

JSC Latvijas Gāze

ANNUAL REPORT

2009

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JSC Latvijas Gāze

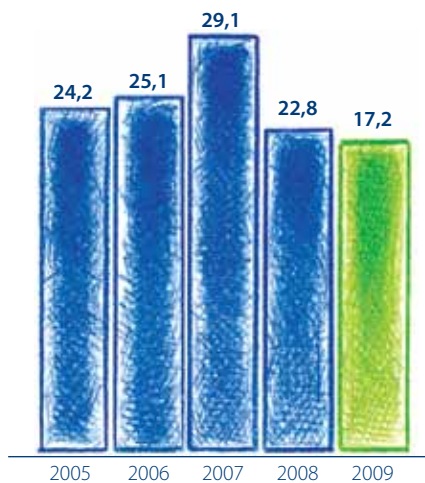
Our objective is to strengthen the JSC *Latvijas Gāze's* position as a leader in the Latvian heating market, by increasing the availability of natural gas, promoting the variety of its consumption, and ensuring Latvia with one of the most stable natural gas supplies in Europe.

Our vision is to transform Latvia into one of Europe's largest natural-gas storage centers, utilizing our country's unique geological formations.

Our mission is to contribute to the Baltic region's economy, by ensuring the safety of energy supply, the development of the sector, and competitive pricing.

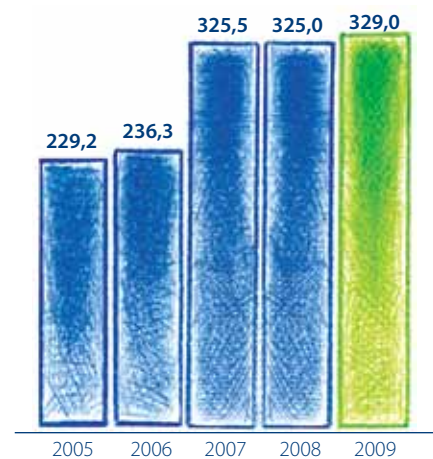
Investment

(LVL million)



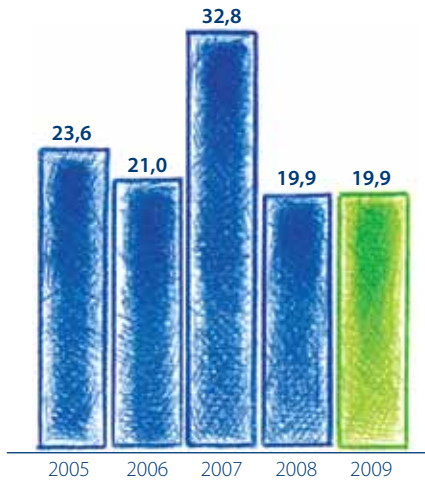
Equity

(LVL million)



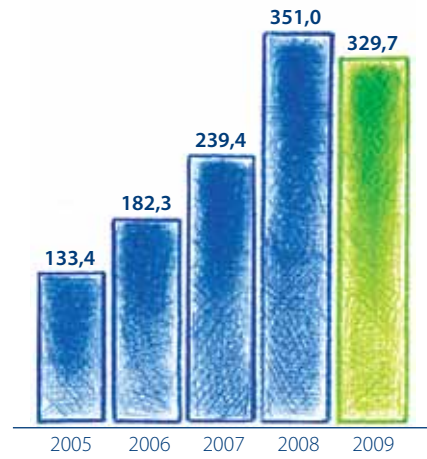
Net profit

(LVL million)



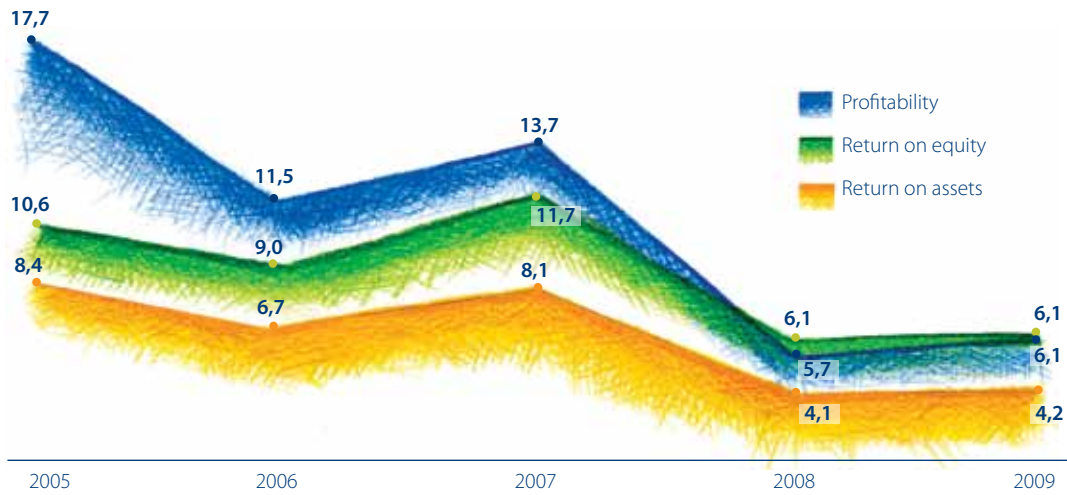
Net turnover

(LVL million)



Main financial indices

(%)



The year 2009 will remain in the human history as time of a profound crisis. In Latvia the economic recession this year was among the sharpest in Europe. The performance of the Joint Stock Company *Latvijas Gāze* (hereinafter – the Company) over this time was influenced not only by the dip of economic activity, but also by the changes in natural gas consumption due to its price fluctuations and the uncharacteristic cold at the end of the year.

The Company's priorities in these complicated and changeable circumstances were still the provision of uninterrupted and secure natural gas supply to its customers, the attraction of new customers by expanding the existing natural gas supply networks and the provision of services to foreign consumers. In order to reduce the costs of services provided, new operation standards were introduced and the number of employees was decreased.

In 2009 the Company sold to consumers 1 492.9 billion m³ of natural gas and the turnover of the Company reached 329.7 million LVL (469.1 million EUR), whereas the net profit amounted to 19.97 million LVL (28.41 million EUR). The Company spent 17.2 million LVL (24.47 million LVL) on modernization, customer attraction, and safety enhancement. The key projects implemented are the reconstruction of wells and the gas drying point at the Inčukalns Underground Gas Storage Facility and the diagnostics of gas transmission pipelines and the elimination of the damage found. Apart from that, 1.1 thousand new customers were attracted over the last year.

In its meetings held in 2009, the Council heard out and discussed the reports prepared by the Board regarding the operation of the Company in the volatile market conditions. The Council issued to the Board orders and recommendations for the improvement of the Company's operation, reviewed and approved amendments to the agreement with the natural gas supplier OJSC *Gazprom*, including changes in the gas storage and transportation service tariffs. In order to ensure sustainable development of the Company, the Council accepted the „JSC *Latvijas Gāze* action plan for the improvement of safety of the gas supply system 2010-2015“ prepared by the Board. Thus, the consumers are guaranteed natural gas supplies for a long period of time and investments in the natural gas system are ensured.

Last year the Council members E. Benke and M. Soehrich ended their work at the Council, and new members – J. Hockertz and M. Nullmeier – were elected instead of them. The Council expresses its gratitude for and acknowledgement of the former members' effort and contribution to the development of the Company and wishes success to J. Hockertz and M. Nullmeier.

The Council became acquainted with the Corporate Governance Report for the previous year, prepared by the Board in compliance with the „Corporate Governance Principles and Recommendations on Their Implementation“ issued by the JSC *NASDAQ OMX Riga*, and concluded that the Board has done significant work in order for the Company to observe the recommended principles of corporate governance. The Council follows these principles, too.

Over the reporting period, the Council regularly received the Board reports on the business operations, economic and financial situation of the Company. The Council has supervised the work of the Board in all main areas and made sure that the Company operates in compliance with the legislation, the Articles of Association of the Company and the resolutions of the Shareholders' meeting, verified and accepted the submitted budget of Company, as well as made proposals on the improvement of the Company's work.

The annual report 2009 of the Company was audited by the international auditor company *PricewaterhouseCoopers* LLC.

The Council has received the auditor's reports stating that the financial accounts provide a true and fair view on the JSC *Latvijas Gāze*, as well as on the financial results of its operation and cash flows in 2009 in compliance with the „Annual Reports Law“ of the Republic of Latvia. The Council has reviewed and accepted the Board report on the activity of the Company in the reporting year, research and development measures, the management of financial risks, as well as proposals regarding the distribution of the profit of 2009.

The Council of the Company acknowledges the successful performance of the Board and employees in 2009 and wishes further success and growth in future.

Chairman of the Council:



K. Seleznev

The Council of the JSC Latvijas Gāze



Kirill Seleznev
Chairman of the Council

Since March 20, 2003 Head of the Gas and Liquid Hydrocarbon Sales and Processing Department, OJSC *Gazprom*; Member of the Board OJSC *Gazprom*

1997 Graduated from Baltic State Technical University of St. Petersburg named after D. F. Ustinov – Engineering of Impulse Devices and Automated Rotation Lines

2002 Graduated from St. Petersburg State University – Credit Theory and Finance Management



Achim Saul
Vice-Chairman of the Council

2005 – 2008 *E.ON Gaz România Group*, Chairman of the Board, Targumures, Romania

Since March 2008 *E.ON Ruhrgas International AG*, Member of the Board of Directors, Essen – responsible for foreign branches, legal issues, human resources and organization

1987 Doctorate (*Dr. Ing.*), University of Ruhr, Bochum



Juris Savickis
Vice-Chairman of the Council

Since 1996 LLC *ITERA Latvija*, president

1970 – 1972 Polytechnical Institute of Riga, Graduate school

1983 - 1984 University of Qualification Raising for Executives, Faculty of International Relations

The Council of the JSC Latvijas Gāze



Joachim Hockertz

2000 – 2002 Head of the Baltic Office of *Ruhrgas AG*

Since 2002 *E.ON Ruhrgas International AG*

1989 – 1992 Max Plank Institute in Mulheim-am-Ruhr, Ph.D.



Uwe Fip

Since 2002 *E.ON Ruhrgas AG* – Senior Vice-President, Head of Eastern Department of Gas Supplies

Master in Oil Engineering, Degree in Business Management (Diploma – Merchant)



Mario Nullmeier

Since 2005 Head of the Baltic Office of *E.ON Ruhrgas International AG* in Tallinn, Estonia

2000 Master Degree in Global Business Administration



Heinz Watzka

Since 2002 Senior Vice-President of *E.ON Ruhrgas AG*, responsible for maintenance of the southern gas pipeline system of *E.ON Ruhrgas*

1986 Studied machine manufacturing at the Technical University of Vienna (Austria) – specialized in pump station welding and hydraulic design for the oil industry



Yelena Karpel

Since 2004 Member of the Board of Directors of OJSC *Gazprom* following the resolution of the shareholders' meeting

1968 Korotchenko Kiev Institute of National Economy getting specialty in Industry Planning



Aleksandr Krasnenkov

Since 2006 General Director of the LLC *Baltijas sašķidrinātā gāze*

Graduated from the International Institute of Finance and Economics, speciality of international economics and international relations



Vlada Rusakova

Since 2003 Head of the Strategic Development Department, OJSC *Gazprom*

Since 2003 Board member of the OJSC *Gazprom*

1977 Graduated from the Moscow Oil and Gas Industry Institute named after I. M. Gubkin and obtained the qualifications of engineer in design, planning and operation of oil and gas pipelines, gas storage facilities and oil tanks



Igor Nazarov

Since 2007 Director of the Export Department, NGK *ITERA* (Moscow, Russia)

1982 Moscow State University of Foreign Affairs (MGIMO) (within the framework of the Ministry of Foreign Affairs), Diploma of Commercial Department, which equals the Master of Economics: an economist with knowledge of foreign languages (Italian and English)

The Board of the JSC *Latvijas Gāze*



Adrians Dāvis
Chairman of the Board

Since 1997 Chairman of the Board of the JSC *Latvijas Gāze*; involved in gas industry since 1965

1997 Physical Energy Institute of Latvian Science Academy, Ph.D. in engineering (Dr.sc.ing.).



Aleksandr Mihejev
Board member, Vice-Chairman of the Board

Since 2003 First Deputy Head of the Marketing, Gas and Liquid Hydrocarbon Processing Department of the OJSC *Gazprom*; involved in gas industry since 1968

1968 Graduated from the Moscow Oil and Gas Industry Institute named after I. M. Gubkin and obtained the qualifications of engineer in design and operation of oil and gas pipelines, gas storage facilities and oil tanks



Joerg Tumat
Board member, Vice-Chairman of the Board

Since 2006 Vice-Chairman of the Board

2001 – 2006 *E.ON Ruhrgas AG / Ruhrgas AG. Eastern Gas Purchase Department*, Head of Division; OJSC *Gazprom* share and eastern gas purchase contracts; involved in gas industry since 1998.

2001 – 2004 the University of Hagen, Diploma in Business Administration (Dipl.-Betriebswirt)



Anda Ulpe
Board member

Since 1997 Board member of the JSC *Latvijas Gāze*; involved in gas industry since 1984

2002 the University of Latvia, Master of Social Sciences in Economics



Gints Freibergs
Board member

Since 1997 Board member of the JSC *Latvijas Gāze*; involved in gas industry since 1984

1984 Polytechnical Institute of Riga, engineer in industrial heat power

Despite the aggravation of the economic situation in Latvia, the JSC *Latvijas Gāze* operated successfully in the reporting year, yielding profit to the company's shareholders.

The capitalization value of the Company at the end of 2009 reached 163.6 million LVL (232.8 million EUR), which is by 17.9 million LVL (25.5 million EUR) less than at the end of the previous reporting period. The decrease of the capitalization value resulted from the influence of the global financial crisis, which made for a negative investment climate in the stock market and its general recession.

By the stock market capitalization value, the JSC *Latvijas Gāze* retained the second place from the previous reporting period among the companies quoted at the *NASDAQ OMX Riga* (before 2009 – *Rīgas Fondu birža*) exchange, whereas among the companies quoted at the *NASDAQ OMX Baltic Exchange* the JSC *Latvijas Gāze* was ninth, which is two positions below its rank in 2008, still an improvement over 2007 when the company was eleventh at the Baltic Stock Exchange.

According to the data of TOP 101 of most valuable enterprises of Latvia compiled by the company of investment bankers *IBS Prudentia*, *NASDAQ OMX Riga* and the magazine of business ideas *Kapitāls* together with the information partner *Lursoft*, the JSC *Latvijas Gāze* was the fifth most valuable enterprise in Latvia in 2009. Back in 2008, the JSC *Latvijas Gāze* was ranked tenth in this list.

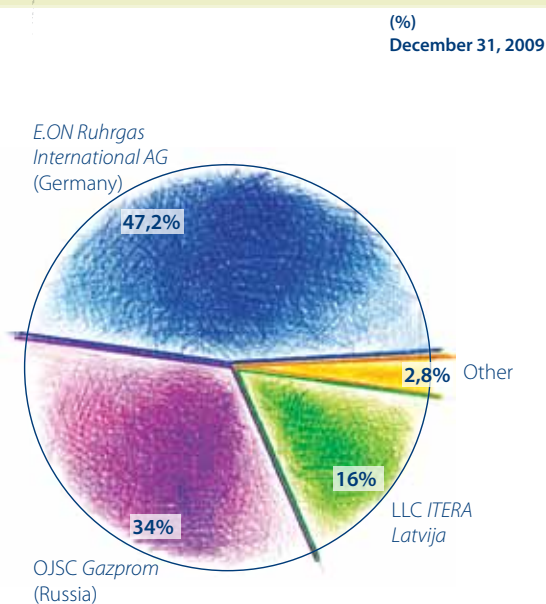
The share capital of the company at the end of the reporting year had not changed and amounted to 39.9 million LVL (56.8 million EUR), which breaks down to as many voting shares with the nominal value of 1.00 LVL (1.42 EUR). The number of publicly traded securities of the JSC *Latvijas Gāze* was 25 328 520.

Shares

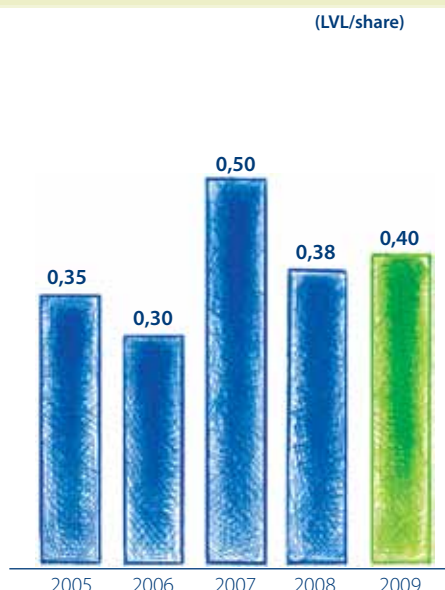
The shares of the JSC *Latvijas Gāze* have been quoted at the *NASDAQ OMX Riga* exchange since February 15, 1999. As of August 1, 2004, the share trade code is GZE1R. On August 1, 2008, the shares of the JSC *Latvijas Gāze* were transferred to the Second list of the Riga and Baltic security market of *NASDAQ OMX*.

ISIN	LV0000100899
Stock symbol	GZE1R
Index	B10GI, B10PI, OMXBBCAPGI, OMXBBCAPPI, OMXBBGI, OMXBBPI, OMXBGI, OMXBPI, OMXRGI

Shareholder Structure



Dividend per Share



JSC Latvijas Gāze Share Prices

OMX Baltic GI, OMX Baltic Energy GI cation index and the change in turnover
(01.01.2007.–31.03.2010.)



The price of one share of the company at *NASDAQ OMX Riga* fluctuated within the range of 3.32 LVL to 6.00 LVL (4.72 EUR to 8.54 EUR) over the reporting year, reaching 4.10 LVL (5.83 EUR) at the end of the year, which is by 9.89% less than in late 2008.

An evaluation of the price fluctuations shows that in 2008 they were more distinct, ranging from 3.62 LVL (5.15 EUR) to 8.20 LVL (11.67 EUR).

The number of transactions at the exchange in 2009 was 1 267, which is 444 transactions below the number of 2008, but relatively more than in the preceding three years.

Over the reporting year, the turnover of shares at *NASDAQ OMX Riga* reached 64 319 shares with the value of 0.277 million LVL (0.39 million EUR), outweighing the figure of 2008 by 17 754 shares.

In the reporting year, the company's shares were included in the *OMX Riga*, *OMX Baltic* and *OMX Baltic Energy* index baskets.

