State joint stock company
"Latvijas dzelzceļš"

Consolidated Annual Report for 2020

TABLE OF CONTENTS

Translation note: This version of Consolidated Annual Report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of Consolidated Annual Report takes precedence over this translation.

INFORMATION ABOUT THE GROUP'S PARENT COMPANY

Name of the Group's parent company	LATVIJAS DZELZCEĻŠ
Legal status of the Group's parent company	State joint stock company
Address	Gogoļa iela 3, Riga, LV-1547
Uniform registration number	40003032065
Date of registration in the Register of Enterprises	01.10.1991
Date of registration in the Commercial Register	10.09.2004
Place of registration	Riga
Date of issue of the merchant registration certificate	10.09.2004
Shareholder	Republic of Latvia (100%)
Holder of capital shares	Ministry of Transport of the Republic of Latvia Gogoļa iela 3, Riga, LV-1743
Supervisory body	Council of the company
Council	Jānis LANGE, chairman of the Council Andris MALDUPS, member of the Council Andris LIEPIŅŠ, member of the Council Reinis CEPLIS, member of the Council Aigars LAIZĀNS, member of the Council until 01.02.2021
Governing body	Management Board of the company
Board	Maris KLEINBERGS, chairman of the Management Board Ēriks ŠMUKSTS, member of the Management Board Vita BALODE-ANDRŪSA, member of the Management Board from 01.06.2020 Andris LUBĀNS, member of the Management Board until 01.06.2020 Ainis STŪRMANIS, member of the Management Board until 13.03.2020
Auditors	SIA PricewaterhouseCoopers Uniform registration No. 40003142793 LACA commercial company licence No. 5 Kr.Valdemāra iela 21-21 Riga, LV-1010 Latvia Responsible sworn auditor Ilandra Lejiņa Certificate No. 168
Reporting year	1 January 2020 – 31 December 2020

Subsidiaries

SIA "LDZ CARGO"	
Uniform registration number	40003788421
Address	Dzirnavu iela 147, k-1, Riga, LV-1050
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
SIA "LDZ ritošā sastāva serviss"	
Uniform registration number	40003788351
Address	Turgeņeva iela 21, Riga, LV-1050
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
SIA "LDZ infrastruktūra"	
Uniform registration number	40003788258
Address	Gogoļa iela 3, Riga, LV-1050
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
SIA "LDZ apsardze"	
Uniform registration number	40003620112
Address	Zasas iela 5-3, Riga, LV-1057
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
AS "LatRailNet"	
Uniform registration number	40103361063
Address	Turgeņeva iela 21, Riga, LV-1050
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
SIA "LDZ Loģistika"	
Uniform registration number	40003988480
Address	Dzirnavu iela 147, k-2, Riga, LV-1050
Shareholding, %	100% shareholder is VAS "Latvijas dzelzceļš"
Reporting year	01.01.2020 – 31.12.2020
Subsidiary of SIA "LDZ ritošā sastāva serviss" SIA "Rīgas Vagonbūves uzņēmums "Baltija""	
Uniform registration number	40103419565
Address	Turgeņeva iela 14, Riga, LV-1050
Shareholding, %	100% shareholder is SIA "LDZ ritošā sastāva serviss"
Reporting year	01.01.2020 – 31.12.2020

MANAGEMENT REPORT

ON THE OPERATING ACTIVITY OF THE LATVIJAS DZELZCEĻŠ GROUP IN 2020

1. AN OVERVIEW OF THE *LATVIJAS DZELZCEĻŠ* GROUP

The *Latvijas dzelzceļš* Group (hereinafter "*the Group"*) operates the railway infrastructure for public use, provides railway transport and related services.

The *Group* consists of the parent company of the *Group* – the state joint stock company "Latvijas dzelzceļš" (hereinafter "*Latvijas dzelzceļš"* or "*the Company"*), SIA "LDZ CARGO", SIA "LDZ ritošā sastāva serviss", SIA "LDZ infrastruktūra", SIA "LDZ apsardze", SIA "LDZ Loģistika", AS "LatRailNet", as well as the subsidiary of SIA "LDZ ritošā sastāva serviss", SIA "Rīgas Vagonbūves uzņēmums "Baltija"".

