40.3	11.8

Forward contracts for buying and selling electricity

The goal of the forward contracts for buying and selling electricity is to manage the risk of changes in the price of electricity or earn income on changes in the price of electricity. All forward contracts have been entered into for the sale or purchase of a fixed volume of electricity at each trading hour and their price is denominated in euros. The transactions, the goal of which is to hedge the risk in the price of electricity, are designated as cash flow hedging instruments, where the underlying instrument being hedged is the estimated electricity sales transactions of high probability on the power exchange Nord Pool. The effective portion of the change in the fair value of transactions concluded for hedging purposes is recognised through other

comprehensive income and is recognised either as revenue or reduction of revenue at the time the sales transactions of electricity occur or other operating income/expenses when it is evident that sales transactions are unlikely to occur in a given period.

The forward contracts of buying and selling electricity the goal of which is to hedge the risk in the price of electricity will realise in 2017 (31 December 2015: in 2016). As at 31 December 2016 1 738 514 MWh had been hedged for the year 2017 (31 December 2015: 1 343 952 MWh had been hedged for the year 2016). The basis for determining the fair value of the instruments is the quotes by Nasdaq OMX.

14. Derivative financial instruments, continued

Future contracts for buying and selling greenhouse gas emissions allowances and contracts with funds

The future contracts (except for own use contracts) for buying and selling greenhouse gas emission allowances and the contracts with funds for buying CERs (certified emission reductions) are classified as trading derivatives. The fair value changes of these transactions are recognised as gains or losses in the income statement. The basis for determining the fair value of transactions is the quotes of ICE EUA and cash flow forecasts. The prices are denominated in euros.

Swap and option contracts for selling fuel oil

The goal of the swap and option contracts for buying and selling fuel oil classified as hedges is to hedge the risk of price changes for shale oil. The transactions have been concluded for the sale of a specified volume of shale oil in future periods and they are designated as cash flow hedging instruments, where the underlying instruments to be hedged are highly probable shale oil sales transactions. The basis for determining the fair value of transactions is the quotes by ICE, Platt's European Marcetscan and Nymex. Hedging instruments, which are combined from various components of derivative instruments, are recognised at fair value with changes through profit or loss until the acquisition of all components.

Liquidity swap transactions, that have been concluded in order to transfer the value changes of previously concluded transactions to partners, where the trading doesn't require daily coverage of market values, are classified as trading derivatives. Also the call option contracts have been classified as trading derivatives.

The prices are denominated in euros and US dollars. The swap and option contracts for selling fuel oil which aim to hedge the risk of price changes of shale oil will realise in 2017-2019 (31 December 2015: in 2016). As at 31 December 2016 286 843 tonnes had been hedged for the year 2017, 179 561 tonnes for the year 2018 and 23 856 tonnes for the year 2019. (31 December 2015: 131 316 tonnes for the year 2016).

15. Credit quality of financial assets

The basis for estimating the credit quality of financial assets not due yet and not written down is the credit ratings assigned by rating agencies or, in their absence, the earlier credit behaviour of clients and other parties to the contract.

in million EUR	31 DECEMBER	
	2016	2015
Trade receivables		
Receivables from new clients (client relationship shorter than 6 months)	0.5	0.7
Receivables from existing clients (client relationship longer than 6 months), who in the last 6 months have not exceeded the due date	113.0	50.9
Receivables from existing clients (client relationship longer than 6 months), who in the last 6 months have exceeded the due date	37.6	29.2
Total trade receivables (Note 13)	151.1	80.8

Under receivables from existing clients (client relationship longer than 6 months), who in the last 6 months have not exceeded the due date is recognised the receivable amount of EUR 57.8 million of the liquidated damages from GE. The amount will be payable to Eesti Energia under an agreed payment schedule by July 2017. (Note 4)

15. Credit quality of financial assets, continued

in million EUR	31 DECEMBER	
	2016	2015
Bank accounts and short-term deposits in banks		
At banks with Moody's credit rating of Aa3	172.6	134.0
At banks with Moody's credit rating of Aa2	50.0	-
At banks with Moody's credit rating of A1	0.2	-
At banks with Moody's credit rating of A2	0.3	25.7
At banks with Moody's credit rating of A3	0.2	0.1
Total bank accounts and short-term deposits in banks (Notes 3.1, 3.2, 12 and 17)	223.3	159.8
Other receivables and accrued income		
Other receivables with Moody's credit rating of Aa3	12.4	5.5
Receivables without credit rating from an independent party	61.9	37.1
Total other receivables (Note 13)	74.3	42.6
Derivative financial instruments		
Derivatives with positive value with Moody's credit rating of Aa3	0.1	3.1
Derivatives with positive value with Moody's credit rating of A1	0.6	17.4
Derivatives with positive value with Moody's credit rating of A2	0.2	10.9
Derivatives with positive value through Nasdaq OMX clearing house	0.3	7.5
Derivatives with positive value without credit rating from an independent party	0.2	1.4
Derivatives with positive value (Notes 3.1, 3.3, 12 and 14)	1.4	40.3

Nasdaq OMX constitutes a clearing house that is subject to official financial regulation, in relation to whom various risk management measures are applied, the most important of which is the requirement for the clearing house members to

issue warrants for their liabilities. Also the requirements for minimum equity amounts are applied on clearing houses and based on that the credit risk is considered

According to the estimate of the management the other receivables and accrued income without a credit rating from an independent party do not involve material credit risk, as there is no evidence of circumstances that would indicate impairment loss.

16. Greenhouse gas allowances

The value of greenhouse gas allowances acquired is recognised as intangible current assets. In 2016 6 267 000 tonnes (2015: 10 577 000 tonnes) of greenhouse gas allowances were acquired and 10 000 tonnes (2015: 17 015 000 tonnes) were sold. In 2016 9 867 612 tonnes (2015: 12 605 938 tonnes) of greenhouse gas emission allowances were returned to state.

in million EUR	1 JANUARY - 31 DECEMBER	
	2016	2015
Greenhouse gas allowances at the beginning of the period	33.5	144.8
Acquired	42.0	55.3
Sold	-	(114.0)
Returned to state for the greenhouse gas emissions (Note 24)	(28.2)	(52.6)
Greenhouse gas allowances at the end of the period	47.3	33.5

17. Cash and cash equivalents

in million EUR	31 DECEMBER	
	2016	2015
Bank accounts	113.3	66.8
Short-term deposits	110.0	93.0
Total cash and cash equivalents (Notes 3.1, 3.2, 12 and 15)	223.3	159.8

Cash and cash equivalents by currencies

in million EUR	31 DECEMBER	
	2016	2015
Euro	222.9	159.7
US dollar	0.2	0.1
Polish zloty	0.2	-
Total cash and cash equivalents (Notes 3.1, 3.2, 12 and 15)	223.3	159.8

In the financial year, the effective interest rates of short term deposits were between 0.1 and 0.5% (2015: 0.1-0.5%).

18. Share capital, statutory reserve capital and retained earnings

As at 31 December 2016, Eesti Energia AS had 621 645 750 registered shares (31 December 2015: 621 645 750 registered shares). The nominal value of each share is 1 euro. The sole shareholder is the Republic of Estonia. The administrator of the shares and the exerciser of the rights of shareholders is the Estonian Ministry of Finance, represented by the Minister of Finance at the General Meeting of Shareholders. According to the articles of association of Eesti Energia AS, the minimum share capital is EUR 250,0 million and the maximum share capital is EUR 1000,0 million.