Structure of shareholders

The structure of shareholders of the *JSC Latvijas Gāze* did not change in the reporting year. At the end of 2009, the Company had three main shareholders – *E.ON Ruhrgas International AG* with 47.2% of shares, the *OJSC Gazprom* with 34% of shares and the LLC *ITERA Latvija* with 16% of shares. The rest of shares are held by minor shareholders, including employees of the *JSC Latvijas Gāze*.

Distribution of profit

The draft distribution of the profit of 2009 prepared by the Board of the *JSC Latvijas Gāze* envisages the payment of dividends in the amount of 0.40 LVL (0.57 EUR) per share or 15.96 million LVL (22.71 million EUR) in total, which equals to 79.9% of the Company's profit in 2009. In comparison to 2008, the amount of dividends due to be paid per one share has increased by 0.02 LVL (0.03 EUR) or 5.5%.

The amount of dividends per one share in 2009 is the second highest since 2007, when 0.50 LVL (0.71 EUR) per one share were allocated for dividends in the draft distribution of profit.

Consumption

Under the influence of the recession of the Latvian economy caused by the global financial crisis, the overall energy consumption in Latvia decreased as well in 2009. According to the provisional data of the Central Statistics Bureau of the Republic of Latvia, consumption of oil products in Latvia in 2009 was by 16% lower than the year before. As indicated by the data of the energy company *Latvenergo*, electricity supplies to the internal market fell from 7 537 gigawatt hours (GWh) in 2008 to 7 030 GWh in 2009, i. e., by 507 GWh or 7.2%.

A similar decrease in 2009 was also present in natural gas consumption, which fell down to 1 493 million cubic metres (m³), which is by 138 million m³ or 8.5% less than in 2008 when 1 631 million m³ of natural gas were consumed in Latvia. The sharpest drop in consumption occurred in industry. Enterprises have either suspended or considerably reduced their production, thus also the volume of natural gas purchase. Overall in 2009, the industrial customers consumed 260 million m³, which is by 70 million m³ of natural gas less than in 2008.

Public and commercial consumers, as well as households have also reduced their natural gas consumption. All these consumer groups have become more economical as to the use of natural gas – there are an increasing number of households and householders getting involved in various state-supported programmes of energy efficiency improvement and investing in this important area themselves.

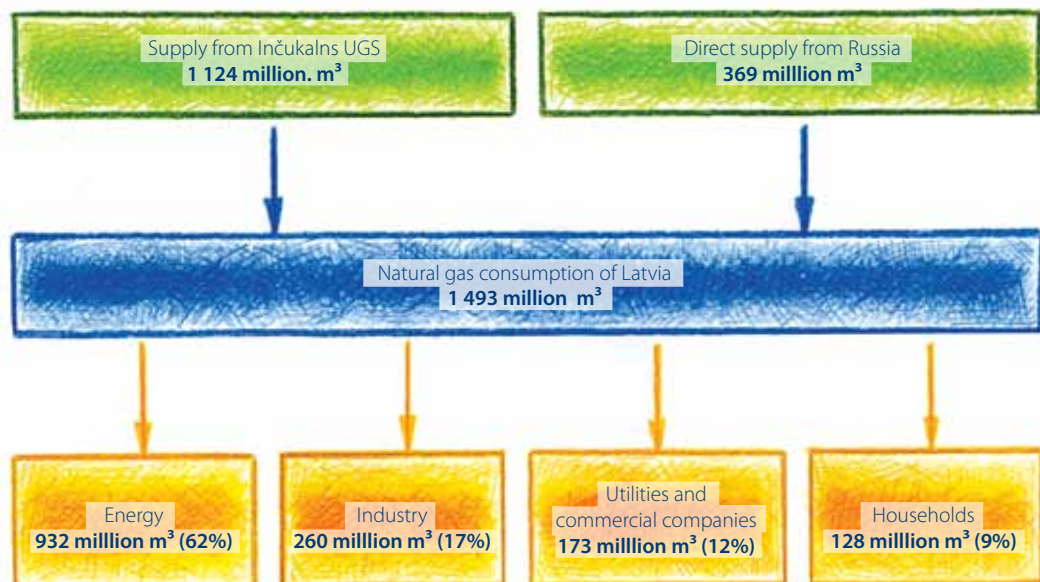
Considering the climate conditions of Latvia, natural gas is primarily consumed in heat production. In the 1st quarter of 2009, compared to the year before, natural gas sales also decreased due to the mild weather conditions, whereas in December 2009 they increased as the air temperature was low.

Prices

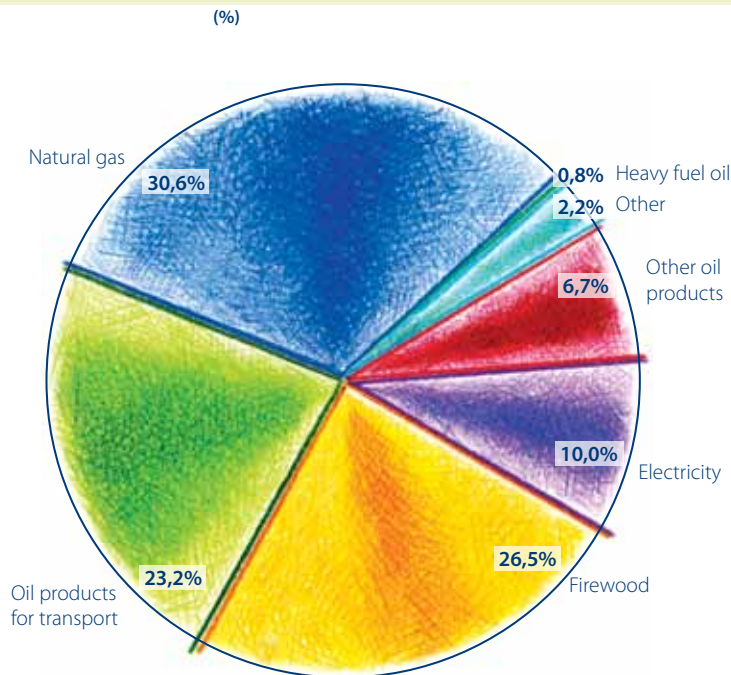
Three main factors influencing the natural gas tariffs are the price of oil, the products of which – heavy fuel oil and diesel fuel – the natural gas purchase price from supplies in Russia is linked to; reserves at the Inčukalns Underground Gas Storage Facility (Inčukalns UGS), which is the only source of natural gas supply during the heating season; and currency values.

In 2009, the changes in the oil market had a considerable impact on the natural gas price. Following the drop of oil prices after their record-high level in 2008, the year 2009 saw reduced natural gas prices of suppliers and consequently the prices for customers in Latvia. For instance, over 2009, from January thru December, the tariffs decreased by 27% for households on heating and by 36% on average in industry and energy.

Natural gas flow in 2009



Energy Balance in 2009



Source: Central Statistical Bureau of LR.

However, Latvia continued to consume natural gas from the reserves at the Inčukalns UGS thru the end of the heating season. This deteriorated the competitiveness of natural gas with other types of fuel and had a negative impact on natural gas consumption in the 1st quarter. Meanwhile, the European natural gas market and competing energy resources were already feeling the drop of prices after the sharp decline from the record prices of oil in 2008. For this reason, some companies, such as the JSC *Daugavpils siltumtikli*, switched to types of fuel that were cheaper at that time.

After the heating season and with natural gas supplies coming directly from Russia, there was a considerable decrease of natural gas tariffs in all customer groups in the 2nd quarter of 2009. In the last quarter of 2009, the natural gas reserves purchased in summer ensured immunity from the rising oil prices in the global market and a favourable price compared to Europe and competing energy resources, in particular in the area of energy and industry.

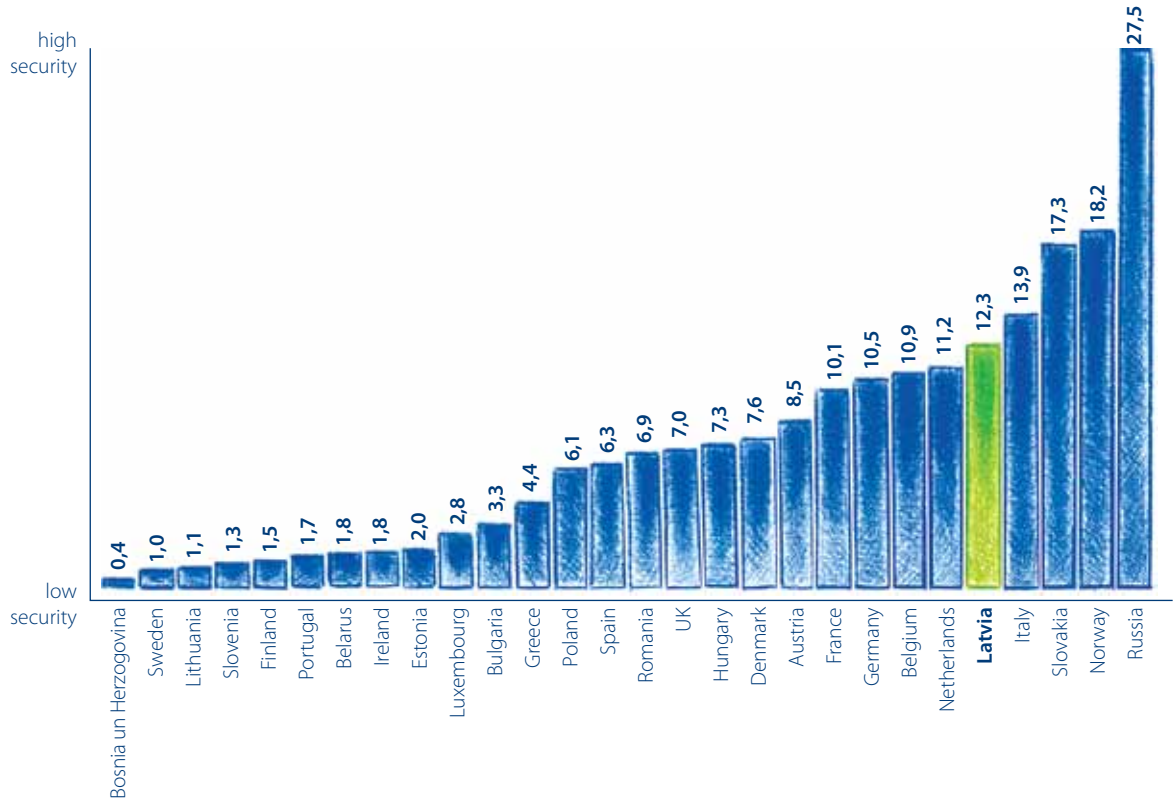
Events influencing the development of natural gas market

The key event of the reporting period with present and future influence on the operation of the JSC *Latvijas Gāze* in Latvia was the launch of the reconstructed first power unit of the Riga second thermal power central (TPS-2). It started operating already during the heating season of 2008/2009, but the official commissioning took place on May 6, 2009. The modern 420 MW power unit had its effect on natural gas consumption already in the first year of operation, mitigating the decline of natural gas consumption in energy as opposed to that in industry.

On the backdrop of the planned closure of the Ignalina Nuclear Power Station (NPS) in 2009, discussions on further reconstruction of the TPS-2 and the construction of a second power unit next to the first one intensified. The decision of the Ministry of Economics of the Republic of Latvia to continue the reconstruction of the TPS-2 was facilitated by both the probable shortage of electricity in the region and the necessity to find a quick and effective solution for the self-provision of electricity. The modernization of the Riga TPS-2 is due to be completed in the second half of 2013. More efficient use of fuel in both new power units of the TPS will also serve as guarantor of stable natural gas consumption in the local market.

It should be noted that in late 2009, with the termination of the Ignalina NPS, the significance of natural gas in the region's power supply substantially increased. For instance, Lithuania replaced nuclear power not only with imported electricity, but also with natural gas, and after the closure of the Ignalina NPS the 1 800 MW Lithuanian power station (*Lietuvos elektrinė*) in Elektrenai is becoming the largest electricity producer in the Baltics.

Security of Supply



The Ramboll security of supply index is based on a set of quantifiable parameters like number of supply countries and pipelines, indigenous gas production, gas storage, LNG terminals, gas substitution and country risks for supply and transit countries, which have been weighted and then compared. (Source: Future Development of the Energy Gas Market in the Baltic Sea Region, Final Report, June 2009 (Prepared for the EU Commission DG TREN C1)).

Safety is priority

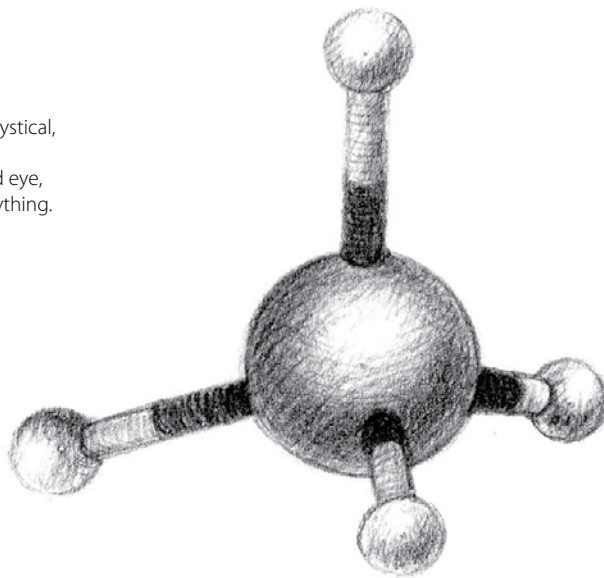
In February 2009, the JSC *Latvijas Gāze* concluded new natural gas supply agreements with the OJSC *Gazprom* and LLC *ITERA Latvija*. The new agreements guarantee for Latvia the necessary natural gas volumes till 2030, which is crucial for long-term security of energy supply of Latvia. The previous contracts were effective till 2015.

Natural gas supply agreements specify the guaranteed volumes of natural gas, while there are separate agreements on prices. Long-term natural gas supply agreements for 20-30 years are widespread in the Western European countries as they provide security to the consumers' long-term investments in gas supply technologies and infrastructure.

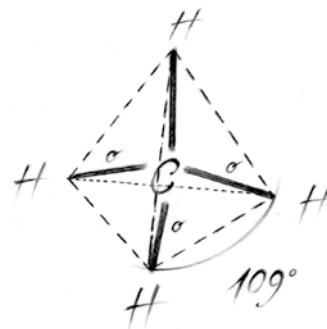
The significance of a long-term natural gas supply agreement and the Inčukalns UGS, which supplies Latvia with natural gas during the whole periods of peak demand – the heating season, for Latvian gas supply and energy in general is invaluable. For instance, according to a study of 2009 by the European Energy Commission on the "Future Development of the Baltic Regional Gas Market", Latvia takes the fourth place in the European Union in terms of security of gas supply. Latvia is featured in the European top six beside such countries with their own fields as the Netherlands and Norway. Russia, for its part, is rated as the most secure and provided country, which is a good signal for us as consumers of Russian natural gas.

Beginning of gas

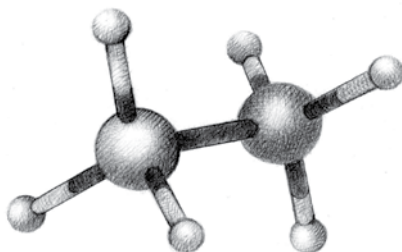
Gas molecules – something mystical, volatile and light. Impossible to see with a naked eye, but still the beginning of everything.



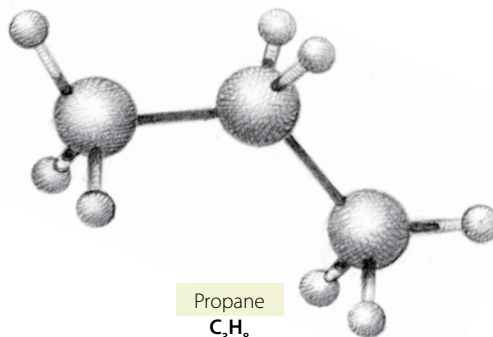
Methane
 CH_4



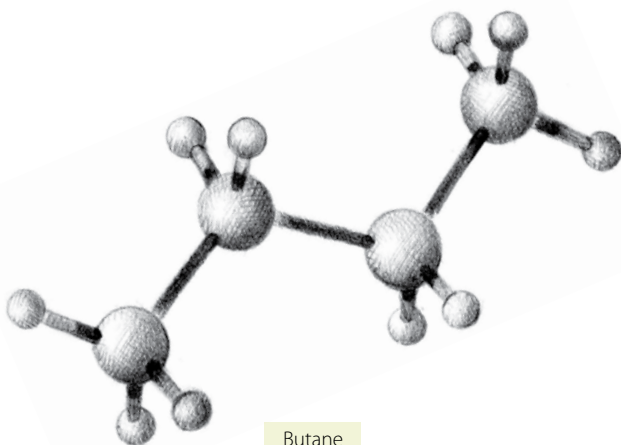
Hydrogen
 H



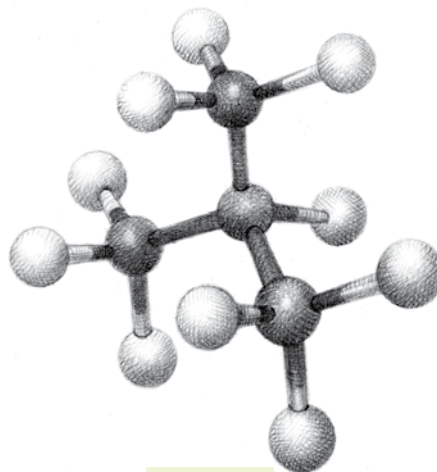
Ethane
 C_2H_6



Propane
 C_3H_8



Butane
 C_4H_{10}



Isobutane
 C_4H_{10}

The reporting year stands out with a number of events that will have a long-term impact on the development of the JSC *Latvijas Gāze*. The start of the projects supported by the European Commission and the approval of a new programme of investments till 2015 are the first to mention.

Preparation of the Baltic Energy Market Interconnection Plan and first projects supported by the European Commission

On June 17, 2009, eight European Union (EU) member states of the Baltic Sea region signed a memorandum of understanding with the Chairman of the European Commission (EC) Jose Manuel Barroso on the *Baltic Energy Market Interconnection Plan* (BEMIP). After signing the memorandum, an action plan was started to implement. The main objective of the plan is to strengthen the energy security in the Baltic Sea region and to establish a fully functioning and integrated energy market with the necessary infrastructure. One of the tasks of BEMIP is also the integration of the three Baltic States and Finland in the EU natural gas market.

