# AS TALLINNA VESI

*Consolidated Annual report*
*for the financial year ended*
*31 December 2013*
*(Translation of the Estonian original)*

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

| | |
|---|---|
| Beginning of the financial year | 1 January 2013 |
| End of the financial year | 31 December 2013 |
| Name of the Company | AS TALLINNA VESI |
| Legal form of the Company | Public limited company |
| Commercial register number | 10257326 |
| Address | Ädala St.10, Tallinn, Estonia |
| Chairman of the Board | Ian John Alexander Plenderleith |
| Telephone | + 372 6 262 200 |
| Fax | +372 6 262 300 |
| E-mail | tvesi@tvesi.ee |
| Web-page | www.tallinnavesi.ee |
| Field of activity | Production, treatment and distribution of water; storm and wastewater disposal and treatment |
| Auditors | AS PricewaterhouseCoopers |
| Documents attached to the Annual Report | Independent auditor's report |

## TABLE OF CONTENTS

# MANAGEMENT REPORT

## CHAIRMAN'S STATEMENT

In 2013, the challenge we set for ourselves was to continue to deliver improvements from the "best in Baltics" standards we were already achieving. I am very proud to state that in most areas we have managed to improve our performance levels still further. This is due to efforts of our people and teams who have once again delivered an excellent standard of service across the entire water and wastewater value chain.

***Operations performance – best ever water quality***

It is imperative that we meet or exceed the levels of services in the contract we signed with the City of Tallinn in 2001. This services contract requires us to maintain a high standard of service to our customers across a range of over 90 levels of service, ensuring that we deliver a service to our customers, that is second to none.

We are especially proud of our water quality compliance. In 2013 we achieved our best ever standards for water quality, with 99.7% of all samples being compliant with EU standards. To put this into context, during the year we took 2965 samples at the customers' tap, and of these only 9 did not meet the required standards.

This high quality product and service has been recognised by our customers. From the results of our 2013 customer satisfaction survey 75% of respondents said they regularly drank tap water, compared with only 48% in 2011. Thanks to the quality of our product and the quality of our communications, more and more of our customers trust the quality of the service we are providing.

***Excellent customer service – one of Europe's best performing utilities for service performance***

This year we achieved a customer satisfaction rating of 79, as measured by the TR*M index. Whilst this is down on last year's record high of 85 it is still significantly above the average for European Utilities and is very close to the top 10% for all European manufacturing companies. This is an excellent outcome and is a good reflection of the hard work we have done to improve all aspects of our service.

In addition to the improvements in the quality of our water and wastewater, we continue to reduce the customer risks related to potential flooding and pollution by making preventative improvements in the performance of our networks. For example in 2013 the number of sewer blockages decreased by 20% compared to the average of the last four years. The level of leakages is decreasing year-on-year due to our investments and preventative actions. In the water network, compared to the period prior to privatisation in 2001 we are saving approximately 13 000 $m^3$ of treated drinking water a day. Finally we have supplemented this improving operational performance with improved customer communications, in 2013 97% of all clients were informed prior to an interruption to supply.

***Our people and teams***

The key to any company's success are the people. Our teams have worked and "hard and smart" in order to deliver the highest levels of service to our customers. I would very much like to thank all of our people for their dedication and flexibility during the year.

A committed, capable and motivated workforce is central to delivering our objectives and we remain fully focused on maintaining high levels of employee development and engagement. We are always looking to develop our people and teams. In 2013 we commenced work a programme of activities to enable our managers to collaborate more effectively and develop themselves personally.

We strive to continuously improve our safety culture. The safety and well-being of our employees is paramount and we believe that everybody in AS Tallinna Vesi, both collectively and individually, has a part to play in maintaining a safe working environment. In 2013, our health and safety performance stood comparison with the performance of the best in class, and we will remain vigilant in our efforts to achieve the same very high standards in the future.

***Responsible company***

We acknowledge that by providing a service compliant with all requirements, we influence the quality of life of the citizens of Tallinn, neighboring municipalities as well as the wider environment in and around the Baltic Sea. This means that our management practices take into account the impact we have on our living environment, and our associations with different stakeholder interests. Our responsibility to all our stakeholder groups, including the environment is a key reason for our ongoing business improvement.

Not only do we aim to do the right things for our stakeholders, we also want to manage our business in the right way by operating to the highest standards of corporate governance. In 2013, we were awarded the Best Investor Relations of all the companies on the NASDAQ OMX Exchanges in all three Baltic Countries. This is the first time an Estonian company has won this award, which is a great honour for ourselves and Estonia. I would like to take this opportunity to thank the NASDAQ OMX in Tallinn and the bank analysts who have worked with us to help improve the quality of our interactions with the investment community.

***Still attractive for shareholders***

We believe our operational and financial performance still makes us an attractive investment for current and future shareholders. We will continue to work hard in our court dispute to ensure that the privatisation contract is respected. Beyond this we will continue to invest in our people and systems to ensure we are well placed to grow across the region if and when the opportunity arises.

For the 2013 financial year our total revenues increased slightly by 0,3% year on year to 53.1m Euros, mainly due to an increase in non-regulated revenues from our subsidiary business Watercom OÜ. However our EPS reduced by 12% year on year to 1.00 Euro per share primarily due to the finishing of the sewerage extension programme that caused a significant reduction in the profit from government grants.

In June 2013 we paid a dividend of 0.87 cents per share, an increase of 3,6% year on year. This is in accordance with our dividend policy, which is to increase dividends by a minimum of CPI each year. We are committed to delivering this dividend policy across the lifetime of the contract, while making further improvements for our customers and the environment.

***Outlook***

Given the lack of progress in our court cases, and the lack of transparent regulatory practice, the outlook for the company remains very uncertain. The Estonian authorities have been unwilling to enter into any meaningful discussions over the privatisation contracts, therefore it appears that the company will be engaged in a long court process that could last a number of years. This ongoing dispute and the unstable regulatory environment severely limit our growth opportunities .As such our primary focus in 2014 will be to improve performance and efficiency in our main services area in Tallinn. We are committed to retain our place as the leading water and wastewater company in the Baltic region, and we fully understand that we can only keep this position by not resting on past performance and achievements.

Finally, I would like to thank my colleagues in AS Tallinna Vesi and Watercom OÜ, and all our suppliers and business partners for all their expertise, energy and support in serving our customers during the past year. It is because of all your efforts that we are able to report a level of operating and service performance that is second to none. I look forward to our continuing success in the year ahead.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## RESULTS OF OPERATIONS – FOR THE YEAR 2013

### *Financial highlights of 2013*

In 2013 the Group continuously focused on the improvement of customer services.

The sales of the Group in 2013 have been flat compared to the same period in 2012, increasing 0.3% to 53.09 mln euros. The decreased sales from stormwater services within and outside the main service area by 20% to 3.6 mln euros was compensated with higher construction revenues, which increased by 226.5% to 1.1 mln euros.

The gross profit in 2013 decreased 6.2% or 2.01 mln euros mainly due to increased pollution tax expenses and increased expenses for repair and maintenance works in 2013. Increase in repair and maintenance works is related to different type of sites needed to be repaired but also mild winter allowed to do more works.

The operating profit from the Group's main business activity decreased by 7.4% to 24.75 mln euros during the twelve months of 2013 compared to the twelve months of 2012. As revenues have been relatively flat, increasing only 0.3% or 0.16 mln euros, then the main reason for a decline comes from the rise in pollution tax expenses (1.53 mln euros year on year), further influenced by the drop in government grant profits (2.04 mln euros year on year). Excluding the pollution tax one off negative impact of 1.13 mln euros in 2013 and positive impact of 0.47 mln euros in 2012, extra construction profit of 0.2 mln euros in 2013 and 0.1 mln euros in 2012 and government grant impact in the amount of 2.0 mln euros in 2012, the operating profit was 1.9% or 0.50 mln euros lower amounting to 25.68 mln euros compared to 26.19 mln euros in 2012.

### *Other main economic indicators*

| million euros | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|
| Sales | 53,1 | 52,9 | 51,2 | 49,7 | 49,4 |
| Gross profit | 30,6 | 32,6 | 30,3 | 29,0 | 31,2 |
| Operating profit | 24,8 | 28,8 | 28,9 | 27,5 | 29,5 |
| Operating profit - main business | 24,8 | 26,7 | 25,4 | 24,2 | 26,9 |
| Profit before taxes | 24,6 | 27,1 | 25,8 | 24,9 | 25,6 |
| Net profit | 19,9 | 22,6 | 21,5 | 16,4 | 21,7 |
| Gross profit margin % | 57,6 | 61,6 | 59,2 | 58,4 | 63,2 |
| Operating profit margin % | 46,6 | 54,4 | 56,4 | 55,3 | 59,8 |
| Profit before taxes margin % | 46,3 | 51,1 | 50,3 | 50,1 | 51,9 |
| Net profit margin % | 37,6 | 42,7 | 42,0 | 33,0 | 44,0 |
| ROA % | 9,8 | 11,3 | 11,2 | 8,9 | 12,3 |
| Debt to total capital employed | 57,0 | 57,8 | 58,9 | 60,1 | 49,7 |
| ROE% | 22,9 | 26,7 | 27,3 | 22,4 | 24,4 |
| Current ratio | 4,2 | 4,3 | 4,1 | 2,1 | 4,2 |
| Number of full-time equivalent employees | 292 | 301 | 299 | 305 | 322 |
| Share capital | 12,0 | 12,0 | 12,0 | 12,8 | 12,8 |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

*Gross profit margin – Gross profit / Net sales*
*Operating profit margin – Operating profit / Net sales*
*Profit before taxes margin – Profit before taxes / Net sales*
*Net profit margin – Net profit / Net sales*
*ROA – Net profit /Total assets*
*Debt to Total capital employed – Total liabilities / Total capital employed*
*ROE – Net profit / Shareholders' equity*
*Current ratio – Current assets / Current liabilities*

***Statement of comprehensive income***

*Sales*

As the company's tariffs are frozen at the 2010 tariff level, the changes in the revenues from main activities ie from sales of water and wastewater services is fully driven by consumption.

In 2013 the Group's total sales increased year on year by 0.3% to 53.09 mln euros. Lower sales from stormwater services within and outside the main service area by 20% to 3.6 mln euros was compensated with higher construction revenues, which increased by 226.5% to 1.1 mln euros.

Sales in the main operating activity principally comprise of sales of water and treatment of wastewater to domestic and commercial customers within and outside of the service area, and fees received from the City of Tallinn for operating and maintaining the storm water system. There is no considerable seasonality in the Group's operation.

Sales of water and wastewater services were 47.74 mln euros, a 0.4% decrease compared to 2012, resulting from the drop in sales volumes as described below.

Within the service area, sales to residential customers decreased by 0.6% to 23.64 mln euros, mainly influenced by the sales to apartment blocks. Sales to commercial customers increased by 1.5% to 19.05 mln euros. Sales to customers outside of the service area decreased by 4.8% to 4.31 mln euros compared to 2012. It was mostly affected by storm water as sales of water and wastewater increased slightly by 3.1% or 0.12 mln euros. Over pollution fees received were 0.73 mln euros, an 11.8% decrease compared to 2012.

| | Year ended 31.12. | | | Variance 13/12 | |
|---|---|---|---|---|---|
| **Revenues from main operating activities** | **2013** | **2012** | **2011** | **€** | **%** |
| Private clients, incl: | 23 642 | 23 789 | 23 711 | -147 | -0,6% |
| Water supply service | 13 022 | 13 096 | 13 072 | -74 | -0,6% |
| Wastewater disposal service | 10 620 | 10 693 | 10 639 | -73 | -0,7% |
| Corporate clients, incl: | 19 053 | 18 767 | 18 234 | 286 | 1,5% |
| Water supply service | 10 585 | 10 248 | 9 881 | 337 | 3,3% |
| Wastewater disposal service | 8 468 | 8 519 | 8 353 | -51 | -0,6% |
| Outside service area clients, incl: | 4 308 | 4 524 | 3 789 | -216 | -4,8% |
| Water supply service | 1 095 | 1 028 | 901 | 67 | 6,5% |
| Wastewater disposal service | 2 730 | 2 684 | 2 450 | 46 | 1,7% |
| Storm water disposal service | 483 | 812 | 438 | -329 | -40,5% |
| Over pollution fee | 734 | 832 | 758 | -98 | -11,8% |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

| | | | | | |
|---|---|---|---|---|---|
| Storm water treatment and disposal service | 3 137 | 3 713 | 3 351 | -576 | -15,5% |
| Fire hydrants service | 287 | 202 | 221 | 85 | 42,1% |
| Construction service and design | 1 146 | 351 | 447 | 795 | 226,5% |
| Other works and services | 780 | 746 | 729 | 34 | 4,6% |

Volumes sold to outside service area were 14.7% lower than in 2012. The main factor in this decrease was lower storm water volumes in 2013 compared to 2012, influenced by lower rainfall.

The sales from operation and maintenance of storm water and fire-hydrant system in the main service area decreased by 12.5% to 3.42 mln euros in 2013 compared to last year. According to the terms and conditions of the contract revenues reflect actual volumes treated and costs for treating the storm water, therefore this cost pass through has no impact on profits.

The sales of construction activities and design services have increased by 226.5% to 1.15 mln euros in 2013 compared to 2012, partly due to mild winter of 2013 allowing construction works.

*Cost of Goods Sold and Gross Margin*

The cost of goods sold for the main operating activity was 22.51 mln euros in 2013, an increase of 2.17 mln euros or 10.7% from the equivalent period in 2012. The cost increase is mainly the result of increased pollution tax expenses (1.53 mln euros), additional construction works services and extra emergency and repair works carried out in 2013.

| **Cost of goods sold** | **Year ended 31.12.** | | | **Variance 13/12** | |
|---|---|---|---|---|---|
| | **2013** | **2012** | **2011** | **€** | **%** |
| Water abstraction charges | -997 | -937 | -897 | -60 | 6,4% |
| Chemicals | -1 734 | -1 631 | -1 433 | -103 | 6,3% |
| Electricity | -3 392 | -3 695 | -2 972 | 303 | -8,2% |
| Pollution tax | -1 872 | -347 | -1 409 | -1 525 | 439,5% |
| **Total direct production costs** | **-7 995** | **-6 610** | **-6 711** | **-1 385** | **21,0%** |
| Staff costs | -4 833 | -4 750 | -4 390 | -83 | 1,7% |
| Depreciation and amortization | -5 115 | -5 167 | -5 182 | 52 | -1,0% |
| Construction service and design | -947 | -277 | -375 | -670 | 241,9% |
| Other costs of goods sold | -3 615 | -3 533 | -4 269 | -82 | 2,3% |
| **Other costs of goods sold total** | **-14 510** | **-13 727** | **-14 216** | **-783** | **5,7%** |
| **Total cost of goods sold** | **-22 505** | **-20 337** | **-20 927** | **-2 168** | **10,7%** |

Total direct production costs increased by 1.39 mln euros or 21.0%. Increased pollution tax expense, the reasons for which are explained below has the major impact on the increased direct production costs. Other changes came from a combination of increase in regulated prices and tax rates and movements in treatment volumes that affected the variable costs together with the following additional factors:

- Water abstraction charges increased only by 0.06 mln euros or 6.3% to 1.00 mln euros in 2013, driven mainly by 5% raise in tax rates and raw water volumes.

- Total chemical costs increased by 0.10 mln euros or 6.3% to 1.73 mln euros. Costs increase was mainly the result of an increase in chemicals price, which was balanced by decrease in volumes used due to less sewage treated.
- Electricity costs in total decreased by 0.30 mln euros or 8.2% in 2013 compared to 2012. Lower electricity costs are mostly derived from the decrease in treatment volumes and used unit costs, worth 0.34 mln euros. Positive effects are reduced slightly by increased electricity price worth 0.04 mln euros.
- Pollution tax increased by 1.53 mln euros or 439.5% in 2013. The pollution tax cost was largely impacted by the incident in the wastewater treatment plant in the beginning of the year. Also by the fact that the Group released a one-off provision related to storm water outlet in 2012 and in the 4th quarter of 2013 the Group was paid an insurance compensation worth 0.15 mln euros. Eliminating the aforementioned one-off effects the pollution tax would have decreased by 0.08 mln euros or 9.3%. The pollution tax increase due to the increase in pollutants concentration (worth 0.01 mln euros) and overall increase in tax rates by 15% (worth 0.09 mln euros) was balanced by the decrease in volumes (worth 0.18 mln euros).