As at 31 December 2016, the Group's statutory reserve capital totalled EUR 62.1 million (31 December 2015: EUR 62.1 million).

As at 31 December 2016, the Group's distributable equity was EUR 770.2 million (31 December 2015: EUR 599.5 million). Corporate income tax is payable upon the distribution of dividends to shareholders. Income tax on dividends is 20/80 of the amount payable as net dividends.

If all retained earnings were distributed as dividends, the corporate income tax would amount to EUR 154.0 million (31 December 2015: EUR 119.9 million). It is possible to pay out EUR 616.2 million (31 December 2015: EUR 479.6 million) as net dividends.

18. Share capital, statutory reserve capital and retained earnings, continued

The Management Board proposes to pay EUR 47.0 million as dividends after the approval of the 2016 Annual Report by the General Meeting of Shareholders. The corresponding income tax totals EUR 11.8 million.

The following table presents the basis for calculating the distributable shareholders' equity, potential dividends and the accompanying corporate income tax.

in million EUR	31 DECEMBER	
	2016	2015
Retained earnings (Note 36)	770.2	599.5
Distributable shareholder's equity	770.2	599.5
Corporate income tax on dividends if distributed	154.0	119.9
Net dividends available for distribution	616.2	479.6

19. Dividends per share

In 2016, Eesti Energia AS did not pay dividends to shareholder (2015: EUR 61,9 million, dividends per share EUR 0,10) (Note 36).

The Management Board proposed to the Annual Meeting to pay dividends of EUR 0.08 per share for the financial year ended 31 December 2016, totalling EUR 47.0 million. These financial statements do not reflect this amount as a liability as the dividend had not been approved as at 31 December 2016.

20. Other reserves

in million EUR	1 JANUARY - 31 DECEMBER	
	2016	2015
Other reserves at the beginning of the period	27.8	52.7
Change in fair value of cash flow hedges	(36.7)	41.9
Recognised as an increase of revenue	(8.6)	(72.1)
<i>of which recognised as an increase of revenue of electricity</i>	<i>(4.8)</i>	<i>(34.3)</i>
<i>of which recognised as an increase of revenue of shale oil</i>	<i>(3.8)</i>	<i>(37.8)</i>
Currency translation differences attributable to foreign subsidiaries	0.9	5.3
Other reserves at the end of the period	(16.6)	27.8

21. Borrowings

Borrowings at amortised cost

in million EUR	31 DECEMBER	
	2016	2015
Short-term borrowings		
Current portion of long-term bank loans	19.3	19.3
Total short-term borrowings	19.3	19.3
Long-term borrowings		
Bonds issued	699.2	691.9
Bank loans	221.4	240.6
Total long-term borrowings	920.6	932.5
Total borrowings (Notes 3.1, 3.2 and 12)	939.9	951.8

21. Borrowings, continued

The fair value of bonds and bank loans:

in million EUR	31 DECEMBER	
	2016	2015
Nominal value of bonds (Note 3.1)	758.3	758.3
Market value of bonds on the basis of quoted sales price (Note 3.3)	816.0	789.7
Nominal value of bank loans with fixed interest rate (Note 3.1)	192.5	210.4
Fair value of bank loans with fixed interest rate (Note 3.3)	197.1	223.1
Nominal value of bank loans with floating interest rate (Note 3.1)	48.5	49.8
Fair value of bank loans with floating interest rate (Note 3.3)	48.5	49.8

The bonds are denominated in euros and listed on the London Stock Exchange. The fair value of the bonds is based on the input that is within level 1 of the fair value hierarchy.

Management estimates that the fair value of the loans with a floating interest rate at the end of reporting and comparative period does not differ from their carrying amounts as the risk margins have not changed. The fair values of bank loans with fixed interest rate are based on cash flows discounted using discount rates between 0.557%-1.010% (2015: 0.839%-1.203%) that are within level 3 of the fair value hierarchy.

In September 2015 the Group carried out a refinancing of bonds due in 2018 and 2020 in the course of which the existing bonds in the nominal value of EUR 441.7 million were exchanged for the new bonds with the nominal value of EUR

500 million and a longer maturity and an amount of EUR 6.0 million was paid out in cash to the bondholders. The maturity of the new bonds is 8 years (redemption in September 2023) and a coupon rate 2.384%. After the transaction, the nominal amounts of the remaining bond commitments due in 2018 and 2020 are EUR 152.0 million and EUR 106.3 million respectively.

The management estimates that the refinancing of bonds was an exchange between an existing borrower and lender of debt instruments, for which the terms were not substantially changed (discounted cash flow value of new bonds varies from discounted cash flow value of previously issued bonds less than 10%), therefore the transaction is reflected as a modification of existing financial liability. For that reason the difference (the premium) is not shown as a loss in income statement, but will be amortized during the remaining maturity of the modified liability.

Long-term bank loans at nominal value by due date

in million EUR	31 DECEMBER	
	2016	2015
< 1 year	19.3	19.3
1 - 5 years	148.7	120.1
> 5 years	73.0	120.8
Total	241.0	260.2

All loans are denominated in euros. As at 31 December 2016 the interest rates of loans were between 0.3 and 3.1% (31 December 2015: 0.5-3.4%).

21. Borrowings, continued

As at 31 December 2016, the weighted average nominal interest rate on loans was 1.4% (31 December 2015: 2.5%). The loan agreements concluded by Eesti Energia AS contain certain financial ratios that the Group needs to comply with. The Group has complied with all attached conditions.

As at 31 December 2016 the Group had undrawn loan facilities of EUR 220.0 million (31 December 2015: EUR 220.0 million), the figure includes bilateral liquidity loan agreements with floating interest rate of EUR 150.0 million in aggregate, with SEB and OP Corporate bank, which will mature in five years (July 2020) and long-term investment loan agreement with EIB of EUR 70.0 million. The loan can be taken into use until October 2017.

Borrowings by period that interest rates are fixed for

in million EUR	31 DECEMBER	
	2016	2015
< 1 year	66.3	67.6
1 - 5 years	329.2	329.2
> 5 years	544.4	555.0
Total (Notes 3.1, 3.2 and 12)	939.9	951.8

Period until earlier of next interest rate repricing date and maturity date.

Weighted average effective interest rates of borrowings

	31 DECEMBER	
	2016	2015
Long-term bank loans	1.4%	2.6%
Bonds	4.3%	4.3%

22. Trade and other payables

in million EUR	31 DECEMBER	
	2016	2015
Financial payables within trade and other payables		
Trade payables	84.2	89.0
Accrued expenses	7.8	8.8
Payables to associates (Note 35)	3.3	4.8
Other payables	2.2	2.9
Total financial payables within trade and other payables (Note 3.1 and 12)	97.5	105.5
Payables to employees (Note 3.1)	19.2	17.8
Tax liabilities (Note 3.1)	33.9	50.2
Prepayments	6.6	6.7
Total trade and other payables	157.2	180.2
<i>of which short-term trade and other payables</i>	<i>155.4</i>	<i>179.0</i>
<i>of which long-term trade and other payables</i>	<i>1.8</i>	<i>1.2</i>

In June 2016, legislators adopted amendments to Estonian legislation which lowered oil shale's resource charges retroactively from July 2015. The amendments took effect from July 2016. The state made the taxation of extraction rights flexible by linking the resource charge rates to the world market price of heavy fuel oil. As a result EUR 9.3 million resource charges were refunded for the third and fourth quarter of 2015 and EUR 4.9 million resource charges were refunded for the first quarter of 2016 to Eesti Energia (Note 27).