Previously, i. e., in November 2008, a management group and two working groups – one for electricity and one for gas – were formed in order to prepare the BEMIP plan. During the reporting year, representatives of the JSC *Latvijas Gāze* were also involved in the working group.

In the summer of 2009, the largest engineering consultation company of the Nordic states *Ramboll Group* presented the research *Future Development of the Energy Gas Market in the Baltic Sea Region* developed at the EC order. In order to eliminate the issue of energy „gas islands”, the research recommends to invest primarily in the increase of the capacity of the gas connections of Latvia-Lithuania and Latvia-Estonia, the elimination of the so-called „bottlenecks”, as well as the construction of gas pipelines connecting Poland-Lithuania (Amber) and Estonia-Finland (Balticconnector).

In December 2009, under the influence of the economic crisis, the EC approved the European Energy Program for Recovery (EEPR), envisaging 1.662 billion LVL (2.365 billion EUR) for energy projects. 56.2 million LVL (80 million EUR) of this amount were due for investment in infrastructure projects for the promotion of reverse flows with a view to improve the security of energy supply.

Applying for the EEPR funding, the JSC *Latvijas Gāze* jointly with the AB *Lietuvos Dujos* prepared the project documentation for the enhancement of capacity of the gas pipeline connection and the improvement of security of gas supply between Latvia and Lithuania. In July it was submitted to the EC.

Within the framework of the project it was planned to reconstruct 15 wells at the Inčukalns UGS, to build a new gas passage over Daugava, to build a new pig receiver in Latvia, as well as to modernize the gas compressor station of Panevėžys and part of the Lithuanian gas pipeline system.

The project jointly prepared by the gas companies of both neighbouring countries was included in the main list of projects to be supported by the EEPR, and in early December the EC resolved to grant to the JSC *Latvijas Gāze* LVL 7.02 million (10 million EUR), i. e., half of the funding needed for the part of the project to be implemented in Latvia. This resolution was approved by the European Parliament.

According to the project, the construction of the passage over Daugava is due to be finalized by the end of 2010, while the reconstruction of 15 wells at the Inčukalns UGS is scheduled for completion by the end of 2011.

Plan for improvement of safety of gas supply system

In the reporting year, in order to ensure uninterrupted natural gas supply to users and safe operation of the gas supply system, the company developed a Plan of measures for the improvement of safety of the gas supply system of the Joint Stock Company *Latvijas Gāze* 2010-2015.

The plan was prepared based on judgments of the Russian companies *Gazobezopasnostj* and *Ļentransgaz*, the institutes *VNIIGAZ* and *Giprospecgaz*, as well as the German companies *Pipeline Engineering GmbH*, *Untergrundspeicher und Geotechnologie – Systeme GmbH*, *E.ON Engineering GmbH*, *E.ON Ruhrgas International AG* and other partners regarding the technical condition of equipment and the possibilities of its modernization.

The plan of measures envisages investment in safety improvement in the total amount of 50.6 million LVL (72 million EUR). The plan includes projects, the implementation of which is required for the enhancement of safety of system operation, the gasification of new objects and the improvement of stability of gas supply throughout the region.

Development of gasification

The total number of gas-enabled objects in Latvia in 2009 reached 442.1 thousand. In 2009, the JSC *Latvijas Gāze* concluded 72 new contracts, under which merchants were supplied 18.2 million m³ of gas.

During the reporting year, against the backdrop of crisis, additional financial and material resources were shifted for the control of natural gas sale and settlements. The company introduced new operation standards of the gas supply system and reorganized the structure of personnel.

At the same time, the investment in new connections and the funding of advertisement and marketing activities was reduced. Just as in previous years, the funding of measures related to system safety was set as priority.

Within the framework of the Company's capital investment programme, 17.2 million LVL (24.5 million EUR) were taken up in 2009. 31.5% were spent on the improvement of operation safety and the modernization of equipment at the Inčukalns UGS, 33.2% - the modernization and repair of the gas transmission pipeline system, and 29.7% on the extension of the existing distribution networks and the renewal of the existing fixed assets.

In the reporting year, the Company completed the programme of reconstruction of gas regulation stations, further implemented programmes of diagnostics and repairs of gas transmission pipelines and the modernization of the wells of the Inčukalns UGS, as well as launched a significant project of the gas transmission system.

Construction of gas pipeline of Riga bypass line

The year 2009 saw the start of construction of a high-pressure gas pipeline of the Riga bypass line. The total length of the bypass line will reach 40 km. The bypass line will consist of the 9.5 km gas pipeline renovated in 2005 and a new gas pipeline in the length of 30.2 km.

The connection of both pipelines will complete the looping, which will stabilize the gas supply of Riga and its surroundings (the right and left bank of Daugava), the Pārdaugava precinct, the rural municipalities of Ķekava, Olaine, Babīte and the town of Jūrmala.

The total costs of this project are 3 million LVL (4.3 million EUR), 2 million LVL (2.8 million EUR) of which were taken up in 2009.

Introduction of new information systems

In order to improve customer treatment, the development of a system of remote control of the ten major consumers' consumption was started in the reporting year. This project is due to be completed at the end of 2010.

In 2009, the company began the introduction of the Information system of document control and content management and finalized the first stage of the Portal of electronic customer services. The development of the portal will continue in 2010 and it will provide the customers of the JSC *Latvijas Gāze* with an efficient and convenient way to obtain information on the actual natural gas consumption and the balance of settlements, to receive electronic bills and submit the consumption meter readings electronically, as well as to make payments for natural gas.

Increased role of Contract Centre

The performance of the Contact Centre proves that the Company makes active use of more efficient ways of operation. In 2009, the Contact Centre served by 8% more callers than in 2008, while the number of calls made rose by 307%. The latter increase was achieved by fulfilling the orders of various structural units of the JSC *Latvijas Gāze*.

Eventually, the total number of customers served was by 19% higher than in 2008.

Over the reporting year, 57% of all contacts (visits, phone calls, e-mails) dealt with by the JSC *Latvijas Gāze* were served by the Contact Centre, and 92% of all calls received by the JSC *Latvijas Gāze* were served by the Contact Centre. Successful operation of the Contact Centre enables the customers and the company to save time and resources.

Apart from the traditional mission of ensuring reliability and stability of gas supply in Latvia and the entire Baltic region, which was of particular importance during the heating season, the Inčukalns UGS in 2009 proved itself to be an important factor for keeping the natural gas price steady.

At the end of 2008, Latvia reached the end of the rise of gas purchase prices to the level of the European natural gas market. Therefore, in the reporting year the natural gas purchase price was only influenced by the changes in the oil product quotations at the exchange, the currency value ratios and the gas supply flows.

In the spring and summer of 2009, the Inčukalns UGS was filled with the natural gas that had been purchased for a relatively low price, and in the heating season 2009/2010 the JSC *Latvijas Gāze* was able to ensure low end-user tariffs for the customers, thereby not only improving the competitiveness of natural gas among other energy resources, but also unburdening the budgets of Latvian households and enhancing the competitiveness of industrial customers during the crisis.

The increased importance of the storage facility is also marked by the visit of the State President V. Zatlers at the Inčukalns UGS, where the President became acquainted with the technology of gas storage and the course of well repairs.

Operational indicators of Inčukalns Underground Gas Storage Facility

The natural gas injection season at the Inčukalns UGS began on May 14, 2009 and ended on October 15, 2009. Over the season of 2009, 1 214 billion m³ of natural gas was injected into the facility. The total volume of active natural gas injected at the facility reached 2 074 billion m³, which is by 250 million m³ less than the year before. Over the reporting period, 1 583 billion m³ of natural gas were withdrawn from the facility.

In comparison to the season of 2008, the natural gas injection volume fell by 36.8%, while the volume of withdrawal – by 19.8%.

Meanwhile, Latvia received 369 million m³ of natural gas for consumption from Russia.

There was a notable decrease in the use of the Inčukalns UGS for the needs of other countries. 252 million m³ of natural gas were supplied to Estonia and 25 million m³ were supplied to Lithuania from the facility, while 163 million m³ of natural gas was transmitted back to Russia.

The reduced supplies stem from both the mild winter in the region and the rise of the storage service tariffs.

Use of investments

The amount of investments in the Inčukalns UGS in 2009 comprised 31.5 % of the investment portfolio of the JSC *Latvijas Gāze*.

The investment in the improvement of operation safety and the modernization of equipment at the Inčukalns UGS within the framework of the capital investment programme amounted to 8,263 million LVL (11.75 million EUR). Two projects of the scope of work planned for the year were not implemented, thus the actual amount of investment taken up over the reporting year was 5.7 million LVL (8.11 million EUR).

Modernization of wells

During the reporting year, seven wells in the gas-carrying zone were modernized for the total amount of 1.96 million LVL (2,8 million EUR).

In cooperation with the company *Gazpromenergodagnostika*, 20 wells of the Inčukalns UGS underwent examination of technical condition in 2009. Analysing the results of diagnostics it was established that two wells needed a capital repair in the nearest future, while the period of operation was extended for the remaining 18 wells.

In order to determine the reasons of gas escape, high-sensitivity thermometry measurements were carried out in the wells of the Inčukalns UGS in collaboration with another Russian company OJSC *Gazprom Geofizika*. The results of these measurements were used when preparing the technological task for the capital repair of wells for 2010/2011.

On the basis of the examination of the technical condition of wells at the Inčukalns UGS, a programme for capital repair of wells and a programme for geochemical inspection of wells was developed for 2010-2014.

In 2009, a tender was announced and part of the equipment needed for the reconstruction of wells planned in 2010 was received.

Modernization of gas drying shop

The year 2009 saw the completion of the design for modernization of the gas drying shop, as well as the purchase of a part of the new equipment. By implementing this project, 2.9 million LVL (4.1 million EUR) were taken up.

The object was designed by the LLC *Olimps*, while the detail design of equipment was developed by the Italian company *Pietro Fiorentini*. This company was contracted on the supply of equipment. The total costs of the equipment for the gas drying shop amount to 5.2 million LVL (7.4 million EUR), and the supply deadline was May 2010.

During the reporting year, the diagnostics of technical condition of the gas collection point №2 of the Inčukalns UGS was conducted. The examination results rendered a recommendation to carry out partial reconstruction of the collection point. The reconstruction would allow for saving funds in future as well as repairs without significant reduction of gas extraction capacities at the Inčukalns UGS. The gas collection point is due for such reconstruction within the next few years.

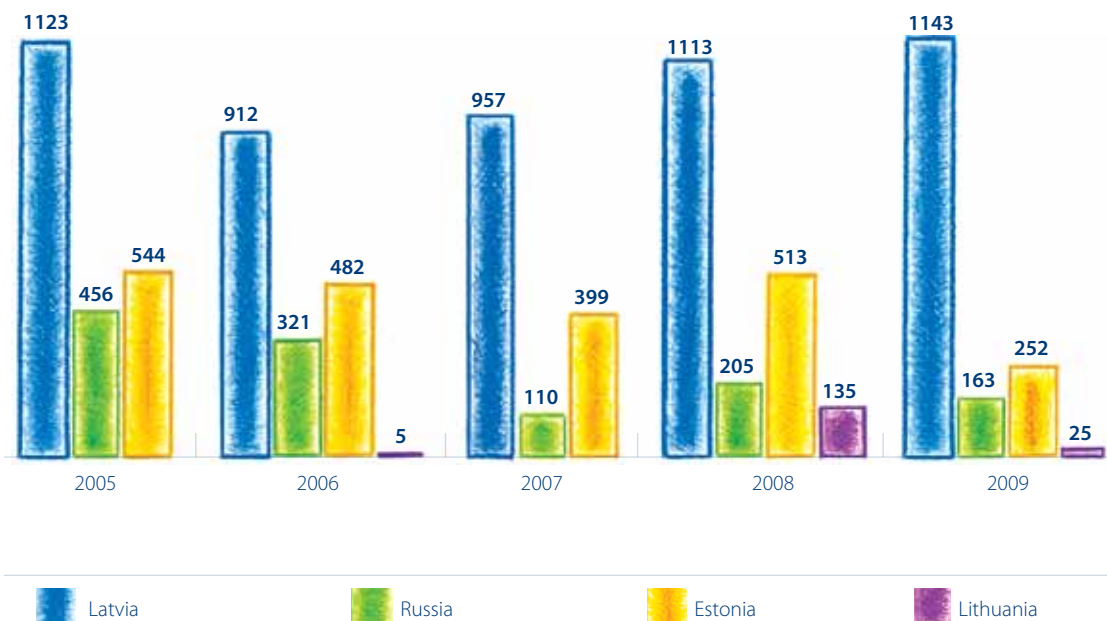
Another notable event to be mentioned is the preparation and implementation of a tender to select the service provider to start the development of the geographical information system (GIS) of the Inčukalns UGS.

News in the area of standardization

During the reporting year, a number of industry standards regulating the operation of the Inčukalns UGS were developed and introduced. Three new standards were registered at the standardization authority: LV NS GS 09-2009 Safety rules of underground gas storage system, LV NS GS 10-2009 Use of methanol in gas transmission pipelines and underground gas storage systems and LV NS GS 08-2009 Terms of operation of underground gas storage wells with inter-colon pressures.

Natural gas deliveries from Inčukalns UGS

(million m³)



The natural gas transmission system of the JSC *Latvijas Gāze* consists of gas transmission pipelines (hereinafter – GTP), gas regulation stations (hereinafter – GRS), underground anti-corrosion equipment for electrochemical protection of pipelines, communication and remote lines, as well as the information system SCADA and the commercial international gas metering station Korneti.

The functions of natural gas system operator at the company are performed by the operation unit *Gas Transport*, the duties of which include the reception of natural gas from Russia, its supply to the natural gas distribution system, as well as transportation abroad. *Gas Transport* also performs the regulation of gas pressure within the natural gas transmission system, gas purification, odourisation and commercial metering.

In 2009, 32% of the total funds of the capital investment programme of the JSC *Latvijas Gāze* were spent on the modernization and repair of the system of gas transmission pipelines.

Completion of the programme of modernization and reconstruction of gas regulation stations

The year 2009 saw the conclusion of the JSC *Latvijas Gāze* programme of GRS modernization and reconstruction. Within the framework of the GRS reconstruction programme, which was launched back in 1998, 43 GRSs were reconstructed till 2009, while 6 were built anew. Full operation control of all GRSs is ensured by the SCADA information system.

During the reporting year, the GRS *Lutriņi* and *Zirņi* were reconstructed. Apart from general construction, the complex of reconstruction works included the installation of new container-type GRSs, their connection to functioning gas pipelines and commissioning.

In early 2009, the general construction and the improvement of station fields at the previously modernized GRS *Koknese*, *Vecbeļi* un *Ziemeļi* was finalized. 2.53 million LVL (3,59 million EUR) were spent on the reconstruction of the aforementioned five GRSs in 2009.

Moreover, in order to enhance the safety of gas transportation, the equipping of 17 GRSs with specialized communication devices was completed in the reporting year. These devices are designed to ensure the control and management of GTPs in case the main communication channels are out of order.

Diagnostics of gas transmission pipelines

During the reporting year, the company continued the internal diagnostics of GTP pipes. The purpose of the diagnostics is to determine the maximum permissible operating pressures of the GTPs in order to be able to sustain higher pressures in the GTP system and consequently improve the efficiency of system operation in future if the gas transmission volume increases. By the end of 2009, the company had performed the diagnostics on gas pipelines for the length equal to 51% of the total length of the GTPs.

Over the reporting period, 16 intelligent pigs were run through the section of km 74.9 to km 209.64 of the GTP Iecava-Liepāja. The treatment of this section began back in 2008 and takes place in co-operation with the company *Weatherford Kopp GmbH*.

In May, the company concluded a contract with the company *Specneftgaz* on the internal diagnostics of the GTP Pskov-Riga. The diagnostics was carried out in June, while the final report on the completed activities was received in mid-October.

In September, a contract was signed with the company *Rosen Europe b.v.* on the internal diagnostics of the GTP Riga-Panevežys in the section of km 14.46 to km 84.03. Following the coordination and the settlement of technological issues with the companies *Rosen Europe b.v.* and *AB Lietuvos Dujos*, the diagnostics is due to continue in 2011.

The company *Rosen Europe b.v.* was also contracted in October concerning the internal diagnostics of the GTP Riga-Inčukalns UGS line I and II.

Furthermore, the internal diagnostics of the GTP Riga-Inčukalns UGS line I (km 7.80 to km 41.48) was fully completed in the reporting year, whereas the internal diagnostics of the GTP Riga-Inčukalns UGS line II continues in January 2010.

Measures for preparing internal diagnostics of gas transmission pipelines

In order to ensure the execution of internal diagnostics, it is necessary to build intelligent plunger launcher or receiver units and replace outdated line valves of gas transmission pipelines with valves of sufficient internal permeability for the movement of pigs along gas pipelines.

In 2009, while preparing gas transmission pipelines for the internal diagnostics, 29 valve units were replaced and six cleaning and intelligent pig launcher units and eight pig receiver units were built.

Preparatory works for the internal diagnostics in 2009 also took place at the GTP Iecava-Liepāja where a pig launcher unit, three valve units and one branch-off was built. The total costs of these activities amounted to LVL 1.36 million (1.93 million EUR).

A piston receiver unit was also built at the GTP Rīga-Panevežys. The construction costs were LVL 0.65 million (0.92 million EUR).

Furthermore in the reporting year, a unified piston receiver unit of the GTP Rīga-Inčukalns UGS line I and II was built and a branch valve to the GRS Rīga-1 was replaced, the total costs of works amounting to LVL 1.58 million (2.24 million EUR).

The preparatory works of internal diagnostics were carried out both by own employees and engaging the companies LLC *Katlinieks* and LLC *Rumba*.

Repair of gas transmission pipelines after assessing the results of diagnostics

After the inspection of the defects found during the internal diagnostics and the analysis of their dangerousness, *Gas Transport* develops and implements the programme of repair of gas pipeline defects. Based on the data of earlier diagnostics, repairs took place at four GTPs during the reporting period. In total, 0.72 million LVL (1.02 million EUR) were spent on the renovation of GTPs in 2009.

In co-operation with the LLC *Euro Enerģijas Serviss*, the external insulation was replaced in several sections of the GTP Rīga-Daugavpils with the total length of 2685 metres, while in co-operation with the LLC *Remus* a pipeline section of 180 metres in length was repaired by replacing the pipes.

Based on the results of the internal diagnostics of the GTP Iecava-Liepāja, a valve unit assembled with the flaws of welded seams was removed in co-operation with the LLC *Katlinieks*. It should be noted that this repair was done without interrupting gas transportation. On the basis of the results of the internal diagnostics and the recommendations of the Belorussian Physical Technical Institute (FTI), a defective 72 metres long section of the GTP Pskov-Rīga was replaced in co-operation with the LLC *Katlinieks*.