Other cost of goods sold (staff costs, depreciation, construction services and other cost of goods sold) in the main operating activity increased by 0.78 mln euros or 5.7%. 0.67 mln euros or 85.8% of the increase in fixed costs is related to construction services and design, which relates to increased revenues from pipeline construction as mentioned above. The remaining increase is related to higher repair and maintenance carried out in 2013. Increase in repair and maintenance works is related to different type of sites needed to be repaired but also mild winter allowed to do more works

As a result of all of the above the Group's gross profit for 2013 was 30.58 mln euros, which is a decrease of 2.01 mln euros, or 6.2%, compared to the gross profit of 32.59 mln euros for the 2012. Excluding the pollution tax one off negative impact of 1.13 mln euros in 2013 and positive impact of 0.47 mln euros in 2012, extra construction profit of 0.2 mln euros in 2013 and 0.1 mln euros in underlying the gross profit was 1.7% or 0.50 mln euros lower amounting to 31.51 mln euros compared to 32.04 mln euros in 2012 .

*Other Operating Costs*

In 2012 the General administration expenses increased in total 0.32 mln euros or 6.8% year on year to 5.06 mln euros, mainly due to higher consultation and legal fees related to the ongoing tariff dispute.

*Other income/expenses*

Other net expense decreased to a net expense of 0.08 mln euros, compared to 1.70 mln euros net income in 2012. The decline in profit from government grants revenues was the main contributor to Other net income decrease in 2013. The sewage network extension program for which the government grant income was earned was finished at the end of 2012. As the payment terms are longer, the collection of the receivables for the program can be seen also in 2014 in the cash flow statement.

*Operating profit*

As a result of above factors the Group's operating profit from main services for 2013 totalled 24.75 mln euros compared to 26.73 mln euros in 2012, which shows a decrease of 1.98 mln euros or 7.4%.

Total operating profit for 2013 was 24.76 mln euros, a decrease of 4.01 mln euros. Year on year the operating profit for 2013 has decreased by 14.0%.

As already mentioned before the underlying operating profit from main services without the impact of increased pollution tax, construction profit and government grants for 2013 was 25.68 mln euros, a 0.50 mln euros or 1.9% decrease compared to 2012. Main reason for decrease comes from the increased consultancy and legal costs related to the tariff dispute.

***Financial expenses***

The Group's net financial expenses amounted to 0.20 mln euros in 2013, which is a positive change of 1.51 mln euros compared to 1.71 mln euros financial expenses in 2012.

Main influence being increase in non-monetary impact of the change in the fair value of the swap contracts the Group has entered. The positive non-monetary impact in 2013 expenses is 2.34 mln euros compared to 2012. Other contributor to financial expenses was decreased interest income by 0.91 mln euros or 57.2% caused by the decrease in the interest bearing receivables.

The standalone swap agreements have been signed to mitigate the majority of the long term floating interest risk. The interest swap agreements are signed for 90 mln euros, with one 15 mln euros contract becoming effective in November, what means 20 mln euros are still with floating interest rate. At the end of the year the estimated fair value of the swap contracts is negative, totalling 2.32 mln euros.

Effective interest rate (incl. swap interests) of Group's loans in 2013 was 3.23%, amounting in the interest costs of 3.11 mln euros, compared to the effective interest rate of 3.32% and the interest costs of 3.21 mln euros in 2012.

***Profit Before and After Tax***

The Group's profit before taxes for 2013 was 24.56 mln euros, which is 2.50 mln euros lower than the profit before taxes of 27.07 mln euros for 2012, resulting mainly from the decreased government grant revenues and increased professional services fees as described above.

The Group's profit after taxes for the 2013 was 19.94 mln euros, which is 2.66 mln euros lower than the profit after taxes of 22.60 mln euros for 2012.

***Statement of financial position***

In the twelve months of 2013 the Group invested 8.65 mln euros into fixed assets. As of 31 December 2013 non-current fixed assets amounted to 152.25 mln euros and total non-current assets amounted to 155.50 mln euros. (2012: 149.40 mln euros and 158.11 mln euros respectively).

The reduction in long-term receivables compared to year end by 5.35 mln euros to 2.21 mln euros is mainly related to the repayment of AS Maardu Vesi's loan to the Group in May in the amount of 3.81 mln euros.

The increase of current assets in the amount if 4.61 mln euros is mainly related to collection of receivables and repayment of AS Maardu Vesi long-term loan.

Current liabilities have increased by 1.32 mln euros to 11.21 mln euros in the twelve months. The increase is related to the fact that in November 2014, there is scheduled the first repayment of the loan in the amount of 2 mln euros. Other movements are related to decreased payments to suppliers in the amount of 0.72 mln euros and change in derivatives by 0.22 mln euros, balanced by the increase in Customer prepayments in the amount of 0.24 mln euros.

The Group has a Total debt/Total assets level as expected of 57.0%, in the agreed range of 55%-65%, reflecting the year end equity profile. This level is consistent with the same period in 2012 when the total debt/total assets ratio was 57.8%.

The Group's loan balance has remained stable at 95 mln euros, of which long term loan amounts to 93 mln euros and short term 2 million euros. The weighted average interest margin for the total loan facility is 0.96%.

Biggest share of the rest of the long term liabilities is deferred income from connection fees amounting to 10.14 mln euros (2012: 7.89 mln euros).

In the 4$^{th}$ quarter of 2011 the Group recorded and noted an exceptional contingent liability, which could cause an outflow of economic benefits of up to 36.0 mln euros. In the 3$^{rd}$ quarter of 2013 the Group re-evaluated the liability, which now stands at 34.0 mln euros, as per note 3 to the accounts.

***Cash flow***

As of 31 December 2013 the cash position of the Group is strong. The cash flows of the Group has continued to be rather stable, during twelve months of 2013 cash balance has increased by 7.85 mln euros (2012: 9.16 mln euros). At the end of 2013 the cash balance of the Group stood at 31.8 mln euros, which is 15.7% of the total assets (2012: 23.9 mln, which is 11.9% of the total assets).

The biggest contributor to the cash flows is the main operations. During the twelve months of 2013, the Group generated 29.78 mln euros of cash flows from operating activities, a decrease of 1.92 mln euros compared to the corresponding period in 2012.

2013 operating cash flows were below 2012 cash flows mainly due to lower operating profit as underlying operating profit continues to be the main contributor to operating cash flows.

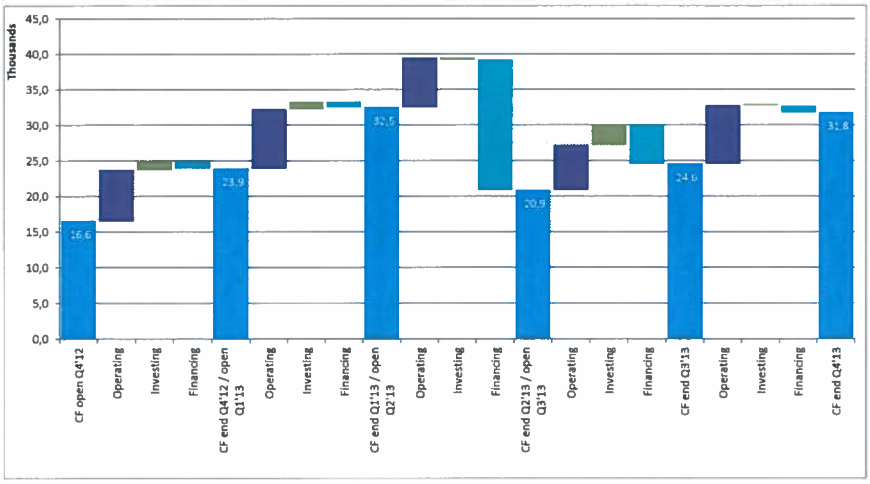
The Group's cash flows from investing activities have been positive for past two years. In the twelve months of 2013 net cash flows from investing activities resulted in a cash inflow of 3.37 mln euros, an increase of 1.33 mln euros compared to an inflow of 2.05 mln euros in the twelve months of 2012. This is made up as follows:

In 2013 AS Maardu Vesi repaid their loan in full in the amount of 3.81 mln euros. In 2013 the Group did not grant any additional loans (in 2012: 0.77 mln euros was granted to AS Maardu Vesi).

In the twelve months of 2013 the investments in fixed assets had decreased 0.82 mln euros compared to 2012 amounting to 9.19 mln euros.

The compensations received for the construction of pipelines were 7.89 mln euros in the twelve months of 2013, a decrease of 3.31 mln euros compared to same period in 2012.

In the twelve months of 2013, cash outflow from financing amounted to 25.32 mln euros, which is 0.72 mln euros more than in the same period of 2012, almost entirely due to higher dividends.




### *Employees*

At the end of 2013, the total number of employees was 304 compared to 313 at the end of 2012. The full time equivalent (FTE) was respectively 292 in 2013 compared to the 301 in 2012. The management continues to work actively for the efficiencies in processes to balance the increase in individual salaries and cost pressure from the market with more productive company structure.

The total salary cost was 6.98 mln euros, including 0.33 mln euros paid to the Management and Supervisory Council members. The off balance sheet potential salary liability would be up to 0.09 mln euros if the Council would want to replace the Management Board members.

### *Dividends*

Dividend allocation to the shareholders is recorded as the liability in the financial statement of the Company at the time when the profit allocation and dividend payment is confirmed by the annual general meeting of shareholders.

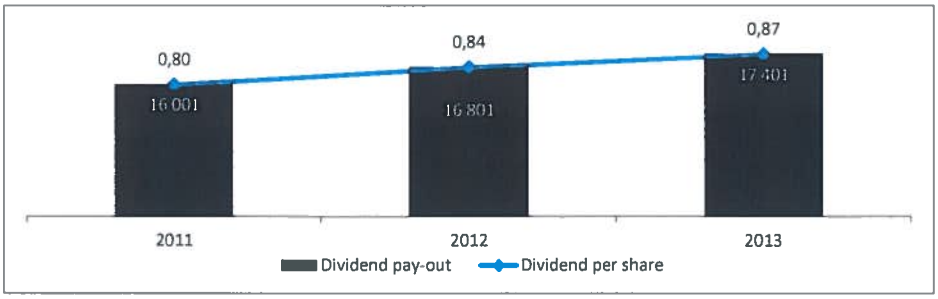
According to the dividend policy, which is also published on Company's website, the Company will maintain dividends to shareholders at the same amount in real terms, i.e. dividends will increase in line with inflation each year.

On the annual general meeting of shareholders held on 21st May 2013, 87 cents dividends per share and the total dividend pay-out from the profit of 2012 net income in the amount of 17.4 mln euros was approved. It is in accordance with the Company's dividend policy. Compared to 2012 dividends of 84 cents per share, the increase is equal to the inflation.

Dividends were paid out on 13th and 14th of June 2013.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

Dividend pay-outs in last three years have been as follows:




### *Share performance*

AS Tallinna Vesi is listed on OMX Main Baltic Market with trading code TVEAT and ISIN EE3100026436.

As of 31 December 2013, the shareholders of AS Tallinna Vesi, with a direct holding over 5%, were:

| | |
|---|---|
| United Utilities (Tallinn) BV | 35.3% |
| City of Tallinn | 34.7% |

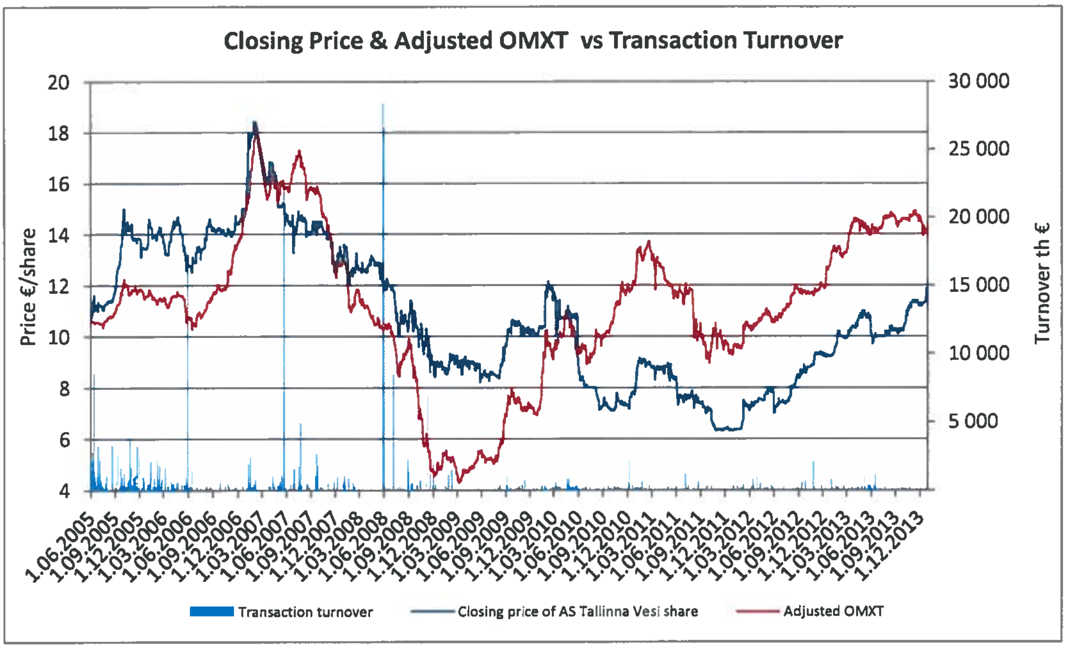
Pension funds have continued to increase their portfolios during 2013, owning 2.56% of the total shares compared to 1.57% at the end of 1st quarter 2012.

As of 31 December 2013, the closing price of the AS Tallinna Vesi share was 11.90 euros, which is a 29.3% increase (in 2012: 46.3%) compared to the closing price of 9.20 euros at the beginning of the year. During the same period the OMX Tallinn index increased by 11.4% (2012: 38.2%).

In 2013 5 469 deals with the Company's shares were concluded (2012: 4 427 deals) during which 1 853 thousand shares or 9.3% exchanged their owners (2012: 2 376 thousand shares or 11.9%).

The turnover of the transactions was 552 thousand euros higher than in 2012 amounting to 19 139 thousand euros. The share price has shown an increase despite of the on-going contractual debate.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)




### *Corporate structure*

At the end of the year, as of 31 December 2013, the Group consisted of 2 companies. The subsidiary Watercom OÜ is wholly owned by AS Tallinna Vesi and consolidated to the results of the Company.

