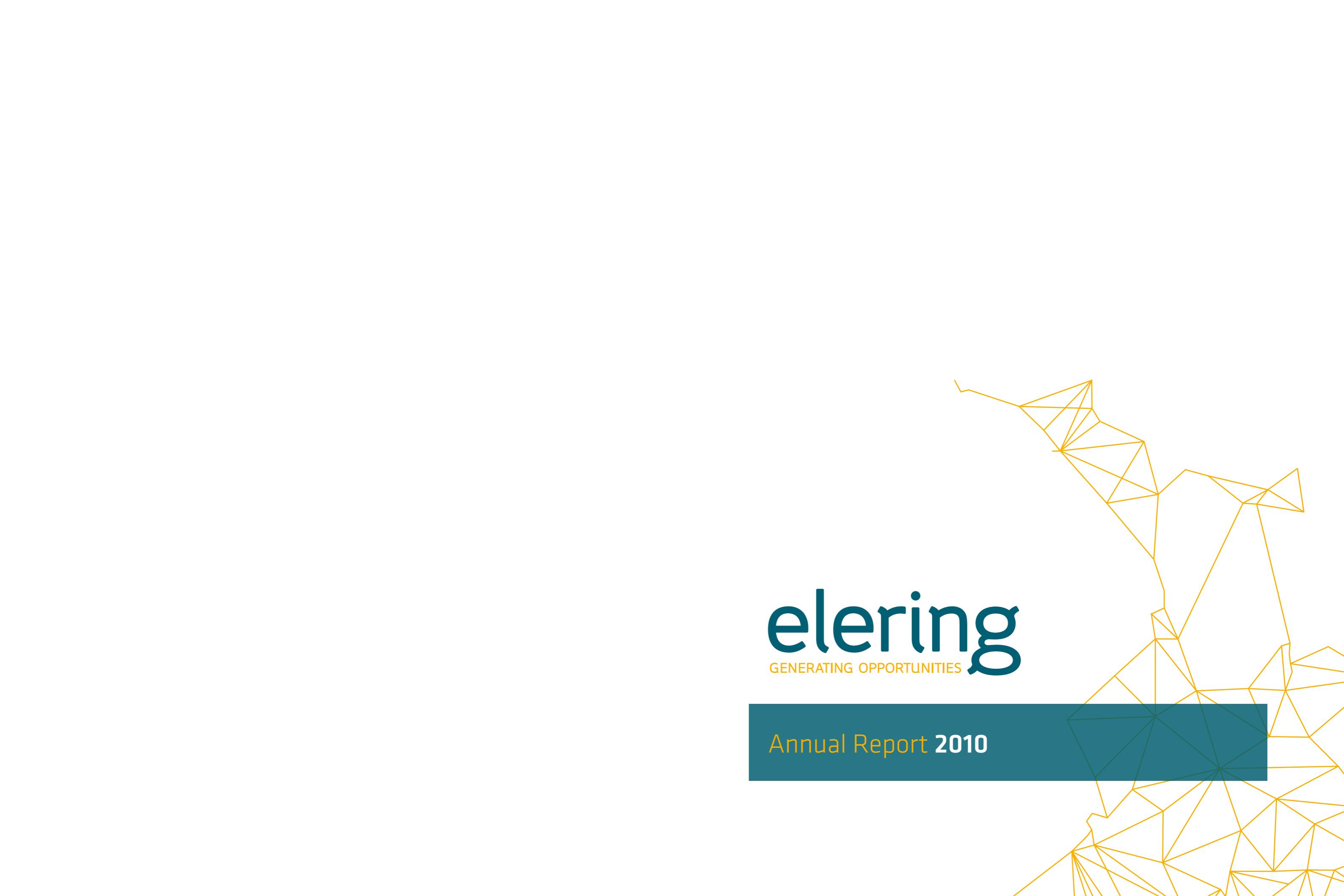




elering

GENERATING OPPORTUNITIES

Annual Report 2010



elering

GENERATING OPPORTUNITIES

Annual Report 2010



“ Estonia is one of the smallest countries in Europe. With our total area of 45,000 square kilometers and a population of 1,5 million, we are fit to be held in the palms of our bigger companions. But it is our culture and our history which make us genuinely part of Europe. Now it is Elering's turn to make the Estonian electrical system part of Europe as well.

Management Report of Elering's Annual Report

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Brief overview of Elering

Our values

Responsibility

We perceive our responsibility to supply the Estonian people with electricity. We are also responsible to all electricity market participants for the functioning of the Estonian electricity system as a whole at all times.

Equality

Elering creates conditions for the functioning of the electricity market. Free movement of energy is possible only if all electricity market participants are treated equally. Therefore, Elering guarantees equal conditions for electricity market participants – producers, sellers and intermediaries.

Dedication

We consider it important that everyone is dedicated to fulfilling their role. Dedication leads to continuous pursuit of development and prevents a standstill. So we can jointly fulfil our promise to the Estonian people to ensure security of energy supply.

Elering is the backbone of Estonian electricity system

Elering is an independent electricity system operator in Estonia whose main duty is to guarantee high-quality electricity supply to Estonian consumers at all times.

To ensure the sustainable functioning of security of supply as a crucial service, Elering maintains and develops a national transmission network and cross-border connections. Elering manages the Estonian electricity system in real time, ensuring the functioning of the transmission network as well as a balance between production and consumption. To this end, fast and competent decisions are continuously required in order to ensure the stable functioning of the electricity system.

To ensure long-term security of supply and energy security, we are working towards joining the energy markets currently isolated from Europe with the rest of Europe. For Elering, it means de-connecting the Estonian electricity system from the Russian one and integration into the electricity system of Central Europe.

The central background for our operations is an open electricity market. We are aware of our responsibility for ensuring the functioning of the electricity market and ensure equal treatment of all electricity market participants – producers, sellers, distribution networks and balance providers.

We believe that consumers must have a possibility and freedom to choose from whom to buy their electricity. We are working towards providing our producers with an unrestricted access to the Northern European market and the producers of that market with a possibility to sell energy to the Baltic market.

VISION 2020

Elering is an innovative leader in regional security of energy supply.

MISSION 2020

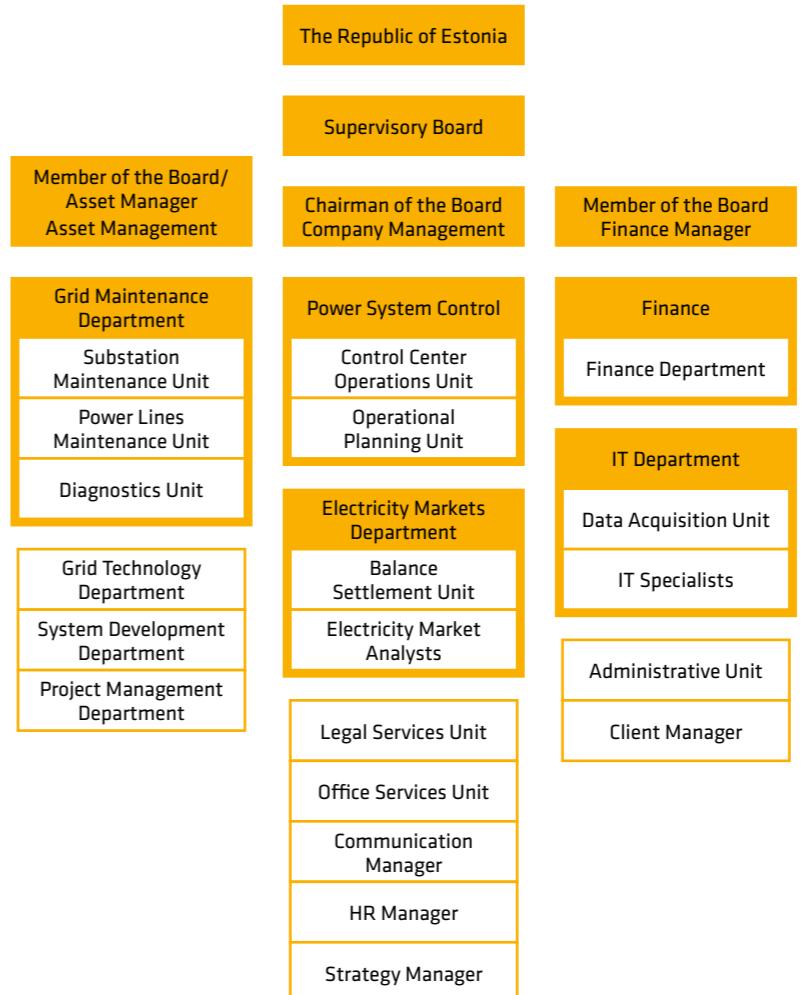
Elering is responsible for the functioning of the Estonian electricity system as a whole so that the high quality of electricity supply is guaranteed to consumers at all times. In order to provide a greater possibility to consumers to choose suppliers and to allow suppliers to freely choose their consumers, we are building a single electricity network and market in the European Union in collaboration with the other European system operators.

Investments in cross-border interconnections that ensure unobstructed movement of electricity between neighbouring systems and markets make up a significant part of our investment plan.

The responsible task imposed on Elering by law and its state ownership raise expectations for transparency of activities of the Company. Therefore, we look at disclosure of our operating information very seriously and with a high sense of responsibility. As the operator of the Estonian electricity system, we keep the public informed of the everyday functioning of our electricity system and contribute to discussions on the strategic choices of the Estonian energy sector.

The activities of Elering are focused on five main directions:

- planning and managing the functioning of the Estonian electricity system in real time
- ensuring the readiness of the main network
- maintaining the capacity balance of the Estonian electricity system
- developing all-Estonian electricity network of 110-330 kV
- providing the conditions necessary for the functioning of electricity market in real time



5252

km of high-voltage overhead and cable lines

150

substations

139

employees

43

average age of employees

350

MW of capacity of Estlink1 submarine cable between Estonia and Finland

Cross-border interconnections with Finland, Latvia and Russia

Elering
ensures the reliability
of the electrical
system at all times.



Statement by the Chairman of the Management Board

Elering has been noticed!

The year 2010 was a year when Elering proved itself as an independent system operator. Our results clearly confirmed that a decision to separate Elering with the assets of the system management and transmission system from Eesti Energia was the right one. We made a huge progress in guaranteeing energy-market-based security of energy supply to the Estonian people today as well as in the future.

Our activities as a centre of excellence for energy have been noticed in society. The current work provides a good basis for developing Elering into an innovative leader of regional security of energy supply in the entire Nordic and Baltic region. We have found a good balance between raising added value for owners and public functions. We wish to achieve the financial targets of the Company, and equally contribute to and actively participate in the process of developing the energy policy.

A sign of the growing role of the Company in the Estonian energy sector is a decision to transform Elering into a public limited company. The share capital of the Company will be EUR 140 million and the balance sheet total will be EUR 419 million. The Company will invest a total of EUR 500 million in development and real-time management of the Estonian electricity system over the next five years.

In addition to usual investments in development of the energy system, Elering faces a strategic challenge to guarantee security of electricity supply under the framework of European energy security policy objectives – to integrate the current so-called isolated energy islands into the rest of Europe. In the electricity sector, it means achievement of technical readiness for de-connecting the Baltic States from the synchronous regime with Russia and Byelorussia, and connection to the synchronous area of Central Europe. To determine a detailed action plan, the system operators of Baltic States, Poland and Germany will carry out a feasibility study concerning full synchronous connection to Central Europe by the end of 2012, after which the monetary amount and time-schedule of the project can be determined in a greater detail.

The vision of the EU energy sector – a single network, a single market – works in the interests of the Estonian energy system and, based on that development perspective, Elering is designing its strategy. The future opportunities of the Estonian energy sector lie in integration of energy systems into a network and we facilitate this process so that Estonian electricity consumers and producers would benefit from such development. In the interests of current and future producers and consumers, Elering must assume a leadership role in integration of energy systems. The uniting of energy networks and markets creates preconditions for developing electricity production, creating an alternative supply chain of natural gas, and guaranteeing security of supply with a good price to consumers. I believe that a single energy system will create a new perspective for our energy sector in terms of quality. The European Commission estimates that integration of electricity systems will make it possible to invest nearly 25% less in production capacities as compared to a situation where investments for guaranteeing security of supply should be made in the current, insufficiently integrated energy systems.

“ 2010 was Elering’s most triumphant year to date. Our biggest victories rose from successful financing and its outcomes which in turn will support the company’s further development.

Taavi Veskimägi
Chairman of the Board

Research shows that investments in the production capacities of an integrated electricity system are 25% more efficient than investments in the production capacities of the current isolated systems. Given the fast growing trend of energy prices, the actual benefit may be even greater.

In spring 2010, Estonia made the first long step towards joining a single electricity market, by opening up a part of the electricity market on 1st of April. Given the tradable quantities as well as general high reliability of the trading venue, the launch of the electricity exchange has proved to be a success in Estonia. With its expertise and experience, Elering will contribute in every possible way to expansion of NPS into Latvia and Lithuania in 2011 so that we could speak about a single Nordic-Baltic electricity market from 2014 onwards which should guarantee the best prices for consumers in a continuously operating competitive market and the best opportunity for suppliers to develop their economic activities.

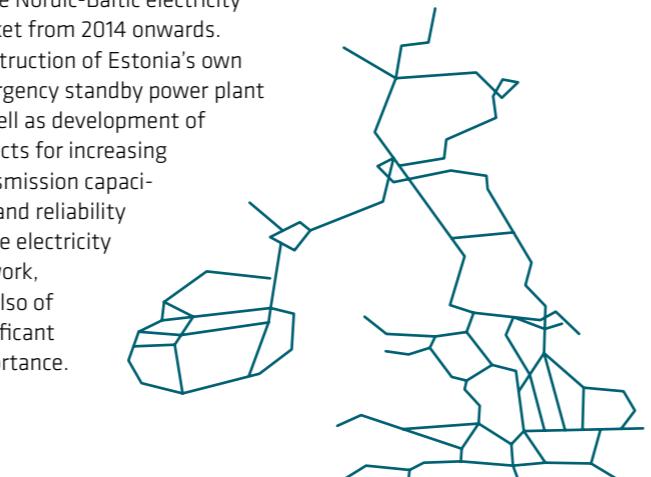
In 2010, the largest fundamental change for companies was shifting the focus from security of electricity supply to wider security of energy supply in Estonia. By a decision of the Government of Republic, the Company was obligated to develop gas-related competence in Elering in addition to its electricity-related competence. While fast and significant positive changes in the electricity sector have recently taken place in the Baltic Sea region according to the agreements between the European Commission and Member States concerning the development of the energy market, then no such development has taken place in the gas sector. Deriving from the developments in the energy sector and a significantly changed situation in global gas markets, the Government of the Republic has set an aim towards faster liberalisation of the gas market in Estonia, notwithstanding an exemption provided by the on directive on the internal market of natural gas.

In addition to preparations for launching a new business line, I would highlight a few examples of the most significant steps made by Elering in 2010 below:

- After separation from Eesti Energia, establishment of a support service system of the Company, notification of society of the role and functions of an independent system operator;
- Based on the assessment of the functioning of Elering's network during the storms in August and December, we may say that we have done excellent work. The greatest acknowledgment of our work is if Elering is unnoticeable for consumers. And fortunately electricity consumers did not have many reasons to notice us a lot in 2010. We guaranteed good security of supply to consumers.
- In 2011, Elering will face new challenges. An important part of them includes investments in cross-border interconnections, purchase of EstLink 1 and establishment of EstLink 2 which will provide an opportunity to develop a single Nordic-Baltic electricity market from 2014 onwards. Construction of Estonia's own emergency standby power plant as well as development of projects for increasing transmission capacities and reliability of the electricity network, are also of significant importance.