23. Deferred income

Connection and other service fees

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Deferred connection and other service fees at the beginning of the period	164.9	154.9
Connection and other service fees received	15.2	14.0
The value of assets transferred for connection fees	1.8	2.5
Connection and other service fees recognised as income (Notes 25 and 32)	(7.0)	(6.5)
Deferred connection and other service fees at the end of the period	174.9	164.9

24. Provisions

in million EUR	Opening balance 31 December 2015	Recognition and reversal of provisions (Note 5)	Interest charge (Note 30)	Use	CLOSING BALANCE 31 DECEMBER 2016	
					Short-term provision	Long-term provision
Environmental protection provisions (Note 29)	28.3	0.3	0.8	(1.8)	5.6	22.0
Provision for termination of mining operations (Notes 28 and 29)	0.7	0.1	-	-	0.1	0.7
Employee related provisions (Note 28)	6.6	0.3	0.1	(1.7)	0.8	4.5
Provision for dismantling cost of assets	3.3	-	0.2	-	-	3.5
Provision for greenhouse gas emissions (Notes 8 and 27)	28.3	46.9	-	(28.2)	47.0	-
Provision for obligations arising from treaties	3.5	0.8	-	-	4.3	-
Total provisions (Note 4)	70.7	48.4	1.1	(31.7)	57.8	30.7

in million EUR	Opening balance 31 December 2014	Recognition and reversal of provisions (Note 5)	Interest charge (Note 30)	Use	CLOSING BALANCE 31 DECEMBER 2015	
					Short-term provision	Long-term provision
Environmental protection provisions (Note 29)	26.5	2.5	0.9	(1.6)	5.8	22.5
Provision for termination of mining operations (Notes 28 and 29)	0.8	-	-	(0.1)	-	0.7
Employee related provisions (Note 28)	4.7	2.7	0.1	(0.9)	2.1	4.5
Provision for dismantling cost of assets	3.2	-	0.1	-	-	3.3
Provision for greenhouse gas emissions (Notes 8 and 27)	68.2	12.6	-	(52.5)	28.3	-
Provision for onerous contracts	0.6	(0.6)	-	-	-	-
Provision for obligations arising from treaties	2.2	1.2	0.1	-	3.5	-
Total provisions (Note 4)	106.2	18.4	1.2	(55.1)	39.7	31.0

Recognition and change in the provisions during financial year 2016 in the amount of EUR 0.4 million (2015: EUR 0.9 million) resulted from the change in discount rate.

Environmental protection provisions and provisions for the termination of mining operations have been set up for:

- restoring land damaged by mining;
- cleaning contaminated land surfaces;

- restoring water supplies contaminated as a result of mining activities;
- ascertainment and compensation of damages caused by blasting work;
- closing landfills and neutralising excess water;
- maintenance of closed ash fields;
- closing of industrial waste dump;
- eliminating asbestos in power plants;

24. Eraldised, järg

- for payment of mining rights fee;
- for dismantling and gathering of equipment and facilities.

Long-term environmental protection provisions will be settled at the Eesti Energia Kaevandused in 2017-2038, and at Narva Elektriijaamad in 2017-2058.

Provisions related to the termination of mining operations will be settled in 2016-2038.

Employee related provisions have been set up for:

- payment of benefits laid down in collective agreements and other acts;
- compensation of work-related injuries;
- payment of termination benefits;
- payments of scholarships.

Long-term employee related provisions will be settled during the periods specified in the contracts or during the remaining life expectancy of the employees, period of which is determined using data from Statistics Estonia on life expectancies by age groups. The provisions for payments of termination benefits in mines and quarries will be set up when the detailed plans for the closure of these mines and quarries have been announced.

The provision for the dismantling costs of assets has been set up to cover the future dismantling costs of the renovated power blocks No. 8 and 11 and industrial waste dump of the Narva power plants. The present value of the dismantling costs of the assets was included in the cost of property, plant and equipment. The provision for the dismantling costs is expected to be settled in 2034-2035.

The provision for greenhouse gas emissions has been set up in the average price of the greenhouse gas emission allowances that are owned by the Group or that are allocated to the Group free of charge for heat production or for the purpose of modernisation of electricity production. In the reporting and comparative period the following amounts of the greenhouse gas emission allowances have been allocated to the Group free of charge:

- a) for the purpose of modernisation of electricity production
 - 2 856 499 tonnes for the investments made in 2016 that will be transferred in 2017; 3 570 624 tonnes for the investments made in 2015 that was transferred in 2016.
- b) for heat production - 242 660 tonnes for heat production in 2016, 275 957 tonnes for heat production in 2015. The greenhouse gas emission allowances allocated free of charge are taken into account for the purpose of calculating the provisions in the period for which the allowances are allocated irrespective of their actual transfer (Note 34).

The provision for obligations arising from treaties has been set up for a part of contractual payment for automatic meter reading system installation works that will be paid after the implementation of the system. The provision will presumably be settled in 2017.

The provision are discounted at the rate of 0.28%-4.60% (2015: 0.74%-4.60%). The discount curve is used for discounting provisions that allows more accurate evaluation of the provisions in different time horizons.

25. Revenue

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
By activity		
Sale of goods		
Electricity	345.8	352.2
Shale oil	67.0	102.7
Heat	37.1	36.9
Power equipment	6.9	4.9
Other goods	17.8	22.1
Total sale of goods	474.6	518.8
Sale of services		
Sales of services related to network	242.9	234.4
Connection fees (Notes 23 and 32)	7.0	6.5
Repair and construction services	6.2	5.4
Rental and maintenance income (Note 7)	1.4	1.6
Other services	10.0	10.0
Total sale of services	267.5	257.9
Total revenue (Note 5)	742.1	776.7

26. Other operating income

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Fines, penalties and compensations	71.2	2.9
Gain from revaluation of derivatives	14.4	9.3
Gain on disposal of property, plant and equipment (Note 32)	1.2	2.0
Government grants (Note 23)	0.3	0.4
Other operating income	2.5	2.1
Total other operating income	89.6	16.7

Under fines, penalties and compensations is recognised agreement with GE in which builder of Auvere power plant agreed to compensate Eesti Energia unearned revenue of EUR 68.6 million caused by the delay in the works (Note 4).

27. Raw materials and consumables used

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Transmission services	81.3	78.7
Greenhouse gases emissions expense (Note 24)	47.0	12.6
Maintenance and repairs	32.7	42.0
Materials and spare parts for production	26.6	32.3
Electricity	26.4	40.5
Technological fuel	26.2	23.8
Gas bought for resale	12.1	15.1
Resource tax on mineral resources*	1.3	28.1
Loss on disposal of greenhouse gas allowances	-	7.4
Other raw materials and consumables used	36.3	46.2
Total raw materials and consumables used	289.9	326.7

* The additional information about reduction of oil shale's resource charges is disclosed in Note 22.