To ensure the development and competitiveness of *the Group's* business units, a coordinated *Group* strategy and objectives have been developed to ensure optimal allocation of production and investment resources between the business units and the *Group's* companies, coordination of decision-making and effective control of their implementation. *Latvijas dzelzceļš* represents the *Group's* interests at the international level.

Latvijas dzelzceļš is one of the largest companies in Latvia, making a significant contribution to the national economy through its economic activity by ensuring the use of the railway infrastructure for passenger and freight traffic.

The main task of *Latvijas dzelzceļš* is to operate the railway infrastructure for public use and provide safe, high-quality, and efficient railway services that serve the best interests of the Latvian State and its national economy. At 31 December 2020, the extended length of the rail network operated by *Latvijas dzelzceļš* as a public-use railway infrastructure operator was 3,158.1 km, including technologically integrated station and access roads and other infrastructure facilities.

Latvijas dzelzceļš provides the minimum package of services required for access to the public railway infrastructure and access to the public railway infrastructure combining the railway infrastructure with service stations, services, freight wagon handling, wagon maintenance and testing, electricity distribution and trading services, leasing services, information technology services, electronic communication services, services of a principal, as well as other specified services in Section 12^1, Paragraph one of the Railway Law.

SIA "LDZ CARGO" is engaged in providing local and international rail freight services, traction services, the use of freight wagons and the organization of international passenger transport services.

SIA "LDZ ritošā sastāva serviss" is engaged in providing repair services of locomotives and wagons, equipment as well as upgrading of locomotives, rental of locomotives.

SIA "LDZ infrastruktūra" is engaged in providing repair and rental services for track equipment, as well as in providing track welding services.

SIA "LDZ apsardze" is engaged in providing physical and technical security services to the Group's companies, other companies, and individuals, as well as on the road guarding of freights.

SIA "LDZ Loģistika" is engaged in providing freight forwarding and logistics services, as well as the acquisition of new flows of goods and the organization of rail freight transport between European and Asian countries.

AS "LatRailNet" is engaged in carrying out the essential functions of the railway infrastructure operator. This company approves the fees for the minimum package of access services, as well as for the infrastructure connecting the infrastructure to service areas, distributes the capacity of the railway infrastructure, and makes decisions on the scheduling of trains of a particular carrier.

The subsidiary of SIA "LDZ ritošā sastāva serviss" is SIA "Rīgas Vagonbūves uzņēmums "Baltija"", it was founded with a view to developing rail wagon construction in Latvia.

To improve good governance practices and develop understanding of social responsibility in the *Group*, as well as to strengthen sustainable yet innovative thinking in the tradition-rich railway sector, Latvijas dzelzceļš has been preparing annual sustainability reports in accordance with the internationally recognised Global Reporting Initiative (GRI) guidelines (currently "the GRI standard") since 2016. The *Group's* companies also participate in the Sustainability Index each year when assessing their sustainability performance. In June 2020, having assessed the performance of the *Group's* companies in terms of sustainable development and good governance practices, Sustainability Index experts repeatedly awarded Platinum rating to *Latvijas dzelzceļš*. SIA “LDZ CARGO” was also awarded the Platinum category. Other dependent companies were awarded the following ratings: SIA “LDZ ritošā sastāva serviss” – the Gold category, SIA “LDZ apsardze” – the Silver category and SIA “LDZ Loģistika” – the Bronze category.

In view of the trends in freight transport, the review of processes in the *Group's* companies continued in 2020, resulting in a reduction in the number of employees.

In 2020, the average number of people employed by the *Group* was 8 539. Compared to 2019, the number of employees declined by 1 616.