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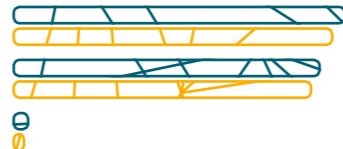
Key indicators of Estonian electricity system

Electricity consumption

TWh

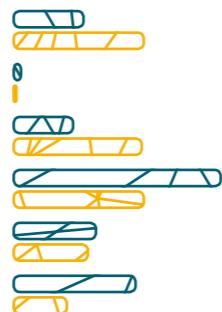
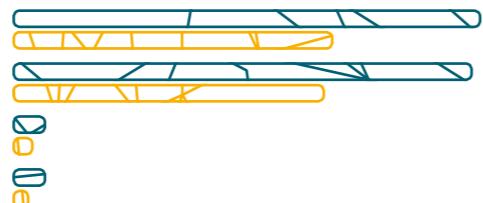
Electricity balance sheet

	2010	2009	Change
Electricity consumption in Estonia	8.01	7.69	4%
Elering's domestic transmission service for consumption	7.43	7.17	4%
Elering's network losses	0.38	0.33	15%
Electricity output in Estonia	11.33	7.69	47%
Electricity output directed to Elering's network	11.13	7.50	48%
Output of renewable energy in Estonia	0.86	0.51	70%
Output of renewable energy directed to Elering's network	0.77	0.41	90%



Physical electricity flows

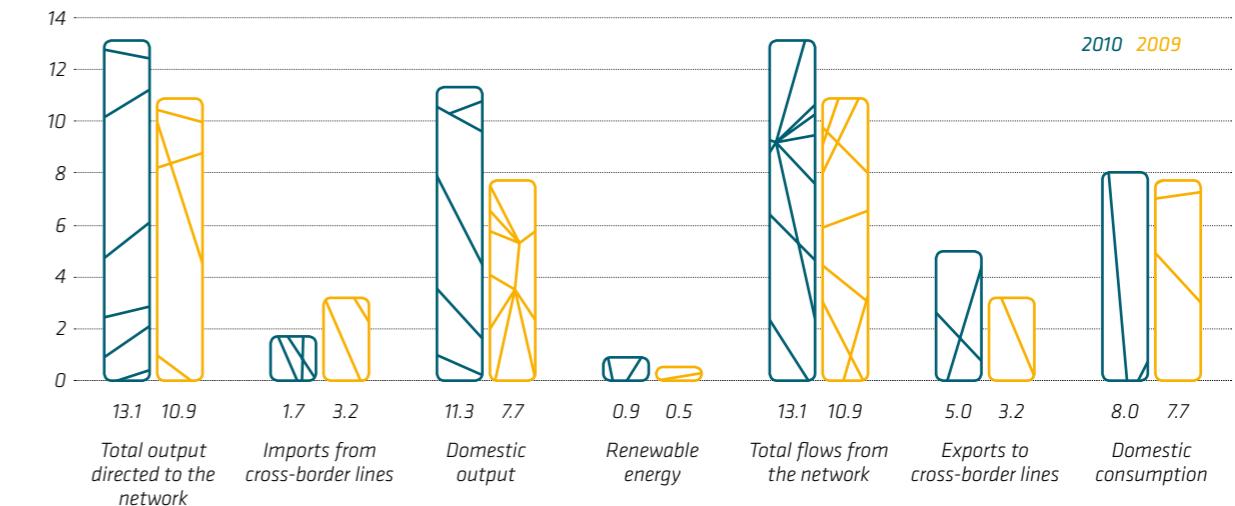
	2010	2009	Change
Imports from cross-border lines	1.73	3.22	-46%
incl. imports from Finland	0.23	0.08	185%
incl. imports from Latvian and Russian lines	1.50	3.14	-52%
Exports to cross-border lines	5.04	3.22	57%
incl. exports to Finland	2.07	1.88	10%
Incl. exports to Latvian and Russian lines	2.98	1.34	122%



In 2010, electricity consumption in Estonia amounted to 8.01 TWh, which corresponds to an increase of 4% as compared to 2009 (7.69 TWh). Elering's domestic transmission service totalled 7.43 TWh, accounting for 93% of the share of Estonian domestic electricity consumption. The quantity of electricity transmitted by Elering for domestic consumption also increased by 4% as compared to 2009.

Electricity production

TWh



While in 2009 the share of electricity produced in Estonia was close to consumption, in 2010, Estonia started to export electricity. In the country, 11.3 TWh of electricity was directed to the network and production increased by 47% as compared to 2009. Growth in production and pick-up in exports was strongly driven by the opening of the electricity market to eligible consumers.

Electricity trade

TWh

	2010	Share
Total imports:	1,34	
incl. Estonian-Latvian border*	1,08	81%
incl. trade between Estonia and Finland	0.26	19%
incl. imports through electricity exchange (from 01.04.2010)	0.53	
incl. imports based on bilateral agreements	0.81	
Total exports:	4,66	
incl. Estonian-Latvian border*	2,67	57%
incl. trade between Estonia and Finland	1,99	43%
incl. exports through electricity exchange (from 01.04.2010)	2,25	
incl. exports based on bilateral agreements	2,41	

Electricity was exported to the Nordic countries and Baltic States. During 2010, electricity was mainly exported to Finland accounting for 43% of total exports. Exports to Latvia were 32% and exports to Lithuania, 25%. Of the total imports of electricity, 54% was made up of imports from Latvia, 27% from Lithuania and 19% from Finland.

* export and import quantities at the Estonian-Latvian border comprise supplies of electricity trade of Estonia-Latvia and Estonia-Lithuania in aggregate.

Quality indicators

In 2010, there were 27 switch-offs involving consumer service interruptions in the electricity system of Elering, which is at the same level as in the previous years.

Due to this, consumers did not receive nearly 207 MWh of electricity which is less than 0.003 % of our total consumption of 7,812 GWh.



Summary of the financial year

Estonia's macroeconomic developments

In 2010, Estonia's economic development and policy were mainly characterised by preparations for the euro changeover and recovery of economic growth. As a result of meeting the criteria of the EU Treaty, the European single currency euro has been in circulation in Estonia since 1st of January 2011. This gives assurance to foreign investors that the environment here is sufficiently reliable for making capital investments. The country's economy recovered quickly from the global economic and financial crisis thanks to the implemented economic policy and turned to growth in the second quarter of 2010.

In addition to the weather conditions and existence of cross-border transmission capacities, the economic development level is the main factor that influences electricity production and consumption quantities. It arises from the relative welfare aspect where electricity consumption per capita is the largest in countries with higher living standards, as well as from the aspect of economic growth rate where several new companies (that consume electricity) emerge during the growth phase of economy.

Estonia's economic growth rate increased as much as to 6.7% in the fourth quarter of 2010, the GDP rose by 3.1% during the year. The major share of annual growth, i.e. 2.6%, is attributed to fast growth of manufacturing industry. The other factors contributing to the GDP growth included an increase in the added value of energy and financial intermediation sectors. In 2010, the output of industrial companies increased by 23% year-over-year. In December, growth in the manufacturing industry reached ca. 40%, while the industrial production remains close to the level of 2005. Growth in industrial production was mainly driven by foreign demand, but also demand in the domestic market continued to rise throughout the year.

In 2010, the output of energy sector increased by 31% year-over-year. Real growth of the electricity output made up nearly 50%.

Positive developments in our main export markets contributed to fast recovery of Estonia's economy and exports. The total export of goods is exceeding the pre-crisis level. With the improved support of foreign demand, the export of goods and services in real volumes increased by 22%, incl. exports of goods by 33%. Growth in exports of services was modest. Total imports of goods and services increased by 21%, including imports of goods by 25%. In summary, Estonia's foreign trade balance improved. The ratio of net export to the GDP was 6.7%, being the best rate over the last 16 years.

Electricity output increased mainly as a result of the joint effect of increased energy demand due to the pick-up boom in production and growth in exports of electricity. Exports of electricity were also significantly influenced by the shut-down of Ignalina nuclear power plant in Lithuania. Exports of electricity increased to EUR 209 million, accounting for 2.4% of the total exports of all goods. At the same time, the share of imported electricity fell to 0.55%. Thus, electricity significantly contributed to improving Estonia's foreign trade balance.

“ We successfully set up an independent financial management system and prepared the financing for the coming years, which will see a sharp leap in investment.

Peep Soone
Member of the Board

EUR '000	Total goods	Electricity	% of goods	incl. Lithuania	incl. Latvia	incl. Finland
Exports, 2009	6,481,386	111,289	1.72%	922	72,006	38,362
Exports, 2010	8,746,841	209,446	2.39%	51,743	73,270	84,434
Imports, 2009	7,271,928	66,310	0.91%	46,846	15,518	3,946
Imports, 2010	9,244,710	50,995	0.55%	8,045	29,867	13,082

During the rest of the year, the financing of investments for the upcoming years were prepared. To this end, long-term loan agreements were concluded with the European Investment Bank (20 years) and Nordic Investment Bank (15 years) in the total amount of EUR 100 million (EEK 1,565 million). The funds will be withdrawn in 2011-2014.

Key financial indicators

The final consumption expenditures of households started to increase in the third quarter and the total capital investments in non-current assets in the fourth quarter. Recovery of private consumption provides a growth incentive mainly to companies focused on domestic demand. Domestic demand is expected to further recover owing to the high level of the consumer confidence that has risen again at the beginning of 2011.

In 2010, the GDP increased despite a decline in the number of the employed and the total number of working hours. As a result of this, labour productivity per hour worked increased by nearly 6% year-over-year. Thus, efficiency of the GDP creation improved in 2010. Despite growth in salaries during the last quarter, the share of labour expenses decreased and the share of profits of companies increased in the added value.

Fast economic recovery, however, led to a significant increase in demand for labour at the end of the year. In the fourth quarter, the number of people employed was 14,700 higher than in the third quarter of the same year and 12,400 higher than in the last quarter of 2009. The Ministry of Finance estimates that unemployment will continue to decline steadily in the next quarters. In the fourth quarter, the rate of unemployment fell for the third successive quarter already and reached 13.6% or 93,300 people.

In the fourth quarter of 2010, the average gross wages increased by 3.9% year-over year to EUR 814. That growth in wages was mainly achieved on account of irregular bonuses and additional remunerations paid at the end of the year, the share of which dropped during the crisis.

In fiscal policy, the government has set an objective to restore the nominal budget balance by 2013. As a result of a strict policy, budgetary expenses have been frozen and reduced during the last years. In 2010, the revenue of EUR 5.61 billion or 103.8% of the target flowed into the state budget. Expenditure amounted to EUR 5.6 billion or 95.8% of the target.

In 2010 the main groups of revenue were:

1. electricity transmission service (~78% of revenue)
2. balance service (~18% of revenue)
3. other services (~4% of revenue).

Elering's revenue totalled EEK 1,392 million (2009: EEK 1,182 million) and operating expenses totalled EEK 1,067 million (2009: EEK 862 million). The increase in revenue and expenses was mainly caused by an increase in the sales of balance service - EEK 145 million in revenue and EEK 141 million in expenses. In addition, growth in expenses is also attributable to a one-off write-down and write-off of transmission lines in the amount of EEK 57 million in conjunction with investments in new lines on the same route.

The Company finished the year with the net profit of EEK 212 million (2009: EEK 82 million) as a result of which return on equity (ROE) was 9.0%. The total profit will be reinvested in electricity transmission equipment.

In the balance sheet, net working capital (current assets less current liabilities) changed significantly. While it was negative at the end of 2009, we managed to achieve positive value by the end of 2010 (EEK 400 million). At the same time, cash in short-term deposits and bank accounts totalled EEK 627 million.

Cash flows from operating activities amounted to EEK 730 million (2009: EEK 467 million), significantly exceeding the amount of EEK 408 million (2009: EEK 490 million) paid for acquisition of non-current assets.

At 8th of January, we refinanced all loans taken from our previous owner Eesti Energia AS with a new syndicated loan (EEK 2,926 million). For financing Estlink 2 project, the European Union granted a total of EUR 50 million (EEK 783 million) to Elering, of which EUR 15 million (EEK 235 million) was transferred in 2010. At the end of the year, the owner increased the share capital of Elering by EEK 91 million with the purpose of increasing the Company's creditworthiness in conjunction with a large-scale investment programme for the upcoming years.

Financial figures

EEK million	2010	2009	2008/09*	2007/08*	2006/07*
Revenue	1,392	1,182	1,278	1,190	1,127
Operating profit	325	320	389	380	329
Income tax	0	128	0	0	0
Net profit	212	82	276	259	209
Equity	2,502	2,200	2,752	2,476	2,218
Assets	6,562	5,756	5,559	5,239	5,280
EBITDA	695	624	695	694	638
Investments	420	485	606	226	585
Dividends	0	480	0	0	0

Ratios

ROE	9,0%	6,1%	10,5%	11,0%	9,9%
Equity/Assets	38%	38%	49%	47%	42%
Net Borrowings/EBITDA	3,3	4,7	3,1	3,3	4,3

Financial figures

EUR million	2010	2009	2008/09*	2007/08*	2006/07*
Revenue	89	76	82	76	72
Operating profit	21	20	25	24	21
Income tax	0	8	0	0	0
Net profit	14	5	18	17	13
Equity	160	141	176	158	142
Assets	419	368	355	335	337
EBITDA	44	40	44	44	41
Investments	27	31	39	14	37
Dividends	0	31	0	0	0

* The financial year lasted from April to March.

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

EBITDA = Operating profit + depreciation

Net debt = Interest bearing borrowing - cash and bank deposits



Development of the electricity network

The Estonian transmission network is developed with a view of guaranteeing long-term security of supply to consumers; therefore it is necessary to look ahead several decades when making current decisions. Security of energy supply combines a high-quality and reliable electricity network as well as access of sufficient production capacities to the network and the well-functioning electricity market. Over the last ten years, Elering has upgraded a large share of major substations. It represents a strong basis for good reliability of the domestic electricity network. During 2010, a substation in Kiisa that is an important pillar for security of supply to Tallinn and a substation in Viljandi were completely upgraded.

In 2010, vigorous progress was made in construction of EstLink 2

In 2010, priority was given to the activities that guarantee access of sufficient production capacities to our electricity market, the activities related to the development of a marketplace necessary for the functioning of electricity markets. Development of the marketplace primarily means stronger connection of the Estonian electricity network with the networks of Nordic-Baltic single market area. In 2010, great progress was made in construction of Estlink 2 interconnection between Estonia and Finland, when construction contracts were signed with the Finnish main grid operator Fingrid. The commissioning of the cable is planned for the beginning of 2014. Immediately before signing of the procurement contracts, the reinforcement of electricity lines in Estonia was completed, which is a precondition for connecting Estlink 2 to the Estonian network at Püssi substation and for granting the total connection capacity to the disposal of the electricity market – full reconstruction of the 330 kV line between Balti and Püssi substations was completed in 2010. The electricity line between Eesti and Püssi substations was already reinforced during partial renovation work in 2009.

For connecting new production equipment to the electricity network in Estonia, Elering completed the construction of two new connection points in 2010 – a wind park in Löpe substation and a combined heat and power station in Metsakombinaadi substation – to be connected to the network. As at 31st of December 2010, the construction of 13 network connections with total capacity of 565 MW was completed which are necessary for connecting wind power plants to Elering's network. Pärnu combined heat and power station, which was connected to Metsakombinaadi substation, is the third similar project in terms of capacity following the stations in Tallinn and Tartu that were connected with Elering's network (with capacity of 25 MW) in recent years.

“ We signed a tender contract with Fingrid for the construction of a second DC cable between Estonia and Finland - making it historically the largest single investment in the Estonian electricity system.

Kalle Kilk
Member of the Board

Development plan of pan-European network simplifies collaboration of transmission system operators (TSO) in developing the network

The year 2010 was a breakthrough year in terms of planning development of pan-European electricity network, as the joint Ten Year Network Development Plan (TYNDP) of all European main transmission system operators was published. The main objective of that plan is to simplify and better coordinate the creation of a European single electricity market. TYNDP also helps electricity market participants perceive which changes of direction may be expected to take place in transmission capacities in the near future in order to make more informed strategic decisions of their company. Without development of a crucial focused network, it is very difficult to fulfil the EU's ambitious objectives of renewable energy development and thus TYNDP as a coordinated development plan cannot be underestimated.