Furthermore, based on the results of the acoustic emission diagnostics performed by *Gazprom Energodagnostika*, the external insulation was replaced for a section of the GTP Rīga-Inčukalns UGS in the length of 381 metres in co-operation with the LLC *Būvenērgo*.

Among the activities completed in the reporting period, one should also mention the reconstruction of eight cathodic protection stations, the repair of numerous valve units at the gas pipelines Rīga-Inčukalns UGS I and II, Rīga-Panevežys and Vilnius-Rīga, the construction of access roads and other construction works at the GTPs Upmāla-Rēzekne, Rīga-Panevežys and Iecava-Liepāja.

In co-operation with the companies LLC *Jūras Vējš*, LLC *Baltic Energo* and LLC *Akvabūve*, the passages of the gas pipeline Izborsk-Inčukalns UGS over water obstructions were renovated and the anti-corrosion coating of the gas pipeline was repaired. The routes of the GTP Pskov-Rīga and Izborsk-Inčukalns UGS in the area of 253.22 hectares were cleared from shrubbery.

Taking into account the changes in the economic situation of Latvia, the JSC *Latvijas Gāze* implemented extensive structural transformations aimed at the optimization of workforce costs and as much improvement of efficiency of the Company's operation as possible.

On December 18, 2009, at a conference of the employees' representatives, the execution of the Collective Agreement was assessed and the new Collective Agreement for the years 2010 and 2011 was approved.

Changes in the structure of employees

As of December 31, 2009, there were 1269 persons employed by the JSC *Latvijas Gāze*, which is by 129 employees less than at the end of the previous reporting period.

The aggravation of the economic situation in the country in 2009 resulted in a lower degree of rotation of employees at the Company. Over the reporting year there was less of the previously noticed unwillingness of new employees to work at one company for a long time, seeking a new job with higher remuneration and other advantages. As a result, there is a higher proportion of employees with less than ten years of service at the Company.

With the implementation of the personnel policy, the number of employees at the age of retirement has considerably decreased, whereas that of employees aged below 30 and between 31 and 40 has increased.

According to the personnel statistics, 14% of the employees of the JSC *Latvijas Gāze* in 2009 were at the age of up to 30, 17% – between 31 and 40, 25% – between 41 and 50, 34% – between 51 and 60, and only 10% were older than 61.

Thus, the trend that had been present at the Company over the last six years, with the proportion of employees aged over 61 up from 11% in 2003 to 17% in 2008, is now broken.

The Company's activity in the implementation of the personnel policy is illustrated by the figures, as 268 employees were dismissed, 139 were hired and 140 were transferred to a different position during the reporting year.

As shown by the personnel statistics of the Company, 51% of the employees of the JSC *Latvijas Gāze* worked at gas distribution, 14% – at gas sales, 12% – at gas transmission, 11% – at administration, 10% at gas storage and 2% – at the department of paid services.

Reorganization

Analysing the breakdown of the Company's employees by areas of activity, one can notice that the sharpest decrease of the number of employees in the reporting year took place in the area of gas distribution where it fell by 59 compared to the end of 2008.

At the same time, the number of people employed in the area of gas sales decreased by 25, the number of those working at the Company's administration fell by 5, whereas in terms of percentage (50%, i. e., from 42 to 21) the sharpest drop took place at the department of paid services. The gas transmission and storage segments, for their part, did not undergo notable changes in terms of the staff quantity.

Among the key structural changes at the Company the organizational changes in the GRS service of the operation unit Gas Transport due to the reconstruction and modernization of gas regulation stations should be mentioned.

The reporting year the reorganization of the Sales Division, the Strategy and Development Department and the Operation and Technical Department of the Operation and Technical Division was performing as they turned into a new Gas Supply Development Division.

Meanwhile, the Emergency Service and the Electric Protection Service were excluded from the structure of the Operation and Technical Division and became structural units of the Riga unit.

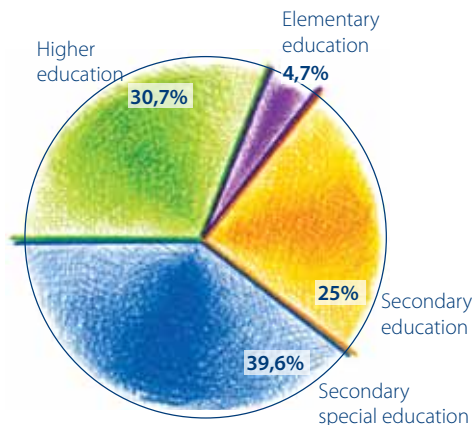
As a part of those changes, the Contact Centre of the JSC *Latvijas Gāze* was included in the Gas Metering and Billing Division as a separate structural unit.

The Gas Metering and Billing Division was also assigned the function of investment recovery control, previously performed by the Sales Division. The company's Training Centre, for its part, was excluded from the Personnel Department and transformed to a standalone structural unit.

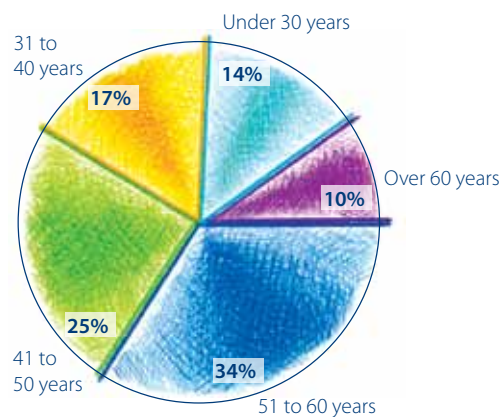
The Geographic Information Service of the Information Technology Division was reorganized with a view to ensure efficient and quality maintenance and use of geospatial information and the development of geo-information technologies, and a Geospatial Information Department was established as a part of the Information Technology Division.

In order for the Company to reduce the natural gas sale costs and ensure efficient work organization, the Gas Metering Department of the Gas Metering and Billing Division was also reorganised. The function of natural gas metering control for commercial users was assigned to the Industrial Customers Department of the Gas Metering and Billing Division, whereas the function of natural gas metering control for household users was assigned to the Internal Gas Supply System Service of the Riga unit.

The structure of employees' education



The age structure of employees



Education

At the end of 2009, 30.7% of the Company's employees had higher education, 39.6% – secondary special education, 25% – secondary education, and 4.7% – elementary education. The trend that has been present throughout the course of development of the JSC *Latvijas Gāze* – increasing proportion of employees with secondary special education – continued in the reporting year.

67 thousand LVL (95 thousand EUR) were spent on the employees' professional training and qualification-raising in 2009.

The JSC *Latvijas Gāze* granted financial support to 19 employees for the obtention of academic education at the higher education establishments of Latvia. The Company covered both the tuition fee for the study year 2009/2010, the compulsory social contributions and the personal income tax in the total amount of 22 118 LVL (31 471 EUR). Studies in the speciality of gas technologies were set as priority in 2009.

Apart from that, financial benefits were disbursed to 24 studying employees in the total amount of 20 094 LVL (28 591 EUR), including 8 778 LVL for the second term of the study year 2008/2009 and 11 316 LVL (16 101 EUR) for the first term of the study year 2009/2010.

It should be noted that two holders of the JSC *Latvijas Gāze* grants studied in the third year and master course of the Oil and Gas Russian State University named after I. M. Gubkin. Two employees of the Company continue their studies at the graduate school of the aforementioned university, while one employee obtained the degree of the candidate of technical sciences in 2009. Currently, the JSC *Latvijas Gāze* employs twelve graduates of the Oil and Gas Russian State University named after I. M. Gubkin, ten of whom are holders of the JSC *Latvijas Gāze* grants.

Training Centre

The Training Centre of the JSC *Latvijas Gāze* also continued its successful work in 2009. There was an increase over the previous reporting year both in terms of the number of employees trained and time dedicated to training.

1064 employees of the JSC *Latvijas Gāze* studied at the Training Centre in 2009. This is by 112.8% more than in 2008. The number of man-hours in the training process in 2009 reached 22 258, outweighing the figure of 2008 by 109.8%.

In the reporting year, one of the strategic objectives of the Training Centre was the organization of training for all employees of the Company. Consequently, as from mid-2009, the employees of Gas Transport and the Inčukalns UGS are also educated by the Training Centre. Further in the reporting year, the Procedure of Training of Employees of the Joint Stock Company *Latvijas Gāze* was developed and approved by the Board of the Company, as well as the existing training curricula were revised, reducing the number of training hours by approximately 20%. The change in the age structure of employees characteristic of the Company in general was also true for the Training Centre. While in early 2009 the centre employed eleven persons, nine of whom had reached the age of retirement, at the end of the year there were nine employees, with only three of them at the age of retirement.

The international co-operation of the JSC *Latvijas Gāze* traditionally develops in three main directions. Firstly, it is co-operation with the Company's shareholders; secondly, co-operation with other gas companies, primarily those of the neighbouring countries – Estonia and Lithuania; and lastly, co-operation with a variety of international organizations.

The European Commission

In the reporting year, a new dimension was added to the Company's international partnership by the European Commission (EC). Joint effort within the framework of the Baltic Energy Market Interconnection Plan (BEMIP) yielded support of the EC both to the project for the increase of capacity of the gas pipeline interconnection and the improvement of security of gas supply between Latvia and Lithuania, jointly developed by the JSC *Latvijas Gāze* and AB *Lietuvos Dujos*, and the already mentioned plan of modernization and expansion of the Inčukalns UGS.

The JSC *Latvijas Gāze* was represented in the working group for implementation of the BEMIP. The agenda of these meetings included issues of the development, regulation and opening of the gas market, yet most attention was paid to infrastructure projects that improve the security of gas supply in the region of Baltic Sea.

Co-operation with the Company's shareholders

In 2009, continued co-operation with specialists from the Company's shareholders, the OJSC *Gazprom*, *E.ON Ruhrgas AG* and *E.ON Ruhrgas International AG*. The main areas of co-operation were further modernization of the Inčukalns UGS, the improvement of operation safety of the gas supply system, issues of GTP operation, as well as the inspection of gas pipelines using intelligent pigs.

Under the co-operation agreements signed by the JSC *Latvijas Gāze*, *E.ON Ruhrgas AG* and *E.ON Ruhrgas International AG*, issues of natural gas sales and customer service were solved together with German colleagues. Furthermore, there were consultations on the organization of purchases, the use of the telemetric systems of automated commercial natural gas metering and issues related to the installation of vehicle natural gas filling stations and the training of employees thereof.

German experts also delivered lectures at the seminar funded by *E.ON Ruhrgas AG* regarding co-operation in the development of gas supply systems among structural units of the JSC *Latvijas Gāze*, the attraction of new customers and the construction of new gas pipelines.

In May, more than 20 employees of the Inčukalns UGS went to Germany on an experience exchange visit. During the visit they got acquainted with the Bierwang and Breitbrunn UGSs and heard reports on technologies used by *E.ON Ruhrgas AG* and *RWE AG* in operating the UGSs.

Also in the reporting year, a seminar on issues of GTP operation took place in Riga. Apart from specialists of the JSC *Latvijas Gāze* it featured colleagues from *Gazprom Transgaz St.-Petersburg*, *E.ON Ruhrgas AG*, *Eesti Gaas AS*, AB *Lietuvos Dujos*, as well as the agency of the OJSC *Gazprom* in Latvia and the Belorussian Physical Technical Institute. There were reports on issues of GTP diagnostics and the elimination of the detected defects.

Co-operation within international organizations

In 2009, the Company continued its participation in the international organizations of the industry and engaged in the activities of the International Gas Union, DVGW (Deutsche Vereinigung des Gas- und Wasserfaches), the World Energy Congress, Eurogas, Baltic Gas and the Inter-republic Association for Applied and Science-Technical Gas Co-operation.

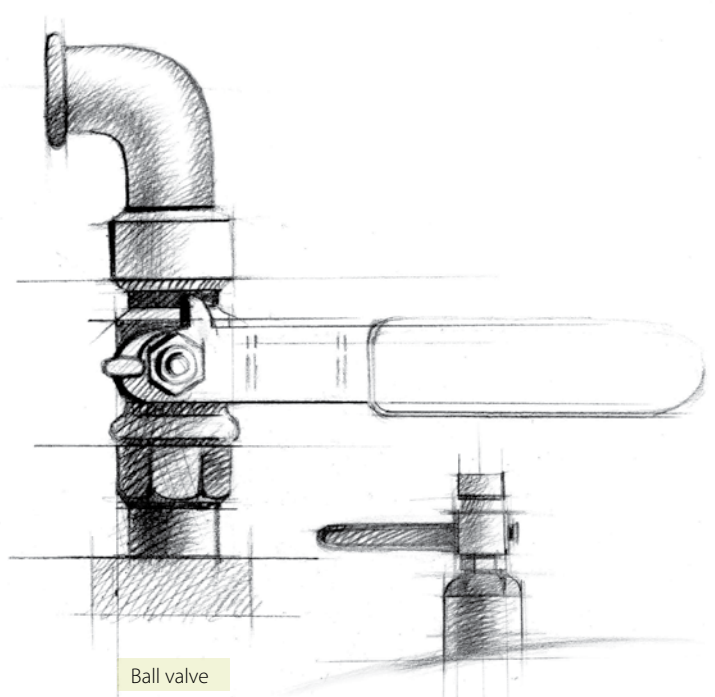
The gas working group of the *European Business Congress* also held a meeting in Riga in the reporting year. It featured representatives of the Latvian agencies of *E.ON Ruhrgas AG* and the OJSC *Gazprom*, as well as *Nord Stream AG* and other companies. They heard reports on the operation of the JSC *Latvijas Gāze*, the development of the Nord Stream project, problems of the gas market in Europe and other topical industry issues.

Among international events for industry professionals attended by the company both the technical meeting on gas drying equipment held in Italy and the seminar on the latest trends in gas pipeline protection against corrosion and welding technologies held in Russia should be mentioned. Further, it should be noted that training of the Inčukalns UGS staff in the performance of fountain-dangerous operations during well repairs also took place in Russia.

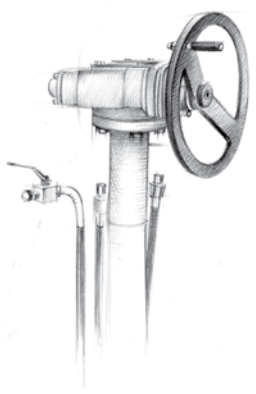
However, the most significant international event where employees of the JSC *Latvijas Gāze* took part was the World Gas Conference and exhibition in Argentina, organized by the World Gas Union. A report *Evaluation of gas supply risk in the Baltic States and UGS risk criteria* prepared by the Company's specialists together with scientists of the Physical Energy Institute of the Academy of Sciences and the Heat and Gas Institute of the Riga Technical University was presented at the conference.

Great and small inventions

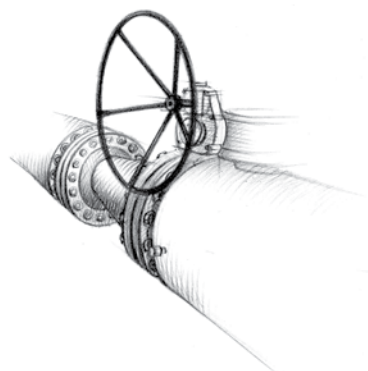
To tame something that unique as gas one should possess vast knowledge. Endless patience. Perseverance. And only then scientific inventions and discoveries followed.



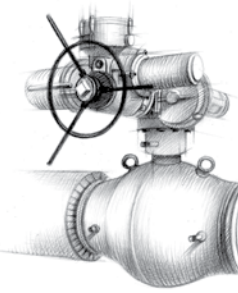
Ball valve



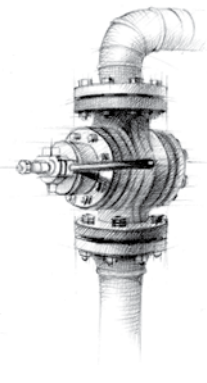
Mechanical manual drive of ball valve of gas transmission pipeline



Ball valve of measuring strips with mechanical manual drive



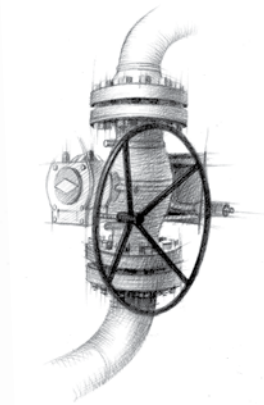
Ball valve of measuring strips with electric drive



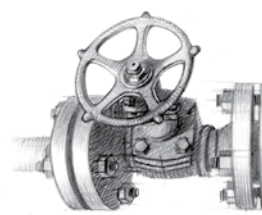
Stopper valve on the engine starter line of aggregate 12z330



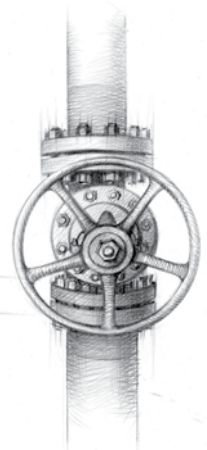
Ball valve of gas separator piping of first gas collection point



Filter separator inlet ball valve of the first collection point with manual mechanical drive



Bolt of gas collection point



Wedge-shaped bolt of gas collection point

In the reporting year, the JSC *Latvijas Gāze* as a tradition-rich and socially responsible Company continued to allocate funds to charity and support for culture, education and sports. Such aid was of particular importance during the time when due to the troublesome economic situation these areas of social life were short of funding and needed support more than ever.

Charity and education

In the reporting year, the Company continued the tradition of supporting the Latvian Children Foundation. With the Company's involvement, the Latgale regional centre *Rasas pērles (Pearls of Dew)* for children having suffered from violence was established in Eglusala, Rugāji Rural District, Balvi District. The company also helped to implement the joint project of the organization *Glābiet bērņus (Save the Children)* and the Faculty of Medicine of the University of Latvia, a book on the development of the medical school for treatment of children and its founders.

In 2009, the JSC *Latvijas Gāze* joined an extensive campaign for the safety of children *Drošās mājas (Safe Home)* where more than 5000 pupils of junior grades were instructed on gas, electric, fire and personal safety. This large-scale project was also supported by the European Social Foundation. During the campaign, pupils of grades 1 to 6 in Vidzeme and Latgale were visited by the main character, the safety glove ToDo and his team, arriving by travelling buses and bringing with them the world's safest dwelling, which had been furnished by experts of the Ministry of Education and Science of the Republic of Latvia, the Institute of Labour Safety and Environmental Health, the JSC *Latvijas Gāze*, the JSC *Latvenergo*, the State Fire and Rescue Service, and other authorities.

