

APPROVED  
by the Order No 1K- of \_\_\_ April 2018  
of the Minister of Finance of the Republic  
of Lithuania

**LETTER**  
**ON THE STATE EXPECTATIONS RELATED TO THE ACTIVITIES of “LIETUVOS ENEGIJA“**  
**UAB GROUP OF COMPANIES**

**Directions of the Company activities**

The activities of "Lietuvos Energija", UAB Group of Energy Companies (hereinafter - the Group of Companies) include production and supply of electricity and heat, trade in and distribution of electricity, trade in and distribution of natural gas, as well as the maintenance and development of the electricity infrastructure.

The Group of Companies manages and operates the most important electricity production capacities in Lithuania that ensure security of energy supply, a distribution network covering the entire territory of the country, and serves more than 1.6 million consumers throughout Lithuania, offers electricity supply services to customers abroad, also operates 8.5 thousand km of distribution pipelines, supplies gas to more than 560 thousand customers, implements development projects of strategic importance, pursues the objectives of the National Energy Strategy.

The Group of Companies consists of: electricity and heat production company “Lietuvos energijos gamyba“, AB, AB “Energijos skirstymo operatorius“, UAB “Lietuvos dujų tiekimas“, UAB LITGAS, UAB *NT Valdovs*, UAB “Transporto valdymas“, UAB “Energijos tiekimas“, UAB “VAE SPB“, UAB Energetikos paslaugų ir rangos organizacija, UAB Duomenų logistikos centras, UAB Technologijų ir inovacijų centras, UAB Verslo aptarnavimo centras, UAB Elektroninių mokėjimų agentūra, UAB Energijos sprendimų centras, *SIA Geton Energy, OU Geton Energy, Geton Energy sp.z.o.o.*, UAB “Eurakras“, *Tuulueenergia OU*, Lietuvos Energija Support Foundation.

By the Order of 7 June 2013 the Minister of Finance of the Republic of Lithuania approved, and by the Order of 1 June 2017 updated the Guidelines for the Corporate Governance Model of the Group of Energy Companies establishing the general principles of corporate governance for the Group of Companies. The aim is to assess, through the application of the principles and model of corporate governance, the expectations of stakeholders, to align them with each other, and to link to measurable objectives and indicators. An integrated management and control system is the main tool for implementing and maintaining corporate governance. The purpose of this system is to ensure the timely and effective achievement of objectives and their compliance with stakeholder expectations.

“Lietuvos energija“, AB (hereinafter - the Company), which is the parent company of the Group, is responsible for the transparent management and coordination of the Group's activities, increase of efficiency in order to provide the customers with competitive services and socially responsible increase of long-term value for the State.

**Performance expectations and evaluation**

*Strategic directions*

Directions of the activities of the Group of Companies in 2018–2025 - sustainable, socially responsible development by further building a modern, globally competitive energy company. The shareholder expects consistent and sustainable growth of the Group of Companies so that the international competitiveness of the Company and of the country would be promoted through modernization of the energy infrastructure and strengthening of new energy competencies.

*Creating added value for Lithuanian economy through the development*

It continues to be important for the Group of Companies to remain a leader in progress and efficiency in the energy sector in order to create added value for Lithuanian economy. It is important to ensure sustainability in the course of development operations by balancing between each other the actions of implementation of strategic generation projects, infrastructure management and green energy development, by implementing innovative energy solutions, and by expanding the directions of commercial organization activities:

- Strategic generation direction: contribution to the implementation of the National Energy Strategy, through the development and support of the existing or new generation capacity, as well as the provision of systemic (reserve, balancing, etc.) services.
- Network infrastructure development: ensuring the implementation of advanced solutions, compliance of the scope of infrastructure with the current needs of the customers, its effectiveness in terms of price and quality, and the digitization of the electricity distribution network which is scheduled to be completed by 2025.
- Green generation direction: investment which is based on market conditions, a significant contribution to the implementation of the green generation objectives referred to in the National Energy Strategy;
- Service direction: the existing services are provided or new - advanced (new generation) services are developed, by focusing on the implementation of modern solutions that meet the modern needs of the local and global market which would ensure sustainable competitiveness and continuous growth.

In implementing each of the identified directions - to seek going beyond the local market, and, where there are preconditions and opportunities, to pursue regional or international competitiveness by applying the principles of partnership with technology companies, international energy companies or financial institutions.

In addition to investment in production capacity and infrastructure development, which allow ensuring efficient activities in the field of energy, competitiveness of the country's economy, provision of quality energy services, the Group of Companies should continue the Company digitization program, and investing in start-ups that develop new services in energy sector.

The Company must also continue implementing the initiative to apply the latest technologies and must innovate. In this way, through close cooperation with the local and international business and with the scientific community, the potential for the export of innovative energy products and services would be developed. By implementing energy efficiency solutions, the Group of Companies would reduce energy costs of the customers, and this way would increase their competitiveness in the domestic and international markets.