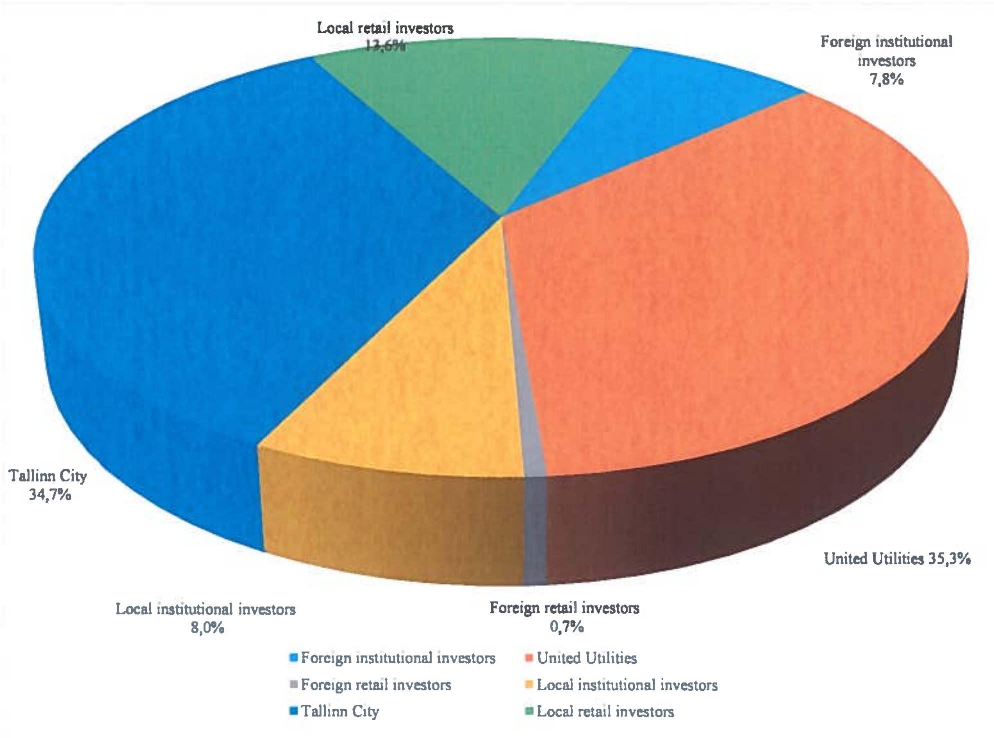
### *Share price statistics*

| euros | 2013 | 2012 | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|
| Share price, open | 9,25 | 6,30 | 7,90 | 10,18 | 9,00 |
| Share price, at the end of the year | 11,90 | 9,20 | 6,29 | 7,89 | 10,00 |
| Share price, low | 9,20 | 6,30 | 6,29 | 7,00 | 8,20 |
| Share price, high | 12,00 | 9,40 | 9,29 | 12,25 | 10,69 |
| Share price, average | 10,42 | 7,91 | 7,76 | 8,95 | 9,28 |
| Traded volume | 1 852 865 | 2 375 967 | 1 927 386 | 2 879 132 | 1 547 108 |
| Turnover, million | 19,1 | 18,6 | 14,9 | 25,6 | 14,5 |
| Capitalisation, million | 238,0 | 184,0 | 125,8 | 157,8 | 200,0 |
| Earnings per share | 1,00 | 1,13 | 1,08 | 0,82 | 1,09 |
| Dividend per share | n/a | 0,87 | 0,84 | 0,80 | 1,60 |
| Dividend / net profit | n/a | 77% | 78% | 98% | 147% |
| P/E | 11,90 | 8,14 | 5,82 | 9,62 | 9,20 |
| P/BV | 2,7 | 2,2 | 1,6 | 2,2 | 2,2 |

*P/E = share price at the end of the year / earnings per share*
*P/BV = share price at the end of the year / book value per share*
*In 2005 the listing price was 9.25 euros*

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

*Shareholders by type as of 31.12.2013*




*Distribution of share capital by size of share ownership as of 31.12.2013*

| | Shareholders | Shareholders % | No. of shares | % of share capital |
|---|---|---|---|---|
| 1 - 100 | 858 | 25,8% | 45 712 | 0,2% |
| 101 - 200 | 583 | 17,5% | 90 177 | 0,5% |
| 201 - 300 | 366 | 11,0% | 95 441 | 0,5% |
| 301 - 500 | 424 | 12,7% | 179 609 | 0,9% |
| 501 - 1 000 | 441 | 13,2% | 336 971 | 1,7% |
| 1 001 - 5 000 | 492 | 14,8% | 1 091 322 | 5,5% |
| 5 001 - 10 000 | 79 | 2,4% | 568 174 | 2,8% |
| 10 001 - 50 000 | 65 | 2,0% | 1 274 947 | 6,4% |
| 50 000 + | 23 | 0,7% | 16 317 647 | 81,6% |
| **TOTAL** | **3 331** | **100,0%** | **20 000 000** | **100,0%** |

***Future actions & risks***

Complaint to European Commission

In parallel, on 10th December 2010 AS Tallinna Vesi lodged a complaint to the European Commission regarding certain measures adopted by the Estonian authorities. The company believes these measures unilaterally alter the terms of AS Tallinna Vesi's privatization regime, and without any objective justification, any form of meaningful prior discussion, or willingness to engage in dialogue. Therefore they violate EU rules on the freedom of establishment and the free movement of capital (articles 49 and 63 TFEU). The process is on-going.

Disclosure of relevant papers and perspectives

The Company has published its tariff application and all relevant correspondence with the CA on its website (http://www.tallinnavesi.ee) and to the Tallinn Stock Exchange and will keep its investors informed of all future developments regarding the further key developments regarding the processing of the tariff application.

In opposite to the Company the CA has requested the Court procedures to be closed. Based on misleading information submitted by the CA the Court approved the CA's request. ASTV has reapplied for open proceedings.

Still, at this point in time the Company is unable to say what is going to happen to the tariffs before Court judgments and what would be the next steps by the European Commission. The outcome and lengths of the Court proceedings is outside the control of the Company.

## CORPORATE GOVERNANCE AND CORPORATE GOVERNANCE RECOMMENDATIONS REPORT

Corporate governance constitutes a system of principles for the management of a company. Generally those principles are regulated by law, the Articles of Association and the internal rules of a company. Since 1st January 2006, the companies listed on the Tallinn Stock Exchange are recommended to follow the "Corporate Governance Recommendations" issued by the Financial Supervision Authority. Throughout 2013 the management of AS Tallinna Vesi has followed those regulations and principles.

AS Tallinna Vesi is committed to high standards of corporate governance for which the Management Board and Supervisory Board are accountable to the shareholders. AS Tallinna Vesi endeavours to be transparent in its ways of operating, corporate disclosures and relations with its shareholders. AS Tallinna Vesi has been recognized several times for this – in 2009, the NASDAQ OMX Baltic awarded AS Tallinna Vesi for the Best Annual Report in NASDAQ OMX Baltic and for the Best Investor Relations in NASDAQ OMX Tallinn. In 2010 the NASDAQ OMX Baltic awarded AS Tallinna Vesi for the Best Investor Relations in NASDAQ OMX Tallinn and the Baltic Corporate Governance Institute awarded AS Tallinna Vesi for the Best Corporate Governance in Estonia. In 2011 the Company was awarded the Best Investor relations on the Tallinn Stock Exchange and second place on all the Baltic Stock Exchanges by NASDAQ OMX. In addition the Company's investors' webpage was highlighted amongst the equal top five and the Annual Accounts were awarded the second place on all the Baltic Stock Exchanges in 2012. In 2013, NASDAQ OMX Tallinn AS awarded AS Tallinna Vesi with the second place for Best Investor Relations in the Baltics. Furthermore, the Company was awarded with the second place for its investors' webpage and Annual Report on all the Baltic Stock Exchanges.

### *Investor Relations and Disclosure of Information*

At the end of the calendar year, AS Tallinna Vesi discloses the next year's financial calendar, including the disclosure dates of the quarterly and annual financial information and the date of the Annual General Meeting (AGM) of the Shareholders via the Tallinn Stock Exchange homepage. All information disclosed via the Tallinn Stock Exchange is also subsequently disclosed on AS Tallinna Vesi's homepage.
In addition, AS Tallinna Vesi discloses the following information on its website before AGM is held:

- AGM notice,
- background information about the agenda, including annual report subject to approval and the Supervisory Board's report and auditor's report;
- information about the Supervisory Board member to be elected and auditor candidate;
- the total number of voting rights and number of voting rights by share type;
- procedure for adding items to the agenda and presenting draft resolutions;
- procedure for inquiring about ASTV's activities from the Management Board, and
- list of identification documents required for attending the general meeting, including the form of the power of attorney.

Resolutions of the General Meetings are published on AS Tallinna Vesi's homepage after seven days have passed from the date of the General Meeting.

After the General Meeting, the following is disclosed on the company's homepage: resolutions of the general meeting, Management Board presentation, as well as the minutes of the General Meeting, which contain questions and answers regarding the topics discussed at the AGM.

AS Tallinna Vesi has a regular dialogue with its major shareholders and potential investors. Presentation materials are disclosed on AS Tallinna Vesi's homepage. To keep AS Tallinna Vesi's shareholders informed, General Meetings of Shareholders are held at least annually to provide the shareholders with the opportunity to ask questions from the Management Board and the Supervisory Board.

Starting from the end of Q3 2013, AS Tallinna Vesi is organising an interactive webinar through Tallinn Stock Exchange for presenting the Company's financial results. All interested parties can take part of webinar, it is an internet-based environment. All webinar recordings are disclosed on Tallinn Stock Exchange webpage. Previously, AS Tallinna Vesi used to hold a conference call at the end of each quarter, where the Company's financial results were presented.

***The General Meeting of Shareholders***

AS Tallinna Vesi is a public limited company, the management bodies of which are the General Meeting of Shareholders, the Supervisory Board and the Management Board. The General Meeting of Shareholders is AS Tallinna Vesi's highest directing body.

In accordance with the Commercial Code and the Corporate Governance Recommendations, AS Tallinna Vesi convenes its General Meetings, both Annual General Meetings and Extraordinary General Meetings (EGMs) by notifying all of its shareholders via the Tallinn Stock Exchange system and by placing an advertisement in one newspaper with Estonian-wide circulation 3 weeks in advance. Changes in the Articles of Association and management of AS Tallinna Vesi and its subsidiary (incl. the election and recalling of the members of the Management Board) are made according to Part VII of the Commercial Code.

The agendas of AGMs and EGMs of AS Tallinna Vesi are pre-approved by the Supervisory Board, who also puts forward proposals for the attention and voting at the General Meeting. The General Meeting agenda items, the Supervisory Board's proposals, with relevant commentaries about the agenda items, procedural instructions for participating at a General Meeting and how and when to propose additional items to the agenda are disclosed within the General Meeting notice.

Specific rights for adding agenda items granted to shareholders whose shareholding represents at least 1/20 of the share capital are explained in the General Meeting notice as well as on AS Tallinna Vesi's homepage. Voting rights are explained to the shareholders on AS Tallinna Vesi's homepage as well as at the beginning of each General Meeting.

On 21 May 2013, AS Tallinna Vesi held an Annual General Meeting (AGM) of its Shareholders to approve the 2012 annual report and distribution of profit, recall the Supervisory Board member and elect the Supervisory Board member, as well as to elect the auditor. The Management Board also made a presentation on the privatisation contract dispute to update the shareholders.

No questions were asked regarding the 2013 AGM agenda. Neither were any additional agenda item proposals made in 2013.

The chairman of any AGM and EGM is an independent person. In 2013, the AGM was chaired by Mr. Raino Paron, who introduced the procedure for conducting the General Meeting, including the procedure for inquiring about the company's activities from the Management Board.

All members of the Management Board, the Chairman of the Supervisory Board and the auditor in charge participated at the AGM in 2013. When a Supervisory Board member or auditor in charge stands for election at the general meeting, the candidate for the respective position usually also participates in the meeting. Therefore, the Supervisory Board member candidate Mr Allar Jõks and candidate for the position of auditor in charge Mr Ago Vilu also participated at the 2013 AGM, among others. The Company does not disclose the amount of the audit fee because its non-disclosure does not affect the reliability of the audit services provided by the auditor.

AS Tallinna Vesi does not enable the shareholders to participate at the General Meetings via electronic communication tools, as it would be too complicated and expensive to establish reliable solutions to identify the shareholders most of whom are overseas' residents.

No shareholder has shares that grant them a right for specific control. AS Tallinna Vesi is not aware that any shareholders have concluded any voting agreements.

As per the Articles of Association of AS Tallinna Vesi amended on 24 May 2011, the Company has issued one registered preferred share with the nominal value of 60 euros (B-share). The B-share grants the holder the right to participate at General Meetings as well as in the distribution of profits and of the assets remaining upon dissolution of the Company, also other rights provided by law and the Articles of Association of the Company. The B-share grants the holder the preferential right to receive a dividend in an agreed sum of 600 euros. The B-share grants the shareholder 1 (one) vote at the General Meeting (restricted right to vote) when deciding on amending the Articles of Association of the company; increasing and reducing the share capital of the company; issuing convertible bonds; acquisition of treasury shares by the company; deciding on the merger, division, transformation and/or dissolution of the company and deciding on issues related to the activities of the company that have not been placed in the sole.

***The Supervisory Board***

The Supervisory Board plans the activities of AS Tallinna Vesi, organises its management and supervises the activities of the Management Board. Pursuant to the Articles of Association of AS Tallinna Vesi, the Supervisory Board consists of nine members with the term of two years. In 2013, five regular and no extraordinary Supervisory Board meetings were held. The Supervisory Board pre-approved the 2012 annual report presented to the Annual General Meeting for approval, and reviewed AS Tallinna Vesi's 2014 budget.

At the time of compilation of this report, AS Tallinna Vesi's Supervisory Board consisted of the following members:

- Mr Robert John Gallienne (United Utilities (Tallinn) B.V.), Supervisory Board member until 22 May 2014;
- Mr Steven Richard Fraser (United Utilities (Tallinn) B.V.), Supervisory Board member until 21 January 2016;
- Mr Simon Gardiner (United Utilities (Tallinn) B.V.), Supervisory Board member until 22 May 2014;
- Mr Brendan Francis Murphy (United Utilities (Tallinn) B.V.), Supervisory Board member until 27 October 2015;

- Mr Priit Lello (Tallinn City), Supervisory Board member until 16 November 2015;
- Mr Rein Ratas (Tallinn City), Supervisory Board member until 22 May 2014;
- Mr Toivo Tootsen (Tallinn City), Supervisory Board member until 7 April 2015;
- Mr Mart Mägi (independent) Supervisory Board member until 22 May 2014;
- Mr Allar Jõks (independent) Supervisory Board member until 21 May 2015.

AS Tallinna Vesi has not made any transactions with the members of the Supervisory Board nor their related parties.

The Supervisory Board has formed three committees to advise the Supervisory Board on audit, nomination and remuneration, and corporate governance matters as described below.

***The Audit Committee and Internal Audit***

At each meeting, an internal audit report was presented to the Supervisory Board. The internal auditor of AS Tallinna Vesi reports directly to the Audit Committee, which consists of two members of the Supervisory Board. Mr Mart Mägi is the Chairman of the Audit Committee and Mr Robert John Gallienne is the second member of the Audit Committee. The Audit Committee follows the Authorised Public Accountants Act and the guidelines issued by the Financial Supervision Authority regarding the composition and working processes of an Audit Committee.

The main tasks of the Audit Committee are:

- to monitor and analyse financial information;
- to monitor and analyse the effectiveness of risk management and internal controls;
- to monitor and analyse the audit processes regarding the consolidated annual accounts;
- to monitor and analyse independence of external auditor and legality of his/her activity regarding ASTV;
- to evaluate the work of external auditors annually and report to the Supervisory Board about the results of such evaluation.
- to monitor independence of external auditor

The appointed external auditor and any member of the external audit team cannot provide any service outside the scope of annual audits without prior approval from the Audit Committee. In 2013, the external auditor did not provide any services to AS Tallinna Vesi outside the scope of the annual audit.

Pursuant to the Articles of Association of AS Tallinna Vesi, an external auditor shall be elected by the General Meeting of Shareholders to conduct the annual audit. The remuneration of the external auditor is regulated in the respective contract, signed between the external auditor and the Management Board. AS Tallinna Vesi chooses an external auditor by following internal procurement procedures (which includes approval by the Supervisory Board of AS Tallinna Vesi), ensuring the best match of service quality and the price offered for the services. Proposals are taken only from internationally respected, high quality audit companies. AS Tallinna Vesi signs up to 3-year audit contract with a clause that requires the re-appointment of the auditor in charge each year and follows the Financial Supervision Authority guidelines of 1 November 2013 "Rotation of the auditors of certain subjects of financial supervision by the state" with regard to the requirement to rotate the auditor in charge after every 5 years. Based on the report of the Audit Committee, the Supervisory Board evaluates the quality of the work of the external auditor annually in the course of the approval of the Annual Accounts and discloses the summary of such evaluation in the AGM notice. The external auditor is present at the AGM and participates where necessary.

***Nomination and Remuneration Committee***

In 2013, the Nomination and Remuneration Committee continued to advise the Supervisory Board on management remuneration issues and Management Board nominations. Until 21 May 2013, Mr. Valdur Laid was the Chairman of the Nomination and Remuneration Committee; since 22 August 2013, the Chairman of the Nomination and Remuneration Committee is Mr Robert John Gallienne. The other member of the Committee is Mr Mart Mägi.