28. Payroll expenses

	1 JANUARY – 31 DECEMBER	
	2016	2015
Number of employees		
Number of employees at the beginning of the period	6,015	6,601
Number of employees at the end of the period	5,840	6,015
Average number of employees	5,696	6,289

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Payroll expenses		
Wages, salaries, bonuses and vacation pay	105.3	111.7
<i>Average monthly pay (in euros)</i>	<i>1,541</i>	<i>1,480</i>
Other payments and benefits to employees	3.4	5.0
Payroll taxes	36.6	39.1
Recognition/reversal of employee related provisions (Note 24)	0.3	2.7
Total calculated payroll expenses	145.6	158.5
Of which remuneration to management and supervisory boards (Note 35)		
Salaries, bonuses, additional remuneration	2.1	2.2
Fringe benefits	0.1	0.1
Total paid to management and supervisory boards	2.2	2.3
Capitalised in the cost of self-constructed assets	(15.2)	(18.6)
Covered from the provisions for the termination of mining operations and environmental protection (Note 24)	(0.2)	(0.3)
Total payroll expenses	130.2	139.6

The Management Board members are appointed by the Supervisory Board. The term of appointment for 5 years.

29. Other operating expenses

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Environmental pollution charges	30.3	30.3
Miscellaneous office expenses	6.2	6.7
Rental expense (Note 7)	5.1	5.5
Research and development costs	2.4	2.0
Recognition of environmental and mining termination provisions (Note 24)	0.1	2.4
Loss from doubtful loan receivables (Notes 5, 13, 32 and 35)	0.9	11.0
Other operating expenses	24.7	31.4
Total other expenses	69.7	89.3

30 Net financial income (-expense)

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Financial income		
Interest income	0.3	6.3
Total interest income	0.3	6.3
Total financial income (Note 32)	0.3	6.3
Financial expenses		
Interest expense		
Interest expenses on bonds and loans	(36.2)	(37.6)
Amounts capitalised on qualifying assets (Note 6)	21.7	24.7
Total interest expenses on borrowings (Note 32)	(14.5)	(12.9)
Interest expenses on provisions (Note 24)	(1.1)	(1.2)
Total interest expenses	(15.6)	(14.1)
Foreign exchange gain/losses	1.6	3.8
Other financial expenses	(0.1)	(0.3)
Total financial expenses	(14.1)	(10.6)
Net financial income (-expense)	(13.8)	(4.3)

31. Corporate income tax

According to the Income Tax Act, the companies are taxed in Estonia upon distribution of dividends. From 1 January 2015, the income tax rate is 20/80 of the net amount of dividends. Dividends distributed by Estonian company are exempt, if these are paid out of dividends received from other companies in which Estonian company has at least 10% participation.

Average effective income tax rate

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Estonia		
Net dividends	0.1	61.9
Income tax applicable for dividends	20/80	20/80
Theoretical income tax at applicable rates	0.0	15.5
Impact of dividends and liquidation proceeds paid by associates	-	-0.6
Effective income tax on dividends	0.0	14.9
Average effective income tax rate	20%	19.2%
Income tax expense arising from the subsidiaries	0.1	-
Total income tax expense	0.1	14.9

Net dividends in 2016 consist of dividends paid by subsidiary to non-controlling interest.

As at 31 December 2016 and 31 December 2015, the Group did not have any deferred income tax assets and liabilities.

32. Cash generated from operations

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Profit before income tax	171.1	55.4
Adjustments		
Depreciation and impairment of property, plant and equipment (Notes 5 and 6)	138.5	176.9
Amortisation and impairment of intangible assets (Notes 5 and 8)	4.9	31.7
Deferred income from connection and other service fees (Notes 4, 23 and 25)	(7.0)	(6.5)
Gain on disposal of property, plant and equipment	(1.1)	(1.6)
Amortisation of government grant received to purchase non-current assets (Note 23)	(0.3)	(0.3)
Profit (loss) from associates using equity method (Note 9)	(1.1)	(2.5)
Unpaid/unsettled gain/loss on derivatives	4.3	16.3
Loss from doubtful loan receivables (Notes 5, 13, 29 and 35)	0.9	11.0
Currency exchange gain/loss on loans granted	(1.3)	(3.8)
Interest expense on borrowings (Note 30)	14.5	12.9
Interest and other financial income (Note 30)	(0.3)	(6.3)
Adjusted net profit before tax	323.1	283.2
Net change in current assets relating to operating activities		
Change in receivables related to operating activities (Note 13)	(70.0)	15.5
Change in inventories (Note 11)	6.7	(31.1)
Net change in other current assets relating to operating activities	(36.5)	118.3
Total net change in current assets relating to operating activities	(99.8)	102.7
Net change in current liabilities relating to operating activities		
Change in provisions (Note 24)	17.0	(36.7)
Change in trade payables (Note 22)	5.4	0.3
Net change in liabilities relating to other operating activities	(0.4)	1.6
Total net change in liabilities relating to operating activities	22.0	(34.8)
Cash generated from operations	245.3	351.1

33. Off-balance sheet assets, contingent liabilities and commitments

(a) Off-balance sheet assets

Oil shale Resources

The overview of the resources of oil shale in the possession of the Group and its associates is presented in the table below. The resources of oil shale of Estonian Republic represent the resources of oil shale in the official balance of natural resources. The resources of oil shale of international development projects are recognised based on the disclosure requirements of international standards of evaluation of resources and reserves. The classification of the resource is performed by the authorized experts and is proved appropriate according to the standard both by the level of exploration and economical perspective. Depending on the development phase the known technical, environmental and social-economical restrictions have been adjusted and taken into account when recognising the resources.

in million EUR	31 DECEMBER	
	2016	2015
Estonia		
Measured*	508	480
Jordan		
Measured*	924	924
Inferred**	2,604	2,604
USA**		
Measured **	3,500	3,500
Indicated**	2,300	2,300
Inferred**	230	230

* Resource represents a part of in place Resource, after it has been modified by desired cut-off grade, technical, economical and already defined modifying factors.

** Resource is defined as amount of total in place oil shale, that has high possibility for commercial interest. This definition is applied for resources before the pre-technical analyses, to which possible modifying factors have not been applied.

Emission rights

On implementation of article 10c of EU Emissions Trading System the Group may receive for the purpose of modernisation of electricity production up to 17.7 million tonnes of greenhouse gas emission allowances free of charge in the period 2013 to 2017. In addition it is possible for the Group according to the article 10a to receive in the period 2013 to 2020 up to 2.1 million tonnes of greenhouse gas emission allowances free of charge for heat production (Notes 16 and 24).

(b) Contingent liabilities

Contingent liabilities arising from potential tax audit

Estonia

Tax authorities have neither started nor performed any tax audits or single case audits at any Group company. Tax authorities have the right to review the company's tax records within 5 years after the reported tax year and if they find any errors they may impose additional taxes, interest and fines. The Group's management considers that there are not any circumstances which may give rise to a potential material liability in this respect.

Foreign countries

The Group's management considers that there are not any circumstances which may give rise to a potential material liability in this respect.