*Strengthening the value chain by increasing operational efficiency and improving the quality of services*

Affordable, reliable, quality services that meet modern customer needs, and competitive energy prices for the customers must remain a priority for the Group of Companies. The following elements are important: the consistent improvement of network reliability indicators (electricity and gas SAIDI and SAIFI), shortening the deadlines for connecting new customers to the electricity and gas networks, digitization of network and management processes (“smart meter“ and other smart solutions), and the implementation of distributed generation solutions.

The Company must continue striving to refine the activities by abandoning non-core activities, and expand and diversify the portfolio of core activities by increasing efficiency of both basic as well as of the service and support functions. The Group of Companies must also actively participate in the process of implementing the National Energy Strategy in order to ensure the development of Lithuanian energy sector and its integration into European energy networks.

The Company should continue to search for ways to increase the volume of electricity production and invest in energy production from renewable energy sources (RES), by encompassing the development of new wind farms and other RES, and the consolidation of the green generation that is managed by the Group of Companies, by allocating investment in the value chain not only for Lithuania, but also for the countries in the region or other countries.

In 2018–2025, during the Strategy implementation phase, the Company must continue to ensure the return on equity (ROE) set by the Government of the Republic of Lithuania, which has been set not less than 5.7 percent for the period 2016–2018. When the investment is made outside Lithuania, the related risks should be adequately assessed, and an appropriate return on capital should be ensured.

The Group of Companies must maintain a consistent implementation of dividend policy<sup>1</sup> by coordinating the implementation of investment that is of strategic importance to the State (for example, securing funding of CHPs projects, the development of Kruonis Pumped Storage Plant, etc.) with the management of debt increase risk until the commissioning of new capacities, to pay, respectively, on average from 60 to 85 percent of the distributable profits of the Group of Companies in dividends to the State budget in the long term.

In investing, it is appropriate to continue applying the balanced financing measures: 1) to pursue for optimal structure of borrowed and equity capital and diversify the sources of financing the activities of the Group also through the use of the instruments of international financial markets, 2) to create, where possible, added value for the shareholder and benefits to the general society from the partnership with a private capital; 3) to allocate part of the profit generated for the development of key activities, thus ensuring the implementation of the expectations of the shareholder, customers and employees. The following indicators should be met to achieve an optimal level of financial debts of the Group of Companies: the ratio of financial debt to equity should not exceed 1.0, and the financial debts of the Group of Companies in the long-term should remain at the level of no more than 4 annual profits before interest, tax, depreciation and amortisation (EBITDA).

*An example of good governance practice*

The Group of Companies must continue to follow the requirements of the Organization for Economic Co-operation and Development (OECD), of *the Baltic Institute of Corporate Governance (BICG)*, and of NASDAQ and LUXEMBOURG Stock Exchanges, and the best international corporate governance practices, and thus to show for other state-owned enterprises an example to follow. The Group of Companies must maintain the level of maturity of corporate governance, and the highest index of the Corporate Governance Level which is awarded through the evaluation made by the Management Coordination Centre. In accordance

with the Transparency Guidelines<sup>ii</sup>, the Group of Companies must apply in all its activities the highest standards of transparency and the principles of depoliticised activities. In the opinion of the shareholder, for a greater transparency and an example of good practice for other state-owned enterprises, the subsidiaries of the Company should also pursue the principles defined in the Transparency Guidelines, i.e. to make publicly available an aggregated information (except for sensitive commercial information) about their strategic directions, the composition of the management and supervisory bodies, the financial and operational results, wages of the employees, and the remuneration of the collegial bodies. It is also important to maintain a purposeful centralized model of service and support activities, to continue the Operational Excellence program, thus seeking to improve the internal processes by increasing operational efficiency and improving quality.

#### *Transparent, responsible and value-based activities*

Creating sustainable value of the Group of Companies is unimaginable without transparent and socially responsible activities, decision-making based on values and ethical norms. Furthermore, the Group of Companies must be a responsible and competitive employer - to maintain and develop the competencies of the employees, to purposefully invest in high qualification, to develop systems of competence and motivation, substitutability and attraction of talents, which are in line with market conditions, and which would allow the organization to operate effectively under the conditions of global competition, and to create long-term value for Lithuanian economy.

#### **Accountability**

It is appropriate for the Supervisory Board, which is the supervisory body of the Company and of the Group of Companies, to maintain the current practice, and submit periodically on a quarterly basis to the shareholder (Ministry of Finance) a summary activity report of the Group of Companies.

The shareholder expects that the Management and Supervisory Bodies of the Group of Companies will continue good corporate governance practices, and will once a year evaluate their activities and will also agree on further steps in order to improve the activities of these management and supervisory bodies.

---

<sup>i</sup> Resolution No 20 of the Government of the Republic of Lithuania of 14 January 1997 on Dividends in Respect of Company Shares owned by the State, and Profit Contributions of State Enterprises

<sup>ii</sup> The Resolution No 1052 of the Government of the Republic of Lithuania of 14 July 2010 on the Approval of the Description of the Guidelines for Ensuring the Transparency of State-owned Enterprises