Supervisory Board approves the remuneration principles of the issuer's managers and appoints the Remuneration Committee. The Remuneration Committee recommends the remuneration principles of the Company and exercises supervision that the principles approved by the Supervisory Board and the requirements of the Securities Market Act are being followed.

The Nomination and Remuneration Committee ensures that the proposed remuneration principles are based on the short- and long-term objectives of the Company, taking into account the financial performance of the company and legitimate interests of investors. The Nomination and Remuneration Committee ensures also that the proportion of remuneration for the principal job and performance related pay (PRP) are in accordance with the duties of the Management Board Member and that the remuneration for principal job forms a sufficient part of the total remuneration. The PRP depends on annual performance and can be adjusted upwards or downwards. If the annual results are worse than expected it can be decided that no PRP is paid.

***Corporate Governance Committee***

The Corporate Governance Committee has been formed to improve corporate governance of AS Tallinna Vesi for the benefit of its Supervisory Board and shareholders. Mr. Robert John Gallienne was the Chairman of the Corporate Governance Committee until 23 October 2013 and Mr Valdur Laid (until 21 May 2013) and Mr Ian John Alexander Plenderleith were other members of the Corporate Governance Committee. Since 23 October 2013, the Chairman of the Corporate Governance Committee is Mr Allar Jõks and other members of the Committee are Mr Robert John Gallienne and Mr Ian John Alexander Plenderleith.

***The Management Board***

The Management Board is a management body that represents and manages the day-to-day activities of AS Tallinna Vesi in accordance with the law and the Articles of Association of the company. The Management Board is obliged to act in the most economically efficient manner. The Management Board can be composed of two to five members according to the Articles of Association. The Management Board always prepares management reports for Supervisory Board meetings and such reports are disseminated to the Supervisory Board members 1 (one) week in advance of the meeting, as required by the Commercial Code. The Management Board also reports *ad hoc* to the Supervisory Board ex-meetings, when it is considered necessary as and when requested by the Chairman of the Supervisory Board.

Both the Management Board and Supervisory Board members are deemed to be insiders who are aware of AS Tallinna Vesi's insider rules and together with their related persons are listed in AS Tallinna Vesi's insider list. Until 31 May 2013 the Management Board consisted of five members;

starting from 1 June 2013 onwards the number of members has been four. The responsibilities of all Management Board members are specified below. All Management Board members are appointed by the Supervisory Board of AS Tallinna Vesi. At the time of compilation of this report, since 1 February 2014, the number of the Management Board members has been three. The members are as follows:

- Mr Ian John Alexander Plenderleith, with the powers of the Management Board member until 1 October 2014;
- Ms Riina Käi, with the powers of the Management Board member until 29 October 2015;
- Mr Aleksandr Timofejev, with the powers of the Management Board member until 29 October 2015.

The duties of the Chairman of the Management Board, Mr. Ian John Alexander Plenderleith were, amongst others, to fulfil the everyday obligations of the Chief Executive Officer (CEO) of AS Tallinna Vesi by leading and representing the Company, ensuring the compliance with contracts and the law, organizing the activities of the Management Board, coordinating preparation the strategies and ensuring their implementation.

Until his leaving on 31 May 2013, the duties of the member of the Management Board, Mr. Leho Võrk, were, amongst others, to fulfil the obligations of the Customer Operations Director of AS Tallinna Vesi, including management of water and sewerage networks' everyday operation. He was also responsible for customer services and relations as well as relations established with external partners.

The duties of the member of the Management Board, Mr. Aleksandr Timofejev, are, amongst others, to fulfil the everyday obligations of the Asset Operations Director of AS Tallinna Vesi by managing and being responsible for the operations of treatment facilities and planning and delivery of long-term investments.. Since 1 June 2013, management of AS Tallinna Vesi's water and sewerage networks' everyday operation is one of the duties of the Management Board member Mr Aleksandr Timofejev.

The duties of the member of the Management Board, Ms. Riina Käi, are, amongst others, to fulfil the everyday obligations of the Chief Financial Officer (CFO) of AS Tallinna Vesi by managing and being responsible for the accounting and financial activities of AS Tallinna Vesi.

Until her leaving on 31 January 2014, the duties of the member of the Management Board, Ms. Ilona Nurmela were, amongst others, to fulfil the role of AS Tallinna Vesi's General Counsel and act as the head of legal and compliance.

AS Tallinna Vesi has signed service contracts with all members of the Management Board. AS Tallinna Vesi has not made any transactions with the members of the Management Board nor their related parties.

According to the Articles of Association of AS Tallinna Vesi, the Chairman of the Management Board has the sole representation right of the company; other Management Board members can represent the company only jointly. In order to make daily decisions, the Management Board has approved a framework of principles, according to which certain management team members are authorized to conclude transactions in small amounts.

The Management Board of AS Tallinna Vesi also acts on behalf of AS Tallinna Vesi as the sole shareholder of OÜ Watercom.

***Conformity with Tallinn Stock Exchange Corporate Governance Recommendations***

Starting from 1st January 2006, the companies whose shares have been admitted for trading on the regulated market operating in Estonia shall describe, in accordance with the 'Comply or Explain' principle, their management practices in a Corporate Governance report and confirm their compliance or non-compliance with the Corporate Governance Recommendations. If the issuer does not comply with the Corporate Governance Recommendations, it shall explain the reasons for its non-compliance in the report.

***Declaration of Conformity by AS Tallinna Vesi***

In 2013, AS Tallinna Vesi has complied with the vast majority of the Corporate Governance Recommendations. However, AS Tallinna Vesi did not comply with certain recommendations, which are listed below together with the reasons for such non-compliance:

*'2.2.3. The basis for Management Board remuneration shall be clear and transparent. The Supervisory Board shall discuss and review regularly the basis for Management Board remuneration. Upon determination of the Management Board remuneration, the Supervisory Board shall be guided by evaluation of the work of the Management Board members. Upon evaluation of the work the Management Board members, the Supervisory Board shall above all take into consideration the duties of each member of the Management Board, their activities, the activities of the entire Management Board, the economic condition of the Issuer, the actual state and future prediction and direction of the business in comparison with the same indicators of companies in the same economic sector. '*

The arrangements undertaken in connection with the privatisation of AS Tallinna Vesi in 2001 provided that, in return for certain fees, United Utilities International Ltd. would provide AS Tallinna Vesi with technical and asset management services and make its personnel available to the company in connection with its operation and management. The working hours, rates of compensation, and all other matters relating to the employment of the individual directly employed by United Utilities International Ltd. are to be determined solely by United Utilities International Ltd., the Supervisory Board does not review the principles of remuneration of this Management Board member.

*'2.2.7. Basic wages, performance pay, severance packages, other payable benefits and bonus schemes of a Management Board member as well as their essential features (incl. features based on comparison, incentives and risk) shall be published in clear and unambiguous form on website of the Issuer and in the Corporate Governance Recommendations Report. Information published shall be deemed clear and unambiguous if it directly expresses the amount of expense to the Issuer or the amount of foreseeable expense as of the day of disclosure.*

AS Tallinna Vesi does disclose the overall Management Board remuneration in the report, appendix 25, but considers that individual remuneration is sensitive and private information and additional disclosure would bring no benefit to the shareholders.

*'3.2.2. At least half of the members of the Supervisory Board of the Issuer shall be independent. If the Supervisory Board has an odd number of members, then there may be one independent member less than the number of dependent members.'*

Pursuant to the Articles of Association of AS Tallinna Vesi, the Supervisory Board consists of nine members. Under the Shareholders` Agreement, United Utilities (Tallinn) B.V. (hereinafter UUTBV) and the City of Tallinn have agreed that the division of seats in the Supervisory Board shall be such that UUTBV shall have four seats, the City of Tallinn shall have three seats and two seats shall be reserved for independent members to be elected to the Supervisory Board as permitted by the Tallinn Stock Exchange on listing in June 2005.

***Information Disclosure***

*'2.2.2. The member of the Management Board shall not be at the same time a member of more than two management boards of an Issuer and shall not be the Chairman of the Supervisory Board of another Issuer. A member of the Management Board can be the Chairman of the Supervisory Board in company belonging to same group as the Issuer.'*

The Management Board Members of AS Tallinna Vesi are not in the Management Boards and Supervisory Boards of other Issuers.

*2.3.2. The Supervisory Board shall approve the transactions which are significant to the Issuer and concluded between the Issuer and a member of its Management Board or another person connected/close to them and shall determine the terms of such transactions.*

The Supervisory Board approves the remuneration principles of the Management Board. In 2013, there were no other transactions between AS Tallinna Vesi and either any member of the Management Board or any persons or companies related to them.

*3.2.5. The amount of remuneration of a member of the Supervisory Board shall be published in the Corporate Governance Recommendations Report, indicating separately basic and additional payment (incl. compensation for termination of contract and other payable benefits).*

According to the decision of the General Meeting the remuneration of Supervisory Board members is set at 6 391 euros per year per person. The fee is paid to six members out of nine. The fee is subject to deduction and payment of applicable taxes and is payable monthly. The Supervisory Board members were not paid any additional benefits in 2013.

*3.2.6. If a member of the Supervisory Board has attended less than half of the meeting of the Supervisory Board, this shall be indicated separately in the Corporate Governance Recommendations Report.*

In 2013, five Supervisory Board meetings were held (24 January 2013, 21 March 2013, 25 April 2013, 1 August 2013 and 23 October 2013).

The following members of the Supervisory Board attended more than 50% of the meetings during the time they were appointed or elected in 2013: Mr. Robert John Gallienne, Mr. Steven Richard Fraser, Mr. Simon Gardiner, Mr. Brendan Francis Murphy, Mr. Rein Ratas, Mr. Toivo Tootsen, Mr. Priit Lello and Mr. Mart Mägi.

*3.3.2. A Supervisory Board member candidate shall inform other members of the Supervisory Board about the existence of conflict of interests before their election and immediately upon arising of it later. Members of the Supervisory Board shall promptly inform the Chairman of the Supervisory Board and Management Board regarding any business offer related to the business activity of the Issuer made to him, a person close to him or a person connected with him.*

All Supervisory Board members are aware of this requirement and at minimum once per annum AS Tallinna Vesi requires all Supervisory Board members to update the record of their business interests. No business transactions took place between AS Tallinna Vesi and either any Supervisory Board member or any persons or companies related to them in 2013.

Management Report which consists of Chairman's statement, Results of operations – for the year 2013, Corporate Governance and Corporate Governance Recommendations Report is an integral part of the annual report of AS Tallinna Vesi for the financial year ended 31 December 2013. The Management Report gives a true and fair view of the trends and results of operations, main risks and doubts of AS Tallinna Vesi.

| Name | Position | Signature | Date |
|---|---|---|---|
| Ian John Alexander Plenderleith | Chairman of the Management Board | I.J.A. Plenderleith | 20/2/14 |
| Aleksandr Timofejev | Member of the Management Board | | 20/2/14 |
| Riina Käi | Member of the Management Board | | 20.02.2014 |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONSOLIDATED FINANCIAL STATEMENTS

### MANAGEMENT CONFIRMATION

The Management Board hereby declares its responsibility for the preparation of the consolidated financial statements of AS Tallinna Vesi (Company) and its subsidiary Watercom OÜ (together referred as Group) for the financial year ended 31 December 2013 on pages 26 to 60.

The financial statements have been prepared according to International Financial Reporting Standards as adopted by the EU, and give a true and fair view of the financial position, results of operations and cash flows of the Group.

The preparation of the financial statements according to International Financial Reporting Standards involves estimates made by the Management Board of the Group's assets and liabilities as of 31 December 2013, and of income and expenses during the financial year. These estimates are based on current information about the Group and consider all plans and risks as of 31 December 2013. The actual results of these business transactions recorded may differ from such estimates.

Any subsequent events that materially affect the valuation of assets and liabilities and have occurred up to the completion of the financial statements on 20 February 2014 have been considered in preparing the financial statements.

The Management Board considers AS Tallinna Vesi and its subsidiary to be going concern entities.

| Name | Position | Signature | Date |
|---|---|---|---|
| Ian John Alexander Plenderleith | Chairman of the Management Board | | 20/2/14 |
| Aleksandr Timofejev | Member of the Management Board | | 20/2/14 |
| Riina Käi | Member of the Management Board | | 20.02.2014 |

Initsialiseeritud ainult identifitseerimiseks
Initialled for the purpose of identification only
Initsiaalid/initials E.K.
Kuupäev/date 25.02.14
PricewaterhouseCoopers, Tallinn

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

| | | as of 31 December | |
|---|---|---|---|
| **ASSETS** | **Note** | **2013** | **2012** |
| **CURRENT ASSETS** | | | |
| Cash and cash equivalents | 6 | 31 786 | 23 935 |
| Trade receivables, accrued income and prepaid expenses | 7 | 15 010 | 18 323 |
| Inventories | | 429 | 356 |
| **TOTAL CURRENT ASSETS** | | **47 225** | **42 614** |
| **NON-CURRENT ASSETS** | | | |
| Other long-term receivables | 8 | 2 213 | 7 560 |
| Property, plant and equipment | 9 | 152 246 | 149 400 |
| Intangible assets | 9 | 1 037 | 1 154 |
| **TOTAL NON-CURRENT ASSETS** | | **155 496** | **158 114** |
| **TOTAL ASSETS** | | **202 721** | **200 728** |
| **LIABILITIES AND EQUITY** | | | |
| **CURRENT LIABILITIES** | | | |
| Current portion of long-term borrowings | 10 | 2 146 | 115 |
| Trade and other payables | 11 | 4 761 | 5 482 |
| Derivatives | 12 | 1 816 | 2 039 |
| Prepayments | 15 | 2 490 | 2 252 |
| **TOTAL CURRENT LIABILITIES** | | **11 213** | **9 888** |
| **NON-CURRENT LIABILITIES** | | | |
| Deferred income from connection fees | | 10 143 | 7 892 |
| Borrowings | 10 | 93 618 | 95 717 |
| Derivatives | 12 | 507 | 2 538 |
| Other payables | | 32 | 20 |
| **TOTAL NON-CURRENT LIABILITIES** | | **104 300** | **106 167** |
| **TOTAL LIABILITIES** | | **115 513** | **116 055** |
| **EQUITY** | | | |
| Share capital | 16 | 12 000 | 12 000 |
| Share premium | | 24 734 | 24 734 |
| Statutory legal reserve | | 1 278 | 1 278 |
| Retained earnings | | 49 196 | 46 661 |
| **TOTAL EQUITY** | | **87 208** | **84 673** |
| **TOTAL LIABILITIES AND EQUITY** | | **202 721** | **200 728** |

Notes to the financial statements on pages 30 to 60 form an integral part of the financial statements.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | | for the year ended 31 December | |
|---|---|---|---|
| | **Note** | **2013** | **2012** |
| Revenue | 17 | 53 087 | 52 924 |
| Costs of goods sold | 19 | -22 505 | -20 337 |
| **GROSS PROFIT** | | **30 582** | **32 587** |
| Marketing expenses | 19 | -690 | -772 |
| General administration expenses | 19 | -5 060 | -4 740 |
| Other income(+)/ expenses(-) | 20 | -75 | 1 696 |
| **OPERATING PROFIT** | | **24 757** | **28 771** |
| Financial income | 21 | 681 | 1 591 |
| Financial expenses | 21 | -877 | -3 297 |
| **PROFIT BEFORE TAXES** | | **24 561** | **27 065** |
| Income tax on dividends | 22 | -4 625 | -4 466 |
| **NET PROFIT FOR THE PERIOD** | | **19 936** | **22 599** |
| **COMPREHENSIVE INCOME FOR THE PERIOD** | | **19 936** | **22 599** |
| Attributable profit to: | | | |
| Equity holders of A-shares | | 19 935 | 22 598 |
| B-share holder | | 0.60 | 0.60 |
| Earnings per A share (in euros) | 23 | 1.00 | 1.13 |
| Earnings per B share (in euros) | 23 | 600 | 600 |