Financial covenants

The loan agreements concluded by the Group set certain covenants on the Group's consolidated financial indicators. The covenants have been adhered to.

33. Off-balance sheet assets, contingent liabilities and commitments, continued

(c) Commitments

Capital commitments arising from construction contracts

As at 31 December 2016, the Group had contractual liabilities relating to the acquisition of non-current assets totalling EUR 86.2 million (31 December 2015: EUR 94.4 million).

Contracts for buying greenhouse gas emissions allowances

As at 31 December 2016 the Group had concluded contracts for buying greenhouse gas emissions allowances in December 2017 in the amount of EUR 51.3 million (31 December 2015: EUR 66.4 million).

34 Earnings per share

Basic earnings per share are calculated by dividing profit attributable to the equity holders of the company by the weighted average number of ordinary shares outstanding. As there are no potential ordinary shares, diluted earnings per share equal basic earnings per share in all the periods. In 2015 and 2016 there were no changes in the share capital.

	1 JANUARY – 31 DECEMBER	
	2016	2015
Profit attributable to the equity holders of the company (million EUR)	170.9	40.5
Weighted average number of shares (million)	621.6	621.6
Basic earnings per share (EUR)	0.27	0.07
Diluted earnings per share (EUR)	0.27	0.07

35 Related party transactions

The sole shareholder of Eesti Energia AS is the Republic of Estonia. In preparing the Group's financial statements, the related parties include associates, members of the management and supervisory boards of the parent company, and other companies over which these persons have control or significant influence. Related parties also include entities under the control or significant influence of the state.

Transactions with associates

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Purchase of goods	17.2	22.0
Sale of services	0.3	1.1
Sale of goods	0.1	0.1
Financial expenses	-	5.8
Loans granted	4.3	2.9

In 2015 the loan granted to associate Enefit Jordan B.V was revalued by EUR 11.0 million and in 2016 by EUR 0.9 million (Notes 5, 13, 29 and 32).

Transactions with entities over which the members of Management and Supervisory Board have significant influence

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Purchases of goods and services	1.5	2.6

35. Related party transactions, continued

The sales of electricity, network services and heat to the entities over which the state has control or significant influence have been taken place under normal business activity. The Group has performed in the reporting and comparative period purchase and sales transactions in the material amounts with Elering AS, which is fully state-owned enterprise.

Tehingud Elering ASiga

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Purchase of services	82.2	75.4
Purchase of goods	9.2	8.4
Purchase of property, plant and equipment and prepayments	1.3	2.4
Sale of goods and services (incl. renewable energy grant)	20.7	22.8
Sale of property, plant and equipment	-	0.7

Receivables from Elering AS and payables to Elering AS

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Receivables (Note 13)	2.8	3.4
Payables (Note 22)	19.9	18.4

The remuneration paid to the members of the Management and Supervisory Boards is disclosed in Note 28. Receivables from associates are disclosed in Note 13 and payables to associates in Note 22. No impairment loss from receivables was recognised in the comparative period.

Upon premature termination of the service contract with a member of the Management Board, the service contracts stipulate the payment of 3 months' remuneration as termination benefits.

In purchasing and selling network services, the prices set by the Estonian Competition Authority are used.

36. Financial information on the parent company

Financial information disclosed on the parent company includes the primary separate financial statements of the parent company, the disclosure of which is required by the Accounting Act of Estonia. The primary financial statements of the parent company have been prepared using the same accounting policies that have been used in the preparation of the consolidated financial statements. Investments in subsidiaries and associates are reported at cost in the separate financial statements of the parent company.

Income statement

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Revenue	288.0	343.5
Other operating income	62.2	13.1
Raw materials and consumables used	(218.1)	(223.9)
Other operating expenses	(17.7)	(53.4)
Payroll expenses	(29.9)	(28.9)
Depreciation, amortisation and impairment	(10.2)	(13.1)
Other expenses	(4.4)	(12.0)
OPERATING PROFIT	69.9	25.3
Financial income	17.6	88.2
Financial expenses	(32.7)	(30.2)
Total financial income and expenses	(15.1)	58.0
PROFIT BEFORE TAX	54.8	83.3
NET PROFIT FOR THE FINANCIAL YEAR	54.8	83.3

Statement of comprehensive income

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
PROFIT FOR THE YEAR	54.8	83.3
Other comprehensive income		
Revaluation of risk hedge instruments	(7.4)	(2.9)
Other comprehensive income for the year	(7.4)	(2.9)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	47.4	80.4

36. Financial information on the parent company, continued

Statement of financial position

in million EUR	31 DECEMBER	
	2016	2015
ASSETS		
Non-current assets		
Property, plant and equipment	25.5	205.9
Intangible assets	4.4	5.8
Investments in subsidiaries	524.2	519.8
Investments in associates	13.2	13.2
Receivables from subsidiaries	253.1	237.8
Total non-current assets	820.4	982.5
Current assets		
Inventories	1.6	-
Greenhouse gas allowances	42.1	12.0
Trade and other receivables	1,250.6	1,145.0
Derivative financial instruments	4.1	16.3
Cash and cash equivalents	211.5	149.6
Total current assets	1,509.9	1,322.9
Total assets	2,330.3	2,305.4

in million EUR	31 DECEMBER	
	2016	2015
EQUITY		
Share capital	621.6	621.6
Share premium	259.8	259.8
Statutory reserve capital	62.1	62.1
Hedge reserve	-	7.4
Retained earnings	346.5	291.7
Total equity	1,290.0	1,242.6
LIABILITIES		
Non-current liabilities		
Borrowings	920.6	932.6
Deferred income	-	0.1
Provisions	0.5	1.0
Total non-current liabilities	921.1	933.7
Current liabilities		
Borrowings	19.3	19.3
Trade and other payables	92.7	97.8
Derivative financial instruments	7.1	11.8
Provisions	0.1	0.2
Total current liabilities	119.2	129.1
Total liabilities	1,040.3	1,062.8
Total liabilities and equity	2,330.3	2,305.4

36. Financial information on the parent company, continued

Cash flow statement

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Cash flows from operating activities		
Profit before tax	54.8	83.3
Adjustments		
Depreciation of property, plant and equipment	8.4	10.7
Amortisation of intangible assets	1.8	2.4
Profit/loss from sale of property, plant and equipment	(0.2)	(0.2)
Gain on disposal of subsidiary	(37.7)	-
Loss from doubtful loan receivables	0.9	36.9
Other gains/losses on investments	(0.2)	(60.0)
Gain/loss on unpaid/unsettled derivatives	0.1	26.0
Currency exchange gain/loss on loans granted	(1.3)	(9.1)
Interest expense on borrowings	36.1	37.5
Interest income	(17.4)	(26.9)
Adjusted net profit	45.3	100.6
Net change in current assets relating to operating activities		
Loss from doubtful receivables	0.6	0.3
Change in receivables relating to operating activities	0.9	1.1
Change in inventories	(1.6)	-
Net change in current assets relating to other operating activities	(75.3)	92.9
Total net change in current assets relating to operating activities	(75.4)	94.3
Net change in liabilities relating to operating activities		
Change in provisions	(0.1)	-
Change in trade payables	(1.3)	0.9
Net change in liabilities related to other operating activities	1.8	1.5
Total net change in liabilities relating to operating activities	0.4	2.4
Interest paid and borrowing costs	(30.3)	(43.8)
Interest received	13.7	17.2
Corporate income tax paid	-	-
Net cash flows from operating activities	(46.3)	170.7