Furthermore, at the beginning of the school year first grade pupils throughout Latvia received the book *Gāzēna stāsts par dabasgāzi (Gāzēns' Story on Natural Gas)* prepared and published by the JSC *Latvijas Gāze*. It contains information on safe usage of natural gas and the explanation of proper action in various situations.

During the reporting year, the JSC *Latvijas Gāze* rendered support to a variety of projects in the area of education, such as the purchase of study aids for Riga Secondary School No. 49 and the organization of the conference History, Politics and Culture of Memories of the State Archive of Latvia. The Company contributed to the events organized by the Museum of the Popular Front of Latvia and the union *Laikmets (Epoch)* and decided upon supporting the award of Atis Kronvalds.

Projects related to natural sciences, and in particular to natural gas technologies, were not disregarded either. The Company contributed to the Foundation for Development of Riga Technical University (RTU), allocating funds to scholarships for students of the specialities of gas technologies and to notable Latvian scientists and prospective talents of science. During the reporting year, funding was also granted to the organizers of the conference Baltic Polymer Symposium 2009 of the Institute of Polymers of Riga Technical University (RTU).

Culture

In order to preserve the national cultural heritage in opera and ballet, to sustain and develop the national opera, operetta, ballet and music culture, as well to popularize it in Latvia and abroad, the Company annually provides support, which did not diminish in 2009 despite the problems of economic development.

The JSC *Latvijas Gāze* has been the main sponsor of the Latvian National Opera (LNO) since 2005, and the amount contributed by the company is the highest in the history of the LNO. The funds donated over this period provided for the artistic improvement of the LNO and helped the opera to succeed internationally as well.

The new season of the theatre traditionally begins with the ceremony of the annual awards of the LNO patron, the JSC *Latvijas Gāze*, and the concert of laureates, which is one of the most significant cultural events in Latvia. It should be noted that the season 2009/2010 was special for the LNO as the theatre celebrated its 90th anniversary.

Another traditional event supported by the JSC *Latvijas Gāze* is the International Opera Festival.

Donations for the performing arts are not limited to the LNO alone. During the reporting year, the Company indirectly supported the Dailes Theatre, contributing to the Foundation of Riga Latvian Society and National Culture Development to purchase tickets of the Dailes Theatre for the purposes of charity programmes. The Latvian National Theatre, on its part, received the Company's aid for staging the Nikolai Gogol's play *The Dead Souls*.

In the reporting year, the Company decided to allocate funds for the organization of the 10th International Festival of Bach's Chamber Music in 2010. The festival organized by Bach's Music Foundation is an event of European

importance assembling stars of baroque music, and Bach's compositions are performed by outstanding, world-renowned musicians. For several years now, the patron of the festival is the German Embassy in Latvia. Here it should be noted that the Company also contributed to events organized in Latvia by the Russian Embassy.

Sports

For more than ten years, the JSC *Latvijas Gāze* has been supporting the development of the Latvian Olympic movement. The Company is a sponsor of the Latvian Olympic Committee (LOK) since 1997, and this co-operation has become a tradition. In 2009, the Company provided financial support to the Latvian Olympic team to prepare for the participation in the XXI Winter Olympics, which took place in Vancouver (Canada) in February 2010.

The funds are spent on co-financing the country's best athletes who prepare for the Olympics as members of the Latvian Olympic Union. Bobsleigh, skeleton, luge and biathlon are prior among the kinds of sport.

During the reporting year, financial aid was also rendered to the Latvian Biathlon Federation and the Latvian Basketball Union, as well as the Latvian federations of tennis, volleyball and bobsleigh.

However, the support is not limited to giving a hand to our Olympians and the professional sport. The company helped with the purchase of sports inventory and video materials for practice, as well as repaired the cultural and sports centre Hi Centrs in Riga, thus improving the sporting facilities for children. In the reporting year, it was decided upon allocating funds to the Latvian power athletes for practice and preparation for the season 2010, as well as for their participation in the Latvian championships and various international competitions. In 2009, the company also supported one of the best power athletes of Latvia Agris Kazēļņiks who is also an employee of the JSC *Latvijas Gāze* and won the first place in Latvia and the second place in the European championships.

Image of the Company

Having regard of the Company's notable influence on the socio-economic situation in the country – the large number of people employed and the significant contribution to the development of national economy – it is important to receive an impartial evaluation of its level of corporate responsibility.

In the reporting year, the JSC *Latvijas Gāze* received the silver award of "Sustainability Index 2009". 138 Latvian companies claimed readiness to take part in the "Sustainability Index". This competition is a quality indication of the company's strengths and an internationally approved acknowledgment of its level of corporate responsibility, as well as a practical tool of management for identifying improvements. The sustainability index was compiled in Latvia for the first time; its methodology is based on the theory of corporate social responsibility and the international indexes *Dow Jones Sustainability Index* and *Corporate Responsibility Index by Business in the Community*. Experts of the Employers' Confederation of Latvia, the Free Trade Union Confederation of Latvia, *NASDAQ OMX Riga*, the World Wildlife Fund, the Partners in Ideas Funds, SKDS, *Lursoft* and the Quality Association of Latvia were involved in the implementation of "Sustainability Index".

In the reporting year, the JSC *Latvijas Gāze* received a diploma of the State Labour Inspectorate (VDI) as the winner of the campaign "The Employment Contract – for Safer Future". The campaign, aimed at explaining the building and maintenance of legal relations in the labour environment, was organized by the VDI and the European Social Fund.

The JSC *Latvijas Gāze* received the title "Socially responsible company 2009" and the acknowledgment of the Free Trade Union Confederation of Latvia (LBAS) for certain contribution to the employment rights and labour safety. The applicants were evaluated by specialists from the LBAS, the Ministry of Welfare, the Employers' Confederation of Latvia, the Safety and Environmental Health Institute, the State Labour Inspectorate.

Despite operating in the circumstances of resource optimization, the JSC *Latvijas Gāze* continued the implementation of the environmental policy developed by the Company.

The main objectives of the environmental policy are the provision of sustainable indications of environmental and economic activity, close links of communication with the state and local authorities and the community in general, active development of the personnel, as well as due identification of key environmental impacts of the Company's economic activity, analysis of the causes thereof, and assessment of the environmental aspects emerging from economic activity. The environmental policy is also designed to ensure the ability of the company to react duly in emergency situations.

Binding changes in the legislation

In the reporting period, there were changes in the environmental regulatory documents that had an effect on the operation of the JSC *Latvijas Gāze*. The Parliament of the Republic of Latvia accepted amendments to the enumeration of activities that are imposed the natural resource tax. These amendments also concern the works that are performed while operating natural gas distribution and transmission system, and involve gas emission in the environment.

Responding to the new requirements, the Company began to work constantly on summarizing the monitoring data related to gas emission in the environment. The amount of the natural resource tax for the natural gas emission in the environment arising from the gas distribution and transmission systems in the course of operation thereof over the reporting period is calculated based on these data.

Reduction of loss in the distribution system

Over the reporting year, the Company managed to reduce the natural gas emission in the environment by 9 700 nm³/a. This was facilitated by focusing the operation of distribution system and its development on contemporary, complex and technically and economically sound measures.

Improvements of the natural gas storage system

Compared to previous years, the natural gas storage system now has the lowest natural gas consumption per 1000 nm³ of natural gas injected in the underground layer. This has been achieved by improving the technical condition of the compressor shop №2 of the Inčukalns UGS, increasing the natural gas inlet pressure, as well as by selecting the optimum mode of natural gas injection and lower intensity.

Moreover, the purchase of a diethylene-glycol storage vessel, the replacement of the layer water vessel of the gas drying point №3 at the Inčukalns UGS, as well as the design of a new gas drying unit and the purchase of equipment will not only enable the expansion of the storage facility, but also reduce the environmental impact of economic activity and the probability of emergency situations in the natural gas storage system.

It should also be noted that during the reporting year there was a decrease in the kilometrage of the cars used by the gas storage unit, while the indications of performance of business measures at the storage system remained unchanged.

Lowest volume of natural gas emission in transmission

With the completion of the reconstruction of GRSs and the modernization of the last two GRSs not reconstructed so far, *Zirņi* un *Lutriņi*, the natural gas transmission system has reached the lowest volume of natural gas emission in the environment during the recurrent maintenance of gas regulation stations.

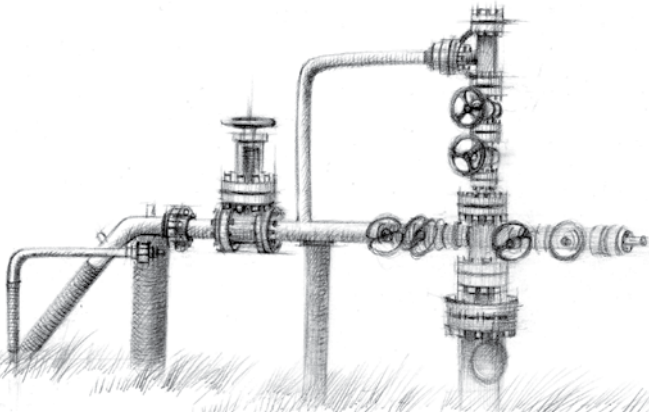
Enhanced labour environment

In the reporting period, the JSC *Latvijas Gāze* also performed the annual evaluation of the risks of labour environment, which resulted in improved labour environment and working conditions for the employees.

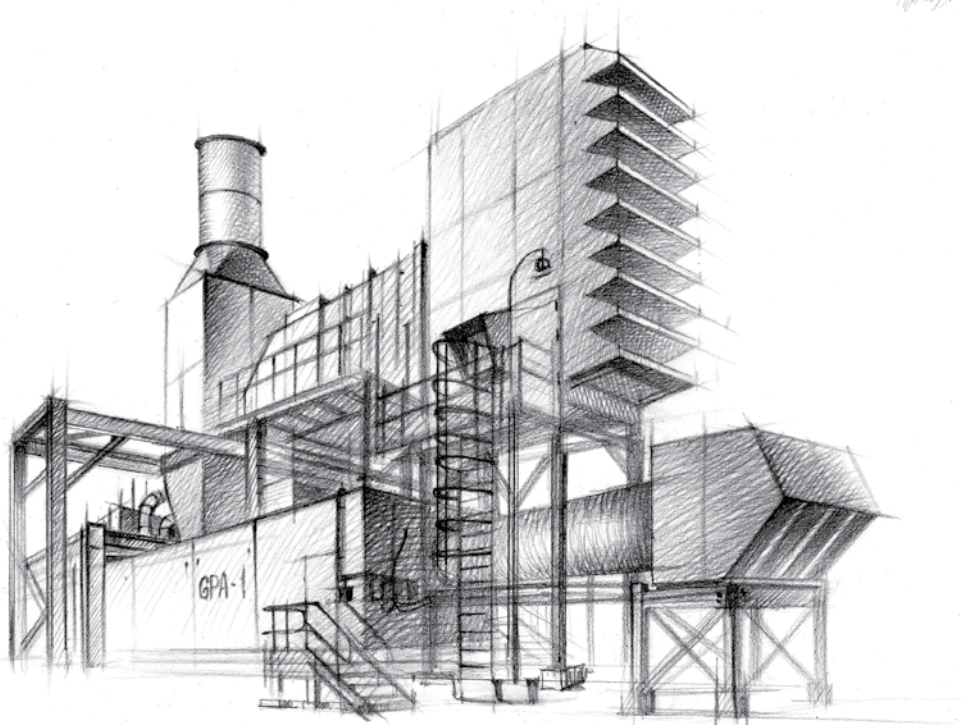
Also in 2009, as an improvement to the Collective Agreement, revision was made to the section of labour protection and the annex on the jobs where the employees of the JSC *Latvijas Gāze* are subject to the health and safety requirements due to harm to health.

A peculiar universe

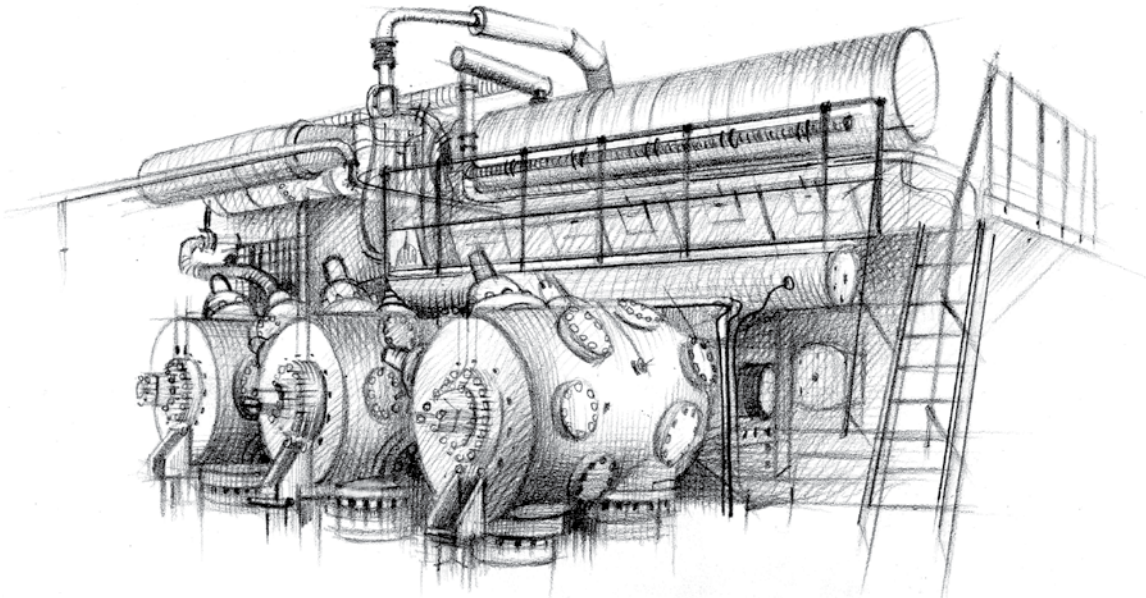
Impressive structures, huge pieces of equipment. A peculiar universe where each detail, every nuance has its meaning, function and sense. And this universe is held together by a noble aim – gas should work for the benefit of people.



Gas well with technological piping (christmas tree)



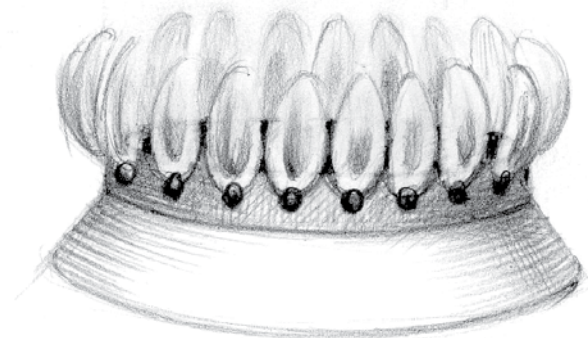
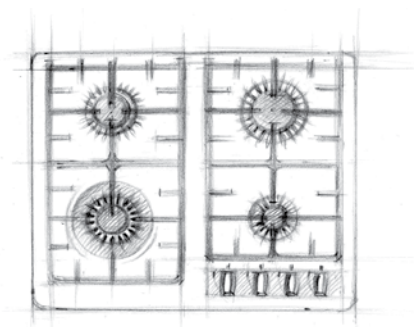
Gas compressor aggregate *Solar Mars 100*
Power – 11 300 KW



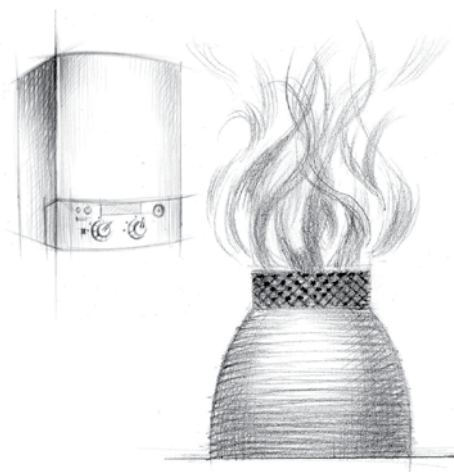
Gas compressor aggregate *Cooper Bessemer 12z330*
Power – 4400KW

The unique has become routine

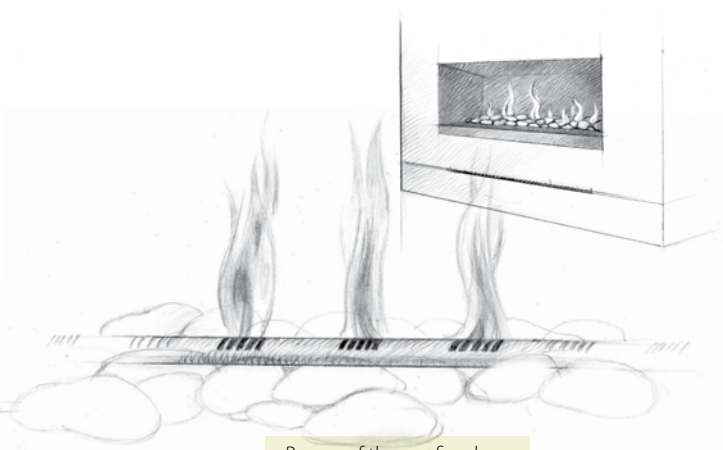
Gas burners – an utter daily necessity and component. Something that elementary – as the air we breathe or water we drink. Sometimes we even forget that gas a and the process of taming it is so special.