Notes to the financial statements on pages 30 to 60 form an integral part of the financial statements.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONSOLIDATED STATEMENT OF CASH FLOW

| | | for the year ended 31 December | |
|---|---|---|---|
| | **Note** | **2013** | **2012** |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Operating profit | | 24 757 | 28 771 |
| Adjustment for depreciation/amortisation | 9,19 | 5 809 | 5 879 |
| Adjustment for income from government grants and revenue from connection fees | 20 | -117 | -2 043 |
| Other non-cash adjustments | | 11 | -153 |
| Profit(-)/loss(+) from sale and write off of property, plant and equipment, and intangible assets | | -138 | -6 |
| Change in current assets involved in operating activities | | -433 | -160 |
| Change in liabilities involved in operating activities | | -92 | -568 |
| **Total cash flow from operating activities** | | **29 797** | **31 720** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Loans granted | 8 | 0 | -765 |
| Repayment of loan | 8 | 3 814 | 0 |
| Acquisition of property, plant and equipment, and intangible assets | | -9 187 | -10 011 |
| Compensations received for construction of pipelines | | 7 885 | 11 198 |
| Proceeds from sale of property, plant and equipment, and intangible assets | | 165 | 38 |
| Interest received | | 693 | 1 585 |
| **Total cash flow used in investing activities** | | **3 370** | **2 045** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Interest paid and loan financing costs, incl swap interests | 21 | -3 154 | -3 272 |
| Repayment of finance lease | | -136 | -61 |
| Dividends paid | 22 | -17 401 | -16 801 |
| Income tax on dividends | 22 | -4 625 | -4 466 |
| **Total cash flow used in financing activities** | | **-25 316** | **-24 600** |
| **Change in cash and cash equivalents** | | **7 851** | **9 165** |
| **CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD** | | **23 935** | **14 770** |
| **CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD** | 6 | **31 786** | **23 935** |

Notes to the financial statements on pages 30 to 60 form an integral part of the financial statements.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | Share capital | Share premium | Statutory legal reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|
| **as of 31 December 2011** | **12 000** | **24 734** | **1 278** | **40 863** | **78 875** |
| Dividends (Note 22) | 0 | 0 | 0 | -16 801 | -16 801 |
| Comprehensive income for the period (Note 23) | 0 | 0 | 0 | 22 599 | 22 599 |
| **as of 31 December 2012** | **12 000** | **24 734** | **1 278** | **46 661** | **84 673** |
| Dividends (Note 22) | 0 | 0 | 0 | -17 401 | -17 401 |
| Comprehensive income for the period (Note 23) | 0 | 0 | 0 | 19 936 | 19 936 |
| **as of 31 December 2013** | **12 000** | **24 734** | **1 278** | **49 196** | **87 208** |

Notes to the financial statements on pages 30 to 60 form an integral part of the financial statements.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 1. GENERAL INFORMATION

AS Tallinna Vesi (Company) is the largest water utility in Estonia providing drinking water and wastewater disposal services to over 400 000 people in Tallinn and in several neighbouring municipalities of Tallinn. AS Tallinna Vesi has the exclusive right to provide water and sewerage services in Tallinn's main service area until the year 2025.

Shareholders of AS Tallinna Vesi having a significant influence are, United Utilities Tallinn B.V. with 35.3% and the City of Tallinn with 34.7%, the balance of 30% of shares is free floating on the Nasdaq OMX Baltic Exchange, in which AS Tallinna Vesi was listed on 1 June 2005

Watercom OÜ (Subsidiary) was founded at 2010 by the Company and its main areas of activity are services related to water business and owner supervision, construction and project management services related to water and sewage.

The Company and the Subsidiary together form a group (Group).

**Contacts:**

| | | |
|---|---|---|
| Name | AS Tallinna Vesi | OÜ Watercom |
| Commercial register number | 10257326 | 11944939 |
| VAT identification number | EE100060979 | EE101374619 |
| Address | Ädala 10, 10614 Tallinn | Ädala 10, 10614 Tallinn |
| Telephone | 62 62 200 | 62 62 620 |
| Fax | 62 62 300 | 62 62 300 |
| E-mail | tvesi@tvesi.ee | watercom@watercom.eu |

## NOTE 2. ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements (hereinafter referred to as 'financial statements') are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (EU) (hereinafter IFRS).

The financial statements have been prepared under the historical cost convention, as modified by the accounting policy for derivatives, measured at fair value through profit and loss, as disclosed in the accounting policies below.

The Management Board of AS Tallinna Vesi authorised these consolidated financial statements for issue at 20 February 2014. Pursuant to the Commercial Code of the Republic of Estonia, the financial statements are subject to approval by the Supervisory Board of AS Tallinna Vesi and the General Meeting of Shareholders. Shareholders have the right not to approve the annual report prepared and approved by the Management Board, and request preparation of a new annual report.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

***Adoption of New or Revised Standards and Interpretations***

The following new or revised standards or interpretations became effective for the Group from 1 January 2013:

***IFRS 13, Fair Value Measurement,*** effective for annual periods beginning on or after 1 January 2013; aims to improve consistency and reduce complexity by providing a revised definition of fair value, and a single source of fair value measurement and disclosure requirements for use across IFRSs. The standard did not have any significant impact on fair value measurements in the Group's financial statements, but additional information related to the change has been disclosed in the financial statements of the Group.

Other new or revised standards or interpretations that became effective for the Group from 1 January 2013 do not have a material impact to the Group.

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

### *Principles of consolidation, accounting for business combinations and subsidiaries*

A subsidiary is an entity in which the Group, directly or indirectly, has interest of more than one half of the voting rights or otherwise has power to govern the operating and financial policies so as to obtain economic benefits. The subsidiary has been consolidated in the Group's financial statements.

In the consolidated financial statements, the financial statements of the subsidiary are combined on a line-by-line basis. Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Group and its subsidiary use uniform accounting policies. Where necessary, the accounting policies of the subsidiary have been changed to ensure consistency with the policies adopted by the Group.

Investment in subsidiary is carried at cost (less any impairment losses) in the separate primary financial statements of the Company.

### *Foreign currency*

*Functional and presentation currency*

Consolidated financial statements for the year ended 31 December 2013 have been presented in euros.

For the convenience of the users, these financial statements have been presented in thousands of euros, unless stated otherwise.

*Foreign currency transactions and balances*

All other currencies except for the functional currency (the functional currency of the Parent Company and subsidiary located in Estonia is Euro) constitute foreign currencies. Foreign currency transactions have been translated to functional currencies based on the foreign currency exchange rates of the European Central Bank prevailing on the transaction date. Monetary assets and liabilities denominated in a foreign currency (monetary receivables and loans) have been translated into functional currency based on the foreign currency exchange rates of the European Central Bank prevailing on the balance sheet date. Foreign exchange gains and losses are recognised in the statement of comprehensive income as income or expenses of that period.

### *Current and non-current distinction of assets and liabilities*

Assets and liabilities are classified in the statement of financial position as current or non-current. Assets expected to be recovered of in the next financial year or during the normal operating cycle of the Group are considered as current. Liabilities whose due date is in the next 12 months or that is expected to be settled in the next financial year or during the normal operating cycle of the Group are considered as current. All other assets and liabilities are classified as non-current.

### *Cash and cash equivalents*

Cash and cash equivalents in the statement of financial position and the cash flow statement comprise of cash on hand, cash in bank accounts and short-term, risk free, highly liquid bank deposits with original maturities of three months or less.

Cash flows from operating activities are reported using the indirect method, whereby profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows. Cash flows from investing and financing activities are reported using the direct method.

***Financial assets***

Financial assets are cash, trade receivables, accrued income, others current and long-term receivables including the derivatives with positive value.

Financial assets are recorded in statement of financial position at value date (i.e. are recognised when the Group becomes the owner of the financial assets and are derecognised when the Group has transferred substantially all risk and rewards incidental to ownership).
According to the purpose of acquisition and management intentions the financial assets are divided into the following groups:

- Financial assets at fair value through profit or loss
- Receivables and loans
- Investments held-to-maturity
- Financial assets available-for-sale

As of 31 December 2013 and 2012 the Group did not have any investments held-to-maturity and financial assets available-for-sale.

Financial assets held for trading are classified as financial assets at fair value through profit or loss (asset is acquired for the purpose of selling in the near term). Financial assets at fair value through profit or loss are initially recorded at fair value, transaction costs are recorded in the profit or loss. Financial assets of this category are subsequently carried at fair value and gains/losses from changes in fair value are recorded in profit or loss of the period. The quoted market price on balance date is their basis for establishing the fair value of financial assets at fair value through profit or loss.

Loans and receivables are initially recognised at a fair value plus the transaction costs. Loans and receivables are subsequently carried at amortised cost, using effective interest method (less any impairment allowances).

As of 31 December 2013 the Company had given no loans (31 December 2012: one loan).

***Receivables***

Trade receivables comprise of short term receivables generated in the ordinary course of business. Trade receivables are recorded using at the amortised cost method.

Allowance for receivables is recorded if there is objective evidence that the Group is not able to collect all amounts due according to the original terms of the agreement. Impairment of individually material receivables is evaluated separately for each customer, considering the present value estimated future cash flows. For receivables which are not individually significant and for which there is no direct information that their value has been decreased, the allowance is evaluated collectively using previous years' experience on impairment of receivables. The amount of the allowance for doubtful receivables is the difference between their carrying amount and present value of future cash flows, using effective interest rate method. The carrying amount of receivables is reduced by the impairment loss and impairment loss is recorded in the statement of comprehensive income on the row „Other income/ expenses". Subsequent recoveries of doubtful receivables are recorded as a decrease of impairment loss.

### *Inventories*

Inventories are initially recorded at cost including purchase costs, non-refundable taxes and transportation and other costs directly connected with the acquisition, less allowances and discounts. The weighted-average cost method has been used to determine the cost of inventories. Inventories are carried in the statement of financial position at the lower of the cost and net realizable value. Net realizable value is the net selling price less estimated costs necessary to make the sale.

### *Non-current assets held for sale*

Non-current assets held for sale are the property, plant and equipment items that are most probably sold within next 12 months and for which the management has begun sales activity and the assets are offered for sale for a reasonable price compared to their fair value.

Non-current assets held for sale are classified in the statement of financial position as current assets and depreciation ended at the moment of reclassification. Non-current assets held for sale are carried in the statement of financial position at the lower of at book value and fair value less costs to sell.

### *Property, plant and equipment, and intangible assets*

Property, plant and equipment are tangible assets used in operating activities of the Group with an expected useful life of over one year. Property, plant and equipment are carried in the statement of financial position at historical cost less accumulated depreciation and any impairment losses.

Intangible assets are recognised in the statement of financial position only if the following conditions are met:
- the asset is controlled by the Group;
- it is probable that the future economic benefits that are attributable to the asset will flow to the Group;
- the cost of the asset can be measured reliably.

#### *Acquired licenses*

Acquired computer software that is not an integral part of the related hardware is recognised as an intangible asset. Development costs of computer software are recognised as intangible assets if these are directly related to the development of such software objects that are identifiable, controllable by the Group and that are expected to generate economic benefits beyond one year. Capitalizable development costs of computer software include staff costs and other expenses directly related to the development. Costs related to the day-to-day maintenance of computer software are recognised as expenses in the statement of comprehensive income. Costs of computer software shall be depreciated over the estimated useful lifetime, the duration of which is up to 10 years.

#### *Other intangible assets*

Expenses for acquiring patents, trademarks, licences and certificates are capitalized if it is possible to estimate the future economic benefits attributable to these assets. Other intangible assets are amortised on a straight line basis over the estimated useful lifetime, the duration of which does not exceed 10 years.

The cost of purchased property, plant and equipment and intangible assets comprises the purchase price, transportation costs, installation, and other direct expenses (incl. internal labour costs) related to the acquisition or implementation. Labour costs are capitalised with employee's hourly index applied to working hours which are needed for taking the asset to the location and condition necessary for it to be capable of operating in the manner intended by the management. Hourly rate is calculated individually for each employee and includes other direct expenses connected with the employee in addition to salary expense.

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

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset.

Subsequent expenditures are added to the carrying amount of the item of property, plant and equipment or are recognised as a separate asset only when it is probable that future economic benefits related to the assets will flow to the Group and the cost of the asset can be measured reliably. A replaced component or proportion of the replaced item of property, plant and equipment is derecognised. Costs related to ongoing maintenance and repairs are charged to the statement of comprehensive income.

Land is not depreciated. Depreciation of other property, plant and equipment is calculated on a straight-line basis on cost over the estimated useful life of the asset.

Applicable depreciation/amortization rates:

- buildings 1,25-2,0 % per annum;
- facilities 1,0-8,33 % per annum;
- machinery and equipment 3,33-50 % per annum;
- instruments and other equipment etc. 10-20 % per annum;
- acquired licenses and other intangible assets 10-33 % per annum.

In exceptional circumstances rates may differ from the above ranges if it is evident that the estimated useful life of the asset varies materially from the ranges of rates assigned to the respective category.

The expected useful lives of items of property, plant and equipment are reviewed during the annual stocktaking, in recognising subsequent expenditures and in case of significant changes in development plans. When the estimated useful life of an asset differs significantly from the previous estimate it is treated as a change in the accounting estimate and the remaining useful life of the asset is changed as a result of which the depreciation charge of the following periods also changes. Assets are written down to their recoverable amount when the recoverable amount is less than the carrying amount. To determine profits and losses from the sale of property, plant and equipment the book value of the sold assets is subtracted from the proceeds. The respective profits and losses are reported in the line "Other income / expenses".

### *Impairment of assets*

Assets that are subject to depreciation/amortisation and property, plant and equipment with unlimited useful lives (land) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The recoverable value of intangible assets in progress is tested annually, by comparing their recoverable amount with the carrying amount.

Assets are written down to their recoverable amount in case the latter is lower than the carrying amount. The recoverable amount of the assets is the higher of the:
- fair value less costs to sell and
- value in use.

In case it is not possible to determine the fair value of assets less costs to sell, the asset's value in use is considered to be its recoverable value. The value in use is calculated as the present value of the estimated future cash flows generated by the assets.

The impairment of assets may be assessed either for an individual asset or a group of assets (cash-generating unit). For the purposes of assessing impairment, the Group is considered to be a single cash-generating unit as it is the lowest level for which there are separately identifiable cash flows. The impairment loss is immediately recognised in the statement of comprehensive income. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

If based on the results of the assessment it appears that the recoverable amount of an asset or the cash-generating unit has increased, the earlier impairment is reversed up to the amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years. The reversal of impairment loss is recorded in the statement of comprehensive income of the period as a decrease in impairment loss.

***Financial liabilities***

Financial liabilities include trade payables, accrued expenses, loans payable and other short term and long term financial liabilities and derivatives. Financial liabilities (except derivatives) are initially recognised at fair value net of transaction cost. Subsequently financial liabilities are carried at the amortised cost.

Amortised cost of short term financial liabilities is usually equal to their nominal value, thus they are carried on statement of financial position at the amount payable. For calculating the amortised cost of long-term financial liabilities these are initially recognized at fair value of amount received (less transaction costs), interest expense is calculated from the liability using the effective interest method subsequently.

Liabilities are classified as current liabilities, unless the Group has an unconditional right to defer the settlement of the liability for at least 12 months after the balance sheet date.

***Derivatives***

With regard to derivatives, the Group uses interest rate swap contracts, in order to mitigate risks related to fluctuations in interest rates. Such derivatives are initially recognised at their fair value at the date of entering into the contract and are subsequently carried at fair value with changes recognised in profit or loss. If fair value is positive, the derivative is recognised as an asset, if negative, as a liability. Derivatives are classified as a current asset or liability if expected to be settled within 12 months; otherwise, they are classified as non-current.

Gains and losses attributable to changes in the fair value of derivatives are recognised in the statement of comprehensive income of the reporting period. Gains and losses from the disposal of derivatives are also recognised in the statement of comprehensive income.

***Corporate income tax***

According to the Income Tax Act, the annual profit earned by enterprises is not taxed in Estonia and thus there are no temporary differences between the tax bases and carrying values of assets and liabilities and no deferred tax assets or liabilities arise.

*Income tax on dividends in Estonia*

According to the Estonian Income Tax Act the accrued profit of a resident legal entity is not subject to tax, as tax is charged only on dividend distributions. Pursuant to the Income Tax Act, resident legal entities are liable to income tax on all dividends paid and other profit distributions irrespective of the recipient. The rate is 21/79 on the amount of the dividends payable (2012: 21/79).