in million EUR	1 JANUARY – 31 DECEMBER	
	2016	2015
Cash flows from investing activities		
Purchase of property, plant and equipment and intangible assets	(2.5)	(8.1)
Proceeds from sale of property, plant and equipment	2.6	0.3
Net change in cash restricted from being used	(6.9)	0.6
Dividends received from financial investments	0.2	61.4
Net change in term deposits with maturities of more than 3 months	-	40.0
Contribution to the share capital of subsidiaries	(3.7)	-
Proceeds from sale of subsidiaries	208.8	-
Reclassification of receivables granted to subsidiaries	(1.7)	-
Loans granted to subsidiaries	-	(0.8)
Repayments of loans granted to subsidiaries	0.3	0.3
Change in overdraft granted to subsidiaries	(63.7)	(125.1)
Other loans granted	(4.4)	(2.9)
Net cash used in investing activities	129.0	(34.3)
Cash flows from financing activities		
Bank loans received	-	29.9
Repayments of bank loans	(19.3)	(6.9)
Change in overnight deposit received from subsidiaries	(0.6)	-
Acquisition of non-controlling interest in a subsidiary	(0.9)	-
Dividends paid	-	(61.9)
Total cash generated from financing activities	(20.8)	(38.9)
Net cash flows	61.9	97.5
Cash and cash equivalents at the beginning of the period	149.6	52.1
Cash and cash equivalents at the end of the period	211.5	149.6
Net increase/decrease in cash and cash equivalents	61.9	97.5

36. Financial information on the parent company, continued

Statement of changes in equity

in million EUR	Share capital	Share premium	Statutory reserve capital	Hedge reserve	Currency translation differences	Retained earnings	Total
Equity as at 31 December 2014	621.6	259.8	59.0	10.3	-	273.4	1,224.1
Carrying amount of holdings under controlling and significant influence						(534.4)	(534.4)
Carrying amount of holdings under controlling and significant influence using equity method				36.7	5.7	885.0	927.4
Adjusted unconsolidated equity as at 31 December 2014				47.0	5.7	624.0	1,617.1
Profit for the year	-	-	-	-	-	83.3	83.3
Other comprehensive income for the year				(2.9)	-	-	(2.9)
Total comprehensive income for the year	-	-	-	(2.9)	-	83.3	80.4
Dividends paid (Note 19)	-	-	-	-	-	(61.9)	(61.9)
Transfer of retained earnings to statutory reserve capital	-	-	3.1	-	-	(3.1)	-
Total contributions by and distributions to owners of the company, recognised directly in equity	-	-	3.1	-	-	(65.0)	(61.9)
Total transactions with owners of the company, recognised directly in equity	-	-	3.1	-	-	(65.0)	(61.9)
Equity as at 31 December 2015	621.6	259.8	62.1	7.4	-	291.7	1,242.6
Carrying amount of holdings under controlling and significant influence						(533.0)	(533.0)
Carrying amount of holdings under controlling and significant influence using equity method				9.4	11.0	840.8	861.2
Adjusted unconsolidated equity as at 31 December 2015 (Note 19)				16.8	11.0	599.5	1,570.8

36. Financial information on the parent company, continued

Statement of changes in equity

in million EUR	Share capital	Share premium	Statutory reserve capital	Hedge reserve	Currency translation differences	Retained earnings	Total
Equity as at 31 December 2015	621.6	259.8	62.1	7.4	-	291.7	1,242.6
Carrying amount of holdings under controlling and significant influence						(533.0)	(533.0)
Carrying amount of holdings under controlling and significant influence using equity method				9.4	11.0	840.8	861.2
Adjusted unconsolidated equity as at 31 December 2015 (Note 19)				16.8	11.0	599.5	1,570.8
Profit for the year	-	-	-	-	-	54.8	54.8
Other comprehensive income for the year	-	-	-	(7.4)	-	-	(7.4)
Total comprehensive income for the year	-	-	-	(7.4)	-	54.8	47.4
Total contributions by and distributions to owners of the company, recognised directly in equity	-	-	-	-	-	-	-
Total transactions with owners of the company, recognised directly in equity	-	-	-	-	-	-	-
Equity as at 31 December 2016	621.6	259.8	62.1	-	-	346.5	1,290.0
Carrying amount of holdings under controlling and significant influence						(537.4)	(537.4)
Carrying amount of holdings under controlling and significant influence using equity method				(28.5)	11.9	961.1	944.5
Adjusted unconsolidated equity as at 31 December 2016 (Note 19)				(28.5)	11.9	770.2	1,697.1

Under the Accounting Act of Estonia, adjusted unconsolidated retained earnings are the amount from which a public limited company can make payments to its shareholders.



INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholder of AS Eesti Energia

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of AS Eesti Energia and its subsidiaries (together the Group) as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

What we have audited

The Group's consolidated financial statements comprise:

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

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

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

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Auditors Activities Act of the Republic of Estonia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the Auditors Activities Act of the Republic of Estonia.

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Our audit approach

Overview



Materiality

Overall Group materiality is 6.5 million euros which represents approximately 2.5% of underlying earnings before interest, tax, depreciation and amortization (EBITDA), adjusted for non-recurring items.

Audit scope

We tailored our audit scope based on the risk and size of entities within the Group and performed either a full scope audit or specific audit procedures over material income statement or balance sheet line items. At the Group level, we tested the consolidation process and performed separate analytical procedures over the components not covered by the above procedures to confirm our conclusion that no material misstatements exist that may affect the consolidated financial statements.

Key audit matters

- Property, plant and equipment impairment assessment
- Hedge accounting for derivative transactions in respect of electricity and shale oil
- Accounting for compensation related to the construction of the Auvere power station

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where the Management Board made subjective judgments; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.



Based on our professional judgment, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall group materiality	6.5 million euros
How we determined it	Approximately 2.5% of underlying earnings before interest, tax, depreciation and amortization (EBITDA), adjusted for non-recurring items.
Rationale for the materiality benchmark applied	We have applied the EBITDA benchmark, as we believe that is the key measure used both internally by management and by external stakeholders in evaluating the performance of the Group. One-off items excluded from EBITDA for materiality calculation purposes are items that have significantly impacted the Group's performance on a non-recurring basis. The significant exclusion is the gain of 68.6 million euros, arising from the compensation received by the Group for the delays in the construction of the Auvere power station.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter

Property, plant and equipment impairment assessment

The significant assumptions used by the management and their impact on the recoverable amount of property, plant and equipment are described on pages 140 and 148 through 151 of the Annual Report.

As at 31 December 2016 the Group has 2,469 million euros of property, plant and equipment, the majority of which relate to the shale mining, shale oil production and power generation assets in Estonia. The difficult global

How our audit addressed the key audit matter

We began our procedures by assessing whether impairment indicators exist for the assets not identified by management. We took into account our knowledge of the Group and its business activities as well as the accumulated knowledge related to the industries where the Group operates. In addition, we performed inquiries with management and key employees and inspected internal documents of the Group. We found the management's conclusions regarding assets with impairment indicators to be consistent with the evidence we obtained.

