

Corporate Governance

A Corporate Governance Code (CGC)¹ is a set of guidelines and recommended rules meant to be followed mostly by stock exchange companies.

Elering is dedicated to following the Corporate Governance Code and wishes to further grow in this area. We consider this a prerequisite for obtaining our strategic goals and shaping our organizational culture.

We confirm that:

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

Elering's CGC report is published on a website www.elering.ee.

EXERCISING SHAREHOLDER RIGHTS



Elering's shares are owned 100% by Government of Estonia.

The Minister of Economic Affairs and Infrastructure represents the owner at a general meeting. The general meeting is Elering's highest governing body. The annual general meetings are held once a year, while the Management Board can convene special general meetings in cases stipulated by law.

Competence of the company's owner includes amending the articles of association; increasing and decrease share capital, electing and removing members of the Supervisory Board, electing auditors, appointing special audit, approving the annual report and allocating profits, deciding upon merger, division, restructuring and/or dissolution of the company. The general meeting must base their actions (convening, disclosure of information, etc.) on the State Assets Act as well as the Commercial Code.

Management Board members, chairman of the Supervisory Board and, if necessary, members of the Supervisory Board, will participate in the general meeting. If new members of the Supervisory Board are being elected at the general meeting, the nominated candidates will also take part in the meeting.

The general meeting is held in Estonian. Allocation of profits is discussed at the general meeting as a separate subject and a separate decision is made thereon.

¹ Initiated by Tallinn Stock Exchange and Financial Supervision Authority of Estonia and issued in 2015

MANAGEMENT BOARD

The Management Board is Elering's governing body. It represents and governs the company's daily activities in accordance with the law and the requirements of the organization's Articles of Association, and organizes the company's accounting. Elering's Management Board has complete freedom of decision, everyday management choices are made independently, without interference by the owner and the Supervisory Board. The Management Board needs the consent of the Supervisory Board for transactions and operations that are beyond the daily economic activities of the company. The Management Board ensures that the members of the Supervisory Board have sufficient information of the company's economic condition, as well as important circumstances, which are related to the economic activities, and informs the Supervisory Board of the important circumstances of the economic activities as necessary.

Members of the Management Board and fees

According to the articles of association, the Management Board can consist of up to three members. The Supervisory Board elects Members of the Management Board for a term of up to five years.

The company's articles of association state that two members jointly or the Chairman of the Management Board separately can represent the company in all legal transactions.

The person authorized by the Supervisory Board concludes contracts with the members of the Management Board, which determine the rights and obligations of the Management Board member regarding the company and their remunerations.

Based on the articles of association, a member of the Management Board may only be paid a fee under the contract concluded with them. A member of the Management Board may also be paid an additional fee based on their performance in the amount of up to four months' fee. Bonuses may be paid based on the annual results or any other grounds based on a resolution of the Supervisory Board. Fees of the members of the Management Board are fixed and stipulated in a Management Board member's contract. Elering has not established any long-term bonus systems. A member of the Management Board may only be paid severance compensation upon removal at the initiative of the Supervisory Board before the term of their authorities has expired in the amount of up to three months' fees.

Conflict of interest

Members of the Management Board do not make decisions based on their own interest, nor do they use commercial offers made to Elering to their own gain. A member of the Management Board must declare any conflict of interest to the Supervisory Board and other members of the Management Board before concluding the contract of service, or immediately after such a conflict arises later on. Member of the Management Board must promptly notify other members of the Management Board and the chairman of the Supervisory Board about any commercial offers related to the company's economic activities made to them, their family members or someone associated with them.

The principles preventing conflict of interests of Members of the Management Board are established in the contract concluded with Members of the Management Board.

A Member of the Management Board avoids conflict between the interests of the company and the Member of the Management Board. He or she declares any direct or indirect interest in the transactions made by the company to Elering's Supervisory Board, and the Supervisory Board of any conflict as soon as it arises or of any situation that could lead to such a conflict. The Supervisory Board decides upon executing transactions with Members of the Management Board or any transactions that could involve personal interests of Members of the Management Board. They also decide upon the terms and conditions of the transaction.

In order to ensure independence, transactions concluded with related parties are declared upon approval of the annual report and in the audit.

SUPERVISORY BOARD

The owner's interests in the company are guaranteed by members of the Supervisory Board (representatives of the Ministry of Finance and the Ministry of Economic Affairs and Communications). The

Supervisory Board gives the Management Board instructions on organizing the management of the company and exercises supervision over the activities of the company's Management Board. The Supervisory Board regularly reviews and assesses the company's strategy, general actions, risk assessments, annual report and annual budget.

According to the company's articles of association, regular meetings of the Supervisory Board are held as needed, but no less than once in every three months. The notification of the Supervisory Board meeting and any related materials are sent to the Board members at least three working days before the meeting will convene.

Members of the Supervisory Board and remuneration

The supervisory Board comprises of three to five members. The number of the members of the Supervisory Board is decided and the members are elected and removed by the representative of the owner, i.e. the Minister of Economic Affairs and Infrastructure. The work of the Supervisory Board is run by the Chairman of the Supervisory Board. The Chairman of the Supervisory Board sets the agenda for the Supervisory Board meeting, runs the meeting, observes the effectiveness of the Supervisory Board's actions, arranges operational data transfers to the Supervisory Board members, provides enough time for the Supervisory Board members for drafting the decisions and familiarizing themselves with the data, and represents the Supervisory Board in interactions with Elering's Management Board. To coordinate to Supervisory Board's work, general meeting has established the Supervisory Board's working procedures.