The contingent tax liability that would occur if all distributable retained earnings were paid out as dividends is not recognized in the statement of financial position. The income tax due on dividend distribution is recorded as a liability and as a tax expense in the statement of comprehensive income during the same period as the dividend is declared regardless of the actual payment date or the period for which dividends are declared. Income tax liability is due on the 10th date of the month following the dividend payment.

***Employee benefits***

*Employee short-term benefits*

Employee short-term benefits include wages and salaries as well as social security taxes, benefits related to the temporary halting of the employment contract (holiday pay or other similar pay) when it is assumed that the temporary halting of the employment contract will occur during 12 months after the end of the period in which the employee worked, and other benefits payable within 12 months after the end of the period during which the employee worked. Social security tax payments include contribution to state pension funds. The Group has no legal or constructive obligation to make pension or similar payments beyond social security tax.

*Termination benefits*

Termination benefits are benefits which are payable after the Group decides to terminate the employment relationship with the employee before the normal retirement date or when the employee decides to leave voluntarily or when the employee and employer have an agreement, in exchange for the benefits outlined. The Group recognises termination benefits as liabilities and expenses only when the Group is obliged to offer termination benefits in order to encourage voluntary leaving.

***Provisions and contingent liabilities***

Provisions are recognized when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

The amount of servitudes likely payable that henceforth must be paid to the owners of private land resulting from the restrictions related to land use in case the Group's pipes are located on their land, are recorded as provisions. On the statement of financial position the liability is classified as short-term, because it can be realized to full extent within 12 months from the balance date.

Provisions have been recognised based on of the best estimates of the Group's Management Board and the actual costs of these transactions can differ from the provided estimates. Commitments and other possible and existing liabilities, the realization of which is unlikely or the amount of accompanying costs cannot be assessed with sufficient reliability but which can become liabilities on certain terms in the future, are disclosed as contingent liabilities in the notes to the financial statements.

***Share capital***

Shares are recorded within the equity capital. Pursuant to the Group's Articles of Association, the Group has two classes of shares: the A-Shares, with a nominal value of 0.60 euros each and a single preference share B-Share, with a nominal value of 60 euros.

***Statutory reserve capital***

Pursuant to the requirements of the Commercial Code the statutory reserve capital is set up comprising of the allocations from net profits. The annual allocation must be at least 5% of the net profit of the accounting year until the reserve capital is equal to 10% of paid-up share capital. As the Group's reserve capital has reached the required level, the reserve capital is no longer increased from net profit.

At the decision of the General Meeting of the Shareholders the reserve capital can be used for the covering of loss in case it is not possible to cover it from the Group's available shareholders' equity, also for increasing the Group's share capital. The reserve capital cannot be distributed to the shareholders.

***Leases***

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

*The Group as the lessee*

Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased asset and the present value of minimum lease payments. Each lease payment is apportioned between the finance charge and the reduction of the outstanding liability. Finance charges are allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. The finance lease liability is reduced by principal payments. The finance charge is recognised as an interest expense in the statement of comprehensive income. The finance lease liability is recognised either within short or long-term borrowing in the statement of financial position. Payments made under operating leases are charged to the statement of comprehensive income over the lease term on a linear basis.

***Government grants***

Government grants are recognised as income over the periods necessary to match them with the related costs which they are intended to compensate. Government grants received for expenses incurred in previous periods or which do not include additional conditions for future compliance are recognised as income in the period when government grant was received. Government grants are not recognised as income before there exists sufficient confidence that Group complies with the conditions relating to government grants and the grants will be received. Government grants received as compensations for the construction of water, sewerage and storm water pipelines shall be deducted from the book value of the pipeline constructed and any amounts exceeding the construction cost of pipeline shall be recognized as income upon delivery of construction works within "Other income/expenses" as income from government grants.

***Revenue***

Revenue is recognised at the fair value of consideration received or receivable, net of VAT and sales discounts. Revenue comprises sales of services.

Sales of water, wastewater, storm water and fire hydrants services and other sales income is recorded in the period when the service has been provided, the amount of the revenue and cost incurred for the transaction can be measured reliably, it is probable that economic benefits associated with the transaction will flow to the entity.

Connection fees received from customers are recognised as income during the period of the duration of useful life of related assets which is 75 years. The acquisition costs of pipelines taken into use and the connection fees received from customers are recorded respectively on the statement of financial position as "Property, plant and equipment" and "Deferred income from connection fees". Income/expense from amortization of assets and liabilities is respectively recorded as "Other income/expenses".

Interest income is recognised in case the receipt of income is likely and the amount of income can be determined reliably. Interest income is recognised using the effective interest method.

***Earnings per share***

Earnings per share are calculated by dividing the net profit of the accounting year with the weighted average number of issued shares of the period. The Group has no instruments that would have a diluting effect on the earnings per share.

***Segment reporting***

Operating segments are reported in a manner consistent with the internal reporting provided to the Management Board, being the chief operating decision-maker. The Management Board, who is responsible for allocating resources and assessing performance of the operating segments, reports to the Supervisory Board which has been identified as the steering committee that makes strategic decisions. The Management Board has determined that the activities of the Group form a single operating segment. The internal reporting reviewed by the Supervisory Board and the Management Board is prepared using the same accounting principles and format of statement of financial position and statement of comprehensive income as provided in these consolidated financial statements.

## NOTE 3. CONTINGENT LIABILITY REGARDING THE TARIFF RISK

On 10th October 2011 the Estonian Competition Authority (CA) issued a prescript for the Company to reduce the tariffs of water and sewerage services in Tallinn by 29%. The Company disagrees with the position of the CA and has turned to the Estonian Administrative Court disputing the prescription that seeks to break the privatization contract without any evidence to support its view that privatization contract should not be honoured. Should the Court uphold the CA's position the privatization contract could cease to be the basis for the tariffs of water and sewerage services in Tallinn. The length of the court process and the decision are not within the Company's control.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

The management has evaluated the amount of the contingent liability as of 31 December 2013 arising from the potential claims against the Company if the Court ruling would support the CA's position. As result of this, the outflow of economic benefits could be up to 34 mln euros (31 December 2012:36 mln euros) that could be claimed within 10 years of the final judgement of the courts.

## NOTE 4. CRITICAL ACCOUNTING ESTIMATES

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of material misstatements to the carrying amounts of assets and liabilities within the next financial year are addressed below.

- Management has estimated the useful lifetime of property, plant and equipment and intangible assets. The results of the estimates are disclosed in the note 2 in section 'Property, plant and equipment, and intangible assets' and the information about the carrying amounts is disclosed in note 9. As of 31 December 2013 Group owns property, plant and equipment, and intangible assets with a book value of 153.3 mln euros (31 December 2012: 150.6 mln euros) and annual depreciation was 5.8 mln euros (2012: 5.9 mln euros). If the depreciation/amortization rates decreased/increased by 5 %, the depreciation/amortization expense would increase/decrease respectively by 290 thousand euros (2012: 295 thousand euros).

- The Group had an obligation to construct water and wastewater and storm water pipelines with construction costs of 41 mln euros (2012: 41 mln euros) in 2008-2012. The construction of pipelines is compensated by local government with the grants receivable in 2008 – 2015 (2012: 2008 – 2014). Compensations received from local government are recognised as government grants - compensations received or recivable are deducted from the book value of the constructed pipeline. Any amount exceeding the construction cost of the pipeline is recognized as income upon the completion of construction works. The part of the compensation that is received after the completion of the construction works is recognized in the statement of financial position as a receivable from local government at its present value.

  As payment of government grant for pipelines will be received until March of 2015 (2012: June of 2014) and the exact extent of compensation depends on water consumption, the value of compensation receivable is also based on estimates. In the estimates compensation is receivable for 2014-2015 and has been discounted using a rate of 3.5% (2012: 7%). If the discount rate would be decreased/increased by 50 basis points, the profit of the accounting period would increase/decrease up to 36 thousand euros (2012: up to 81 thousand euros).

- Accounts receivable - for the evaluation of doubtful debts the individual debts are grouped by age and, based on past experience, the following percentages are applied in the doubtful debt calculation:

  | | |
  |---|---|
  | 61 to 90 days over due date | 10%; |
  | 91 to 180 days over due date | 30%; |
  | 181 to 360 days over due date | 70%; |
  | over 360 days over due date | 100%. |

  Impairment of individually material receivables can differ from the rates above.

## NOTE 5. FINANCIAL RISK MANAGEMENT

### 5.1 Financial risk factors

In its business activities the Group is exposed to different financial risks: market risk (including currency risk, price risk, cash flow interest rate risk and fair value interest rate risk), credit risk and liquidity risk. The Group's financial risk management focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.
The Group's financial risks are managed under the control and supervision of the Management Board by the financial department. Financial department identifies, evaluates and manages financial risks in co-operation with the Group's operating units.

***Market risk***

*Foreign exchange risk*

Foreign exchange risk arises when future commercial transactions or recognised assets or liabilities are denominated in a currency that is not the entity's functional currency. The Group's foreign exchange risk is related to purchases done and amounts owed in foreign currencies.

Majority of Group's purchases are made in euros. The proportion of purchases in other currencies in 2013 was less than 2.0% (2012: less than 0.5%). Because of the small proportion of transactions in foreign currencies the Group has not taken any special activities to reduce this risk.

On 31 December 2013 the Group's bank accounts balances (including deposits) totalled 31 786 thousand euros (31 December 2012: 23 935 thousand euros) from which no sums were in foreign currencies (31 December 2012: no foreign currencies). There were no other significant exposures to foreign currencies arising from Group's other financial assets and financial liabilities.
Due to the above the Group considers its currency risk level to be low.

*Price risk*

The Group has no price risk regarding financial instruments because it has no investments into equity instruments.

*Cash flow interest rate risk and fair value interest rate risk*

Fair value interest rate risk is the risk that the fair value of financial instruments will fluctuate in the future due to changes in market interest rates. Cash flows interest rate risk is the risk that financial expenses arising from financial liabilities with floating interest rate will increase when interest rates on the market increase.

The Group's interest rate risk arises mostly from long-term borrowings. Borrowings issued at variable interest rates (Note 10) expose the Group to cash flow interest rate risk. The Group's policy is to maintain approximately 75% of its borrowings at fixed rate. In order to mitigate the cash flow interest rate risk, the Group has concluded 6 (2012: 5) floating-to-fixed interest rate swap contracts (Note 12). As of 31 December 2013 the interest rate swap contracts have the notional amount of 90 mln euros (31 December 2012: 75 mln euros), with one contract becoming effective in November 2015, therefore only borrowings in the amount of 19.9 mln euros from total of 94.9 mln euros (31 December 2012: 19.9 mln euros from total of 94.9 mln euros) remain exposed to the cash flow interest rate risk.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

**Financial assets**

| **as of 31 December 2012** | **Balance** | **Not due** | **Overdue** Not impaired (up to 2 months) | Impaired | Impairment |
|---|---|---|---|---|---|
| Cash and cash equivalents (Note 6) | 23 935 | 23 935 | 0 | 0 | 0 |
| Trade receivables (Note 7) | 10 470 | 10 353 | 83 | 533 | -499 |
| Commercial entities | 7 278 | 7 201 | 51 | 480 | -454 |
| Private persons | 3 192 | 3 152 | 32 | 53 | -45 |
| Accrued income (Note 7) | 21 | 21 | 0 | 0 | 0 |
| Loan to co-partner and other receivables (Note 7, 8) | 3 916 | 3 916 | 0 | 0 | 0 |
| Government grant receivable (Note 7, 8, 25) | 10 868 | 10 868 | 0 | 0 | 0 |
| **Total** | **49 210** | **49 093** | **83** | **533** | **-499** |

The Group's maximum credit risk is equal to the carrying amount of the financial assets and is considered to be low.

***Liquidity risk***

Liquidity risk is the risk that the Group is unable to fulfil its financial obligations due to insufficient cash funds or inflows. This risk realizes when the Group does not have enough funds to serve its loans, to fulfil its working capital needs, to invest and/or to make declared dividend payments.

**Financial liabilities in terms of payment (undiscounted amounts):**

| **as of 31 December 2013** | **Up to 1 month** | **1 - 3 months** | **3 - 12 months** | **1 - 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|---|---|
| Trade and other payables | 2 003 | 38 | 0 | 0 | 10 | 2 051 |
| Derivatives | 1 816 | 0 | 0 | 507 | 0 | 2 323 |
| Borrowings (incl finance lease) | 87 | 187 | 3 039 | 94 929 | 2 010 | 100 252 |
| **Total** | **3 906** | **225** | **3 039** | **95 436** | **2 020** | **104 626** |

| **as of 31 December 2012** | **Up to 1 month** | **1 - 3 months** | **3 - 12 months** | **1 - 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|---|---|
| Trade and other payables | 2 863 | 38 | 0 | 0 | 9 | 2 910 |
| Derivatives | 2 039 | 0 | 0 | 2 538 | 0 | 4 577 |
| Borrowings (incl finance lease) | 78 | 168 | 953 | 55 876 | 44 038 | 101 113 |
| **Total** | **4 980** | **206** | **953** | **58 414** | **44 047** | **108 600** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

As of 31 December 2013, if the interest rates of the Group's borrowings, that are exposed to the cash flow interest rate risk, had been 50 basis points (31 December 2012: 50 basis points) higher/lower with all other variables held constant, profit for the year would have been EUR 101 thousand (2012: EUR 101 thousand) lower/higher.

Overnight and fixed term deposits have fixed interest rate and therefore expose the Group to fair value interest rate risk. As all these instruments are carried at amortised cost, the change in market interest rates would not have an effect on the financial statements of the Group.

***Credit risk***

Credit risk expresses potential loss that can arise if counterparty fails to fulfil its contractual obligations. Cash in bank accounts and deposits, financial assets at fair value through profit and loss, trade and other receivables are exposed to credit risk.

According to the Group's risk management policies the Group's short term resources can be deposited only in accounts, overnight deposits and fixed term deposits opened in credit institutions. For fixed term depositing counterparties with at least a long term Baa1 rating (by Moody's) is used. As of 31 December 2013 85% of Group's fixed term deposits were deposited with counterparty with higher rating than A3 and 15% with counterparty with rating Baa1 (31 December 2012: 100% higher than A3). The Group is also monitoring European Banking Authority's recommendations regarding banks' recapitalization needs and fixed term deposits are opened only in banks with no capitalization shortfall.

The selling of Group's products and services is done in compliance with internal procedures. To reduce credit risk related to accounts receivable the customers' payment discipline is consistently observed. In the case of overdue debt the clients are contacted by billing group. At the end of December 2013 only one client's (31 December 2012: one client's) receivables (Note 25) exceeded 5% of total trade receivables constituting 8.4% of it (31 December 2012: 47.0%).

**Financial assets**

| **as of 31 December 2013** | **Balance** | **Not due** | **Overdue** Not impaired (up to 2 months) | Impaired | Impairment |
|---|---|---|---|---|---|
| Cash and cash equivalents (Note 6) | 31 786 | 31 786 | 0 | 0 | 0 |
| Trade receivables (Note 7) | 6 495 | 6 271 | 184 | 408 | -368 |
| Commercial entities | 3 321 | 3 147 | 143 | 362 | -331 |
| Private persons | 3 174 | 3 124 | 41 | 46 | -37 |
| Accrued income (Note 7) | 9 | 9 | 0 | 0 | 0 |
| Loan to co-partner and other long-term account receivables (Note 7, 8) | 52 | 52 | 0 | 0 | 0 |
| Government grant receivable (Note 7, 8, 25) | 10 315 | 10 315 | 0 | 0 | 0 |
| **Total** | **48 657** | **48 433** | **184** | **408** | **-368** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

In liquidity risk management the Group has taken a prudent view, maintaining sufficient cash balance and short term deposits to be able to fulfil its financial liabilities at every moment of time. Continuous cash flow forecasting and control are essential tools in the day-to-day liquidity risk management of the Group.