We evaluated management's key assumptions and estimates used in the calculation



economic environment as well as the low market prices for oil and electricity have continued to put pressure on the Group and are an indication that the recoverable amount of the assets may be below their carrying amount. Despite the fact that the overall economic environment has remained challenging, the situation has improved compared to the low point reached in the last quarter of 2015 and the first quarter of 2016.

The recoverable amount of the Group's property, plant and equipment is determined by either their value in use or their fair value less cost of disposal, both of which are based on discounted future cash flows.

Impairment assessment of these assets is subjective and requires significant judgments due to the inherent uncertainty involved in the forecasting and discounting of future cash flows. Many of the key underlying assumptions are impacted by global and country-specific political and economic factors. Consequently, there is a high risk that due to the judgemental factors, potential impairment may be unidentified or the impairment loss be miscalculated. Due to the above reasons we considered this area to be a key audit matter.

of the recoverable value of the assets identified for impairment, including the assumptions related to operational performance, such as operating cost forecasts, electricity and oil shale production volumes and reliability of production assets. We challenged management's assumptions by corroborating the information with the information received from operational level management and by referencing them to the actual performance of the Group and to internal documents of the Group, such as budget forecasts and minutes of meetings of governing bodies. Where management had used market inputs, such as oil, electricity and CO₂ emissions quota prices, we reconciled them to available third party information sources, such as commodity price forecasts. We involved PwC valuation specialists to help us assess the reasonableness of the discount rates used by management. We benchmarked these to external data and challenged the assumptions based on our knowledge of the Group and its industry. Based on the audit evidence obtained from the above procedures, we did not identify any material misstatements, contradictions or omissions in the key assumptions and estimates used by management in the calculation of the recoverable value of property, plant and equipment.

As noted on pages 148 through 151, a key assumption that management has made in determining the future cash flows for assets in Estonia, is regarding the ability of the Group to take part in the Estonian nationally regulated auctions for the sale of renewable energy and, consequent potential additional revenue from the sale of renewable energy on these auctions. We challenged this assumption by inspecting and assessing information about the latest available implemented and proposed legislative changes of the Estonian electricity market. We also read the disclosures in respect of the impact of the inherent uncertainty to the estimated cash flows.

Based on our audit procedures we found the management's judgment to be consistent with available information and the disclosures to appropriately reflect the sources of sensitivity and related impacts on the recoverable value in accordance with the requirements of IAS 36 and IAS 1.



Hedge accounting for derivative transactions in respect of electricity and shale oil

Refer to pages 141 and 160 through 161 of the Annual Report for details on the accounting for derivative contracts and effectiveness of hedge instruments.

The Group has entered into a number of derivative transactions to help it protect and optimise the value of its underlying shale mining, shale oil production and power generation assets. Majority of the derivatives are accounted for using the general rule in IAS 39, at fair value through profit or loss. The Group has designated certain of those arrangements as cash flow hedge instruments and accounts for the changes in their fair value through other comprehensive income until the underlying hedged transactions take place. As of the balance sheet date the total fair value of derivative instruments, designated as hedge instruments and related to electricity and shale oil trading, that have accumulated to the equity reserve amount to 28.5 million euros.

Judgment is required both in determining the fair value of these derivative contracts and in assessing the effectiveness of those derivative contracts designated as hedge instruments. The Group uses separate bespoke models that are specific to the derivatives to determine their fair value and to assess the effectiveness of those derivatives designated as hedge instruments. This area is significant to our audit due to the inherent judgment involved in applying these models and due to the magnitude of the derivative transactions.

We assessed the overall derivative trading process, including internal risk management procedures and the controls around origination and maintenance of complete and accurate information relating to derivative contracts. We evaluated the controls implemented by the Group, however we placed no reliance on said controls due to the robust nature and effectiveness of the performed substantive audit procedures.

We obtained the listing of derivative contracts and assessed the accuracy and the completeness of the list by reconciling it to third-party confirmations (received directly by us from said third parties), and found no material misstatements.

We gave particular focus to the valuation of the derivative contracts at the balance sheet date, and to the assessment of effectiveness tests of the hedge instruments throughout the financial year. A sample of derivative contracts at the balance sheet date and of hedge instrument effectiveness tests throughout the financial year formed the basis for the audit procedures performed by us. We evaluated the models and key assumptions used by management to determine the fair value of derivatives and the effectiveness of hedge instruments. We assessed the integrity of these models as well as verified key inputs and assumptions by reconciling or comparing them to third party confirmations, external pricing information and historical data. The performed audit procedures did not identify any material misstatements in the models or underlying data and key assumptions used by management. We read the disclosures in respect of derivatives and found them to be consistent with the requirements of requirements in IFRS



Accounting for compensation related to the construction of the Auvere power station

Refer to pages 141 and 170 of the Annual Report for details on the accounting for the compensation.

In 2011 the Group began the construction of a new modern power plant that was planned to be more efficient than the existing power generation assets and that would be able to utilise shale, natural gas and biofuel simultaneously. The power plant was scheduled for completion in November 2015 by the lead contractor General Electric (the Lead Contractor). Due to the issues faced by the Lead Contractor in the design and construction of air filters and the associated difficulties in complying with the required air pollution emission standards the delivery of the power plant has not been finalised as of the date of signing of our auditor's report.

In 2016, management demanded and the Lead Contractor agreed to compensate for the first 12-month delay in the construction completion date, in the amount of 66 million euros. Additional compensation in the amount of 2.6 million euros relates to the remaining period up to the balance sheet date. Management has exercised judgment when determining the accounting treatment of the 68.6 million euro compensation and has recorded it through profit or loss rather than as a decrease of the cost of the investment in the Auvere power plant, as a compensation for incremental losses caused by the delay.

We focused on the assessment of the key assumptions used by management in relation to the compensation. We read the original contract for the construction of the Auvere power plant to identify and assess the basis for the compensation demands made by management. We also read the separate agreement signed by the Group and the Lead Contractor in relation to the compensation of 66 million euros. Additionally, the latter contract forms the basis for the subsequent compensation of 2.6 million euros. Both contracts provided evidence that the commercial substance of the payment made by the Lead Contractor was to compensate the Group for the loss of business incurred due to the delays in construction, thus we concluded that in light of evidence obtained, management's judgment regarding the amount of the compensation as well as the decision to account for it through profit or loss were appropriate.

We also reconciled to bank statements partial payments made by the Lead Contractor both during 2016 and subsequent to the balance sheet date, up to the date of the signing of our auditor's report, in the total amount of 27 million euros. The payments made by the Lead Contractor were in line with the payment schedule included in the signed compensation agreement and provide evidence to support management's estimates that the Lead Contractor will be able to and is likely to meet its obligations under the signed agreement.

We did not identify any information that would contradict the key assumptions used by management in their assessment. We read the disclosures regarding the compensation and found these to be consistent with the requirements of IAS 37, IAS 1 and the audit evidence we obtained.

How we tailored our audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.