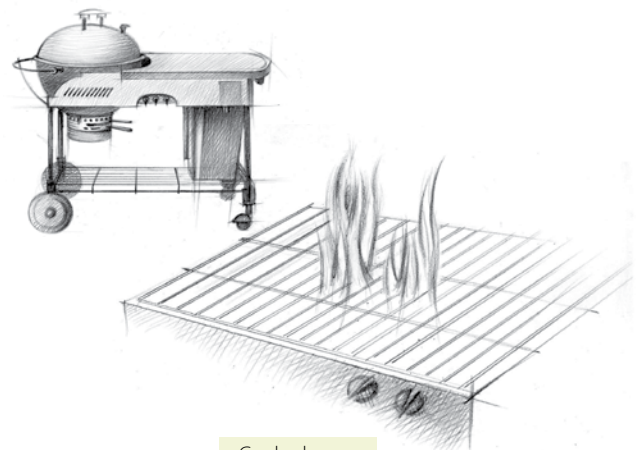
Household gas burner



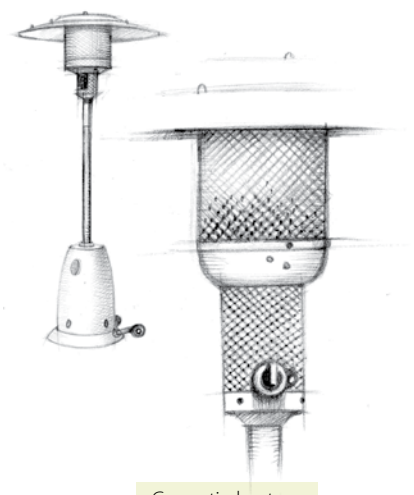
Burner of the gas boiler



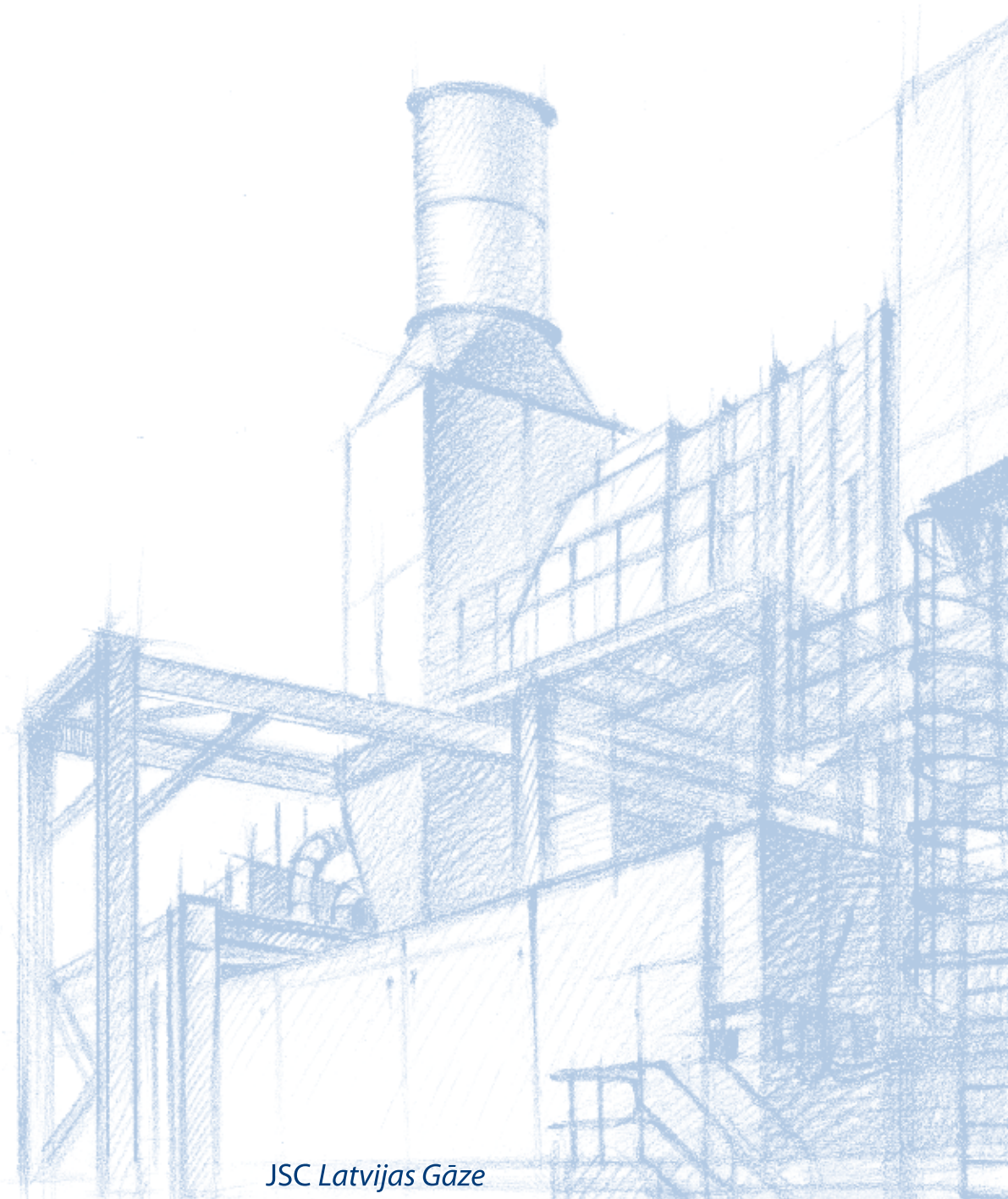
Burner of the gas fireplace



Gas barbecue



Gas patio heaters



JSC Latvijas Gāze

FINANCIAL REPORT

2009

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1. Operation of the Company in the reporting year

The Joint Stock Company *Latvijas Gāze* (hereinafter – the Company) is an energy supply company, which deals with natural gas transmission, storage, distribution and sale. In 1997, the Energy Supply Regulation Council of the Republic of Latvia granted to the Company exclusive licences for the provision of regulated public services until February 10, 2017. On January 31, 2007, the Council of the Public Utility Commission (hereinafter – PUC) issued to the Company a licence for natural gas sale until February 10, 2012. Pursuant to the Energy Law, the Company is the natural gas supply system operator, which, avoiding overloads of system capacity, ensures uninterrupted and secure natural gas supply to consumers in Latvia.

Over the reporting year, users were supplied with 1 492.9 million m³ of natural gas. In comparison to 2008, natural gas sales in m³ have decreased by 8.5%. During the reporting period, customers of the Company were influenced by the financial crisis and economic recession in Latvia, which had an impact on the Company's economic performance and natural gas consumption. Due to the relatively high natural gas prices, the first half of 2009 resulted in reduced demand for natural gas and users switching to alternative types of fuel. At the end of the year an opposite trend was witnessed as the low air temperature and the cheap natural gas reserves at the Inčukalns Underground Gas Storage Facility (hereinafter – Inčukalns UGS) raised the demand for natural gas above that of the 1st half and the European market. The average consumption by households also decreased during the reporting year. This was due to the changes in the average temperature, which was higher than in previous years throughout the year, except for December, and optimisation of use of resources.

In late 2008, natural gas suppliers finalised the gradual increase of purchase prices reaching the price level of the European natural gas markets, and in 2009 the natural gas purchase prices were only influenced by the changes in oil product quotations at the stock exchange, currency value fluctuations and gas supply flows.

During the reporting period, natural gas was sold for the differential natural gas sale end tariffs, approved by the PUC Council on July 24, 2008, with the resolution No. 247 "On natural gas supply tariffs of the Joint Stock Company *Latvijas Gāze*".

The applied differential natural gas sale end tariffs consist of two parts: fixed tariffs for regulated services and the natural gas sale price, which changes with a step of 5 Ls/thous.nm³ depending on the actual natural gas purchase costs. The natural gas sale end tariff applied to users with the annual consumption volume over 25 thousand nm³ changes monthly, whereas to users with the annual consumption up to 25 thousand nm³ – once in half year, on January 1 and July 1.

Over the reporting year from January to December, the tariffs for households for heating decreased by 27%, while for industrial customers – by 36% on average.

In 2009, the Company sold natural gas and provided services to consumers for Ls 329.7 million (EUR 469.1 million), which is by 6% less than in the respective period of 2008; the expenses of the reporting year (excluding administrative costs) are Ls 293.9 million (EUR 418.2 million) and the gross profit – Ls 35.8 million (EUR 51 million). The decrease of net turnover relates to changes in the natural gas sale price and the natural gas sales volume.

Also in 2009, the Company incorporated a number of measures in order to keep its profit at the level of 2008. The Company introduced new standards for operation of the gas supply system and re-organized the organizational

structure, reducing the number of employees by 9.2%. Working under conditions of crisis, additional financial and material resources were shifted for the control of natural gas sales and billing, reducing the financing for the provision of new connections, advertising and marketing activities. Like in previous years, the funding of measures related to the system safety was set as a priority. Additional saving of funds was facilitated by the decreased prices and the increased competition of outsourced services used when organizing purchase tenders.

The Company closed the year 2009 with a net profit of Ls 19.97 million (EUR 28.4 million), which did not considerably differ from that of 2008 (Ls 19.93 million or EUR 28.4 million), still being Ls 12.9 million (EUR 18.3 million) below the figure of 2007. The net profitability of business activity was 6.1% in 2009 and 5.7% in 2008.

In 2009, 1.21 billion m³ of natural gas was injected into the Inčukalns UGS, while 1.97 billion m³ was withdrawn. In comparison to the 2008, these volumes have fallen by 36.8% and 19.8% respectively. During the reporting period a considerable decrease of usage of the Inčukalns UGS for the needs of other countries was noted, which was due to the mild winter and the increase of the tariffs of gas storage services.

In 2009, the Company invested Ls 17.2 million (EUR 24.5 million) in the modernization of the gas supply system and acquisition of new fixed assets. 33% of the total investment was spent on the modernization of the gas transmission pipeline system, 31% – on the improvement of the operational safety and the modernization of equipment at the Inčukalns UGS, while 30% - on the expansion of the distribution networks and the renewal of fixed assets. 1.1 thousand new users were connected to the gas supply system. The total number of gas-enabled objects at the end of year reached 442.1 thousand.

In the reporting period, the reconstruction of seven wells at the Inčukalns UGS in the gas-carrying zone was completed with the total costs reaching Ls 1.96 million (EUR 2.8 million). In cooperation with the LLC *Gazpromenergodagnostika*, an investigation of technical condition was carried out, and the reconstruction of further wells began under the plan of measures for the improvement of safety of gas supply system 2010-2015. The reconstruction of the gas drying unit CS-1 is in progress. Over the reporting year, Ls 2.9 million (EUR 4.1 million) were invested, whereas the total costs of the Project are planned in the amount of Ls 5.2 million (EUR 7.2 million). The object is due for commissioning in late 2011. The elimination of damages found in diagnostics of gas transmission pipelines, as well as construction of a pig launcher and receiver for the gas pipelines Riga – Inčukalns UGS, Iecava – Liepāja and Riga – Panevežys is in progress. Ls 2.9 million (EUR 4.1 million) were spent on the construction of gas pipelines in 2009. The major project was the construction of a gas pipeline along the Riga bypass road. The total length of the bypass line will reach 40 km and after the commissioning of a cross-connection in 2011, a looping will be completed, allowing for stabilization of gas supply of Riga and its suburbs. The total costs of the project are Ls 3 million (EUR 4.3 million); Ls 2 million (EUR 2.8 million) were utilised in 2009.

2. Research and development measures

In order to ensure uninterrupted gas supply to users and secure operation of the gas supply system, the Company has developed a „Plan of measures for the improvement of operation safety of the gas supply system 2010-2015” which is based on the conclusions made by the Russian companies *Gazobezopasnostj and Lentransgaz*, the institutes *VNIIGAZ and Giprospecgaz*, as well as the German companies *Pipeline Engineering GmbH, Untergrundspeicher und Geotechnologie – Systeme GmbH, E.ON Engineering GmbH, E.ON Ruhrgas International AG* and other partners regarding the technical condition of equipment and modernization options.

The plan of measures envisages investment in the improvement of safety for the total amount of Ls 50.6 million (EUR 72 million). This basically includes projects that are required to be implemented for the improvement of the system operation safety, the gasification of new objects and the improvement of gas supply stability throughout the region.

3. Management of financial risks

The operation of the Company is subject to a variety of financial risks, including credit risks and the risk of fluctuation of currency and interest rates. The administration of the Company attempts to minimize the negative impact of potential financial risks on the financial state of the Company.

The Company is not directly subject to the risk of fluctuation of foreign currency rates, as the gas purchase price is set in USD and then recalculated into EUR, whereas the gas sale tariffs are in Ls. Settlements for supplied natural gas are made in EUR. With the lat rate being pegged to the euro rate since January 1, 2005, the Ls/EUR rate undergoes limited fluctuations that are unlikely to have a serious influence on the further financial results. Changes of gas purchase prices in USD depending on the quotation of oil products are covered by the PUC-approved natural gas sale tariffs, which to a certain extent cover the fluctuations of both Ls/EUR and EUR/USD rate. The risk of fluctuations of foreign currency rates in relation to debts to suppliers is controlled by keeping a considerable amount of cash assets deposited in the respective currency.

As of the end of the reporting year, the Company has no loans, thus it is not subject to the credit risk.

The financial assets subject to the credit risk mainly consist of customer debts and cash. The Company's credit risk is of high degree as a large share of the net turnover is concentrated in a limited number of customers. Four of the Company's customers comprise up to 45.5% (in 2008 – 48.6%) of the natural gas sales income; as of December 31, 2009, one of these debtors accounted for 25.5% (in 2008 – 17.2%), the second and the third largest debtors' constituted 9.3% un 8% respectively (in 2008 – 7.2% and 6.3%) of the total amount of the customer debt. The Company has introduced and observes a credit policy that envisages sale of goods on credit only to customers with good credit history, controlling the credit amount set for each customer.

Customer debts are shown at their recoverable value. The Company's partners in monetary transactions are local financial institutions with adequate credit history.

The Company pursues prudent liquidity risk management by ensuring sufficient credit resources that allow settling liabilities when they fall due.

4. Post balance sheet events

During the period between the last day of the reporting year and the date of signing of this report there have been no significant events that would have a material effect on the year end result.

5. Distribution of profit 2009 as suggested by the Board

	2009 Ls	2009 EUR
Profit of the reporting year	19 966 697	28 410 050
Share of profit not available for distribution (credit of deferred tax not distributed due to revaluation of fixed assets)	(1 636 688)	(2 328 798)
Distributable share of profit	18 330 009	26 081 252
Suggested distribution of profit:		
dividends to shareholders (79.9%)	15 960 000	22 709 034
dividends per one share (Ls per 1 share)	0,40	0,569
Statutory reserve	2 370 009	3 372 218

Certain members of the Council and the Board of the Company own shares and interests in numerous companies registered in the Registry of Enterprises of the Republic of Latvia, and they have managerial functions there. Within the reporting year the Company has not made transactions of considerable amount with these companies, except for those mentioned in the financial statement).

Information on the shares of the Company held by the members of the Board and the Council of the Company is available at the Board of the Company.

6. Future prospect


In the light of the investments made in the improvement of the system operation safety, the expansion of the gas pipeline network and the attraction of new customers, as well as taking into account the situation in the fuel market in Latvia, the Board of the Company believes that in 2010 the Company will continue its successful development and will take a stable place in the fuel supply market.

Chairman of the Board

A. Dāvis

Board meeting minutes No. 15 (2010)

Riga, April 29, 2010



Profit and loss account for the year ended December 31, 2009

	2009 Ls	2008 Ls	2009 EUR	2008 EUR
1 Net sales	329 705 288	351 004 620	469 128 360	499 434 579
2 Cost of sales	(293 889 591)	(320 027 733)	(418 167 215)	(455 358 440)
3 Gross profit	35 815 697	30 976 887	50 961 145	44 076 139
5 Administrative expenses	(7 357 915)	(7 517 856)	(10 469 369)	(10 696 945)
6 Other operating income income	1 420 125	2 339 440	2 020 656	3 328 723
7 Other operating expenses	(2 427 984)	(1 525 871)	(3 454 711)	(2 171 119)
10 Other interest income and similar income	2 952 736	1 861 260	4 201 365	2 648 334
11 Changes of long term financial investments and short term securities	(190)	261	(270)	371
12 Interest expenses and similar expenses	(1 202 833)	(435 982)	(1 711 478)	(620 347)
13 Provisions for bad and doubtful debtors, net	(5 184 331)	(2 106 835)	(7 376 638)	(2 997 756)
14 Provisions for obsolete and slow moving inventories, net	(36 918)	(93 025)	(52 529)	(132 362)
16 Profit before taxes	23 978 387	23 498 279	34 118 171	33 435 038
17 Corporate income tax for the reporting year	(3 941 679)	(4 177 756)	(5 608 504)	(5 944 411)
18 Deferred income tax	92 113	757 706	131 066	1 078 119
19 Other taxes	(162 124)	(150 003)	(230 683)	(213 435)
20 Current year's profit	19 966 697	19 928 226	28 410 050	28 355 311
Unrealised deferred tax gain related to fixed assets revaluation	(1 636 688)	(1 770 008)	(2 328 798)	(2 518 494)
Current year's profit available for distribution	18 330 009	18 158 218	26 081 252	25 836 817

Balance sheet as at December 31, 2009

(1)

	31.12. 2009. Ls	31.12. 2008. Ls	31.12. 2009. EUR	31.12. 2008. EUR
Assets				
Long-term investments				
I. Intangible assets:				
1. Research and development	1 705	32 452	2 425	46 174
2. Concessions, patents, licences, trademarks and similar rights	2 306 915	2 188 698	3 282 445	3 114 238
5. Advance payments for intangible assets	122 974	81 569	174 976	116 062
Total intangible assets:	2 431 594	2 302 719	3 459 846	3 276 474
II. Fixed assets:				
1. Land, buildings, constructions and gas transmission system	263 359 486	264 981 500	374 726 789	377 034 707
3. Equipment and machinery	41 660 762	44 408 779	59 277 925	63 188 002
4. Other fixed assets	4 960 979	4 658 746	7 058 835	6 628 796
5. Advances for fixed assets and fixed assets under construction	5 125 997	5 970 558	7 293 636	8 495 339
Total fixed assets:	315 107 224	320 019 583	448 357 185	455 346 844
V. Long-term financial investments:				
3. Investment in associated companies	80	80	114	114
5. Other securities and investments	3 787	5 937	5 388	8 447
9. Trade debtors	-	5 090	-	7 242
Total long-term financial investments:	3 867	11 107	5 502	15 803
Total long-term investments:	317 542 685	322 333 409	451 822 533	458 639 121
Current assets				
I. Inventories:				
1. Raw materials and consumables	83 532 693	115 680 757	118 856 315	164 598 887
5. Advances for goods receivable	1 793	2 476	2 551	3 523
Total inventories:	83 534 486	115 683 23	118 858 866	164 602 410
III. Debtors:				
1. Trade debtors	20 631 192	39 298 457	29 355 542	55 916 667
3. Receivables from affiliated companies	1 571 574	243 826	2 236 148	346 933
4. Other debtors	1 909 682	4 445 007	2 717 233	6 324 677
7. Deferred expenses	494 387	382 433	703 450	544 154
Total debtors:	24 606 835	44 369 723	35 012 373	63 132 431
IV. Short-term financial investments:				
5. Other securities and investments	198	15 281	282	21 743
Total short-term financial investments:	198	15 281	282	21 743
V. Cash and bank:	35 810 287	6 446 083	50 953 448	9 171 950
Total current assets:	143 951 806	166 514 320	204 824 969	236 928 534
Total assets	461 494 491	488 847 729	656 647 502	695 567 655

Balance sheet as at December 31, 2009

(2)