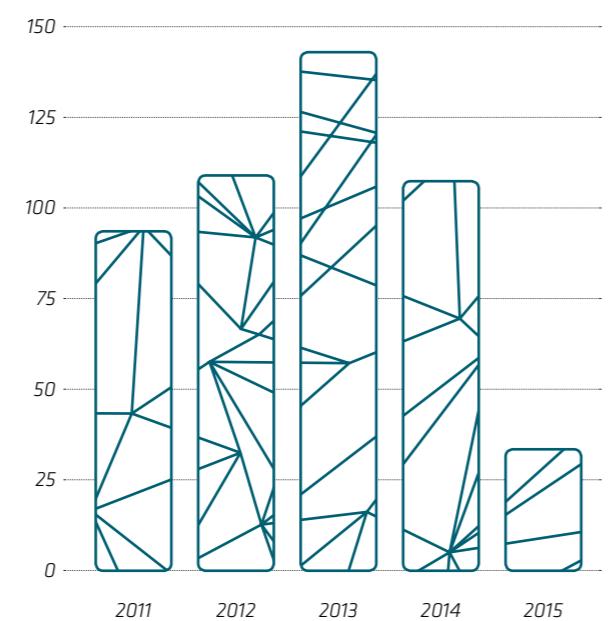
It is also important that TYNDP functions as a certain kind of awareness raiser for energy-related issues because with the help of this development plan, the EU vision shapers as well as the people who are dealing with energy issues through their business or private interests may get a better understanding as to which trends in electricity systems will result from the EU general policies.

While the key word in 2010 for developing the Estonian electricity network was internationalisation, while keeping focus on the security of supply of domestic consumers, the investment plans for the next five years are prepared on the exact same basis.

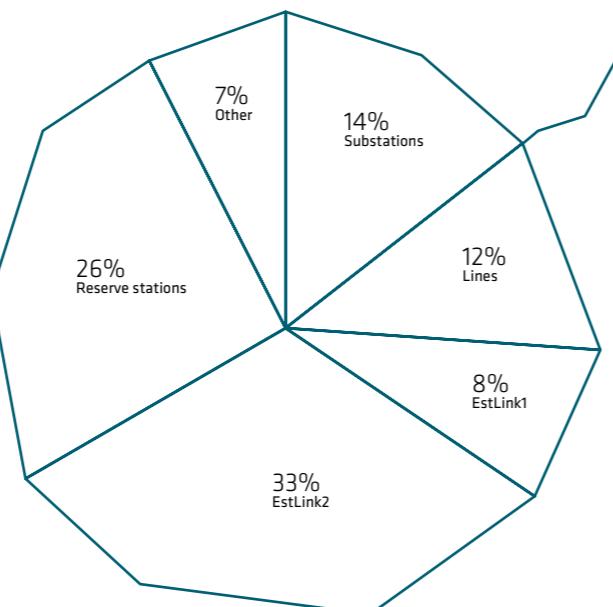
Of the projects with a more significant financial impact on Elering, we may highlight the completion of EstLink 2, the buy-out of EstLink 1 from its current owners, construction of an emergency reserve power plant, and construction of 330 kV overhead transmission line of Tartu-Viljandi-Sindi.

The total volume of capital expenditures in 2011-2015 is EUR 500 million, the chart below illustrates their distribution by years.

Elering's investments 2011-2015 / MEUR



Investments by objects 2011-2015



Development of the electricity market

One of the most important objectives of the EU energy policy is the creation of a smoothly functioning single electricity market where the security of supply as well as the fair and transparent price of electricity is guaranteed in the competition of producers. For Estonia, a single Nordic-Baltic electricity market is a precondition for this. As a system operator, Elering is responsible for providing preconditions in the electricity market for its functioning – existence of an electricity exchange, sufficient transmission capacities, and existence of legislation and electricity market rules that are harmonised with the neighbouring systems. Current activities must ensure that we are ready for integration and are competent in order to have a say in developing the principles of a single electricity market. The decisions and action plan that were made under the Baltic Electricity Market Interconnection Plan (BEMIP) in summer 2009 form a very good basis for this.

2010 was a year of significant changes for the Estonian electricity market:

- | | |
|--|-------------|
| ▪ Elering's spin-off | 27 January |
| ▪ Adoption of amendments to the Electricity Market Act by the Riigikogu (Parliament) | 28 January |
| ▪ Implementation of amendments to the Electricity Market Act | 28 February |
| ▪ Notice by Nord Pool Spot (NPS) of opening a price area in Estonia | 01 February |
| ▪ Opening up 35% of the electricity market | 01 April |
| ▪ Opening a price area of NPS Estlink | 01 April |
| ▪ Renaming NPS Estlink to NPS Estonia | 01 October |
| ▪ Joining NPS Elbas | 20 October |

After entry into force of the legal amendments that was a prerequisite for opening up the electricity market, it was possible to open an electricity power exchange in Estonia. As a system operator, we decided to join the platform that has been in place in the Nordic countries for nearly 15 years and concluded a contract with Nord Pool Spot. The electricity power exchange was introduced with a view to mainly offer equal opportunities to market participants to sell their products or purchase electricity. Trading on the electricity power exchange mainly represents an alternative to bilateral contracts. It is also important that a transparent, market-based price will be created for electricity; analysis of price dynamics provides investors and producers a basis for assessing the market situation and making investment decisions.

Today, Nord Pool Spot represents the values that are manifested in provision of their service: reliability, safety, innovation, certainty, openness and competence.



“ Our goals for the coming years are the integration with the Nordic electricity market and the full opening of the electricity market in 2013.

Ingrid Arus
Head of Electricity
Markets Department

Allocation of transmission capacities

One of the preconditions for opening the NPS Estonian price area also included the existence of transmission capacities and, in case of their insufficiency, mechanisms for market-based allocation of transmission capacity.

A significant decision was made by the owners of EstLink 1 submarine cable with the capacity of 350 MW between Estonia and Finland to lease the total cable capacity to Estonian and Finnish main network operators – Elering and Fingrid, and through this also to the NPS electricity exchange. In the priority order, the cable is made available to a day-ahead market and the remaining free part of the cable is made available for allocation to an intra-day market. NPS allocates transmission capacity by using the so-called implicit auction method that is currently the most efficient allocation model in the electricity market, because due to this electricity always flows from the lower price area to a higher price area and both systems will benefit.

The chart below illustrates energy flows between Estonia and Finland by month, compared to regions with average prices.

To allocate free transmission capacity on the border of Estonia and Latvia, a special method was developed in collaboration with NPS – optimisation of capacities. An implicit auction as a mechanism for allocating transmission capacities requires the existence of an electricity exchange as a market participant and hour-based electricity prices in both systems. Optimisation of capacities on the border of Estonia and Latvia will be used until the opening of the NPS price area in Latvia.

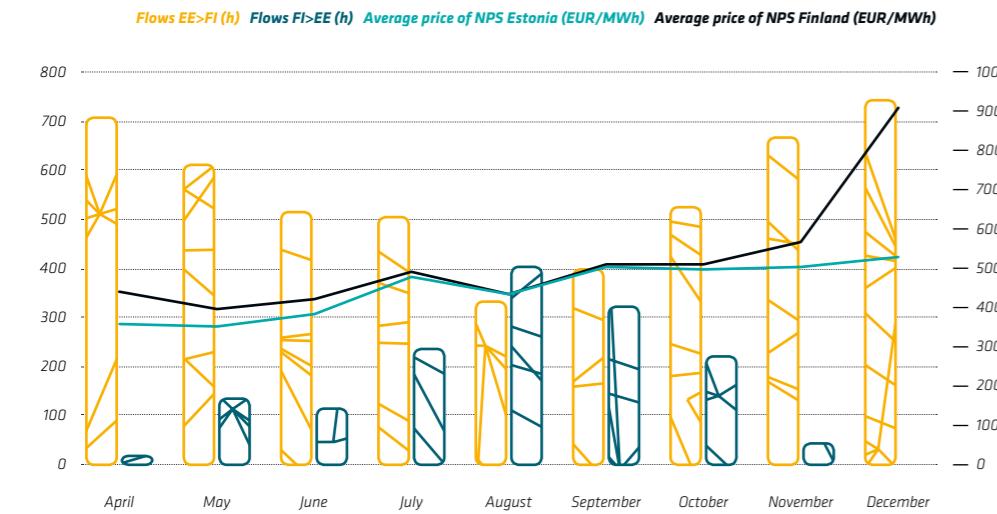
By agreement with the Latvian system operator, part (20%) of the transmission capacity on the border of Estonia and Latvia will also be allocated at a weekly explicit capacity auction. The functions of an explicit auction organiser are currently fulfilled by Elering, auctions will be organised until the opening of NPS Latvia price area. As a result of the explicit auction of transmission capacities organised since last May, a total of EUR 433.5 thousand was earned from selling capacities, which were divided between Latvian system operator AST and Elering in equal parts. In accordance with the requirements of the EU regulations, income received from congestion will be used to cover investments for reducing congestion.

Results for the first nine months of the open electricity market:

- Actual openness of electricity market 28.4%
- Eligible consumers 208*
- Traders on electricity exchange in the Estonia price area 15
- Volumes of electricity purchased from the power exchange 2.8 TWh, of which 1.8 TWh was purchased in Estonia
- Share of domestic consumption purchased from electricity exchange 32% on average
- Volumes of electricity sold to power exchange 3.8 TWh, of which 3.5 TWh was sold from Estonia
- Daily average purchase volumes 4.5 GWh - 14.3 GWh
- Daily average sales volumes 9.5 GWh - 16.4 GWh
- Congestion income earned by owners of EstLink1 cable EUR 18.9 million

* As of January 2011

Energy flows vs. average price of NPS Estonia and Finland



The price area of NPS Estonia, unlike other NPS price areas, allows Latvian and Lithuanian market participants to trade there on the condition that a trade guarantee agreement is concluded between system operators of those countries (AST and LITGRID) and Elering. The existence of this contract obligates the parties to be an open supplier for market participants that are part of their system but operate in Estonia.

The following table presents comparison of average prices of NPS Finland, NPS Estonia and Lithuanian electricity power exchange Baltpool (EUR/MWh).

Month	Average price of NPS Estonia	Average price of NPS Finland	Average price of Baltpool
April	35.79	43.71	37.50
May	34.81	39.47	43.34
June	38.45	41.96	44.08
July	47.90	48.76	49.92
August	56.62	43.21	59.74
September	50.63	51.20	54.28
October	49.47	51.24	51.78
November	50.35	56.63	45.70
December	52.77	91.34	47.82

Reasons for price differences that had an impact in 2010:

- Large export capacity of Estonian producers;
- Deficit in Lithuania and Latvia: the total import of electricity in Lithuania made up over 60% of the total domestic consumption, mainly caused by the shutdown of Ignalina nuclear plant at the end of 2009, also absence of production with inexpensive variable costs in Lithuania;
- Low fulfilment of hydro-reservoirs in Nordic countries – on average only 53% in 2010, dropping by ca. 15% as compared to last year;
- Overloads on the border of Estonia and Latvia.

In the upcoming years, work will be continued for integrating the Estonian electricity market into the Nordic electricity market. Accession to the balance market is also still ahead. Of the major steps, we should also mention the action plans and preparations to be made for the complete opening up of the electricity market in 2013.

Estonian power system operation and control



“ Every day, the dispatch centre performs its utmost best so that consumers would never have to worry about the poor quality or unstable electricity supplies.

Valeri Peterson
Head of Power System Control Centre

Elering's Power System Control Centre has the obligation to guarantee security of supply at all times and has been responsible for the balance of the Estonian electricity system.

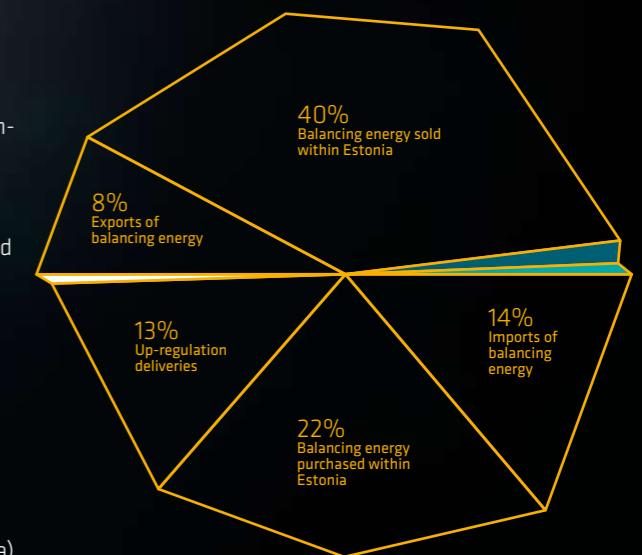
Operational planning, monitoring of power system parameters, supervision of switching, monitoring of the state and network power equipment – this are the most vital targets for reliable and safe real time operation of Estonian Power System.

As the Estonian main network is closely integrated into the main grid of the neighbouring systems mainly in a synchronous manner (except for Finland), one of the important functions of Elering's Power System Control Centre is to collaborate with Power System Control Centres of TSO's of neighbouring countries (Latvia, Lithuania, Byelorussia, Russia).

Elering's Power System Control Center is responsible for keeping the balance of Power System due to prescheduled timetable according to conditions specified by inter-governmental agreements. For that purpose Control Centre people activate the regulation offers in the case of imbalance condition and put into use the emergency reserves in emergency situations.

According to the legislation, the balance of each market participant must be in equilibrium, i.e. the amount of electricity produced and purchased by it must correspond to the amount of electricity sold and consumed by it. During those hours when the balance of a balance provider is negative, Elering shall sell to the market participant the deficient part and in the opposite case, shall purchase the excessive part.

In 2010, we imported 94 GWh of balancing energy to the Estonian electricity system and exported 53 GWh of balancing energy. To guarantee Estonian capacity balance, Elering purchased 88 GWh upward regulation of supplies and 10 GWh of downward regulation of supplies. In addition, 4 GWh of the system service was sold as management supplies that were used by other system operators to maintain their balance or resolve any emergency situations in their system – e.g. to reduce overload in the cross-section.



Prices of balancing energy

In 2010, the highest sales price of balancing energy was 485.85 EUR/MWh that was fixed at 29 November when regulation supply was purchased from Finland to compensate for the deficit balance in the system caused by falling temperatures.

Prices of balancing energy in 2010	Unit	Average price	MAX price	MIN price
Sales price of balancing energy	€/MWh	47.87	485.85	16.40
Purchase price of balancing energy	€/MWh	44.69	334.00	2.00
Prices of balancing energy in 2009				
Sales price of balancing energy	€/MWh	31.12	109.32	0.56
Purchase price of balancing energy	€/MWh	30.15	108.33	7.34

Research and development activities at Elering

Elering

is setting up a centre of excellence for the energy industry, which will work closely with every other competent party.

Elering considers it strategically important to increasingly contribute to research and development activities. In 2010, direct expenses of research and development activities (exclusive of personnel and general expenses) accounted for 0.3% of the total expenses of Elering. In the upcoming years, we want to contribute more resources to research related to electricity markets, networks and management.

Modelling of the electricity system in Elering

All European system operators prepare national development plans for the electricity network based on the analysis of the electricity market stimulating electricity production and consumption in the region as well as on network calculations stimulating the actual technical possibilities. Elering has both the technical (network calculation and market models) and human competence for continuous performance of such market analyses. We will also involve different partners in conducting research in the future.

The main objective of an electricity market analysis is to find intra-regional bottlenecks (technical restrictions on transmission capacities) on the basis of different electricity production and consumption scenarios, and to identify as to which additional investments in increasing transmission capacities would lead to the largest socio-economic benefits.



Possibilities for connecting wind power plants to the system

In 2010, the project "Technical possibilities for connecting wind power plants to the Estonian electricity system" was completed. In order to identify the opportunities of system operator for wider and more efficient integration of wind energy into the Estonian electricity system, research was conducted with a goal to analyse technical restrictions on integration of electricity produced from wind into the Estonian and Baltic electricity system and its impact on the functioning of electricity market until 2016.