2. OPERATING PERFORMANCE

In 2020, the consolidated revenue of the *Group* was EUR 253 866 thousand. Compared to 2019, consolidated revenue decreased by EUR 83 779 thousand (24.8%), due to the decrease of EUR 68 253 thousand (33.2%) in freight revenue, which represents the largest part of the *Group's* consolidated net revenue.

Most of the *Group's* revenues are generated by SIA “LDZ CARGO”, which is a major transport and logistics company in Latvia.

In 2020, 24 113 thousand tonnes of freight were transported by rail, which is about 17 377 thousand tonnes or 41.9% less than in 2019, when 41 490 thousand tonnes were transported. The largest share – 67.6% was accounted for by import cargo, the volume of which was 16 305 thousand tonnes in 2020, which was 50.5% less than in the previous year. As for the origin of cargo transported by SIA “LDZ CARGO”, the largest counterparty is Russia, which accounted for 61.2% of the total cargo. The share of other countries in the volume of transported cargo is as follows: Belarus - 27.0%, Lithuania - 9.0%, Ukraine - 1.5%, Kazakhstan - 0.4%, Estonia - 0.2%, Uzbekistan - 0.2% and others - 0.5%.

The largest share of transport (almost half of the total) consisted of the transport of oil and oil products (26.6%) and coal (16.8%). Fertilizer transport accounted for 9.5% of total transport, wood and wood products for 8.6%, and feedstuff transport for 8.5%. The share of other types of goods amounted to 30% of total freight transport in 2020.

In freight transport, *Latvijas dzelzceļš* railway infrastructure transported 7 755 million tonne-kilometres. Compared to the previous year, its volume decreased by 46.5%. SIA “LDZ CARGO” ran 6 017 million tonne-kilometres in 2020.

The *Group's* consolidated revenue for the use of infrastructure decreased by EUR 11 016 thousand (19.1%) compared to 2019, with a decrease in revenues from both private freight operators and passenger transportation under the public service agreement.

The *Group* company SIA “LDZ CARGO” is the only company in the land transport sector in Latvia offering passenger transport by rail in international traffic. SIA “LDZ CARGO” provides passenger transport in international traffic on the routes Riga-Moscow, Riga-St. Petersburg, as well as offers Belarusian Railway train on the route Riga-Minsk, Ukrainian Railway train on the route Riga-Vilnius-Minsk-Kiev. SIA “LDZ CARGO” in international rail passenger traffic 2020 carried 17 737 passengers during the year, between January and March, which was 89.6% less compared to the 12 months of 2019. International passenger traffic declined due to the Covid-19 pandemic, as containment measures were introduced in March 2020, and all international rail passenger traffic was halted.

The *Group's* after-tax loss was EUR 35 515. The *Group's* consolidated equity amounted to EUR 393 919 thousand at 31 December 2020, which is about EUR 3 119 thousand or 0.8% less than in 2019.

The *Group's* companies pursue prudent liquidity risk management by ensuring that sufficient borrowing resources are available to pay liabilities as they fall due. As at 31 December 2020, the Group's current assets exceeded current liabilities by EUR 35 140 thousand, resulting in an overall liquidity ratio (current assets to current liabilities) of 1.4. Current liabilities include deferred revenue of EUR 19 341 thousand related to the investment of EU projects and state budget funds in public railway infrastructure, therefore there is a low risk that financial resources will be required to cover these obligations. The overall liquidity ratio, excluding the deferred revenue related to the investment of EU projects and state budget funds in public railway infrastructure, would be 1.7. As at 31 December 2020 and the beginning of 2021, none of the long-term loan agreements was breached on covenants.

Despite the decrease in freight volumes, the *Group* has continued to ensure the quality of infrastructure and services, as well as an adequate level of safety, and the *Group's* total investments in 2020 amounted to EUR 16 044 thousand (excluding investments within the *Group*). Financial resources are invested in the repair, upgrade and acquisition of property, plant and equipment, intangible investments and the construction of new facilities.