	31.12. 2009. Ls	31.12. 2008. Ls	31.12. 2009. EUR	31.12. 2008. EUR
Liabilities				
Shareholders' funds:				
1. Share capital	39 900 000	39 900 000	56 772 585	56 772 585
2. Share premium	14 320 210	14 320 210	20 375 823	20 375 823
3. Long-term investments revaluation reserve	186 218 357	186 917 922	264 964 851	265 960 242
5. Reserves				
c) statutory reserve	61 706 378	58 710 159	87 800 266	83 537 030
6. Retained earnings				
a) previous years' retained earnings	6 948 488	5 178 481	9 886 808	7 368 314
b) current year's retained profit	19 966 697	19 928 226	28 410 050	28 355 311
Total shareholders' funds:	329 060 130	324 954 998	468 210 383	462 369 305
Creditors:				
Long-term creditors:				
12. Deferred income	13 824 375	13 459 780	19 670 313	19 151 542
15. Accruals for post employment benefits and other employee benefits	4 415 984	4 672 646	6 283 380	6 648 577
16. Deferred tax liability	29 699 793	29 915 358	42 258 998	42 565 719
Total long-term creditors:	47 940 152	48 047 784	68 212 691	68 365 838
Short-term creditors:				
3. Borrowings from credit institutions	-	1 787 886	-	2 543 933
5. Advances received	6 640 438	5 376 924	9 448 492	7 650 674
6. Trade creditors	59 120 418	78 315 274	84 120 776	111 432 596
8. Accounts payable to related companies	1 469 909	7 744 443	2 091 492	11 019 350
10. Taxes and state compulsory social insurance contributions	9 492 572	8 572 974	13 506 713	12 198 242
11. Other creditors	655 563	4 348 923	932 782	6 187 959
12. Deferred income	823 691	3 673 803	1 172 007	5 227 351
15. Accrued liabilities	6 291 618	6 024 720	8 952 166	8 572 407
Total short-term creditors:	84 494 209	115 844 947	120 224 428	164 832 512
Total creditors:	132 434 361	163 892 731	188 437 119	233 198 350
Total liabilities and shareholders' funds	461 494 491	488 847 729	656 647 502	695 567 655

Statement of changes in equity for the year ended December 31, 2009

	Share capital	Share premium	Long-term investments revaluation reserve	Statutory reserve	Retained earnings	Total
	Ls	Ls	Ls	Ls	Ls	Ls
Balance as at 31.12.2007.	39 900 000	14 320 210	187 441 623	47 582 358	36 256 282	325 500 473
Dividends	-	-	-	-	(19 950 000)	(19 950 000)
Transferred to reserves	-	-	-	11 127 801	(11 127 801)	-
Revaluation of fixed assets	-	-	1 501 617	-	-	1 501 617
Deferred tax liability arising on the revaluation of fixed assets	-	-	(225 243)	-	-	(225 243)
Disposal of revalued fixed assets	-	-	(1 890 511)	-	-	(1 890 511)
Deferred tax on disposal of revalued fixed assets	-	-	90 436	-	-	90 436
Profit for the year	-	-	-	-	19 928 226	19 928 226
Balance as at 31.12.2008.	39 900 000	14 320 210	186 917 922	58 710 159	25 106 707*	324 954 998
Dividends	-	-	-	-	(15 162 000)	(15 162 000)
Transferred to reserves	-	-	-	2 996 219	(2 996 219)	-
Revaluation of fixed assets	-	-	119 952	-	-	119 952
Deferred tax liability arising on the revaluation of fixed assets	-	-	(17 993)	-	-	(17 993)
Disposal of revalued fixed assets	-	-	(942 969)	-	-	(942 969)
Deferred tax on disposal of revalued fixed assets	-	-	141 445	-	-	141 445
Profit for the year	-	-	-	-	19 966 697	19 966 697
Balance as at 31.12.2009.	39 900 000	14 320 210	186 218 357	61 706 378	26 915 185*	329 060 130

Statement of changes in equity for the year ended December 31, 2009 (continued)

	Share capital	Share premium	Long-term investments revaluation reserve	Statutory reserve	Retained earnings	Total
	EUR	EUR	EUR	EUR	EUR	EUR
Balance as at 31.12.2007.	56 772 585	20 375 823	266 705 402	67 703 596	51 588 041	463 145 447
Dividends	-	-	-	-	(28 386 293)	(28 386 293)
Transferred to reserves	-	-	-	15 833 434	(15 833 434)	-
Revaluation of fixed assets	-	-	2 136 608	-	-	2 136 608
Deferred tax liability arising on the revaluation of fixed assets	-	-	(320 492)	-	-	(320 492)
Disposal of revalued fixed assets	-	-	(2 689 955)	-	-	(2 689 955)
Deferred tax on disposal of revalued fixed assets	-	-	128 679	-	-	128 679
Profit for the year	-	-	-	-	28 355 311	28 355 311
Balance as at 31.12.2008.	56 772 585	20 375 823	265 960 242	83 537 030	35 723 625*	462 369 305
Dividends	-	-	-	-	(21 573 581)	(21 573 581)
Transferred to reserves	-	-	-	4 263 236	(4 263 236)	-
Revaluation of fixed assets	-	-	170 677	-	-	170 677
Deferred tax liability arising on the revaluation of fixed assets	-	-	(25 602)	-	-	(25 602)
Disposal of revalued fixed assets	-	-	(1 341 724)	-	-	(1 341 724)
Deferred tax on disposal of revalued fixed assets	-	-	201 258	-	-	201 258
Profit for the year	-	-	-	-	28 410 050	28 410 050
Balance as at 31.12.2009.	56 772 585	20 375 823	264 964 851	87 800 266	38 296 858*	468 210 383

* The retained earnings brought forward include accumulated revaluation reserve of disposed fixed assets of Ls 110 538 or EUR 157 281 (2008: Ls 62 325 (EUR 88 680)).

Changes in Statutory reserves can only be made with shareholders' approval. Revaluation reserve and share premium cannot be distributed to shareholders.

Cash flow statement for the year ended December 31, 2009

	2009 Ls	2008 Ls	2009 EUR	2008 EUR
I Cash flows from operating activities				
1. Profit before taxes	23 978 387	23 498 279	34 118 171	33 435 038
Adjustments for:				
- fixed asset depreciation and write-down of intangible assets	21 034 911	19 311 381	29 929 983	27 477 619
- difference between the actual and forecasted purchase cost of natural gas and income from participation charge	(3 411 381)	2 657 242	(4 853 958)	3 780 915
- change in provisions for inventories	36 918	93 025	52 529	132 362
- change in provisions for long-term financial investments	2 150	(261)	3 059	(371)
- change in accrued expenses for bonuses for reporting year's financial results	298 000	(96 000)	424 015	(136 594)
- change in accrued unused annual leave expenses	(179 804)	206 196	(255 839)	293 390
- change in other provisions	148 702	120 939	211 583	172 081
- changes in accruals for post employment benefits and other employee benefits	(256 662)	2 172 646	(365 197)	3 091 397
- other interest and similar income	(2 952 736)	(1 861 260)	(4 201 365)	(2 648 334)
- interest and similar expense	1 202 833	435 982	1 711 478	620 347
- loss / (profit) on sale of fixed assets	148 686	(538 426)	211 561	(766 111)
Adjustments for:				
Trade debtors decrease / (increase)	17 344 606	(14 767 019)	24 679 151	(21 011 576)
Inventories decrease / (increase)	32 539 603	(29 332 051)	46 299 683	(41 735 749)
Trade creditors' (decrease) / increase	(25 469 390)	23 157 755	(36 239 677)	32 950 517
Other debtors' decrease / (increase)	3 343 957	(2 329 777)	4 758 022	(3 314 974)
Other creditors' (decrease) / increase	(5 585 330)	7 485 744	(7 947 209)	10 651 254
3. Cash generated from operations	62 223 450	30 214 395	88 535 990	42 991 211
Interest and similar payments	(21 050)	(150 569)	(29 951)	(214 240)
Interest and similar income	2 695 446	2 366 000	3 835 275	3 366 515
Corporate income tax paid	(1 445 232)	(9 443 867)	(2 056 380)	(13 437 412)
6. Net cash flows generated from operating activities	63 452 614	22 985 959	90 284 934	32 706 074
II. Cash flows from investing activities				
Acquisition of fixed assets and intangible assets	(17 188 207)	(22 772 950)	(24 456 615)	(32 402 989)
Proceeds from sale of fixed assets	47 723	120 398	67 904	171 311
Dividends received	1 960	-	2 789	-
9. Net cash used in investing activities	(17 142 444)	(22 652 552)	(24 385 922)	(32 231 678)
III. Cash flows from financing activities				
Repayment of borrowings	(1 787 886)	(20 029 914)	(2 543 933)	(28 500 000)
Received loans	-	1 787 886	-	2 543 933
Dividends paid	(15 162 000)	(19 950 000)	(21 573 581)	(28 386 293)
7. Net cash used in financing activities	(16 949 866)	(38 192 028)	(24 117 514)	(54 342 360)
Net increase / (decrease) in cash and cash equivalents	29 364 204	(37 858 621)	41 781 498	(53 867 964)
Cash and cash equivalents at the beginning of the reporting year	6 446 083	44 304 704	9 171 950	63 039 914
Cash and cash equivalents at the end of the reporting year	35 810 287	6 446 083	50 953 448	9 171 950

Accounting policies

(a) Information on the Company

The legal address of the Joint Stock Company *Latvijas Gāze* is Vagonu street 20, Riga (until January 3, 2009 Aristīda Briāna street 6, Riga). The Company is registered in Commercial Register with common registration number 4000 300 0642. The Company's main shareholders are *E.ON Ruhrgas International AG* (47.23%), *JSC Gazprom* (34.0%) and LLC *Itera Latvija* (16.0%). The Board of the Company consists of Adrians Dāvis (Chairman of the Board), Aleksandrs Mihejevs (Александр Михеев) (Member of the Board, Deputy Chairman of the Board), Jörg Tumat (Member of the Board, Deputy Chairman of the Board), Anda Ulpe (Member of the Board) and Gints Freibergs (Member of the Board). The Company's auditor is the certified audit company *SIA PricewaterhouseCoopers* and responsible certified auditor Lolita Čarpeviča.

(b) Financial statements preparation basis

Financial statements are prepared in accordance with the Accounting Act and Annual Accounts Act of the Republic of Latvia and the effective Latvian accounting standards (LAS).

The profit and loss account is prepared in accordance with turnover method.

Cash flow statement is prepared using indirect cash flow method.

The accounting policies used by the Company are consistent with those used in the previous accounting period.

Instability in the global and Latvian financial markets and economies

Along with changes caused by the economic and financial crisis since 2008, among other things, financial markets have experienced material changes in the form of diminishing financial assets and increasing financing costs, and uncertainty in the business and investment environment has increased. Changes in the global financial markets have caused banks and other financial institutions to go bankrupt, with bank rescues being undertaken in many countries including Latvia. Although the recovery trend is strengthening in the global economy, it is currently not possible to predict reliably when Latvia's economy will begin to grow again.

Management is unable to estimate reliably the possible effects on the Company's financial position of any further instability in the economies and financial markets of Latvia and other countries in the region as well as the economic downturn in Latvia. Management believes it is taking all the necessary measures to support sustainable growth of the Company's business in the present circumstances.

Impact on liquidity:

The volume of wholesale financing has significantly diminished since 2008. Such conditions may affect the Company's ability to obtain new borrowings and to refinance its existing borrowings on terms similar to those applied to earlier transactions. Maturities of the loans repayable by the Company are disclosed in Note 20.

Impact on asset valuation:

Solvency of the Company's customers may be affected by their reduced liquidity and ability to continue business operations during a prolonged economic downturn. Customers' deteriorating operating conditions may affect management's cash-flow forecasts and assessment of the impairment of financial and non-financial assets. Management's assumptions about recoverable amounts of the assets are based on the information available, however it is not possible to determine reliably the full impact of the economic downturn.

(c) Net sales and income recognition

Sales are recognised upon delivery of gas or performance of services. Net sales represent the total of goods and services sold during the year net of discounts, value added tax and the difference between the actual and forecasted purchase cost of natural gas, which is used for determination of applicable natural gas selling price for the following month. Applicable natural gas selling price is calculated based on latest available data. The exchange rate for EUR/USD set by ECB in the last day of the previous month, actual gross calorific value as well as planned volume of received and delivered gas are used in the calculation. Actual purchase costs of natural gas are calculated based on methodology approved by the the Public Utility Commission (PUC's) Council, taking into account the exchange rate of EUR/USD at the last day of the month when gas is delivered, actual gross calorific value as well as actual volume of gas received from suppliers.

Accrual of interest income is ceased, if it's recoverability is uncertain. Based on prudence principle, penalties, including fines for late payments for gas, are recognised when received.

The income from residents and enterprises contribution to financing of construction works of gas pipelines is accounted for as deferred income and recognised in the profit and loss account over the expected useful life of constructed fixed assets of 30 to 40 years.

(d) Foreign currency translation

The Company maintains its accounts in Latvian Lats. All transactions denominated in foreign currencies are converted to Lats at the exchange rate set by the Bank of Latvia prevailing on the day on which the transactions took place. Monetary assets and liabilities denominated in foreign currencies are translated in Lats in accordance with the official Bank of Latvia exchange rate for the last day of the reporting period. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit and loss account.

	31.12.2009.	31.12.2008.
	Ls	Ls
1 USD	0,489	0,495
1 EUR	0,702804	0,702804

Euro financial statements are prepared using account closing balances in Ls at the last day of the reporting period, performing conversion to EUR by using the official fixed EUR / Ls rate set by the Bank of Latvia 1 EUR = Ls 0.702804 (1 EUR = Ls 0.702804, determined by Bank of Latvia as of December 30, 2004 reposing to resolution of the Council of Bank of Latvia) for all period January 1, 2009 till December 31, 2009.

(e) Intangible assets

Intangible assets are recorded at historic cost net of accumulated amortisation. Amortisation is calculated on a straight-line basis to write down each intangible asset to its estimated residual value over its estimated useful life. Generally, intangible assets are amortised over a period of 5 years.

(f) Fixed assets

Fixed assets are recorded at historic cost or revalued amount net of accumulated depreciation and impairment charge.

Increase in value arising on revaluation is shown in equity under "Long-term investments revaluation reserve". Decrease that offsets a previous increase of the same asset's value recognised in the said reserve is charged against that reserve; any further decrease is charged to the current year's profit and loss account.

Depreciation is calculated on a straight-line basis to write down each fixed asset to its estimated residual value over its estimated useful life using following rates set by management:

	% per annum
Buildings	1 - 3
Gas transmission system	2 - 2,5
Machinery and equipment	5 - 20
Furniture and fittings	10 - 20
Computers and equipment	30

Depreciation is not calculated for land and buffer gas, advances for fixed assets and assets under construction.

The Company capitalises fixed assets with cost exceeding Ls 150 (EUR 213) and useful life exceeding 1 year.

Direct charges related to the particular fixed asset under construction are capitalised, during the period of time that is required to complete and prepare the asset for its intended use, as part of the cost of the asset.

Where the carrying amount of a fixed asset exceeds its estimated recoverable amount, it is written down immediately to its recoverable amount and the impairment loss is recognised as an expense in the profit and loss account or off-set against the revaluation reserve if the fixed asset is carried at revalued amount. Recoverable amount is the higher of the fair value less costs to sell and the value in use of the related fixed asset.

Subsequent costs are included in the asset's carrying amount or recognised as 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. Such costs are depreciated over the remaining useful life of the related asset. Capitalising the cost of mounted spare parts, the carrying value of the part replaced is written off to the profit and loss account.

Repairs and maintenance are charged to the profit and loss account during the period in which they are incurred. Gains or losses on disposals are determined by comparing carrying amount with proceeds and gains from related asset's revaluation reserve write-off and are charged to the profit and loss account during the period in which they are incurred.

(g) Inventories

The cost of natural gas in Inčukalna UGS and in gas transmission pipelines is determined separately using the first-in first-out (FIFO) method based on total natural gas movement. The cost of natural gas comprises cost of gas purchased. Materials, spare parts, gas meters and other inventories cost is determined by the weighted average method. Direct labour, other direct costs and related production overheads are recognised on an accruals basis and charged to the profit and loss account in the period when incurred.

Inventories are recorded at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the costs of completion and selling expenses. When the net realisable value of inventories is lower than its cost, provisions are created to reduce the value of inventories to its net realisable value.

(h) Accounts receivable

Accounts receivable are recorded in the balance sheet at their amortised cost less provisions made to cover anticipated loss on bad and doubtful accounts receivable. Provisions for bad and doubtful accounts receivable are established when there is an objective evidence that the Company will not be able to collect all amounts due according to the original terms of receivables. The amount of provisions for bad and doubtful accounts receivable is the difference between the amortised cost and the recoverable amount. The amount of the provision for bad and doubtful accounts receivable is recognised in the profit and loss account.

(i) Other long-term investments

Other long-term investments are disclosed at the cost less provisions created to cover losses on other than temporary diminution of value of investments. Assessment of investments is made each year based on latest available financial information.

(j) Borrowings

Borrowings are recognised initially at the proceeds received net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective yield method; any difference between proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account.

(k) Taxes

Corporate income tax for the reporting period is included in the annual accounts based on the management's calculations prepared in accordance with Latvian Republic tax legislation.

Deferred tax is provided for using liability method on all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the annual accounts. The deferred tax is calculated based on currently enacted tax rates that are expected to apply when the temporary differences reverse. The principal temporary differences arise from different fixed assets depreciation and intangible asset amortisation rates, accrued unused annual leave and bonus expenses, accruals for post employment and other benefits and provisions for bad and doubtful debts where the management is of the opinion that they will meet the criteria stated in Article 9 of the law "On Corporate Income Tax", and other accrued expenses and provisions for write down to net realizable value of inventory. The deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Increase in deferred tax liability that results from revaluation of fixed assets is charged to equity as respective increase in 'Long-term investments revaluation reserve' decrease. Decrease in deferred tax liability that results from depreciation of revalued fixed assets is charged to the profit and loss account and the respective unrealised tax gain is shown in the notes to the annual accounts.

(l) Accrued unused annual leave expenses and accrued liabilities

Accrued liabilities are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Amount of accrued unused annual leave expenses is determined by multiplying the average daily wage of employees for the last six months of the reporting year by the amount of accrued but unused annual leave at the end of the reporting year.

The Company provides defined benefits upon retirement and in the period of employment for employees whose employment conditions meet defined criteria according to the Employment contract. Amount of benefit liability is calculated based on current salary level and number of employees, which are entitled or may become entitled to receive those payments, as well as based on actuarial assumptions. Once a year an independent actuary evaluates these liabilities. Expected benefit expenses are accrued during the employment period.