The research highlighted that wind power plants with the total capacity of up to 900 MW can be technically connected to the electricity system in 2016. In such a case, the quantity of energy is quite small which can be potentially restricted by Elering. Today, wind energy with the total capacity of 162 MW has been installed in the Estonian electricity system. Capacity is expected to double by 2012. The most important preconditions for connecting wind energy of 900 MW to the system include sufficient interconnections with Nordic countries (EstLink2), an open and well-functioning electricity market of the Baltic States and Estonia, and raising the accuracy of forecast output of wind power plants.

Impact of wind energy on the stability of the system

In 2008-2010, research was conducted with a goal of analysing the impacts derived from the given scenarios on stability of the electricity system. The programme used for the analysis may also be used as additional means of analysis in the future for analysing connections of wind turbines and future scenarios (perspective developments).

Feasibility study on connection to Central European frequency area

In collaboration with system operators of neighbouring countries, a feasibility study will be carried out to connect the Baltic States to the Central European frequency area. Synchronous work with the Central European frequency area means that the frequency of the electricity system in our region would be regulated by European and Baltic power plants. The frequency of electric current of the Baltic States is now rigidly related to the frequency of Russian joint energy system to which the Estonian, Latvian and Lithuanian energy systems belong together with the Russian and Byelorussian systems.

The initial results of the working group concerning the technical, economic and organisational aspects of a change-over to the synchronous work with the Central European frequency area will become clear by the end of 2012 when actual preparations may be launched for performance of activities necessary for the synchronous work. It will then be also possible to determine the time period required, in case of different connection options, for full integration into the Central European frequency area.

A precondition for the synchronous work is the enforcement of national electricity networks as well as the creation of additional connections between the Lithuanian and Polish energy systems. In addition, it is probably necessary to update the management and regulation systems of existing power plants.

Forecasting systems for system management

To make the management of the electricity system more efficient, two projects were prepared and will be implemented during 2011:

- load forecasting system – with the objective to outsource a full solution for short-term forecasting of the electricity system load (up to 14 days in advance);
- forecasting system for wind turbines – with the objective to outsource the service to forecast the output of wind power plants 0-72 hours in advance.

Concept of a smart electricity grid

Elering considers it important to develop a smart electricity grid. To this end, we continue to perform the necessary activities at the level of the transmission network and carry out projects related to management of the consumption side in collaboration with partners in 2011-2012.

In comparison with the current electricity network, the smart grid includes innovative solutions and services, including smart monitoring, management and data connection as well as self-correcting technologies in order to make a better use of the electricity network and existing production equipment, and to allow consumers to participate in optimising the system.

Elering continues to develop smart grid technologies in transmission network according to its strategy and investment plan. By using new technologically advanced measures, high-voltage transmission systems can be changed to self-correcting smart grids. We may state that the current transmission network is already quite similar to a smart grid as the criteria of a smart grid that are used for describing transmission networks are substantially met or will be met in the near future.

Future energy savings largely depend on active participation of electricity consumers in the electricity market. This may be understood as follows:

- flexibility upon choosing an electricity seller, based on the offered price;
- possibility to make a choice among different producers and electricity produced from different energy sources;
- possibility to (automatically) regulate the volumes and time period of electricity consumption of different equipment, lighting sources and heating dependent on the current need and electricity price;
- possibility to store electricity (e.g. batteries of electrical cars) and to use the stored electricity during higher price hours;
- sending energy stored by consumers back to the network.

EU climate and environmental policy, Elering's activities for achieving the objectives



Energy and its security of supply are of critical importance for the functioning of a modern society. At the same time, the majority of energy is received by using fossil fuels that are non-renewable energy sources and their use causes creation of hazardous emissions in the environment and leads to climate changes. Furthermore, resources of fossil fuels are unevenly spread around the world; therefore a majority of the EU's need for energy is imported. Those facts underpin the EU energy policy that focuses on environmental protection and combating potential consequences of the climate change on the one hand and increasing energy security and security of supply on the other hand. In addition, the EU's priority and important policy direction is to improve the functioning of the EU internal energy supply system through market-based mechanisms, competition, integration of different market parts and energy savings. By achieving those objectives, it is possible to reduce the EU's dependence on fluctuations of oil and gas prices, to create a more competitive EU energy market, and to facilitate development of sectoral technologies and creation of jobs.

As a result of implementing the climate and energy package, the EU should be able to achieve the objectives set for 2020:

- To reduce energy consumption by 20%.
- To reduce greenhouse gas emissions by 20% as compared to 1990; by 30% if the rest of the world joins the global climate agreement and also developing countries assume obligations.
- To increase the share of renewable energy in energy consumption to 20% (currently approx. 8.5%).
- To increase the share of bio-fuel in fuels used in the EU transport to 10%.

Renewable energy in Estonia

Based on the EU renewable energy directive 2009/28/EC, in order to achieve the established objectives, Estonia must ensure that the share of renewable energy will account for 25% of the final consumption of energy, incl. 10% of fuels used in transport.

Estonia as well as the other EU Member States view development of renewable-energy-based electricity production and integration of energy networks as one of the main measures to achieve the objectives established for renewable energy. In order to perform the EU climate and energy saving objectives, each Member State has promised to increase production of electricity from renewable energy sources and facilitate saving of primary energy through adoption of more efficient technologies.

To perform the assumed obligations, Estonia has established grant schemes with a view to increase investments in production of electricity from renewable energy sources and in efficient combined production of heat and power which ensures primary energy savings through efficient combined production process.

Elering's role in supporting renewable energy and electricity produced by an efficient combined production mode is to be the payer of grants and the collector of service fees to be paid to finance the grants. The fee is paid by all network operators that provide network services, giving us relevant information. To receive the grants, producers have to submit applications and invoices to us. Network operators to whom producers have been connected are also required to give us information on hourly energy quantities supplied to the network.

Renewable electricity is expected to account for 5.1% of gross consumption according to the target for 2010 under the development plan of the electricity sector until 2018. The share of electricity produced in combined heat and power plants should be at least 20% in 2020 according to the target.

The share of renewable energy in the total consumption of electricity increased sharply in 2010.

The share of electricity produced from renewable energy sources increased by more than 76% in 2010, reaching to 862 GWh and accounting for nearly 10% of total electricity consumption in Estonia. In the previous year, that figure was 6%. The share of electricity produced in heat and power combined plants was 16.5% of gross consumption.

Renewable energy produced from waste and biomass increased more than twice (total of 0.5 TWh), the share of wind energy also significantly increased by 44% (total of 0.28 TWh). The share of hydroenergy in Estonia is very small and it dropped by 11% in 2010.

The proportion of energy generated from renewable sources has risen dramatically, constituting 10% of the Estonian consumption in 2010.

Grants in the total amount of EEK 711.3 million (nearly EUR 45 million) were paid to renewable energy and combined production of heat and power. Grants have increased by 76% as compared to 2009. Grants paid to wind turbines amounted to EEK 128 million (EUR 8.2 million), grants to electricity produced from biomass EEK 450 million (EUR 28.9 millions). The quantity of electricity produced from hydro-energy for which grants are paid remained at the same level. The grant for electricity produced from biomass amounted to ca. EEK 9 million, increasing by ca. 40% year-over-year.

Quantities produced from renewable energy / GWh



According to the forecast of Elering, a total of nearly EUR 57.7 million (EEK 900 million) will be paid to support combined heat and power production in 2011.

Elering and the society

Elering is responsible for Estonia's security of electricity supply. Such a main activity has developed us into a company that has its face towards the entire society – despite the fact that our main everyday cooperation partners and clients are mostly producers and large consumers. Our success also depends on competence of people – those who work at Elering as well as the Estonian people who work for our partners and clients. Therefore, we find it important to collaborate with universities in order to promote and encourage development of the Estonian thought on energy in a wider sense as well as learning and self-improvement of good people in a narrower sense.

Our success will also depend on the opinion of other important social groups, media and its consumers with regard to the key questions of energy. Therefore, as a centre of excellence for energy we find it important to speak about our activities, introduce the main challenges and basic problems of energy. The relevant channels include media intended for a wider audience as well as specific publications and seminars. Each year, Elering gives an assessment of the most important indicators of the Estonian electricity system in the reports on security of supply and sufficiency of output.

While transmission of electricity is a physical phenomenon invisible to eyes, a large part of our activities –our physical infrastructure – is continuously before the public's eyes. To maintain and promote quality of the Estonian living environment, we collaborate with land owners, local authorities and other involved parties in maintaining and developing our lines. We in Elering have approved our environmental policy principles that we carefully observe in our everyday work. The future of Elering is closely related to that of Estonia – we need to take into account the long-term perspective when preparing our business plans. It means cooperation, openness, environmental sustainability and contributions to society.

Elering's
environmental footprint is shrinking.
We are setting an example for the
efficient use of energy.

Elering and development of Estonian thought on energy – to become strong through partnership relations

Elering is responsible for developing a good electricity market and electricity network. This requires as large as possible concentration of energy-related competence in Elering. It means not only a strict personnel policy, but also cooperation with all other organisations that contribute to the development of Estonian energy.

In order to involve companies who are influenced by decisions and action plans as well as experts, representatives of executive authorities, two advisory councils were launched under leadership of Elering in 2010 – Advisory Council for Electricity Market and Advisory Council for developing the Estonian electricity Network.

The advisory councils add transparency to the process of making decisions that ensure security of supply of the Estonian electricity system. Cooperation enables to increase predictability in the electricity market to be opened up and to analyse the key issues of strategic development of the electricity network with the market participants.

The goal of the advisory council for development of electricity market is to exchange information and prepare positions that enable the parties to reach joint agreements for developing the electricity market at the regional level and for international cooperation.

Elering finds it important to pay special attention to involvement of parties at a time of significant changes in the electricity sector. Through informing the market participants and transparency in the decision-making process, we create an environment for market participants where decisions shaping their activities are predictable. The work of the advisory council for electricity market is led by Chairman of the Management Board of Elering, Taavi Veskimägi, and Head of Electricity Market department, Ingrid Arus.

Representatives of companies engaged in selling electricity, distribution networks, producers, consumers and experts from state authorities are involved in the work of the advisory council for development of the electricity market. Given the development and ambitions of the regional electricity market, it is certainly necessary to additionally involve foreign partners in the future.

With the advisory council for development of electricity, Elering wishes to involve expertise of partners for developing the Estonian electricity network and Elering. In developing security of supply and strategic development of the Estonian electricity network, Elering looks ahead several decades so that the current decisions would also guarantee security of supply for the Estonian electricity network in the future.

The continuous consultation process through the advisory councils legitimates the strategic view of Elering itself and also enables other market participants to take plans of the system operator into account. The advisory council for development of electricity network is lead by member of the Management Board of Elering, Kalle Kilk.

In 2010, three meetings were held on the issues of development of the electricity market and the electricity network. All meetings were productive, full of lively discussions and have found a positive feedback.

Elering and philanthropy

Elering's philanthropic activities are based on the principle that our contribution to any undertaking must change something. It means that Elering prefers specific projects that are well planned and thorough, and where the achievable effect is related to Elering's strategic directions of activities.

Elering's own contribution must not necessarily be a monetary one – apart from the infrastructure, the main assets of our company are people who are the best specialists and leaders in their area of responsibility. The skills and social network of our employees, if well elaborated, could add positive additional value to any project. Several Elering's team members are voluntarily contributing their time and resources to charity projects.

A good example of Elering's best practices in that area is provision of Doctoral study grants to young researchers on the condition that after defending the Doctor's degree, the future Doctor will make a contribution as a lecturer to teach other students. It is appropriate to mention here that Elering's cooperation with Tallinn University of Technology is the main focus of our social projects. In addition to participation of Elering's team members as lecturers in educating students, our further plans include development of the Estonian thought on energy in collaboration with Tallinn University of Technology.

Elering and the environment

Elering is mindful of its environmental footprint and takes reasonable steps to efficiently limit it. Elering is and will remain to be related to Estonia and its environment for a long time – its responsible and perspective-sensitive behaviour is reflected in the principles and values of Elering.

Our main activity – guaranteeing security of electricity supply in Estonia – is directly related to changes in society. The infrastructure of electricity, including substations and cables, is physically located in our surrounding environment. Therefore, continuous environmental impact assessment, in a narrow sense arising from legislation us well as in a wider, holistic sense, is part of our main activity.

A significant part of our environmental responsibility arises from compliance with the environmental legislation and requirements applicable in the Republic of Estonia. For example, it is required to comply with the requirements of different legal regulations for avoiding environmental damage during maintenance of transformers and for treatment, storage and disposal of hazardous waste during maintenance work related to creation of oils and hazardous waste in substations. Strict compliance with such requirements is part of our normal work process. Our staff has the necessary expertise, training and qualification.

In addition to the external environment, Elering considers it important to ensure health-related welfare of our people. It means mainly guaranteeing occupational health and safety – the operation of substations as well as the whole work related to electricity transmission is complicated and requires good education and preparation of employees and responsible attitude of the employer. As a company we make all our best efforts to ensure that our people could work every day in a carefree and serious manner.

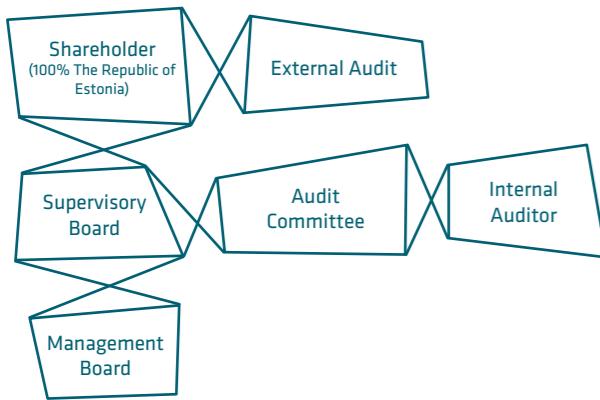
In addition to exemplary compliance with the legislation regulating environmental protection and maintenance, both in form and essence, which is a precondition for performing our functions, we have also established our principles of environmental responsibility at Elering:

- We make our employees and suppliers aware of legal and other environmental requirements and obligate them to fulfil such requirements;
- We avoid environmental pollution and reduce waste creation, and apply the best possible technology for this;
- We use our resources economically;
- In our tender documents, we request that suppliers demonstrate environmental awareness and use environment-friendly technologies in their activities;
- The Company's environmental policy and aspects are public – each employee may freely disseminate them outside the company, they are also available on the company's website.

Good corporate governance

We are dedicated to complying with good corporate governance practices and wish to make continuous improvement in that area. We consider this as a prerequisite for achieving our strategic objectives and designing our organisational culture. The directing bodies of Elering are responsible for developing the company as a whole. Elering publishes its good corporate governance report on website www.elering.ee.

Management



Elering's articles of association describe the roles and responsibilities of the shareholder, directing bodies and the audit committee. The directing bodies of the company are the Supervisory Board and Management Board. The rules of procedure of the Management Board are set out in the contract with the member of the Management Board, articles of association, sectoral statutes and rules of procedure, Electricity Market Act and other legislation. The work of the Supervisory Board is organised on the basis of the requirements specified in the Commercial Code, State Assets Act and other legislation, Elering's articles of association and rules of procedure of the Supervisory Board.

General Meeting

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

Company will not be used for other activities. Elering has also established a dividend policy that describes the requirements concerning payment of dividends to the owner.

Competence of the Company's owners includes: to amend the articles of association; to increase and decrease share capital; to elect and remove members of the Supervisory Board; to elect auditors and determine the procedure for paying their fees; to designate a special audit; to approve the annual report and allocate profit; to divide shares; to decide on merger, division, transformation and/or dissolution of the company; to file a claim against a member of the Management Board or Supervisory Board; also to decide on conclusion and terms and conditions of transactions with members of the Supervisory Board; to appoint a representative of Elering in such claims or transactions; to decide on other matters placed in the competence of owners by owners' decisions.

Supervisory Board

The Supervisory Board gives the Management Board instructions for organising the management of the company and exercises supervision over the activities of the company's Management Board. The Supervisory Board determines, regularly reviews and assesses the Company's strategy, general action plan, principles of risk management and annual budget.