### 5.2 Capital management

The Group's objectives when managing capital is to safeguard the Group's ability to continue as a going concern, to be in accordance with Business Plan's capital structure approved by Supervisory Board and the long-term borrowing contracts that limit the Company's equity ratio to a minimum of 35% of the total assets.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (Note 10; including 'current and noncurrent borrowings' as shown in the consolidated balance sheet) less cash and cash equivalents (Note 6). Total capital is calculated as 'equity' as shown in the consolidated balance sheet plus net debt.

| | | **as of 31 December** |
|---|---|---|
| | **2013** | **2012** |
| *Borrowings* | *95 764* | *95 832* |
| *Cash* | *-31 786* | *-23 935* |
| **Net debt** | **63 978** | **71 897** |
| **Equity** | **87 208** | **84 673** |
| **Total capital** | **151 186** | **156 570** |
| *Net debt and total capital ratio* | *42,3%* | *45,9%* |
| *Total assets* | *202 721* | *200 729* |
| *Proportion of equity to total assets* | *43,0%* | *42,2%* |

### 5.3 Fair value estimation

Fair values of cash and cash equivalents, trade receivable, other long-term receivables, short-term borrowings and trade payable do not vary significantly from their carrying amount because their realization will take place within 12 months or these were recognised close to the balance sheet date. The fair values of the government grant receivables have been measured using unobservable inputs (level 3) (Note 4).

At the end of 2013 all Group's long-term borrowings had floating interest rates. The fair values of long-term borrowings are based on discounted cash flows using the borrowing rate of 1.66% - 1.84% (2012: 1.53% - 1.74%) and are within level 3 of the fair value hierarchy. Because Group's contractual long-term borrowings risk margins were smaller, than market's risk margin currently applicable to the Group, the fair value of its long-term borrowings on 31 December 2013 was 948 thousand euros smaller than their carrying amount (31 December 2012: 1 240 thousand euros smaller).

Smaller interest risk margins compared to market situation means that if the Group would like to refinance its long-term borrowings on existing market conditions it would bring along higher interest expenses compared to the existing agreements.

The fair value of financial instruments carried at fair value (interest rate swap contracts, Note 12) has been determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2. The fair value of interest rate swap contracts is calculated as the present of estimated future cash flows based on observable yield curves.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 6. CASH AND CASH EQUIVALENTS

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Cash in hand and in bank | 3 295 | 1 859 |
| Short-term deposits | 28 491 | 22 076 |
| **Total cash and cash equivalents** | **31 786** | **23 935** |

## NOTE 7. TRADE RECEIVABLES, ACCRUED INCOME AND PREPAID EXPENSES

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Accounts receivable | 6 863 | 10 969 |
| Allowance for doubtful receivables | -368 | -499 |
| **Total trade receivables** | **6 495** | **10 470** |
| | | |
| **Allowance for doubtful receivables at the beginning of the period** | **-499** | **-514** |
| Proceeds from doubtful receivables during the period | 211 | 150 |
| Allowance for doubtful receivables recognised during the period | -166 | -319 |
| Receivables written off balance sheet during the period | 86 | 184 |
| **Allowance for doubtful receivables at the end of the period** | **-368** | **-499** |

Impairment losses recognised during the period are reported in profit or loss as "Other income (+) / expenses (-)". For further information on ageing of receivables (including overdue receivables), please see Note 5.

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Accrued interest | 9 | 21 |
| Government grant receivables | 8 154 | 7 123 |
| Prepaid expenses | 351 | 709 |
| **Total accrued income and prepaid expenses** | **8 514** | **7 853** |
| | | |
| **Total trade receivables, accrued income and prepaid expenses** | **15 010** | **18 323** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

The Company's current assets (incl. trade receivables, accruals and inventory) in the amount of 15 439 thousand euros (31 December 2012: 18 679 thousand euros) have been pledged as a security for the bank loans (Note 10), as a part of commercial pledge.

## NOTE 8. OTHER LONG-TERM RECEIVABLES

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Government grant receivables | 2 161 | 3 746 |
| Long-term accounts receivables | 52 | 0 |
| Loan to co-partner | 0 | 3 814 |
| **Total other long-term receivables** | **2 213** | **7 560** |

The loan to co-partner was repaid in full in 2013. The Company's long term receivables in the amount of 2 213 thousand euros (31 December 2012: 3 746 thousand euros) have been pledged as a security to the bank loans (Note 10), as a part of commercial pledge.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 9. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

| | Property, plant and equipment | | | | Assets in progress | | | Intangible assets | |
|---|---|---|---|---|---|---|---|---|---|
| | Land and buildings | Facilities | Machinery and equipment | Other equipment | Construction in progress | Unfinished pipelines | Unfinished intangible assets | Acquired licenses and other intangible assets | Total property, plant and equipment and intangible assets |
| **as of 31 December 2011** | | | | | | | | | |
| Acquisition cost | 24 247 | 162 106 | 40 594 | 1 175 | 2 849 | 1 677 | 222 | 5 363 | 238 233 |
| Accumulated depreciation | -5 110 | -52 920 | -27 837 | -808 | 0 | 0 | 0 | -4 008 | -90 683 |
| Book value | **19 137** | **109 186** | **12 757** | **367** | **2 849** | **1 677** | **222** | **1 355** | **147 550** |
| **Transactions in the period 01 January 2012 - 31 December 2012** | | | | | | | | | |
| Acquisition in book value | 0 | 0 | 0 | 0 | 7 862 | 3 153 | 293 | 0 | 11 308 |
| Write off and sale of property, plant and equipment, and intangible assets in book value | 0 | 0 | -1 | 0 | -32 | 0 | 0 | 0 | -33 |
| Compensated by government grants (Note 13) | 0 | 0 | 0 | 0 | 0 | -2 392 | 0 | 0 | -2 392 |
| Reclassification | 545 | 5 361 | 3 713 | 153 | -8 421 | -1 398 | -490 | 537 | 0 |
| Depreciation (Note 19) | -273 | -2 701 | -2 062 | -80 | 0 | 0 | 0 | -763 | -5 879 |
| **as of 31 December 2012** | | | | | | | | | |
| Acquisition cost | 24 793 | 167 389 | 44 018 | 1 302 | 2 258 | 1 040 | 25 | 5 899 | 246 724 |
| Accumulated depreciation | -5 384 | -55 543 | -29 611 | -862 | 0 | 0 | 0 | -4 770 | -96 170 |
| Book value | **19 409** | **111 846** | **14 407** | **440** | **2 258** | **1 040** | **25** | **1 129** | **150 554** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

| | Property, plant and equipment | | | | Assets in progress | | | Intangible assets | |
|---|---|---|---|---|---|---|---|---|---|
| | **Land and buildings** | **Facilities** | **Machinery and equipment** | **Other equipment** | **Construction in progress** | **Unfinished pipelines** | **Unfinished intangible assets** | **Acquired licenses and other intangible assets** | **Total property, plant and equipment and intangible assets** |
| **Transactions in the period 01 January 2013 - 31 December 2013** | | | | | | | | | |
| Acquisition in book value | 0 | 0 | 0 | 0 | 6 127 | 2 103 | 421 | 0 | 8 651 |
| Write off and sale of property, plant and equipment, and intangible assets in book value | 0 | 0 | -7 | -8 | 0 | -99 | 0 | 1 | -113 |
| Reclassification | 58 | 7 724 | 2 030 | 52 | -7 808 | -2 056 | -419 | 419 | 0 |
| Depreciation (Note 19) | -278 | -2 717 | -2 195 | -80 | 0 | 0 | 0 | -539 | -5 809 |
| **as of 31 December 2013** | | | | | | | | | |
| Acquisition cost | 24 851 | 175 032 | 44 874 | 1 321 | 577 | 988 | 27 | 5 517 | 253 187 |
| Accumulated depreciation | -5 662 | -58 179 | -30 639 | -917 | 0 | 0 | 0 | -4 507 | -99 904 |
| Book value | **19 189** | **116 853** | **14 235** | **404** | **577** | **988** | **27** | **1 010** | **153 283** |

Property, plant and equipment and intangible assets are written off if the condition of the asset do not enable further usage for production purposes. As of 31 December 2013 the book value of the assets (Machinery and equipment) leased under financial lease is 861 thousand euros (31 December 2012: 886 thousand euros).

The Group's non-current assets in the amount of 14 287 thousand euros (31 December 2012: 14 573 thousand euros) have been pledged as a security for the bank loans (Note 10), as a part of commercial pledge. A mortgage for the Group's non-current assets (land, buildings and facilities) in the book value amount of 32 147 thousand euros (31 December 2012: 32 766 thousand euros) serves as a security to the bank loans (Note 10).

During the year, the Group has capitalised borrowing costs amounting to 31 thousand euros (2012: 57 thousand euros) on qualifying assets. Borrowing costs were capitalised at the weighted average rate of its general borrowings of 1.13% (2012: 1.39%).

Initsialiseeritud ainult identifitseerimiseks
Initialled for the purpose of identification only
Initsiaalid/initials E.K.
Kuupäev/date 25.02.14
PricewaterhouseCoopers, Tallinn

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 10. BORROWINGS

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| **Current borrowings** | | |
| Current portion of long-term bank loans | 2 000 | 0 |
| Current portion of long-term finance lease liabilities | 146 | 115 |
| **Total current borrowings** | **2 146** | **115** |
| **Non-current borrowings** | | |
| Long-term bank loans | 92 934 | 94 919 |
| Long-term finance lease liabilities | 684 | 798 |
| **Total non-current borrowings** | **93 618** | **95 717** |

| **Bank loans at 31 December 2013** | | |
|---|---|---|
| Currency EUR (euro) | **Balance** | **Effective interest rate** |
| Borrowings at floating interest rate (based on 1- and 6-month Euribor) | 94 934 | 0.93%-1.66% |
| Finance lease liabilities | 830 | 2.27%-3.05% |

| **Bank loans at 31 December 2012** | | |
|---|---|---|
| Currency EUR (euro) | **Balance** | **Effective interest rate** |
| Borrowings at floating interest rate (based on 1- and 6-month Euribor) | 94 919 | 0.82%-1.55% |
| Finance lease liabilities | 913 | 2.27%-3.05% |

Company's loan agreements mature in November 2015 (31 December 2012: November 2015) in the sum of 37 500 thousand euros and in November 2018 (31 December 2012: November 2018) in the sum of 37 500 thousand euros. Third loan agreement in the sum of 20 000 thousand euros will be repaid in ten equal semi-annual repayments from November 2014 to May 2019 (31 December 2012: November 2014 to May 2019).

| **Collateral of loans and pledged assets** | | **Collateral at book value as of 31 December** | |
|---|---|---|---|
| **Type of collateral** | **Specification and location of collateral** | **2013** | **2012** |
| Commercial pledge | Movables of the Company (Notes 7, 8, 9) | 31 939 | 36 998 |
| Mortgage | Real Estates located at Paljassaare põik 14 and Järvevana tee 3, Tallinn, Estonia (Note 9) | 32 147 | 32 766 |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 11. TRADE AND OTHER PAYABLES

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Trade payables - operating expenditures | 1 564 | 1 743 |
| Trade payables - capital expenditures | 214 | 834 |
| Payables to related parties (Note 25) | 197 | 187 |
| Payables to employees | 900 | 869 |
| Interest payable | 33 | 50 |
| Other accrued expenses | 65 | 135 |
| Guarantee deposit | 26 | 28 |
| Taxes payable incl: | | |
| Income tax | 141 | 142 |
| VAT | 823 | 744 |
| Water abstraction charges | 257 | 236 |
| Pollution taxes | 209 | 181 |
| Social security tax | 283 | 284 |
| Other | 49 | 49 |
| **Total trade and other payables** | **4 761** | **5 482** |

## NOTE 12. DERIVATIVES

| **Liabilities** | **Balance amount** | **Short-term portion** | **Long-term portion** |
|---|---|---|---|
| **as of 31 December 2013** | | | |
| SWAP contracts | **2 323** | 1 816 | 507 |
| **as of 31 December 2012** | | | |
| SWAP contracts | **4 577** | 2 039 | 2 538 |

| | | as of 31 December |
|---|---|---|
| | **2013** | **2012** |
| Contracts start date | May 2010 – November 2015 | May 2010 – November 2011 |
| Contracts maturity date | May 2015 – November 2018 | November 2013 – November 2015 |
| Contracts notional amount | 90 000 | 75 000 |

## NOTE 13. GOVERNMENT GRANTS

***Government grants for* assets**

Government grants receivable accrued during the financial year for completed constructions of pipelines amounted to 0 euros (2012: 4 429 thousand euros) (Note 25). The book value of property, plant and equipment compensated by the government grant was decreased by 0 euros (2012: 2 392 thousand euros) (Note 9). The remainder of the compensation is recognised in the statement of comprehensive income (Note 20).

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 14. OTHER CONTINGENT LIABILITIES

Tax authority is entitled to check the Group's tax accounting within 5 years after the term for the submission of tax declaration and when mistakes are detected to impose an additional amount of tax, interests and fines. According to the Group's Management Board there are no circumstances as a result of which tax authority could impose a significant additional amount of tax to the Group.

The Group's distributable retained earnings as at 31 December 2013 amounted to 49 196 thousand euros (2012: 46 661 thousand euros). Consequently, the maximum possible tax liability which would become payable if retained earnings were fully distributed is 13 077 thousand euros (2012: 12 404 thousand euros).

## NOTE 15. PREPAYMENTS

| | as of 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Prepayments for water and sewerage services | 55 | 76 |
| Prepayments for connection fee | 2 435 | 2 176 |
| **Total prepayments** | **2 490** | **2 252** |

## NOTE 16. SHARE CAPITAL

At 31 December 2013 the nominal value of the share capital was 12 000 060 (twelve million and sixty) euros, composed of 20 000 000 (twenty million) A-shares with the nominal value of 0.60 euros (sixty eurocents) per share and 1 (one) preferred B-share with a nominal value of 60 (sixty) euros.

The one B-share has been issued with the right of veto to the shareholder when voting on the following issues: amending the Articles of Association, increase and decrease of share capital, issuance of convertible bonds, acquisition of own (treasury) shares, deciding on the merger, division, transformation and/or dissolution of AS Tallinna Vesi, and, deciding other issues related to the activities of the AS Tallinna Vesi that have not been placed in the sole competence of the General Meeting by law that either the Management Board or the Supervisory Board have put to the vote of the General Meeting. In 2013 and 2012, the B-share granted the holder the preferential right to receive a dividend in an agreed sum of 600 (six hundred) euros.

The General Meeting of the Shareholders has the authority to decide the emission and buyback of the shares, following the principles established in the Articles of Association. The Management Board does not have any respective authorities.

As of 31 December 2013 and 2012 United Utilities (Tallinn) B.V. owned 7 060 870 (35.3%) A-shares, the City of Tallinn owned 6 939 130 (34.7%) A-shares and 1 (one) B-share, with 6 000 000 shares in free float. Other direct shareholders each owned less than 5% of the shares as of 31 December 2013 and 2012.

As of 31 December 2013 from all Supervisory Board and Management Board members Riina Käi owned 100 shares (2012: Riina Käi 100 and Leho Võrk 179 shares). Dividends declared and paid are disclosed in note 22.

Contingent income tax on the dividend payments from retained earnings is described in note 14.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 17. REVENUE

| | for the year ended 31 December | |
|---|---|---|
| **Revenues from main operating activities** | **2013** | **2012** |
| Total water supply and waste water disposal service, incl: | 47 737 | 47 912 |
| Private clients, incl: | 23 642 | 23 789 |
| Water supply service | 13 022 | 13 096 |
| Waste water disposal service | 10 620 | 10 693 |
| Corporate clients, incl: | 19 053 | 18 767 |
| Water supply service | 10 585 | 10 248 |
| Waste water disposal service | 8 468 | 8 519 |
| Outside service area clients, incl: | 4 308 | 4 524 |
| Water supply service | 1 095 | 1 028 |
| Waste water disposal service | 2 730 | 2 684 |
| Storm water disposal service | 483 | 812 |
| Over pollution fee | 734 | 832 |
| Storm water treatment and disposal service | 3 137 | 3 713 |
| Fire hydrants service | 287 | 202 |
| Construction service and design | 1 146 | 351 |
| Other works and services | 780 | 746 |
| **Total revenues** | **53 087** | **52 924** |

100 % of AS Tallinna Vesi revenue was generated within the Estonian Republic.