Liabilities for the employee benefits are presented in the balance sheet at their present value. Employee benefit liabilities are calculated for each year using Projected Unit Credit method. Both actuary defined and publicly available assumptions are used in calculations regarding changes in demographic and financial variables.

(m) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, balances of current account with banks and short-term deposits, which can be easily converted to cash and are not subject of significant change in value.

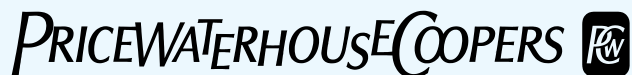
(n) Related parties

Related parties are defined as the Company's major shareholders, which have a significant influence, members of the Council and members of the Board, their close relatives and companies in which they have a significant influence or control.

(o) Profit available for distribution

On revaluation of fixed assets additional temporary difference arises between fixed asset values for financial and tax purposes. According to Accounting policies section (k) the respective increase in deferred tax liability is attributed to the 'Long-term investments revaluation reserve'. Decrease in deferred tax liability that results from depreciation of revalued fixed assets is charged to the profit and loss account as tax income.

In order to comply with the "Annual Accounts Act" of the Republic of Latvia Section 29 article 4, the said income cannot be distributed. Therefore, the profit available for distribution is calculated as net difference between net profit and unrealised deferred tax income related to fixed asset revaluation and is shown separately in profit and loss account.

**PricewaterhouseCoopers SIA**

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INDEPENDENT AUDITORS' REPORT**To the Shareholders of JSC Latvijas Gāze****Report on the Summarised Financial Statements**

The accompanying summarised financial statements have been derived from the financial statements of JSC *Latvijas Gāze* (the Company) for the year ended 31 December 2009, which are prepared in accordance with the Annual Accounts Act of the Republic of Latvia. These summarised financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on whether these summarised financial statements are consistent, in all material respects, with the financial statements from which they were derived.

We have audited the financial statements of the Company for the year ended 31 December 2009, from which these summarised financial statements were derived in accordance with International Standards on Auditing. In our report dated 29 April 2010 we expressed an unqualified opinion on the financial statements of the Company for the year ended 31 December 2009 from which the summarised financial statements were derived.

In our opinion, the accompanying summarised financial statements are consistent, in all material respects, with the financial statements from which they were derived.

For a better understanding of the Company's financial position and the results of its operations for the period and of the scope of our audit, the summarised financial statements should be read in conjunction with the financial statements from which the summarised financial statements were derived and our audit report thereon.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ahmed Abu Sharkh
Chairman of the Board

Lolita Čapkeviča
Certified auditor in charge
Certificate No. 120

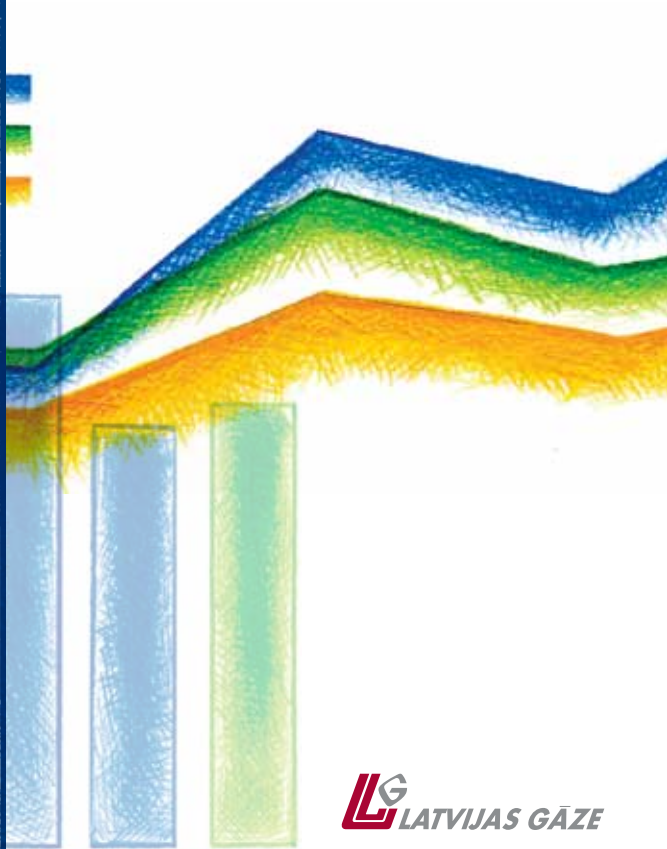
Rīga, Latvia
17 June 2010

* This version of our report is a translation from the original, which was prepared in Latvian. 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.

Publication prepared by *JSC Latvijas Gāze*
Public Relations Department

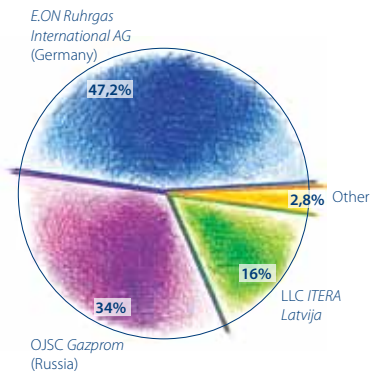
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Facts and Figures



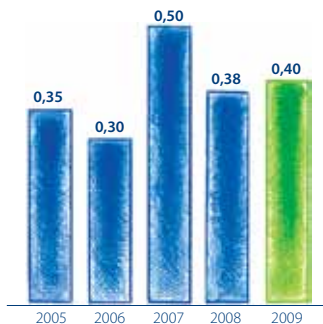
Shareholder structure

(%)
31.12.2009.



Dividend per share

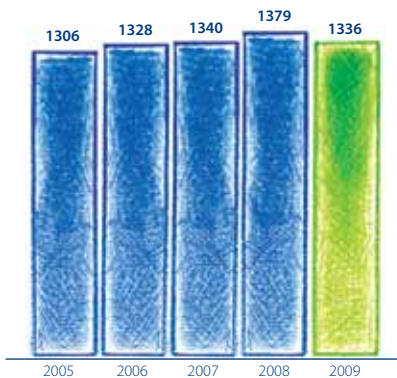
(LVL/share)



Trade statistics

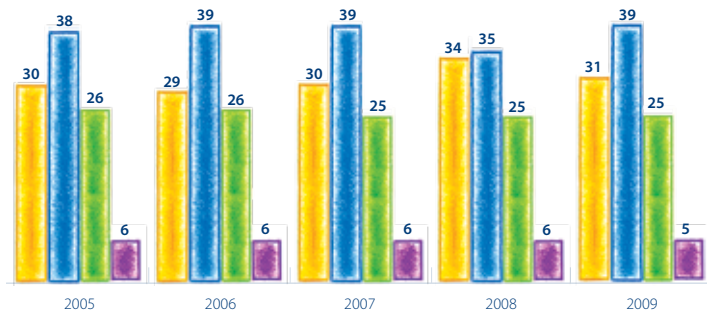
Price (LVL)	2005	2006	2007	2008	2009
First	6,2	9,95	10,35	7,25	4,55
Maximum	9,9	11,13	11,25	8,20	6,00
Minimum	6,15	9,27	7,05	3,62	3,32
Average	7,67	10,22	10,34	6,77	4,39
Price of last transaction	9,61	10,32	7,12	4,55	4,10
Turnover (shares)	63 360	128 844	154 825	46 565	64 319
Turnover (LVL million)	0,49	1,32	1,6	0,315	0,277
Capitalisation at the end of the period (LVL million)	383,44	411,77	284,09	181,545	163,59
Profit per share	0,59	0,52	0,81	0,48	0,48

Average number of employees



Education profile of employees

(%)



Higher

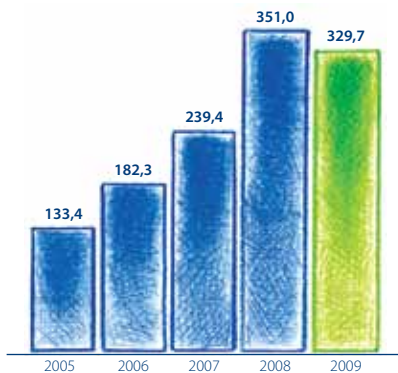
Secondary Special

Secondary

Elementary

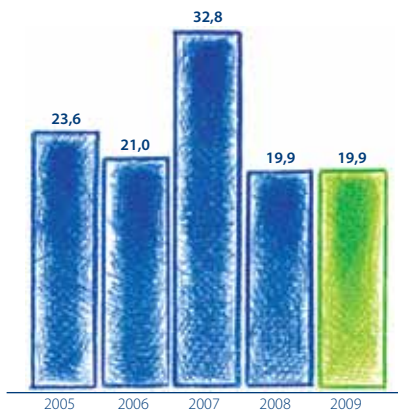
Net turnover

(LVL million)



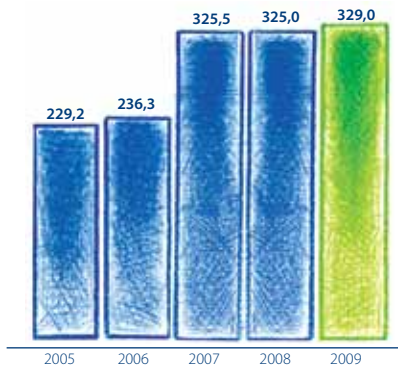
Net profit

(LVL million)



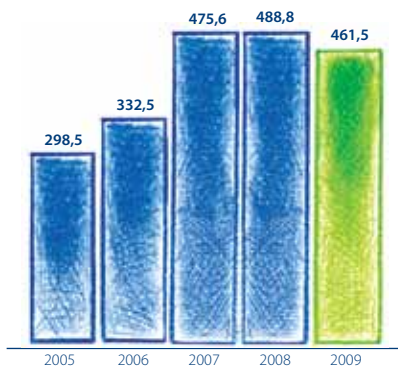
Equity

(LVL million)



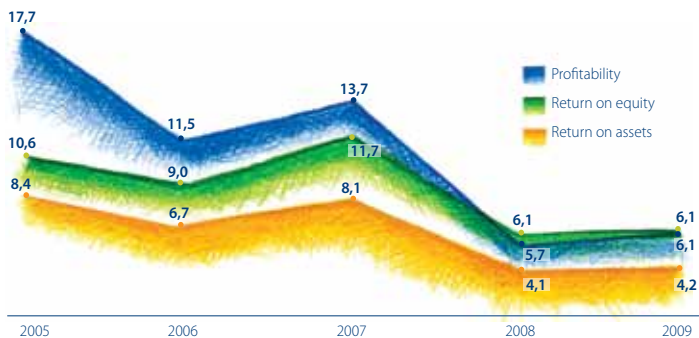
Assets

(LVL million)



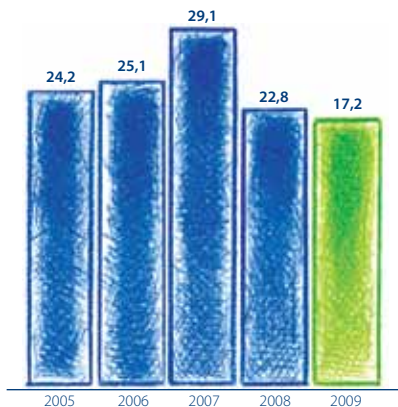
Main financial indices

(%)



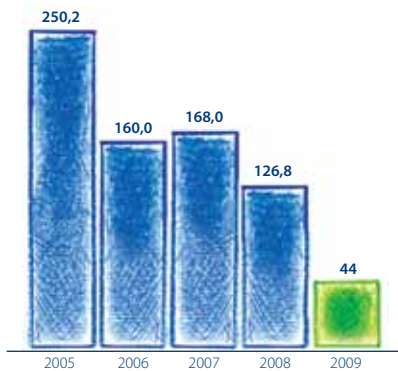
Investment

(LVL million)



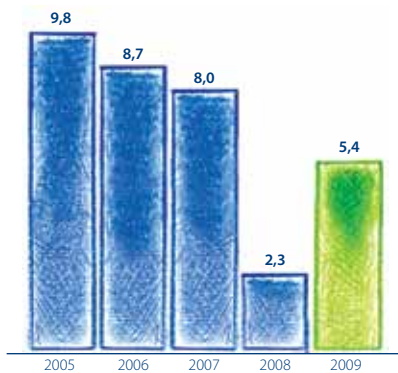
Construction of new gas pipelines

(km)



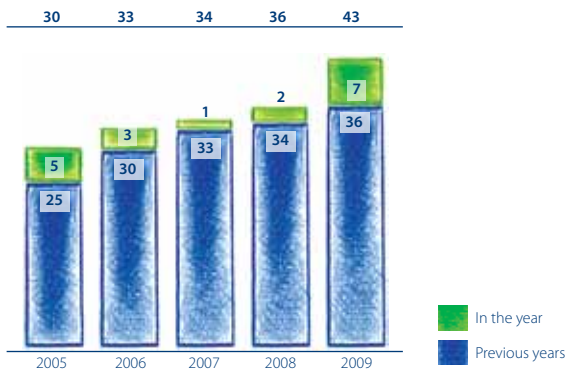
Investment

(LVL million)



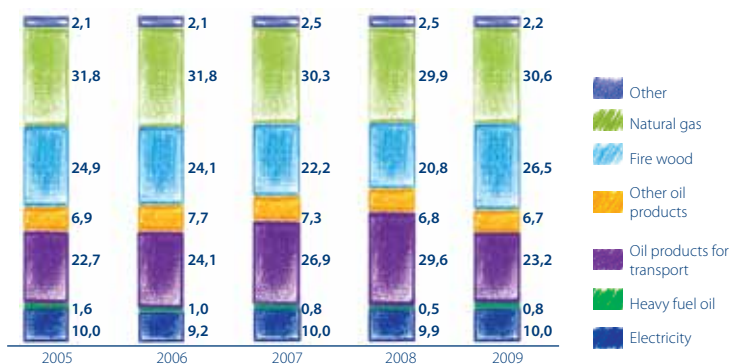
Modernization of gas regulation stations

(quantity)



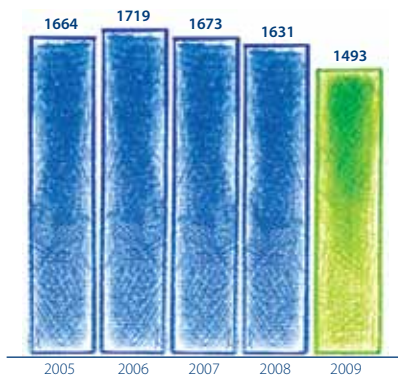
Primary energy resources balance of Latvia

(%)



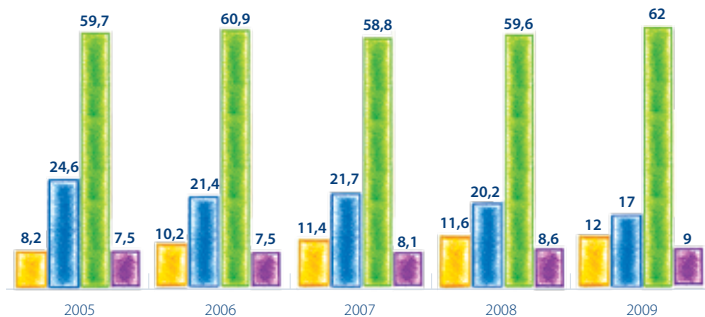
Volume of natural gas sales

(million m³)



Natural gas sales in Latvia by industries

(%)



 Municipal and commercial enterprises

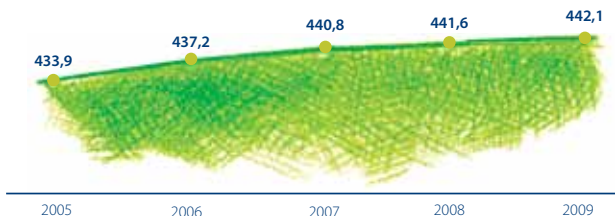
 Industry

 Power industry

 Residential customers

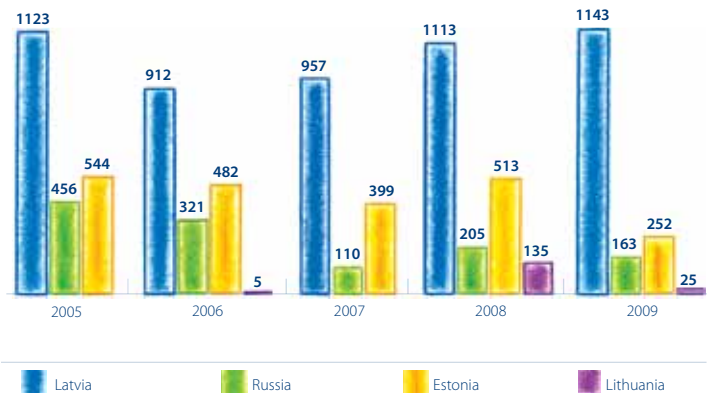
Number of customers

(thousands)



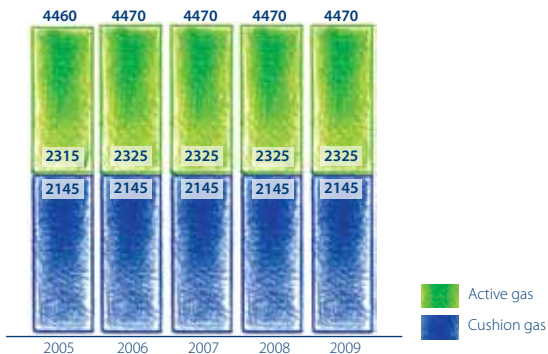
Natural gas deliveries from Inčukalns UGS

(million m³)



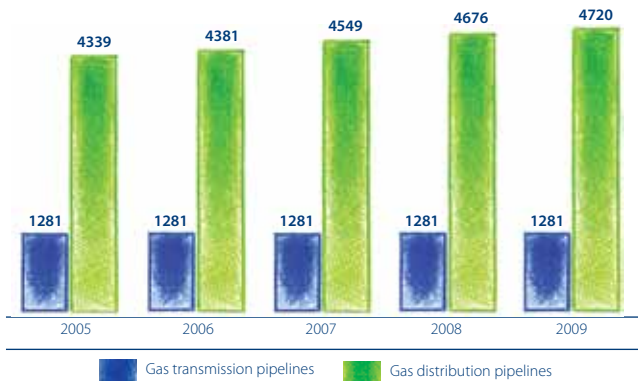
Gas volume in Inčukalns UGS

(million m³)



Company-owned gas transmission and distribution pipelines

(km)



Facts and Figures