Members of the Supervisory Board are solidarily liable for any damage wrongfully caused by violation of the requirements of legislation or the Company's articles of association and non-performance of their obligations.

In order to fulfil its tasks, the Supervisory Board has the right to examine all documents of the Company, to audit the accuracy of accounting, the existence of assets and the conformity of the activities of the Company with the law, the articles of association and resolutions of the general meeting. The supervisory board has the right to obtain information concerning the activities of the Company from the Management Board and to demand an activity report and preparation of a balance sheet from the Management Board.

The Supervisory Board comprises three to five members. The number of the members of the Supervisory Board is decided and the members are elected by the owners. Currently, the Supervisory Board of Elering has five members. The articles of association set out restrictions on the selection of members of the Supervisory Board.

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

Members of the supervisory board are elected and removed by the owner, i.e. the Minister of Economic Affairs and Communications.

Fees of the members of the Supervisory Board are determined by a directive of the Minister of Economic Affairs and Communications.

Members of the Supervisory Board

Lauri Tammiste

Chairman of the Supervisory Board,
Head of the Energy Department, Ministry of
Economic Affairs and Communications

Heiki Tammoja

Director of Electrical Power Engineering Institute,
Tallinn University of Technology

Thomas Auväär

Head of the Financial Markets Department,
Ministry of Finance

Jüri Raatma

Adviser of the Ministry of Economic Affairs and
Communications

Aivar Söerd

CEO of Tallink Hotels

Audit Committee

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

The Audit Committee comprises five members. Members of the Audit Committee are elected and removed by a decision of the Supervisory Board. Members of the Audit Committee are elected for a term of three years. Members of the Audit Committee elect from among themselves the chairman to organise the activities of the Audit Committee. The Chairman of the Supervisory Board may not be the chairman

of the Audit Committee. The members of the Supervisory Board are paid an additional fee for participation in the Audit Committee.

The chairman of the Audit Committee is Thomas Auväär. Members of the Audit Committee are Lauri Tammiste, Heiki Tammoja, Jüri Raatma and Aivar Söerd.

Management Board

The Management Board of Elering has complete freedom of decision and everyday management decisions are made independently, without interference by the owner and the Supervisory Board. The Management Board needs the consent of the Supervisory Board for transactions and operations that are beyond the everyday economic activities of the Company.

The Management Board ensures that the members of the Supervisory Board have sufficient information of the Company's economic condition as well as more important matters related to the economic activities, and informs the Supervisory Board of the more important matters of the economic activities as necessary, including but not limited to: changes in the everyday economic activities and economic condition of the Company, conclusion of transactions that are important for the Company, adoption of management decisions that are important for the Company, events and circumstances that may result in an unreasonably large financial risk for the Company, as well as other circumstances relevant to the economic activities of the Company.

Members of the Management Board

Taavi Veskimägi
Chairman of the
Management Board

Peep Soone
Member of the
Management Board

Kalle Kilk
Member of the
Management Board

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

A member of the Management Board may be paid a fee only on the basis of a contract of management board member concluded with him or her. If a member of the Management Board fulfils also other tasks necessary for the Company in addition to his or her tasks as a member of the Management Board, a fee for such tasks may be paid only in case it is prescribed by a management board member contract.

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

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

According to the articles of association, the term of office of a member of the Management Board is five years that may be extended by the Supervisory Board by the period of the term of office with the consent of that member of the Management Board. A member of the Management Board may be removed by the Supervisory Board and a member of the Management Board may resign with a three months' notice.

Employees

Elering's major assets are right people in right places, performing tasks and fulfilling roles that are most suitable to their personal characteristics, expertise and abilities. In the financial year 2010, the average number of employees in Elering was 139, of whom 76% were men and 24% women. As at the end of the year, the average age of employees was 43.

In our employees, we value competence, openness, helpfulness and responsibility. As arises from the survey on dedication of employees, those values are also considered important by the employees themselves. The trend of results of that regular survey in the recent years shows high and increasing dedication of the employees. In the judgement of the employees, the main strengths of Elering lie in variety in work, constructive relations with managers, common traditions, competent colleagues, work-related training, developing and innovative employer that offers a stable job. Stability of work relations in Elering is also confirmed by extremely low labour turnover that was 4% in 2010.

We attach value to active contribution of employees with their thoughts and acts to development of the Company and organisation of events. We elect and recognise our best employees with the annual title "Person of a year".

Reproduction and development of employees are of critical importance for ensuring continuous success of the Company. We collaborate with several institutions of higher education and offer the selected students a thorough practical training programme. Of the employees, 80% have higher education and many employees combine work with education. As at the end of 2010, approx. 20% of Elering's staff simultaneously studied for a degree in higher education institutions. In collaboration with Tallinn University of Technology, we organise energy-related in-service training courses to our engineering and technical staff.

The age composition of the staff is a cross-section of different generations. The strength of the Company lies in equal representation of different generations in the staff. Senior specialists with their experience of several years and young people with their recently acquired academic education complement each other.

Risk management and internal control system

The Management Board of Elering confirms that:

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

In 2010, the principles and policy of risk management were updated in Elering, their implementation ensures a functioning system of risk management and internal control based on the Company's area of activity.

The Management Board is responsible for the functioning of the internal control system of the Company. To ensure the functioning of the internal control system, the position of an internal auditor will be created on the basis of the articles of association or the internal auditor service will be outsourced to an audit company. The Management Board has concluded a contract with AS PricewaterhouseCoopers for outsourcing the internal auditor service. In accordance with the articles of association, the owner – Ministry of Economic Affairs and Communications – has the right to demand a special audit and use a structural unit under its governance for this.

Risk management objectives in Elering are:

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



“ In 2010, Elering's risk management principles and policy were renewed, resulting in the enhancement of the current risk management and internal audit systems.

Kalle Kukk
Strategy Manager

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

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

Roles and responsibilities

Responsibility of the Management Board for risk management is to ensure that the organisational culture and processes encourage identification of any potential violations resulting from risks. On the basis of information received from the risk manager, the Management Board reviews the identified risks and gives an assessment as to whether all relevant risks arising from the Company's activities have been taken into account.

The Management Board reports its conclusions to the Supervisory Board that gives its assessment of the conclusions and, before approving the annual report, accepts the Management Board's confirmation that risk management is applied and it is functioning in the Company.

The Supervisory Board has delegated certain tasks to the audit committee. The audit committee reports to the Supervisory Board the recommendations and conclusions arising from observations of the internal and external auditors.

The risk manager is responsible for general organisation of risk management in the Company and coordinates risk assessment and performance of necessary follow-up activities. In this work, the risk manager is supported by risk administrators who include:

- Head of Power System Control Centre of the electricity system;
- Head of the electricity markets department;
- Financial Manager;
- Head of the legal division;
- Strategy Manager.

On the basis of the information received from risk administrators, the risk manager gives an overview of the functioning of risk management in the Company. The risk manager reports the risks to the Management Board twice a year, using the risk maps and register of risks prepared by the risk administrators. The report includes an overview of the identified risks, probability of risk occurrence, their potential impact on the Company's activities, and the control mechanisms for risk management.

Risk administrators give regular information on risk management to the risk manager and such information is analysed by the committee for risk management. The committee for risk management is led by the risk manager and its members also include risk administrators.

Assessment of risks

The main categories of risks within which risk administrators identify and assess risks are as follows

- risks of sustainable functioning of the service of vital importance;
- risks of the functioning of electricity markets;
- financial risks;
- risks arising from the external environment;
- strategy risks.

Risks related to the sustainable functioning of the service of vital importance include risks related to ensuring the preparedness of the transmission network and risks related to real-time management of the Estonian electricity system. The risks related to the functioning of electricity markets include risks related to identification of the balance, movement of market information and disclosure of data.

Financial risks include credit, liquidity, currency and other risks that have a direct impact on the financing and profitability of the Company. Risks arising from the external environment include regulative, legal, owner-based and other external risks over which the Company does not have any direct control. Strategy risks include risks related to the strategic planning of the Company, network planning, IT developments, development of reputation, work environment and personnel policy.

Periodic risk assessment is conducted in Elering twice a year:

- risks are assessed simultaneously with updating the Company's strategy;
- risk assessment is reviewed in the process of preparing the annual report.

Disclosure of information

The Company's website is clearly structured, posting the annual reports, financial results, operating information, main activities, structure, strategy, news and notices as well as other information that is necessary for investors and the public at large. The website is also available in English. The information on website www.elering.ee (incl. news and notices) is continuously updated.

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Statement of Financial Position

	<i>In thousands of Estonian kroons</i>	<i>Note</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
ASSETS					
Current assets					
Cash and cash equivalents	6	626,866	0	0	
Trade and other receivables	7	342,159	208,568	192,246	
Total current assets		969,025	208,568	192,246	
Non-current assets					
Property, plant and equipment	8	5,544,548	5,516,156	5,346,928	
Intangible assets	10	48,497	31,001	17,837	
Total non-current assets		5,593,045	5,547,157	5,364,765	
TOTAL ASSETS		6,562,070	5,755,725	5,557,011	
LIABILITIES					
Current liabilities					
Borrowings	11	0	2,935,838	386,121	
Trade and other payables	12	568,608	273,838	206,722	
Total current liabilities		568,608	3,209,676	592,843	
Non-current liabilities					
Borrowings	11	2,905,493	0	2,046,586	
Deferred income	13	349,385	346,541	319,961	
Prepayments related to government grants	13	237,033	0	0	
Total non-current liabilities		3,491,911	346,541	2,366,547	
TOTAL LIABILITIES		4,060,519	3,556,217	2,959,390	
EQUITY					
Share capital	14	2,190,524	2,100,000	2,100,000	
Statutory reserve capital	14	44,039	44,039	30,261	
Retained earnings	14	266,988	55,469	467,360	
TOTAL EQUITY		2,501,551	2,199,508	2,597,621	
TOTAL LIABILITIES AND EQUITY		6,562,070	5,755,725	5,557,011	

The notes on pages 50 to 81 are an integral part of these financial statements.

Statement of Comprehensive Income

	<i>In thousands of Estonian kroons</i>	<i>Note</i>	<i>2010</i>	<i>2009</i>
Revenue		15	1,390,429	1,181,313
Other income		16	1,348	283
Goods, raw materials and services		17	-590,753	-452,203
Other operating expenses		18	-46,045	-47,888
Staff costs		19	-59,521	-56,574
Depreciation and amortisation		8,10	-369,872	-304,826
Other expenses		20	-649	-770
Operating profit			324,937	319,334
Finance income			1,356	0
Finance costs		21	-114,774	-109,736
Profit before income tax			211,519	209,598
Income tax expense		14	0	127,619
Profit for the year			211,519	81,979
Total comprehensive income for the year			211,519	81,979

The notes on pages 50 to 81 are an integral part of these financial statements.

Cash Flow Statement

	Note	2010	2009
<i>In thousands of Estonian kroons</i>			
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before income tax		211,519	209,598
Adjustments for:			
▪ Profit from sale of property, plant and equipment	16	-961	-244
▪ Depreciation, amortisation and impairment	8,10	369,872	304,826
▪ Interest expenses	21	114,674	109,716
▪ Interest income		-1,334	0
Changes in working capital:			
▪ Changes in receivables and prepayments related to operating activities	7	-136,568	-13,084
▪ Changes in liabilities and prepayments related to operating activities	12	256,143	66,947
▪ Changes in deferred income from connection and other service fees	13	2,844	26,580
Cash generated from operations, excl. interest and income tax		816,189	704,339
Income tax paid	14	0	-127,619
Interest paid	21	-87,501	-109,716
Interest received		1,061	0
NET CASH USED IN OPERATING ACTIVITIES		729,748	467,004
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property, plant and equipment, and intangible assets	8,10	-408,392	-490,408
Foreign grants to acquire non-current assets	13	237,033	0
Proceeds from sale of property, plant and equipment		5,059	365
NET CASH USED IN INVESTING ACTIVITIES		-166,300	-490,043
CASH FLOWS FROM FINANCING ACTIVITIES			
Repayment of short-term borrowings	11	-2,046,586	0
Net change in overdraft	11	-889,252	503,131
Long-term bank loans received	11	2,908,732	0
Contribution to share capital	14	90,524	0
Dividends paid	14	0	-480,092
NET CASH USED IN FINANCING ACTIVITIES		63,418	23,039
Net increase/(decrease) in cash and cash equivalents		626,866	0
Cash and cash equivalents at the beginning of the year	6	0	0
Cash and cash equivalents at the end of the year	6	626,866	0

The notes on pages 50 to 81 are an integral part of these financial statements.

Statement of Changes in Equity

	<i>In thousands of Estonian kroons</i>	<i>Share capital</i>	<i>Statutory reserve capital</i>	<i>Retained earnings</i>	<i>Total</i>
Balance as at 1.1.2009	2,100,000	30,261	467,360	2,597,621	
Comprehensive income for financial year	0	0	81,979	81,979	
Transfers to statutory reserve capital	0	13,778	-13,778	0	
Dividends paid	0	0	-480,092	-480,092	
Balance as at 31.12.2009	2,100,000	44,039	55,469	2,199,508	
Contribution to share capital	90,524	0	0	90,524	
Comprehensive income for financial year	0	0	211,519	211,519	
Balance as at 31.12.2010	2,190,524	44,039	266,988	2,501,551	

More detailed information on share capital and other equity items is set out in Note 14.

The notes on pages 50 to 81 are an integral part of these financial statements.

Notes to the Financial Statements

Note 1

ELERING OÜ AND ITS OPERATIONS

The financial statements of Elering OÜ (the "Company") for the year ended 31 December 2010 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

Elering OÜ is domiciled in the Republic of Estonia. The Company's registered address is Kadaka tee 42, 12915 Tallinn, Estonia. The Company's principal business activity is electricity transmission within the Republic of Estonia. The economic activities of the Company are regulated by Estonian legislation, which stipulates that the Estonian Competition Board regulates the Company's economic activities, monitors its operations and fixes the tariffs for the transmission services.

From 27.01.2010, the sole shareholder of the Company is the Republic of Estonia, until then, the Company's immediate parent company was Eesti Energia AS whose sole shareholder is the Republic of Estonia.

The Management Board approved these financial statements at 11 April 2011. Pursuant to the Commercial Code of the Republic of Estonia, the annual report shall be presented for approval to the Company's Supervisory Board and the General Meeting of Shareholders.

Note 2

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Bases of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union under the historical cost convention. The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

The Company changed its financial year in 2009. Before that, the Company's financial year lasted from 1 April to 31 March. The purpose of the change was to make financial years coincide with the calendar year. The Company's financial statements for the year ended 31.12.2009 presented the results of operations for the period of 1.04.2009-31.12.2009 (9 months) and the comparative period 1.04.2008-31.03.2009 (12 months). These financial statements present the results of operations for the periods 1.01.2009 - 31.12.2009 and 1.01.2010 - 31.12.2010, i.e. the length of the comparative period has been changed as compared to the period presented in the financial statements for 2009. The comparative period was changed to be 12 months long in order ensure better comparability of the financial statements across financial years.

Functional and presentation currency

The functional currency of the Company is the Estonian kroon. All amounts in these financial statements are presented in thousands of Estonian kroons ("EEK"), unless otherwise stated.

Foreign currency translation

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

Financial assets

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

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

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

At 31 December 2010 (as well as 31 December 2009 and 1 January 2009), the Company had no other classes of financial assets than those classified under the category loans and receivables.

Loans and receivables

Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Company intends to sell in the near term. Loans and receivables are initially recognised at fair value plus transaction costs. After initial recognition, loans and receivables are accounted for at amortised cost using the effective interest rate method unless the payment date falls within 30 days.

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

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

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

Cash and cash equivalents

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

Prepayments

Prepayments are carried at cost less a provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which itself will be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the

Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying amount of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss.

Property, plant and equipment

Property, plant and equipment are stated at cost, less any accumulated depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost includes borrowing costs incurred on specific or general funds borrowed to finance construction of qualifying assets.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

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

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

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

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

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

Intangible assets

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

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

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

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

	<i>Useful lives in years</i>
Software licences	3 years
Personal rights of use	50-100 years

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

Impairment of non-financial assets

Land and assets that are subject to depreciation/amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered an impairment loss are reviewed for possible reversal of impairment at each reporting date.

Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made or received under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Financial liabilities

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

Other financial liabilities are initially recognised at fair value, net of transaction costs incurred and are subsequently carried at amortised cost. The amortised cost of current liabilities normally equals their nominal value; therefore current liabilities are stated in the balance sheet in their redemption value. Non-current liabilities 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 borrowings using the effective interest rate method.

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

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

Provisions and contingent liabilities

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

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

Development costs

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

Share capital

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

Dividends

Dividends are recorded as a liability and deducted from equity in the period in which they are declared and approved. Any dividends declared after the balance sheet date and before the financial statements are authorised for issue are disclosed in the note "Events after the Balance Sheet Date".

Statutory reserve capital

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

Revenue recognition

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

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

Sales of services are recognised in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. The sales of network services and balancing energy fall into this category.

- **Recognition of connection fees**

When connecting to the electricity network, the clients must pay a connection fee based on the actual costs of infrastructure to be built in order to connect to the network. The revenue from connection fees is deferred and recognised as income evenly over the estimated customer relationship period. The amortisation period of connection fees is 20 years. Deferred connection fees are carried in the balance sheet as long-term deferred income.

- **Interest income**

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

- **Recognition of government grants**

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

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

If the government grant is received in the form of a transfer of a non-monetary asset, the grant and the asset are recognised at the fair value of the asset transferred.

Subsidies to electricity producers

The Electricity Market Act obliges the Company to participate in supporting mechanism for renewable and efficient cogeneration electricity producers. The electricity consumer bears the costs of support in proportion to the volume of network services consumed. The Company collects subsidies on behalf of eligible producers and pays it out to them.

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

The customers are charged according to the estimated charge per kWh. Due to the different reasons the actual amounts paid out and received as subsidies always differ from the estimated amounts. Over or under collected subsidies are shown in the balance sheet as either Trade and other payables (in case of surplus) or Trade and other receivables (in case of deficit). These balances are taken into account when determining the charge for the next period as described above. Collecting and paying of subsidies has no impact on the comprehensive income of the Company. See also Note 12.

Employee benefits

Wages, salaries, contributions to the state pension, paid annual leave, sick leave and bonuses, along with social and unemployment taxes are recognised in the income statement in the year in which the associated services are rendered by the employees of the Company. Any amounts unpaid by the balance sheet date are recognised as a liability.

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

Income tax

According to the Income Tax Act, the annual profit earned by entities is not taxed in Estonia. Corporate income tax is paid on dividends, fringe benefits, gifts, donations, costs of entertaining guests, non-business related disbursements and adjustments of the transfer price. From 1 January 2008, the tax rate on the net dividends paid out of retained earnings is 21/79. The corporate income tax arising from the payment of dividends is recognised as a liability and an income tax expense in the period in which dividends are declared, regardless of the period for which the dividends are paid or the actual payment date. An income tax liability is due at the 10th day of the month following the payment of dividends.

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

Value added tax

Output value added tax related to sales is payable to tax authorities at the earlier of (a) collection of receivables from customers or (b) delivery of goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis.

Other taxes in Estonia

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

Tax	Tax rate
Social security tax	33% of the paid payroll to employees and fringe benefits
Unemployment insurance tax	Until 31.05.2009: 0.3%, until 31.07.2009: 1%, from 01.08.2009: 1.4% of the payroll paid to employees,
Fringe benefit income tax	21/79 of fringe benefits paid to employees
Land tax	1-2.5% on taxable value of land per annum
Excise tax on electricity	Until 28.02.2010: 50 kroons per MWh of electricity, from 01.03.2010: 70 kroons per MWh of electricity
Corporate income tax on non-business related expenses	21/79 on non-business related expenses

Note 3

CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

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

Revenue recognition (connection fees)

The Company recognises all connection and other service fees (Note 13) as income over the estimated customer relationship period as the entity has a constructive obligation to provide a supply of electricity to the end customer and to meet certain performance standards regarding availability of supply, the Company also has an ongoing obligation to maintain the connection. Thus a new connection has no standalone value without ongoing access to the network.

The customer relationship period is 20 years based on management's estimate. In the reporting period, income from connection and other service fees totalled EEK 17,942 thousand (2009: EEK 15,483 thousand). If the estimated customer relationship period were increased by 25%, the annual income from connection fees would decrease by EEK 3,588 thousand (2009: EEK 3,097 thousand).

Useful lives of property, plant and equipment

The estimated useful lives of items of property, plant and equipment (Note 8) are based on management's estimates regarding the period during which the asset will be used. The estimation of economic lives is based on historical experience and takes into consideration production capacity and physical condition of the assets. Previous experience has shown that the actual useful lives have sometimes been longer than the estimates. In the reporting period, depreciation amounted to EEK 307,472 thousand (2009: EEK 303,638 thousand). If depreciation rates were increased/decreased by 20%, the depreciation charge for the year would increase/decrease by EEK 61,494 thousand (2009: EEK 60,728 thousand).

Note 4

NEW ACCOUNTING PRONOUNCEMENTS

Adoption of new or revised standards and interpretations

Following new standards, amendments to published standards and interpretations became effective for the Company from 1 January 2010:

IFRIC 18, Transfers of Assets from Customers. The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost at initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. The Company assessed the effect of IFRIC 18 on recognition of connection fees and concluded that the current accounting method (connection fees are amortised into income over the estimated duration of the customer relationship) is in compliance with the principles of IFRIC 18, therefore, the interpretation had no effect on the financial statements.

Following new standards, amendments to published standards and interpretations became effective for the Company from 1 January 2010, but are not relevant for the Company's operations:

- Improvements to International Financial Reporting Standards, issued in April 2009
- IFRIC 12, Service Concession Arrangements
- IFRIC 15, Agreements for the Construction of Real Estate
- Embedded Derivatives - Amendments to IFRIC 9 and IAS 39, issued in March 2009
- IFRIC 16, Hedges of a Net Investment in a Foreign Operation
- IFRIC 17, Distributions of Non-Cash Assets to Owners
- IAS 27, Consolidated and Separate Financial Statements, revised in January 2008
- IFRS 3, Business Combinations, revised in January 2008
- Amendment to IFRS 5, Non-current Assets Held for Sale and Discontinued Operations (and consequential amendments to IFRS 1)
- Eligible Hedged Items—Amendment to IAS 39
- IFRS 1, First-time Adoption of International Financial Reporting Standards, revised in December 2008
- Group Cash-settled Share-based Payment Transactions - Amendments to IFRS 2
- Additional Exemptions for First-time Adopters - Amendments to IFRS 1

Adoption of new or revised standards and interpretations before their effective date:

Amendment to IAS 24, Related Party Disclosures, issued in November 2009 (effective for annual periods beginning at or after 1 January 2011). IAS 24 was revised in 2009: (a) the definition of a 'related party' was simplified, its intended meaning was clarified and some inconsistencies were removed from the definition, and (b) disclosure requirements were reduced for public entities. Disclosures about related parties were prepared in accordance with the revised IAS 24 in these financial statements.

New or revised standards and interpretations not early adopted by the Company:

Following new or amended standards and interpretations were issued and will become effective for the Company from 1 January 2011 or later periods and which the Company has not early adopted

IFRS 9, Financial Instruments Part 1: Classification and Measurement (effective for annual periods beginning at or after 1 January 2013; not yet adopted by the EU). IFRS 9 issued in November 2009 replaces those parts of IAS 39 relating to the classification and measurement of financial assets. IFRS 9 was further amended in October 2010 to address the classification and measurement of financial liabilities. Key features are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and (ii) the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.
- 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 as at fair value through profit or loss in other comprehensive income.

The Company is considering the implications of the standard, the impact on the Company and the timing of its adoption by the Company.

Improvements to International Financial Reporting Standards, issued in May 2010 (effective dates vary standard by standard, most improvements are effective for annual periods beginning at or after 1 January 2011; the improvements have not yet been adopted by the EU).

The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: IFRS 1 was amended (i) to allow previous GAAP carrying value to be used as deemed cost of an item of property, plant and equipment or an intangible asset if that item was used in operations subject to rate regulation, (ii) to allow an event driven revaluation to be used as deemed cost of property, plant and equipment even if the revaluation occurs during a period covered by the first IFRS financial statements and (iii) to require a first-time adopter to explain changes in accounting policies or in the IFRS 1 exemptions between its first IFRS interim report and its first IFRS financial statements;

IFRS 3 was amended (i) to require measurement at fair value (unless another measurement basis is required by other IFRS standards) of non-controlling interests that are not present ownership interest or do not entitle the holder to a proportionate share of net assets in the event of liquidation, (ii) to provide guidance on acquiree's share-based payment arrangements that were not replaced or were voluntarily replaced as a result of a business combination and (iii) to clarify that the contingent considerations from business combinations that occurred before the effective date of revised IFRS 3 (issued in January 2008) will be accounted for in accordance with the guidance in the previous version of IFRS 3; IFRS 7 was amended to clarify certain disclosure requirements, in particular (i) by adding an explicit emphasis on the interaction between qualitative and quantitative disclosures about the nature and extent of financial risks, (ii) by removing the requirement to disclose the carrying amount of renegotiated financial assets that would otherwise be past due or impaired, (iii) by replacing the requirement to disclose fair value of collateral by a more general requirement to disclose its financial effect, and (iv) by clarifying that an entity should disclose the amount of foreclosed collateral held at the reporting date and not the amount obtained during the reporting period; IAS 1 was amended to clarify that the components of the statement of changes in equity include profit or loss, other comprehensive income, total comprehensive income and transactions with owners and that an analysis of other comprehensive income by item may be presented in the notes; IAS 27 was amended by clarifying the transition rules for amendments to IAS 21, 28 and 31 made by the revised IAS 27 (as amended in January 2008); IAS 34 was amended to add additional examples of significant events and transactions requiring disclosure in a condensed interim financial report, including transfers between the levels of fair value hierarchy, changes in classification of financial assets or changes in business or economic environment that affect the fair values of the entity's financial instruments; and IFRIC 13 was amended to clarify measurement of fair value of award credits. The Company is currently assessing the impact of the amended standard on its financial statements.

New or revised standards and interpretations that are not yet effective and not early adopted by the Company, and not expected to have a significant effect on the Company's financial statements:

Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (effective for annual periods beginning at or after 1 July 2011; not yet adopted by the EU).

Deferred Tax: Recovery of Underlying Assets – Amendment to IAS 12 (effective for annual periods beginning at or after 1 January 2012; not yet adopted by the EU).

Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters – Amendment to IFRS 1 (effective for annual periods beginning at or after 1 July 2011; not yet adopted by the EU).

Classification of Rights Issues - Amendment to IAS 32, issued in October 2009 (effective for annual periods beginning at or after 1 February 2010).

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments (effective for annual periods beginning at or after 1 July 2010).

Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14 (effective for annual periods beginning at or after 1 January 2011).

Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters - Amendment to IFRS 1 (effective for annual periods beginning at or after 1 July 2010). The Company does not expect the amendment to have any material effect on its financial statements.

Note 5**FINANCIAL RISK MANAGEMENT**

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

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

Loans and receivables

<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Cash and cash equivalents (Note 6)	626,866	0	0
Trade and other receivables (Note 7)	337,234	189,133	184,424
▪ Trade receivables	336,949	189,115	184,377
▪ Other receivables	285	18	47
TOTAL FINANCIAL ASSETS	964,100	189,133	184,424

Financial liabilities at amortised cost

<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Trade and other payables (Note 12)	558,430	257,366	180,566
Borrowings (Note 11)	2,905,493	2,935,838	2,432,707
TOTAL FINANCIAL LIABILITIES	3,463,923	3,193,204	2,613,273

Credit risk

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

The Company's maximum exposure to credit risk by class of assets is as follows:

<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Cash and cash equivalents (Note 6)	626,866	0	0
Trade and other receivables (Note 7)	337,234	189,133	184,424
▪ Trade receivables	336,949	189,115	184,377
▪ Other receivables	285	18	47
Total exposure of assets to credit risk in the statement of financial position	964,100	189,133	184,424

The Company structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to counterparties or groups of counterparties. Limits on the level of credit risk are approved regularly by management. Such risks are monitored on an ongoing basis and they are subject to a biannual review.

The Company's Accounting Department reviews ageing analysis of outstanding trade receivables and follows up on past due balances each week. The results are reported to the CFO of the Company. The Company has identified circumstances under which the collection of debt is passed over to a collection agency. Management therefore considers it appropriate to provide ageing and other information about credit risk as disclosed in Note 7.

Credit risk concentration

The Company is exposed to concentrations of credit risk. Management monitors and discloses concentrations of credit risk by reports, which list exposures to counterparty with aggregated balances in excess of 5% of the Company's equity. At 31.12.2010, the Company had 1 counterparty (distribution network operator) (31.12.2009 and 1.1.2009: 1 counterparty) with an aggregated receivables balance of EEK 247,340 thousand (31.12.2009: EEK 142,722 thousand; 1.1.2009: EEK 127,808 thousand) or 73% of the gross amount of trade and other receivables (31.12.2009: 75%; 1.1.2009: 69%).

Market risk

The Company is exposed to market risk. Market risk arises from open positions in (a) foreign currencies, and (b) interest bearing assets and liabilities. Management sets limits on the value of risk that may be accepted, which is monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

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

Currency risk

Currency risk does not arise from transactions and balances denominated in euros, as the Estonian kroon is pegged to euro at the fixed exchange rate. As most of the Company's transactions and balances are denominated either in Estonian kroons or euros, the Company is not exposed to significant currency risk.

Transactions in other currencies are insignificant; there were no financial instruments denominated in other currencies as at 31.12.2010, 31.12.2009 and 01.01.2009.

Interest rate risk

The Company is not exposed to fair value risk as it has no interest bearing financial instruments carried at fair value and no financial instruments with fixed rate. Cash flow interest rate risk arises from borrowings with a floating interest rate. Until 8.01.2010 the Company had a loan and overdraft agreement with its parent company. The interest rate for both of them was fixed once a year. At 8.01.2010, the

aforementioned liabilities were refinanced through a borrowing from a bank syndicate. The interest rate on the new loan is Euribor + 300 basis points. Pursuant to the loan contract, the Company has the right to choose between 3-month and 6-month Euribor for each following interest period. Euribor is fixed one day prior to the beginning of the new interest period: the Company's management decides whether to fix the interest rate for three or six months, depending on which option is more favourable. The table below summarises the Company's exposure to interest rate risks. The table presents the aggregated amounts of the Company's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest repricing and maturity dates.

	<i>In thousands of Estonian kroons</i>	<i>On demand and less than 1 month</i>	<i>From 3 to 12 months</i>	<i>Total</i>
31.12.2010				
Cash and cash equivalents (Note 6)	626,866	0	626,866	
Long-term borrowings (Note 11)	2,905,493	0	2,905,493	
Net interest sensitivity gap at 31.12.2010	-2,278,627	0	-2,278,627	
31.12.2009				
Short-term borrowings (Note 11)	2,046,586	0	2,046,586	
Overdraft (Note 11)	889,252	0	889,252	
Net interest sensitivity gap at 31.12.2009	-2,935,838	0	-2,935,838	
01.01.2009				
Long-term borrowings (Note Note 11)	0	2,046,586	2,046,586	
Overdraft (Note Note 11)	386,121	0	386,121	
Net interest sensitivity gap at 01.01.2009	-386,121	-2,046,586	-2,432,707	

In the long run, the Company's interest rate risk is limited because the interest rate risks of income and expenses greatly offset each other. In accordance with the legislator's methodology in respect of determination of the tariffs, the market interest rate is used for determining the weighted average cost of capital (WACC) of regulated assets which is used for calculating regulated income. When market interest rates increase, the network tariffs increase as well.

If at 31.12.2010, interest rates had been 10 basis points lower (31.12.2009: 10 basis points) or 100 basis point higher (31.12.2009: 100 basis points) with all other variables held constant, profit for the year would have been EEK 2,905 thousand (2009: EEK 2,936 thousand) higher or EEK 29,055 thousand (2009: EEK 29,359 thousand) lower, mainly as a result of a lower/higher interest expense on variable interest liabilities.