## NOTE 18. STAFF COSTS

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Salaries and wages | -5 233 | -5 150 |
| Social security and unemployment insurance taxation | -1 744 | -1 718 |
| **Total staff costs** | **-6 977** | **-6 868** |
| **Number of employees at the end of reporting period** | **304** | **313** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 19. COST OF GOODS SOLD, MARKETING AND ADMINISTRATIVE EXPENSES

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| **Cost of goods sold** | | |
| Water abstraction charges | -997 | -937 |
| Chemicals | -1 734 | -1 631 |
| Electricity | -3 392 | -3 695 |
| Pollution tax | -1 872 | -347 |
| Staff costs (Note 18) | -4 833 | -4 750 |
| Depreciation and amortization | -5 115 | -5 167 |
| Construction service and design | -947 | -277 |
| Other costs of goods sold | -3 615 | -3 533 |
| **Total cost of goods sold** | **-22 505** | **-20 337** |
| **Marketing expenses** | | |
| Staff costs (Note 18) | -375 | -373 |
| Depreciation and amortization | -244 | -326 |
| Other marketing expenses | -71 | -73 |
| **Total marketing expenses** | **-690** | **-772** |
| **Administrative expenses** | | |
| Staff costs (Note 18) | -1 769 | -1 745 |
| Depreciation and amortization | -339 | -295 |
| Other general administration expenses | -2 952 | -2 700 |
| **Total administrative expenses** | **-5 060** | **-4 740** |

## NOTE 20. OTHER INCOME / EXPENSES

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Profit from government grant | 0 | 2 037 |
| Connection fees | 117 | 96 |
| Depreciation of single connections | -111 | -91 |
| Doubtful receivables expenses (-)/expense reduction (+) | 45 | -169 |
| Other income (+)/expenses (-) | -126 | -177 |
| **Total other income / expenses** | **-75** | **1 696** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 21. FINANCIAL INCOME AND EXPENSES

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Interest income | 681 | 1 591 |
| Interest expense, loan | -1 087 | -1 358 |
| Interest expense, swap | -2 024 | -1 851 |
| Increase/decrease of fair value of swap | 2 255 | -89 |
| Other financial income(+)/expenses(-) | -21 | 1 |
| **Total financial income / expenses** | **-196** | **-1 706** |

## NOTE 22. DIVIDENDS

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Dividends declared during the period | 17 401 | 16 801 |
| Dividends paid during the period | 17 401 | 16 801 |
| Income tax on dividends paid | -4 625 | -4 466 |
| **Income tax accounted for** | **-4 625** | **-4 466** |

Income tax rates in 2013 and 2012 were 21/79.

| | | |
|---|---|---|
| *Paid-up dividends per shares:* | | |
| Dividends per A-share (in euros) | 0.87 | 0.84 |
| Dividends per B-share (in euros) | 600 | 600 |

## NOTE 23. EARNINGS PER SHARE

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |
| Net profit minus B-share preferred dividend rights | 19 935 | 22 598 |
| Weighted average number of ordinary shares for the purposes of basic earnings per share (in pieces) | 20 000 000 | 20 000 000 |
| Earnings per A share (in euros) | 1.00 | 1.13 |
| Earnings per B share (in euros) | 600 | 600 |

Diluted earnings per share for the periods ended 31 December 2013 and 2012 are equal to earnings per share figures stated above.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## NOTE 24. OPERATING LEASE

| **Leased assets** | **for the year ended 31 December** | |
|---|---|---|
| | **2013** | **2012** |
| Total operating lease expenses for computers and vehicles | 415 | 319 |
| Operating lease (compensated by customers) | 808 | 770 |

| Following periods operating lease payments from the non-cancellable contracts are as follows: | **as of 31 December** | |
|---|---|---|
| | **2013** | **2012** |
| Less than 1 year | 199 | 255 |
| 1-5 years | 224 | 296 |
| **Total minimum lease payments** | **423** | **551** |

The underlying currency of all lease contracts is euro. Leased assets have not been subleased.

## NOTE 25. RELATED PARTIES

Transactions with related parties are considered to be transactions with members of the Supervisory Board and Management Board, their relatives and the companies in which they have control or significant influence and transactions with shareholder having the significant influence. Dividend payments are indicated in the Statement of Changes in Equity.

**Shareholders having the significant influence**

| | **as of 31 December** | |
|---|---|---|
| **Balances recorded in on the statement of financial position of the Group** | **2013** | **2012** |
| Accounts receivable (Note 7) | 550 | 4 919 |
| Government grant receivables (Note 7) | 8 154 | 7 123 |
| Long-term government grant receivables (Note 8) | 2 161 | 3 746 |
| Trade and other payables | 197 | 187 |

| | **for the year ended 31 December** | |
|---|---|---|
| **Transactions** | **2013** | **2012** |
| Revenue | 3 424 | 3 877 |
| Government grant receivable accrued for constructing new pipelines | 0 | 4 429 |
| Purchase of administrative and consulting services | 1 020 | 998 |
| Financial income | 434 | 1 226 |
| **Short-term employee benefits to Management Board (excluding social tax)** | 294 | 326 |
| **Supervisory Board fees (excluding social tax)** | 40 | 40 |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

The Group's Management Board and Supervisory Board members are considered as key management personnel who have received only the contractual salary payments as disclosed above. In addition to this some Board Members have also received direct compensations from the companies belonging to the group of United Utilities (Tallinn) B.V. as overseas secondees. Such compensations are recorded on line "Purchase of administrative and consulting services".

18 thousand euros were paid to the Management Board members as termination fees in the year that ended on 31 December 2013 (in the year that ended on 31 December 2012: 45 thousand euros). The off balance sheet potential salary liability would be up to 93 thousand euros (excluding social tax) if the Supervisory Board would want to replace all Management Board members.

The information about AS Tallinna Vesi shares belonging to the related parties is disclosed in note 16. Paid-up dividends are described in note 22.

## NOTE 26. SUBSIDIARIES

| | | | Holding (%) as of 31 December | |
|---|---|---|---|---|
| | | | **2013** | **2012** |
| **Subsidiary** | **Location** | **Activity** | | |
| Watercom OÜ | Tallinn, Estonia | Provision of non-core services related to water business | 100 | 100 |

AS Tallinna Vesi registered Watercom OÜ on 25th May 2010.

## NOTE 27. SUPPLEMENTARY DISCLOSURES ON THE PARENT COMPANY OF THE GROUP

Pursuant to the Accounting Act of the Republic of Estonia, information of the unconsolidated financial statements (primary statements) of the consolidating entity (Parent Company) shall be disclosed in the notes to the consolidated financial statements. In preparing the primary financial statements of the Parent Company the same accounting policies have been used as in preparing the consolidated financial statements. The accounting policy for reporting subsidiaries has been amended in the separate primary financial statements disclosed as supplementary information in the Annual Report in conjunction with IAS 27, Consolidated and Separate Financial Statements.

In the parent separate primary financial statements, disclosed to these consolidated financial statements (Supplementary disclosures), investments into the shares of subsidiaries are accounted for at cost less any impairment recognised.

### The separate reports on the Parent Company

According to the Estonian Accounting Law, the amount which can be distributed to the shareholders is calculated as follows: adjusted unconsolidated equity less share capital, share premium and reserves.

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## STATEMENT OF FINANCIAL POSITION

| | as of 31 December | |
|---|---|---|
| **ASSETS** | **2013** | **2012** |
| **CURRENT ASSETS** | | |
| Cash and cash equivalents | 29 879 | 23 354 |
| Trade receivables, accrued income and prepaid expenses | 14 579 | 18 246 |
| Receivables from subsidiary | 39 | 35 |
| Inventories | 424 | 353 |
| **TOTAL CURRENT ASSETS** | **44 921** | **41 988** |
| **NON-CURRENT ASSETS** | | |
| Other long-term receivables | 2 212 | 7 559 |
| Investment in subsidiary | 527 | 527 |
| Property, plant and equipment | 153 305 | 149 133 |
| Intangible assets | 1 003 | 1 087 |
| **TOTAL NON-CURRENT ASSETS** | **157 047** | **158 306** |
| **TOTAL ASSETS** | **201 968** | **200 294** |
| **LIABILITIES AND EQUITY** | | |
| **CURRENT LIABILITIES** | | |
| Current portion of long-term borrowings | 2 042 | 19 |
| Trade and other payables | 4 080 | 4 486 |
| Derivatives | 1 816 | 2 039 |
| Payables to subsidiary | 743 | 1 369 |
| Prepayments and deferred income | 2 488 | 2 221 |
| **TOTAL CURRENT LIABILITIES** | **11 169** | **10 134** |
| **NON-CURRENT LIABILITIES** | | |
| Deferred income from connection fees | 10 144 | 7 892 |
| Borrowings | 92 959 | 94 953 |
| Derivatives | 507 | 2 538 |
| Other payables | 9 | 9 |
| **TOTAL NON-CURRENT LIABILITIES** | **103 619** | **105 392** |
| **TOTAL LIABILITIES** | **114 788** | **115 526** |
| **EQUITY** | | |
| Share capital | 12 000 | 12 000 |
| Share premium | 24 734 | 24 734 |
| Statutory legal reserve | 1 278 | 1 278 |
| Retained earnings | 49 168 | 46 756 |
| **TOTAL EQUITY** | **87 180** | **84 768** |
| **TOTAL LIABILITIES AND EQUITY** | **201 968** | **200 294** |

## STATEMENT OF COMPREHENSIVE INCOME

| | for the year ended 31 December | |
|---|---|---|
| | **2013** | **2012** |

| | | |
|---|---|---|
| Revenue | 51 693 | 52 437 |
| Costs of goods sold | -21 578 | -20 014 |
| **GROSS PROFIT** | **30 115** | **32 423** |
| Marketing expenses | -690 | -731 |
| General administration expenses | -4 734 | -4 553 |
| Other income(+)/ expenses (-) | -76 | 1 291 |
| **OPERATING PROFIT** | **24 615** | **28 430** |
| Financial income | 2 932 | 1 587 |
| Net financial expenses | -3 109 | -3 285 |
| **PROFIT BEFORE TAXES** | **24 438** | **26 732** |
| Income tax on dividends | -4 625 | -4 466 |
| **NET PROFIT FOR THE PERIOD** | **19 813** | **22 266** |
| **COMPREHENSIVE INCOME FOR THE PERIOD** | **19 813** | **22 266** |
| Attributable profit to: | | |
| Equity holders of A-shares | 19 812 | 22 265 |
| B-share holder | 0.60 | 0.60 |
| Earnings per A share (in euros) | 0.99 | 1.11 |
| Earnings per B share (in euros) | 600 | 600 |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CASH FLOW STATEMENT

| | for the year ended 31 December 2013 | 2012 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Operating profit | 24 614 | 28 431 |
| Adjustment for depreciation/amortisation | 5 660 | 5 786 |
| Adjustment for income from government grants and connection fees | -117 | -2 043 |
| Other non-cash adjustments | 27 | 7 |
| Profit (-)/loss(+) from sale and write off of property, plant and equipment, and intangible assets | -134 | 30 |
| Change in current assets involved in operating activities | -210 | -262 |
| Change in liabilities involved in operating activities | -383 | -10 |
| **Total cash flow from operating activities** | **29 457** | **31 939** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Loans granted | 0 | -765 |
| Repayment of loan | 3 814 | 0 |
| Acquisition of property, plant and equipment, and intangible assets | -10 284 | -10 530 |
| Compensations received for construction of pipelines | 7 884 | 11 198 |
| Proceeds from sale of property, plant and equipment, and intangible assets | 159 | 2 |
| Interest received | 690 | 1 581 |
| **Total cash flow used in investing activities** | **2 264** | **1 486** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Interest paid and loan financing costs | -3 130 | -3 242 |
| Repayment of finance lease | -40 | -4 |
| Dividends paid | -17 401 | -16 801 |
| Income tax on dividends | -4 625 | -4 466 |
| **Total cash flow used in financing activities** | **-25 196** | **-24 513** |
| **Change in cash and cash equivalents** | **6 525** | **8 912** |
| **CASH AND EQUIVALENTS AT THE BEGINNING OF THE PERIOD** | **23 354** | **14 442** |
| **CASH AND EQUIVALENTS AT THE END OF THE PERIOD** | **29 879** | **23 354** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## *STATEMENT OF CHANGES IN EQUITY*

| | Share capital | Share premium | Statutory legal reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|
| **as of 31 December 2011** | **12 000** | **24 734** | **1 278** | **41 291** | **79 303** |
| Dividends | 0 | 0 | 0 | -16 801 | -16 001 |
| Comprehensive income for the period | 0 | 0 | 0 | 22 266 | 22 266 |
| **as of 31 December 2012** | **12 000** | **24 734** | **1 278** | **46 756** | **84 768** |
| Carrying amount of investments under control and significant influence | 0 | 0 | 0 | 0 | -527 |
| Value of investments under control and significant influence using the equity method | 0 | 0 | 0 | 0 | 432 |
| **Adjusted unconsolidated equity as of 31 December 2012** | **12 000** | **24 734** | **1 278** | **46 756** | **84 673** |
| **as of 31 December 2012** | **12 000** | **24 734** | **1 278** | **46 756** | **84 768** |
| Dividends | 0 | 0 | 0 | -17 401 | -17 401 |
| Comprehensive income for the period | 0 | 0 | 0 | 19 813 | 19 813 |
| **as of 31 December 2013** | **12 000** | **24 734** | **1 278** | **49 168** | **87 180** |
| Carrying amount of investments under control and significant influence | 0 | 0 | 0 | 0 | -527 |
| Value of investments under control and significant influence using the equity method | 0 | 0 | 0 | 0 | 555 |
| **Adjusted unconsolidated equity as of 31 December 2013** | **12 000** | **24 734** | **1 278** | **49 168** | **87 208** |

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2013 (thousand EUR)

## CONFIRMATION OF THE MANAGEMENT AND SUPERVISORY BOARDS

The Management Board has prepared the management report and the financial statements of AS Tallinna Vesi on 20 February 2014. The Supervisory Board of AS Tallinna Vesi has reviewed the annual report, prepared by the Management Board, consisting of Management Report and the financial statements, the Management Board's proposal for profit distribution and the independent auditors' report, and has approved the annual report for presentation on the Shareholders' General Meeting.

The annual report has signed by all the members of the Management Board and Supervisory Board.

| Name | Position | Signature | Date |
|---|---|---|---|
| Ian John Alexander Plenderleith | Chairman of the Management Board | | 20/2/14 |
| Aleksandr Timofejev | Member of the Management Board | | 20/2/14 |
| Riina Käi | Member of the Management Board | | 20.02.2014 |
| Robert John Gallienne | Chairman of the Supervisory Board | | 20.03.2014 |
| Steven Richard Fraser | Member of the Supervisory Board | | 19.03.14 |
| Simon Gardiner | Member of the Supervisory Board | | 19.03.2014 |
| Brendan Francis Murphy | Member of the Supervisory Board | BF Murphy | 19.03.2014 |
| Mart Mägi | Member of the Supervisory Board | | 19.03.2014 |
| Rein Ratas | Member of the Supervisory Board | | 19.03.2014 |
| Toivo Tootsen | Member of the Supervisory Board | | 19.03.2014 |
| Allar Jõks | Member of the Supervisory Board | | 19.03.2014 |
| Priit Lello | Member of the Supervisory Board | | 19.03.2014 |

**INDEPENDENT AUDITOR'S REPORT**

(Translation of the Estonian original)*

To the Shareholders of AS Tallinna Vesi

We have audited the accompanying consolidated financial statements of AS Tallinna Vesi and its subsidiary, which comprise the consolidated statement of financial position as of 31 December 2013 and the consolidated statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

## Management Board's Responsibility for the Consolidated Financial Statements

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

## Auditor's Responsibility

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

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

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

## Opinion

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

**Emphasis of Matter**

We draw attention to Note 3 to these consolidated financial statements, which describe the uncertainty related to the outcome of the lawsuit between AS Tallinna Vesi and Estonian Competition Authority. Our opinion is not qualified in respect of this matter.

AS PricewaterhouseCoopers

Ago Vilu
Auditor's Certificate No.325

Stan Nahkor
Auditor's Certificate No.508

25 February 2014

---

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