The number of Supervisory Board meetings held in a year is indicated clearly in the annual CGC report. In addition, the report specifies, whether a member of the Supervisory Board has participated in less than half of the meetings within a financial year.

Fees paid to members of the Supervisory Board are set in a directive signed by the Minister of Economic Affairs and Infrastructure. The exact amount and the arrangements of the fees are determined on a general meeting and will be published in Elering's CGC report.

Members of the Supervisory Board must meet the requirements set to Supervisory Board members in the Commercial Code, as well as in the State Assets Act, and they must follow all their obligations.

AUDIT COMMITTEE

The Supervisory Board will elect the Audit Committee, comprising of up to five members. The Committee is responsible for exercising supervision over risk management, internal control and financial reporting. The Audit Committee advises the Supervisory Board in the area of accounting, checking the independence of the statutory auditor, risk management, internal control and audit, exercising supervision and preparation of the budget as well as legality of activities.

Members of the Audit Committee are elected for a term of three years and they elect from among themselves the chairman to organize the activities of the Audit Committee. The chairman of the Audit Committee cannot hold the position of the chairman of the Supervisory Board. The members of the Audit Committee are paid a fee for participating in the Audit Committee's activities.

The times of the Audit Committee meeting and the list of internal control audits covered are published in Elering's CGC report.

COOPERATION BETWEEN THE MANAGEMENT BOARD AND THE SUPERVISORY BOARD

Management Board and Supervisory Board will cooperate closely to best protect Elering's interests. Management Board and Supervisory Board work together on developing the company's strategy. The Management Board bases their management decisions on the strategic guidelines given by the Supervisory Board.

The Management Board informs the Supervisory Board regularly of any important matters that bear on the planning and business activities of the company and especially draws attention to important changes in Elering's business activities. The Management Board forwards data to the Supervisory Board, including financial reports, with sufficient time before Supervisory Board meeting. If the Supervisory Board requires

more information about the operations of the Management Board or the company, the member of the Management Board gives the necessary data either verbally or in writing. They also ensure Supervisory Board's access to any data relevant to the actions of the Management Board and the company.

The company's management principles are based on legislations, the articles of association, decisions and objectives set in general meetings and Supervisory Board meetings.

DISCLOSURE OF INFORMATION

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

FINANCIAL REPORTING AND AUDITING

The Management Board of Elering publishes an annual report once every year and mid-term reviews during the financial year. The annual report is compiled in accordance with the IFRS² standards and audited according to ISA³ principles. At the invitation of the Supervisory Board, the auditor of the company will also participate in the meeting of the Supervisory Board to review the annual report. The annual report signed by the Management Board members is submitted to the general meeting for approval. Along with the annual report, the Supervisory Board's opinion on the annual report is submitted to the general meeting.

Elering elects an external auditor following the procurement procedures and ensures the best possible value for money for the auditing services. Only internationally recognized quality service providers are asked to submit a tender. Elering follows the requirements of the Auditors Activities Act by rotating the auditors every 7 years.

External auditor is appointed by the resolution of the general meeting; a contract for auditing services is concluded by the Management Board. In the contract concluded with the auditor, his or her tasks, timeframe and fees are settled. This contract can, in no way, hamper auditors' work in assessing the company's activities.

The Audit Committee will monitor the external auditor's progress in accordance with the Auditors Activities Act.

RISK MANAGEMENT AND INTERNAL CONTROL SYSTEM

Elering's risk management is in compliance with ERM (*Enterprise Risk Management*) principles. Risk management objectives in Elering are as follows:

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

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

- the culture, processes and structure of the company encourage the fulfilment of the company's strategic objectives and at the same time also the identification, management, monitoring and, if possible, the hedging of risks;

² International Financial Reporting Standards

³ International Standards on Auditing

- the monitoring and management of the company's risks and the internal control system are based on the internationally recognized Enterprise Risk Management (ERM) Model developed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), a voluntary organization that promotes good corporate governance;
- all relevant legislations, standards, regulations and contractual obligations, as well as requirements and expectations arising from society have been taken into account upon management of the company's risks;
- we are continuously improving the risk management activities in the company.

The Management Board is responsible for the functioning of the internal control system of the company. To ensure the functioning of the internal control system, the internal auditor service will be outsourced to an audit company. The internal auditor will report to the Audit Committee.

The internal audit is an independent and objective action to provide security and advice, designed to add value to the actions of the company and to improve it. This helps the company to reach its goals by using systematic and orderly approach to assess and improve risk management and effectiveness of control and management processes. The function of the internal audit is independent from the areas being assessed and to report to the Audit Committee of the company.

EQUAL TREATMENT

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

In order to ensure equal treatment, Elering has established internal procedures and, based on Estonian and European Union legislation (including network codes), has compiled standard terms and conditions, methodologies and other rules that have been published on company's website and approved by the Estonian Competition Authority if required by law.