The Company monitors interest rates of its financial instruments. The table below summarises effective interest rates during the respective financial years on the basis of reports reviewed by key management personnel:

	<i>In % p.a.</i>	<i>2010</i>	<i>2009</i>
Liabilities			
Long-term borrowings (Note 11)	4.28	4.81	
Overdraft (Note 11)	3.53	4.81	

Other price risk

The Company has no exposure to equity price risk as it does not hold financial instruments open to price risk.

Liquidity risk

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

The table below shows liabilities at 31.12.2010, 31.12.2009 and 01.01.2009 by their remaining contractual maturity. The amounts disclosed in the maturity table are contractual undiscounted cash flows.

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the reporting date. Foreign currency payments are translated using the spot exchange rate at the balance sheet date.

The maturity analysis of financial liabilities at 31.12.2010 is as follows:

<i>In thousands of Estonian kroons</i>	<i>On demand and less than 1 month</i>	<i>From 1 to 12 months</i>	<i>From 12 months to 5 years</i>	<i>Total</i>
Trade and other payables (Note 12), excl. accrued interest	531,257	0	0	531,257
Borrowings (Note 11), incl. accrued interest	27,173	118,542	3,022,944	3,168,659
Total future payments	558,430	118,542	3,022,944	3,699,916

The maturity analysis of financial liabilities at 31.12.2009 is as follows:

<i>In thousands of Estonian kroons</i>	<i>On demand and less than 1 month</i>	<i>From 1 to 12 months</i>	<i>From 12 months to 5 years</i>	<i>Total</i>
Trade and other payables (Note 12)	257,366	0	0	257,366
Bank and parent company overdrafts (Note 11)	889,252	0	0	889,252
Borrowings (Note 11)	2,055,220	0	0	2,055,220
Total future payments	3,201,838	0	0	3,201,838

The maturity analysis of financial liabilities at 01.01.2009 is as follows:

<i>In thousands of Estonian kroons</i>	<i>On demand and less than 1 month</i>	<i>From 1 to 12 months</i>	<i>From 12 months to 5 years</i>	<i>Total</i>
Trade and other payables (Note 12)	180,566	0	0	180,566
Bank and parent company overdrafts (Note 11)	395,905	0	0	395,905
Borrowings (Note 11)	0	123,460	2,056,874	2,180,334
Total future payments	576,471	123,460	2,056,874	2,756,805

For ensuring liquidity and better management of cash flows, the Company has concluded overdraft contracts with the banks in the amount of EEK 312 932 thousand as at 31.12.2010. In addition to overdraft, the Company has undrawn borrowing facilities in the amount of EEK 1,564,660 thousand as at 31.12.2010. As at 1.1.2009 and 30.12.2009 the Company had overdraft and loan agreements with its then parent entity. See further information in Note 11.

Capital Management

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

According to the widespread industry practice, the Company uses the equity to asset ratio for monitoring the Company's capital, arrived at by dividing total equity by total assets as at the balance sheet date. In 2010, similarly to 2009 and 2008, the Company's goal was to preserve the ratio of equity to assets at 35 - 55%.

According to the terms set forth in the loan contract, the Company also uses the equity ratio to monitor the Company's capital. The equity to asset ratio was 38% as at 31.12.2010, 38% as at 31.12.2010, and 47% as at 01.01.2009.

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
Interest-bearing liabilities (Note 11)	2,905,493	2,935,838	2,432,707
Cash and cash equivalents (Note 6)	626,866	0	0
Net debt	2,278,627	2,935,838	2,432,707
Equity	2,501,551	2,199,508	2,597,621
Total capital	4,780,178	5,135,346	5,030,328
Total assets	6,562,070	5,755,725	5,557,011
Equity to asset ratio	38%	38%	47%

Fair Value of Financial Instruments

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

Estimated fair values of financial instruments have been determined by the Company using available market information, where it exists, and appropriate valuation methodologies. However, judgement is also required to interpret market data to determine the estimated fair value.

Financial assets carried at amortised cost

Carrying amounts of trade and other financial receivables approximate their fair values.

Liabilities carried at amortised cost

Carrying amounts of trade and other payables as well as overdraft approximate their fair values.

The estimated fair value of non-current borrowings with a fixed interest rate or fixed risk margin is determined using valuation techniques, based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

Management estimates that the fair value of loans as at 31.12.2010, 31.12.2009 and 01.01.2009 does not significantly differ from their carrying amount because the risk margins have not changed.

Note 6

CASH AND CASH EQUIVALENTS

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
Bank accounts	276,866	0	0
Short-term deposits	350,000	0	0
Total cash and cash equivalents	626,866	0	0

Bank accounts and deposits:

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
with Moody's credit rating of Aa3	350,139	0	0
with Moody's credit rating of Aa2	110,936	0	0
Without generally accepted credit rating*	165,791	0	0
Total accounts and deposits at banks	626,866	0	0

* SEB Pank AS and Swedbank AS no longer have a separate Moody's credit rating. The parent of Swedbank AS, Swedbank AB has Moody's credit rating of A2, the parent of SEB Pank AS, Skandinaviska Enskilda Banken AB has Moody's credit rating of A1.

Note 7

TRADE AND OTHER RECEIVABLES

	31/12/2010	31/12/2009	01/01/2009
Trade receivables			
Accounts receivable	336,949	189,115	184,377
incl: trade receivables from related parties (Note 22)	273,389	162,523	149,035
Allowance for doubtful receivables	-376	-388	0
Other receivables	285	18	47
incl: interest receivable	274	0	0
Total financial assets within trade and other receivables	337,234	189,133	184,424
Tax receivables	3,958	15,371	6,402
incl: VAT recoverable	3,883	12,243	6,318
Prepayments	967	4,064	1,420
Total trade and other receivables	342,159	208,568	192,246
Analysis by credit quality of trade receivables is as follows:			
<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Accounts receivable not yet due			
■ Related parties excluding distribution networks	22,944	19,801	21,227
■ Distribution networks	267,818	154,008	135,870
■ Other clients	45,710	14,755	23,547
Total accounts receivable not yet due	336,472	188,564	180,644
Accounts receivable past due but not classified as doubtful			
■ 1 to 30 days overdue	385	230	3,720
■ 31 to 60 days overdue	80	179	8
■ 61 to 90 days overdue	12	142	5
Total accounts receivable past due but not classified as doubtful	477	551	3,733
Accounts receivable classified as doubtful			
■ 90 to 180 days overdue	32	345	0
■ 180 to 360 days overdue	325	43	0
■ over 360 days overdue	19	0	0
Total accounts receivable classified as doubtful	376	388	0
Total accounts receivable past due	853	939	3,733
Total trade receivables	336,949	189,115	184,377

Note 8

PROPERTY, PLANT AND EQUIPMENT

Movements in the carrying amount of property, plant and equipment were as follows:

In thousands of Estonian kroons	Land	Buildings	Facilities	Machinery and equipment	Other	Construction in progress	Total
Property, plant and equipment at 01.01.2009							
Cost at 01.01.2009	49,600	182,840	3,553,498	2,472,351	297	0	6,258,586
Accumulated depreciation	0	-37,336	-759,975	-594,246	-16	0	-1,391,573
Carrying amount 01.01.2009	49,600	145,504	2,793,523	1,878,105	281	0	4,867,013
Construction in progress	0	0	0	0	0	479,915	479,915
Total property, plant and equipment at 01.01.2009	49,600	145,504	2,793,523	1,878,105	281	479,915	5,346,928
Movements 1.1.2009-31.12.2009							
Additions	8,554	0	0	1,675	465	453,312	464,006
Reclassified from construction in progress	0	76,116	92,276	455,042	0	-623,434	0
Capitalised borrowing costs (Note 21)	0	0	0	0	0	7,898	7,898
Disposals	-10	0	0	-110	0	0	-120
Depreciation charge	0	-7,337	-148,843	-147,330	-128	0	-303,638
Impairment charge	0	0	-12	-801	0	-80	-893
Total movements 1.1.2009-31.12.2009	8,544	68,779	-56,579	308,476	337	-162,304	167,253
Property, plant and equipment at 31.12.2009							
Cost at 31.12.2009	58,144	254,601	3,643,599	2,884,274	762	0	6,841,380
Accumulated depreciation	0	-40,318	-906,655	-697,693	-144	0	-1,644,810
Carrying amount at 31.12.2009	58,144	214,283	2,736,944	2,186,581	618	0	5,196,570
Construction in progress	0	0	0	0	0	317,611	317,611
Prepayments	1,975	0	0	0	0	0	1,975
Total property, plant and equipment at 31.12.2009	60,119	214,283	2,736,944	2,186,581	618	317,611	5,516,156
Movements 1.01.2010-31.12.2010							
Additions	8,319	0	0	885	0	377,051	386,255
Reclassified from construction in progress	0	11,664	117,201	307,849	0	-436,714	0
Capitalised borrowing costs (Note 21)	0	0	0	0	0	15,361	15,361
Disposals	-18	0	0	-4,080	0	0	-4,098
Depreciation charge	0	-7,563	-146,758	-152,965	-186	0	-307,472
Impairment charge	0	0	-56,034	-909	0	-4,711	-61,654
Total movements 1.01.2010-31.12.2010	8,301	4,101	-85,591	150,780	-186	-49,013	28,392
Property, plant and equipment at 31.12.2010							
Cost at 31.12.2010	66,445	263,417	3,684,744	3,153,076	762	0	7,168,444
Accumulated depreciation	0	-45,033	-1,033,391	-815,715	-330	0	-1,894,469
Carrying amount 31.12.2010	66,445	218,384	2,651,353	2,337,361	432	0	5,273,975
Construction in progress	0	0	0	0	0	268,598	268,598
Prepayments	1,975	0	0	0	0	0	1,975
TOTAL PROPERTY, PLANT AND EQUIPMENT AT 31.12.2010	68,420	218,384	2,651,353	2,337,361	432	268,598	5,544,548

Construction in progress mainly consists of construction of substations and electricity transmission lines. Upon completion, assets are transferred to buildings and facilities.

In the financial year ended 31.12.2010, additions to construction in progress include capitalised borrowing costs of EEK 15,361 thousand (2009: EEK 7,898 thousand). The capitalisation rate was 4.4%.

In 2010, the Company launched preparations for the construction of the second connection between Estonia and Finland (Estlink 2), including thorough renovation of the current lines for the purpose of increasing their throughput capacity. As a result of the activities mentioned above, some of the obsolete assets related to the lines were written down (2010: EEK 42,930 thousand, 2009: EEK 0) and the lines were renovated.

Note 9

OPERATING LEASE

Company as a lessor

Operating lease revenue:

<i>In thousands of Estonian kroons</i>	2010	2009
Buildings	6,434	1,525
Transmission equipment	12,823	9,618
Total operating lease revenue (Note 15)	19,257	11,143

Transmission equipment

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

Information about assets (facilities) leased out under operating leases:

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
Cost	90,675	73,811	71,024
Accumulated depreciation at the end of period	-33,975	-28,097	-22,489
Carrying amount	56,700	45,714	48,535

Depreciation charge

<i>In thousands of Estonian kroons</i>	2010	2009
Depreciation charge	5,709	5,621

Estimated future lease payments under operating leases:

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009
Not later than 1 year	12,824	12,823
Later than 1 year and not later than 5 years	51,296	51,292
Later than 5 years	118,622	131,436
Total future minimum lease payments	182,742	195,551

Company as a lessee

Operating lease expenses:

<i>In thousands of Estonian kroons</i>	2010	2009
Buildings	564	6,537
Transport equipment	873	1,368
Other machinery and equipment	1,470	26
Total operating lease expenses	2,907	7,931

All lease contracts are cancellable at short notice.

Note 10**INTANGIBLE ASSETS**

	<i>In thousands of Estonian kroons</i>	<i>Acquired software</i>	<i>Right of use of land</i>	<i>Total</i>
Intangible assets at 1.1.2009				
Cost at 1.1.2009	262	12,141	12,403	
Accumulated amortisation	-110	-360	-470	
Carrying amount at 1.1.2009	152	11,781	11,933	
Intangible assets not yet available for use	5,904	0	5,904	
Total intangible assets at 1.1.2009	6,056	11,781	17,837	
Movements 1.1.2009-31.12.2009				
Additions	9,181	3,935	13,116	
Capitalised borrowing costs (Note 21)	344	0	344	
Amortisation charge	-146	-150	-296	
Total movements 1.1.2009-31.12.2009	9,379	3,785	13,164	
Intangible assets at 31.12.2009				
Cost at 31.12.2009	630	16,075	16,705	
Accumulated amortisation	-257	-509	-766	
Carrying amount at 31.12.2009	373	15,566	15,939	
Intangible assets not yet available for use	15,062	0	15,062	
Total intangible assets at 31.12.2009	15,435	15,566	31,001	
Movements 1.01.2010-31.12.2010				
Additions	14,780	2,621	17,401	
Capitalised borrowing costs (Note 21)	841	0	841	
Amortisation charge	-556	-190	-746	
Total movements 1.01.2010-31.12.2010	15,065	2,431	17,496	
Intangible assets at 31.12.2010				
Cost at 31.12.2010	3,364	18,696	22,060	
Accumulated amortisation	-813	-699	-1,512	
Carrying amount at 31.12.2010	2,551	17,997	20,548	
Intangible assets not yet available for use	27,949	0	27,949	
Total intangible assets at 31.12.2010	30,500	17,997	48,497	

Note 11**BORROWINGS**

<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Overdraft (Note 22)	0	889,252	386,121
incl: bank overdraft	0	243	0
Current portion of long-term loans from parent company	0	2,046,586	0
Total current borrowings	0	2,935,838	386,121
Long-term bank loan	2,905,493	0	0
Long-term loan from parent company (Note 22)	0	0	2,046,586
Total non-current borrowings	2,905,493	0	2,046,586
Total borrowings	2,905,493	2,935,838	2,432,707

The Company's borrowings are denominated in currencies as follows:

<i>In thousands of Estonian kroons</i>	<i>31/12/2010</i>	<i>31/12/2009</i>	<i>01/01/2009</i>
Borrowings denominated in: EEK	0	2,935,595	2,432,707
Borrowings denominated in: EUR	2,905,493	243	0
Total borrowings	2,905,493	2,935,838	2,432,707

The Company has used two types of credit for financing purposes:

Loan

At 28.12.2009, the Company entered into a syndicated loan contract in the amount of EUR 187 million (EEK 2,925,914 thousand) with the due date of 28.12.2012. The total loan amount was taken out at 8.01.2010. The interest rate is Euribor + 3.00%.

In 2009, the Company had a loan agreement with Eesti Energia AS. According to the agreement, Eesti Energia AS lent the Company EEK 2 046 586 thousand for an unspecified term, with the right of recall with advance notice of 13 months. Interest rates were established by Eesti Energia AS for a period of one year in accordance with the average actual interest expenses charged on the borrowings of Eesti Energia AS, and the Company's risk margin. The effective interest rate of the loan was 4,88% in 2009. The syndicated loan agreement obliged the Company to return the loan to the parent company in full. On 8.1.2010 the Company repaid the loan to the Parent company.

As at 31.12.2010, the Company had undrawn loan facilities in the amount of EEK 1,564,660 thousand. The right to take out a portion of the loan granted by the European Investment Bank (EEK 1,173,495 thousand) or the full amount of it is effective during 36 months from the signing of the contract at 18.11.2010. In accordance with the contract entered into with Nordic Investment Bank at 20.10.2010, either a portion or the full amount of the loan (EEK 391,165 thousand) can be taken during the period of 8.07.2011-31.12.2014. For both contracts, the interest rate will be agreed prior to taking out each portion.