Accordingly, based on the size and risk characteristics, we performed a full scope audit of the financial information for the following entities within the Group: Enefit Energiatootmine AS (electricity generation), Enefit Kaevandused AS (shale mining), Eesti Energia Õlitööstus AS (shale oil production), Elektrilevi OÜ (transmission grid), Eesti Energia AS (parent company). In addition, specific audit procedures over significant balances and transactions were performed for sales revenue of Enefit SIA (electricity sale in Latvia) and for the potential impairment of assets of Enefit American Oil (shale mining development rights in USA), Enefit Solutions (manufacturing of metal structures). At the Group level we tested the consolidation process and performed separate analytical procedures over the components not covered by the above procedures to confirm our conclusion that no material misstatements exist that may affect the consolidated financial statements. Information describing the structure of the Group is included in note 10 of the consolidated financial statements.

Other information

The Management Board is responsible for the other information contained in the Group's 2016 Annual report, in addition to the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Management Board and those charged with governance for the consolidated financial statements

The Management Board is responsible for the preparation and fair presentation of the consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Management Board is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Management Board either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

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



Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management Board.
- Conclude on the appropriateness of the Management Board's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.



We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

AS PricewaterhouseCoopers

A handwritten signature in blue ink, appearing to read 'Tiit Raimla', written in a cursive style.

Tiit Raimla
Auditor's Certificate No.287

A handwritten signature in blue ink, appearing to read 'Jüri Koltsov', written in a cursive style.

Jüri Koltsov
Auditor's Certificate No.623

22 February 2017

** 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.*

This independent auditor's report (translation of the Estonian original) should only be used with an annual report initialled for identification purposes by AS PricewaterhouseCoopers.

PROFIT ALLOCATION PROPOSAL

The retained earnings of Eesti Energia Group as at 31 December 2016 were EUR 770 215 905.65, of which the net profit for the year 2016 amounted to EUR 171 851 445.77.

The Management Board proposes under section 332 of the Commercial Code of Estonia to allocate the retained earnings of Eesti Energia Group as at 31 December 2016 as follows:

1. to pay EUR 47 000 000 as dividends to the shareholder;
2. not to distribute the remaining retained earnings of EUR 723 215 905,65 due to the continuing financing needs of the Eesti Energia Group.

SIGNATURES OF THE MANAGEMENT BOARD TO THE ANNUAL REPORT FOR FINANCIAL YEAR 2016

In the 2016 financial year, the Eesti Energia Management Board complied as required with the duties of members of the Management Board, and led the Eesti Energia Group to achieve its targets. The Management Board has regularly reported to the Supervisory Board, has acted within its powers and has submitted all of the information necessary for decision-making to the Supervisory Board. The Management Board is aware of and hereby confirms its responsibility for the preparation of the annual report and for the data therein.

21 February 2017

Chairman of the
Management Board

Hando Sutter



The Annual Report of the Eesti Energia Group for the financial year ended on 31 December 2016 consists of the management report, the consolidated financial statements, the auditor's report and the profit allocation proposal. The Management Board has prepared the management report, the consolidated financial statements and the profit allocation proposal.

Members of the
Management Board

Andri Avila



Raine Pajo



Andres Vainola



Margus Vals



GLOSSARY

Arbitrage – Concurrent purchase and sale of goods or securities of the same kind in different markets to earn a profit on the difference in market prices

Maintenance and repair expenditures – Expenditures incurred to maintain the existing production capacities

MWh – megawatt hour. 1 MWh is the unit of energy generated (or consumed) in one hour by a device operating at a constant power of 1 MW (megawatt)

1,000,000 MWh = 1,000 GWh = 1 TWh

Circulating fluidised bed (CFB) technology – Circulating fluidised bed combustion technology whereby larger (unburnt) particles are returned to the furnace

Clean Dark Spread (CDS) – Eesti Energia's margin between the price of electricity (in NP Estonia) and oil shale costs and CO₂ costs (taking into account the price of CO₂ allowance futures maturing in December and the amount of CO₂ emitted in the generation of a MWh of electricity)

CO₂ emission allowance – According to the European Union Emissions Trading System (ETS), one emission allowance gives the holder the right to emit one tonne of carbon dioxide (CO₂). The limit on the total number of emission allowances available gives them a monetary value

EBITDA margin – Earnings before interest, taxes, depreciation and amortisation divided by revenues

Eesti Energia market share on electricity retail market – Electricity sales to the final consumer divided by total electricity consumption in the area (including network losses)

FFO – Funds from operations. Cash flow from operations, excluding changes in working capital

Financial leverage – Net debt divided by the sum of net debt and equity

Future – A contract between counterparties which obligates to buy or sell an underlying asset (e.g. a commodity) at a pre-agreed price

Green paper on industrial policy – a document prepared by the state and employers' associations which outlines the bottlenecks of industrial development and suggests solutions for their elimination and improving industrial development

Level of water reservoirs – The largest part of the Nordic countries' electricity generation is based on hydro power whose output depends on the level of water reservoirs.

Liquidity – Amount of liquid assets. Sum of cash and cash equivalents, short term financial investments and deposits with a maturity of more than 3 months

Net debt – Debt obligations (amortised) less cash and cash equivalents (incl. bank deposits with maturities exceeding 3 months), units in money market funds and investments in fixed income bonds

Network losses – The amount of electricity delivered to customers is somewhat smaller than the amount supplied from power plants to the network because during transfer a part of electricity in the power lines and transformers converts into heat. To a lesser extent, network losses are caused by power theft and incorrect measuring. The network operator has to compensate energy losses and for this a corresponding amount of electricity has to be purchased every hour

NP system price – The price on the Nord Pool power exchange that is calculated on the basis of all purchase and sale bids without taking into account transmission capacity limitations

OHSAS, ISO 14001, HAZOP – International standards which deal with risk management in the area of occupational health and safety, the environment management system, and accident prevention

Oil shale resource charge – A charge to be paid to the state for the use of 1 tonne of oil shale located in the mineral deposit

OSAMAT – Management of Environmentally Sound Recycling of Oil Shale Ashes into Road Construction Products. Demonstration in Estonia – a project carried out to test the use of oil shale ash in road construction

Position hedged with forward transactions – The average price and the corresponding amount of electricity and shale oil sold and emission allowances purchased in the future is previously fixed.

RAB – Regulated Asset Base, which represents the value of assets used to provide regulated services

Return on Fixed Assets (ROFA) – Operating profit (rolling 12 months) divided by average fixed assets excluding assets under construction (allocated to specific product).

ROIC – Return on Invested Capital, calculated by dividing operating profit by average invested capital

SAIDI – System Average Interruption Duration Index. The sum of all customer interruption durations in minutes divided by the total number of customers served

SAIFI – System Average Interruption Frequency Index. The total number of customer interruptions divided by the total number of customers served

Tax footprint – An indicator which reflects the contribution made to society through taxes

Variable profit – Profit after deducting variable costs from sales revenue

INVESTOR INFORMATION

The Group's results concerning the financial year 2016 are released as follows

- Q1 interim report – 28 April 2017.
- Q2 interim report – 28 July 2017.
- Q3 interim report – 31 October 2017.
- The audited results for the financial year 2016 – 28 February 2018.

Eesti Energia's financial results and contacts for investor relations are available on the Group's web page:
<https://www.energia.ee/en/ettevottest/investorile>

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