Overdraft

During the period of 1.01.2010-8.01.2010 and in 2009, the Company used the overdraft obtained from its then parent Eesti Energia AS. The interest rate was 4.88% (2009: 4.81%). At the date of taking out the syndicated loan referred to in the previous section, the total amount of the overdraft was paid back to Eesti Energia AS and the respective overdraft contract was terminated. Simultaneously with the conclusion of the syndicated loan contract, four overdraft contracts were concluded with the banks which participate in the syndicate with the total limit amount of EUR 20 million (EEK 312,932 thousand). The due dates of all contracts and interest on the drawn portion are the same as those of the syndicated loan. As of the balance sheet date, the Company had not used the overdraft (31.12.2009: EEK 889,252 thousand, 01.01.2009: EEK 386,121 thousand).

Note 12**TRADE AND OTHER PAYABLES**

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
Trade payables	255,207	124,847	71,195
Incl: trade payables to related parties (Note 22)	126,913	59,490	32,049
Payables for purchased property, plant and equipment and intangible assets	38,824	27,393	30,428
Incl: payables to related parties (Note 22)	53	36	0
Subsidies due to electricity producers (Note 2)	236,021	104,126	77,803
Accrued interest	27,173	0	0
Other payables	1,205	1,000	1,140
Incl: payables to related parties (Note 22)	500	500	500
Total financial liabilities within trade and other payables	558,430	257,366	180,566
Taxes payable:	6,522	5,017	4,950
Social security tax	2,910	2,241	2,215
Personal income tax	1,692	1,302	1,236
Unemployment insurance tax	306	232	50
Contributions to mandatory funded pension	72	22	82
Corporate income tax and income tax on fringe benefits	49	0	37
Excise tax	1,493	1,220	1,330
Accrued expenses - employee benefits:	3,491	5,245	6,999
Wages and salaries	0	2,301	2,203
Bonuses	782	0	1,474
Holiday pay	1,816	2,186	2,117
Social security and unemployment insurance tax	893	751	1,195
Withheld amounts	0	7	10
Other payables	165	6,210	14,207
Total trade and other payables	568,608	273,838	206,722

Note 13**INCOME FROM CONNECTION AND OTHER SERVICE FEES**

<i>In thousands of Estonian kroons</i>	Deferred income from connection and other service fees at 1.1.2009	319,961
Movements 1.1.2009-31.12.2009		
Connection and other service fees received		42,063
Connection and other service fees recognised as revenue		-15,483
Deferred income from connection and other service fees at 31.12.2009		346,541
Movements 1.01.2010-31.12.2010		
Connection and other service fees received		20,786
Connection and other service fees recognised as revenue		-17,942
Deferred income from connection and other service fees at 31.12.2010		349,385
Prepayments related to government grants at 01.01.2009		0
Prepayments related to government grants at 31.12.2009		0
Subsidies received from European Union*		237,033
Prepayments related to government grants at 31.12.2010		237,033
Incl. Non-current prepayments		237,033

* See additional information in Note 23.

Note 14**EQUITY**

The Company's share capital consists of one share with the nominal value of EEK 2,190,524 thousand (31.12.2009: EEK 2,100,000 thousand, 01.01.2009 EEK 2,100,000 thousand). The share has been paid for in full.

In 2010, with the resolution of the sole shareholder, the share capital was increased by EEK 90,524 thousand. The payment for the increase in the nominal value of the share was made in December 2010.

In the financial year 1.1.2010- 31.12.2010, no dividends were paid (in 2009 dividends were declared and paid in the amount of EEK 480,092 thousand and the resulting income tax amounted to EEK 127,619 thousand).

As at 31.12.2010, the Company's statutory reserve capital totalled EEK 44,039 thousand (31.12.2009: EEK 44,039 thousand, 01.01.2009: EEK 30,261 thousand). As at 31.12.2010, the Company has the obligation to additionally transfer EEK 10,576 thousand (31.12.2009: EEK 0, 01.01.2009: EEK 13,778 thousand) to reserve capital.

The retained earnings of the Company as at 31 December 2010 amounted to EEK 266,988 thousand (31.12.2009: EEK 55,469 thousand; 01.01.2009: EEK 467,360 thousand). The income tax rate applicable to the net profit distributable as dividends is 21/79 from 1 January 2008. As at 31.12.2010, it would be possible to distribute EEK 202,565 thousand as net dividends (31.12.2009: EEK 43,821 thousand, 01.01.2009: EEK 358,330 thousand) and the corresponding income tax would amount to EEK 53,847 thousand (31.12.2009: EEK 11,648 thousand, 01.01.2009: EEK 95,252 thousand).

Note 15**REVENUE**

Analysis of revenue by activity:

<i>In thousands of Estonian kroons</i>	2010	2009
Sales of balancing and control electricity	247,736	102,385
Sales of network services		
Transmission fees	1,052,067	1,010,800
Revenue from connection fees (Note 13)	17,942	15,483
Other network services*	36,598	35,490
Total sales of network services	1,106,607	1,061,773
Sales of other goods and services		
Lease of transmission equipment (Note 9)	12,823	12,626
Sales of scrap metal	11,048	634
Lease of buildings (Note 9)	6,434	1,525
Sales of other services*	5,739	2,309
Other goods	42	61
Total sales of other goods and services	36,086	17,155
TOTAL REVENUE	1,390,429	1,181,313

* In the financial statements of 2009, the dispatcher and regulation services were classified within network services. In these financial statements these services are included within other services and the expenses in the comparative period in the amount of EEK 2,089 thousand have been reclassified accordingly.

Analysis of revenue by geographical location of customers:

<i>In thousands of Estonian kroons</i>	2010	2009
Estonia	1,360,985	1,109,117
Latvia	19,511	35,976
Russia	5,945	35,927
Lithuania	3,724	293
Finland	264	0
Total revenue	1,390,429	1,181,313

Note 16**OTHER INCOME**

<i>In thousands of Estonian kroons</i>	2010	2009
Fines, penalties and compensations received	308	0
Profit on disposal of property, plant and equipment	961	244
Net gain from exchange rate changes	0	37
Other	79	2
Total other income	1,348	283

Note 17**GOODS, RAW MATERIALS AND SERVICES**

<i>In thousands of Estonian kroons</i>	2010	2009
Electricity purchased to provide the balancing service		
Purchase of balancing electricity	149,132	94,871
Purchase of power regulation service	92,212	5,313
Total electricity purchased to provide the balancing service	241,344	100,184
System services expenses		
Purchased electricity reserves	67,246	64,903
Reactive energy	2,528	2,391
Total system services expenses	69,774	67,294
Electricity to compensate for network losses		
Electricity from non-renewable sources	178,317	174,170
Total electricity to compensate for network losses	178,317	174,170
Maintenance and repair works		
On facilities and equipment related to core activities	68,175	66,276
On production buildings and sites	11,414	6,514
Disassembly works and waste processing	2,028	2,693
Other expenses	3,077	1,163
Total maintenance and repair works	84,694	76,646
Other expenses		
Operative switching and dispatching management expenses	9,024	9,054
Other expenses	7,600	24,854
Total other expenses	16,624	33,909
Total goods, raw materials and services	590,753	452,203

Note 18**OTHER OPERATING EXPENSES**

<i>In thousands of Estonian kroons</i>	2010	2009
Transportation and tools	1,235	1,596
Security, insurance and occupational safety	4,323	3,335
Office expenses	6,456	8,229
Research and consulting	6,169	5,781
Telecommunication	14,065	14,024
Information technology	6,752	6,484
Training and other operating expenses	7,045	8,439
Total other operating expenses	46,045	47,888

Note 19**STAFF COSTS**

<i>In thousands of Estonian kroons</i>	2010	2009
Basic salaries, additional remuneration, bonuses, vacation pay	42,607	39,611
Other benefits	236	289
Termination benefits	187	1,247
Other remuneration	1,267	898
Total remuneration to employees	44,297	42,045
Social security tax	14,669	14,131
Unemployment insurance tax	555	398
Total staff costs	59,521	56,574

Including compensations to the members of the Management and Supervisory Board:

Salaries, additional remuneration bonuses, vacation pay	3,140	2,836
Fringe benefits	278	143
Termination benefits	0	340
Social security tax	1,151	1,095
Total compensations to the members of the Management and Supervisory Boards	4,546	4,414

The average monthly pay was EEK 26,301 (2009: EEK 26,198).

Termination benefits

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

Note 20**OTHER EXPENSES**

<i>In thousands of Estonian kroons</i>	2010	2009
Non-business related expenses	434	606
Fines, penalties and compensations paid	1	23
Net loss from exchange rate changes	5	2
Income tax from expenses not related to business	75	136
Other	134	3
Total other expenses	649	770

Note 21**FINANCE INCOME AND COSTS**

<i>In thousands of Estonian kroons</i>	2010	2009
Finance income		
Interest income	1,334	0
Foreign exchange gains	22	0
Total finance income	1,356	0
Finance costs		
Interest expenses	-130,876	-117,958
Foreign exchange losses	0	-20
Total finance costs	-130,876	-117,978
Less: capitalised finance costs (Notes 8, 10)	16,202	8,242
Total finance income and costs recognised in the statement of comprehensive income	-114,674	-109,736

Detailed information about the borrowings is disclosed in Note 11.

Note 22**BALANCES AND TRANSACTIONS WITH RELATED PARTIES**

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

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

- I Republic of Estonia and the entities under its control or significant influence;
- II Management and supervisory boards;
- III close relatives of the persons described above and the entities under their control or significant influence;
- IV until 27.01.2010 parent company and other entities in the consolidation group of the parent company (i.e fellow subsidiaries)

The outstanding balances with related parties were as follows:

<i>In thousands of Estonian kroons</i>	31/12/2010	31/12/2009	01/01/2009
Trade receivables (Note 7)			
Parent company	0	4,033	118
Fellow subsidiaries	0	144,403	135,699
Companies controlled or significantly influenced by the State	273,389	14,087	13,218
Total trade receivables (Note 12)	273,389	162,523	149,035
incl. from network operators	250,445	144,500	128,928
Trade payables and other liabilities			
Parent company	0	17,539	13,206
Fellow subsidiaries	0	42,290	19,316
Companies controlled or significantly influenced by the State	127,466	197	27
Total trade payables and other liabilities	127,466	60,026	32,549
Overdraft (Note 11)			
Parent company	0	889,009	386,121
Current borrowings (Note 11)			
Parent company	0	2,046,586	0
Non-current borrowings (Note 11)			
Parent company	0	0	2,046,586

Income and expense items with related parties were as follows:

<i>In thousands of Estonian kroons</i>	<i>Related party</i>	<i>2010</i>	<i>2009</i>
Revenue from sale of goods and services	Parent company ¹	7,839	30,473
	Fellow subsidiaries ¹	131,239	871,589
	Companies controlled or significantly influenced by the State	1,090,187	93,990
Total revenue from sale of goods and services		1,229,265	996,052
Purchase of goods and services	Parent company ¹	5,427	57,949
	Fellow subsidiaries ¹	29,550	212,071
	Companies controlled or significantly influenced by the State	214,891	3,970
Total purchase of goods and services		249,868	273,990
Interest cost	Companies controlled or significantly influenced by the State	0	0
	Parent company ¹	2,783	117,950
	Incl. Capitalised borrowing costs (Note 21)	- 301	- 8,242
Expenditures on non-current assets	Parent company ¹	379	65,247 ²
	Fellow subsidiaries ¹	2,108	16,436
	Companies controlled or significantly influenced by the State	928	3,805
Total expenditures on non-current assets		3,415	85,488

¹ the Company was part of Eesti Energia Group until 27.01.2010. The sales to related parties in 2010 also include the transactions with the entities of Eesti Energia Group concluded in January 2010.

² the Company separated from Eesti Energia Group: it purchased a commercial building at Kadaka tee 42 and the adjoining land for the total amount of EEK 64 million.

Transactions with companies, in which the members of the Supervisory and Management Boards as well as their close relatives have significant influence

<i>In thousands of Estonian kroons</i>	<i>2010</i>	<i>2009</i>
Sales of services	5	5
Purchases of services	21	0

Key management personnel compensations are disclosed in Note 19.

Note 23

CONTINGENCIES AND COMMITMENTS

Network development obligations

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

Capital expenditure commitments At 31.12.2010, the Company has contractual capital expenditure commitments in respect of property, plant and equipment totalling EEK 3,618,496 thousand (31.12.2009: EEK 283,748 thousand, 01.01.2009: EEK 233,565 thousand). The largest of them are the contracts for the construction of the second undersea electricity cable Estlink 2 between Estonia and Finland in 2011-2014. The contribution of Elering is EEK 2,845,299 thousand.

As at 31.12.2010, the Company had already concluded two long-term (15-20 years) loan contracts in the total amount of EUR 100 million (EEK 1,564,660 thousand) for funding the commitments related to Estlink 2. Also, the European Union has allocated non-returnable aid in the amount of EUR 50 million (EEK 782,330 thousand) for the construction of Estlink 2, of which EUR 15 million (EEK 234,699 thousand) had already been paid out to the Company. The Company believes that future net income and funding will be sufficient to cover these and any similar commitments.

Tax legislation

The tax authorities have the right to verify the Company's tax records up to 6 years from the time of submitting the tax declaration and upon finding errors, impose additional taxes, interest and fines. The Company's management estimates that there are not any circumstances which may lead the tax authorities to impose additional significant taxes on the Company.

Other legal requirements

Other legal requirements which have an effect on profitability:
In accordance with the methodology for calculating the network fees of electricity networks used by the Competition Board, the network tariffs are calculated for each year, using the known electricity transmission throughput over the 12 months prior to the tariff application. When the actual transmission throughput falls short of the budgeted one, the Company will not receive a portion of revenue and compensation for it. But when the actual transmission throughput turns out to be larger than that used in the calculation, the Company does not need to repay the excess revenue in the following periods.

Note 24

EVENTS AFTER THE BALANCE SHEET DATE

Adoption of the euro

At 01.01.2011, the Republic of Estonia joined the Euro area and adopted the euro as its national currency, replacing the Estonian kroon. Therefore, starting from 01.01.2011, the functional currency of Elering OÜ is the euro and the statutory financial statements of future periods will be presented in euros. The comparative figures will be recalculated into euros using the conversion rate of EUR 1 / EEK 15.6466 which was also the fixed exchange rate during previous periods.

Transformation of the Company into a public limited company

At 25.02.2011, the Company's sole shareholder proposed to transform Elering OÜ into a public limited company. The share capital of the public limited company will consist of 140,000 shares with the nominal value of EUR 1,000 each. According to the resolution, the members of the Management and Supervisory Boards and the auditor will remain the same. The aforementioned transformation entry was made with the Commercial Register on 08.04.2011.a.



INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

Report on the Financial Statements

To the Shareholder of Elering AS (former Elering OÜ)

We have audited the accompanying financial statements of Elering AS (the Company), which comprise the statement of financial position as of 31 December 2010 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management Board's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation, and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Company as of 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Report on the Legal and Regulatory Requirements

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

AS PricewaterhouseCoopers

Ago Vilu
Auditor's Certificate No.325

Aleksei Kadõrko
Auditor's Certificate No.557

11 April 2011

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

PROFIT ALLOCATION PROPOSAL

The retained earnings of Elering OÜ as at 31 December 2010 were EEK 266,988,122.

Management Board of Elering OÜ proposes to the sole shareholders to allocate the retained earnings as follows:

statutory legal reserve: EEK 10,575,958

retained earnings: EEK 256,412,164

SIGNATURES OF THE MANAGEMENT TO THE 2010 ANNUAL REPORT

The signing of Elering OÜ 2010 Annual Report on April 11, 2011.



Taavi Veskimägi
Chairman of the Management Board



Kalle Kilk
Member of the Management Board



Peep Soone
Member of the Management Board

THE REVENUE OF ELERING OÜ ACCORDING TO EMTAK 2008

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

EMTAK* area of activity	2010	2009
35121 Transmission of electricity – transmission through the transmission network	1,106,607	1,063,862
35141 Trade of electricity (balancing electricity)	247,736	102,385
77399 Renting and leasing of other machinery, equipment and tangible goods n.e.c.	12,823	12,626
47799 Retail sale of other second-hand goods	11,090	695
68201 Renting and operating of own or leased real estate	6,359	1,643

* EMTAK – classification of Estonian economic activities



GENERATING OPPORTUNITIES

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