Of these, the total investments of *Latvijas dzelzceļš* in 2020 amounted to EUR 11 256 thousand. EUR 9,680 thousand was invested in capital repairs of the railway infrastructure, EUR 185 thousand was invested in the restoration of existing IT systems. In the reporting year, EUR 653 thousand was spent on the purchase of technological equipment for the repair and maintenance of tracks, as well as equipment for the further development of information systems and means of communication and other intangible assets. EUR 738 thousand was invested in the expansion of infrastructure.

Of these, the total amount invested by SIA “LDZ CARGO” was EUR 2 122 thousand in 2020, which were invested in the restoration, upgrading and acquisition of property, plant and equipment. In 2020, funds were invested in the capital repairs, upgrading of diesel locomotives and the introduction of new technologies to improve the technological process of the work.

Of these, a total of EUR 1 971 thousand was invested by „LDZ ritošā sastāva serviss” in 2020. Of this, the largest projects were: capital repairs of locomotives according to the rules of repair of diesel locomotives - 2TE116 locomotives in the amount of VR (medium repairs) and GR (main repairs) were carried out in order to provide carriers with the necessary traction rolling stock for freight transport for EUR 1 742 thousand, ROBOKON 4155 semi-automatic device for inspection and sorting of storage rolls (works performed for the total amount of EUR 38 thousand) and ROBOKON 4156 semi-automatic device for inspection and sorting of storage rolls (works performed for the total amount of EUR 48 thousand).

3. OBJECTIVES AND FUTURE DEVELOPMENT

With a sharp decline in freight volumes, work will continue to drive efficiencies of the *Group's* operations by reviewing business, organizational and technological processes to increase the efficiency of the *Group's* operations and reduce costs, as well as to ensure the competitive and sustainable operation of the *Group* in the future.

As a significant part of the costs is related to employee resources (labour costs), the review of organizational and technological processes started by the Group as well as the reduction of staff will continue in 2021.

In 2020, the Management Board of *Latvijas dzelzceļš* and the broader management team actively worked on resolving the Group's existing financial situation, optimising costs and promoting the Group's overall efficiency, as well as paying special attention to the issues of the Group's future development - developing a new business model and planning the further development of passenger rail transport infrastructure.

Pursuant to resolution No. VL-38/237 of Management Board of *Latvijas Dzelzceļš* dated 12.06.2020, the future directions of the Company in the field of railway infrastructure development, freight transport and maintenance of rolling stock and ancillary services have been approved and considered by the Council pursuant to resolution No. PA 1.2/16-1 dated 17 June 2020.

The *Group's* new business model is based on the assets at its disposal – a high-quality infrastructure, a qualified team and many years of experience. At the same time, the *Group's* existing areas of activity will be significantly expanded by developing expeditionary activities, including sea expedition, road expedition, warehousing services, additional post-processing services, etc.

The future priorities of the business direction of cargo transportation and logistics are cargoes to and from Belarus, Ukraine, special cargoes, close cooperation with port authorities and port terminals, a unified logistics offer.

To increase the efficiency and productivity of the *Group's* companies, further emphasis is placed on the thoughtful use of the human and material resource base and the reduction of costs. Consequently, the *Group's* technological processes, functions to be performed and management capabilities will continue to be reviewed.

Upon completion of work on the *Group's* new business model and in accordance with the resolution No. A 1.1/2-1 of the shareholder meeting of 30 April 2020, *Latvijas dzelzceļš* has developed the *Company's* medium-term operational strategy until 2025, for which the opinions of the Ministry of Transport and the Cross-Sectoral Coordination Centre have been received.

On 18 January 2021, the Management Board of *Latvijas dzelzceļš*, pursuant to resolution No. VL-3/10, adopted the updated draft strategy and action plan, considering the recommendations of the Ministry of Transport and Cross-Sectoral Coordination Centre. The medium-term operational strategy of the Company will be approved after the Cabinet approves the overall strategic goal of the Company.

Considering the development of *Latvijas dzelzceļš* and its future competitiveness, along with regular capital expenditure in maintaining the level of quality and safety of the infrastructure within the limits of financial possibilities, work will continue on the implementation of the project “Upgrading of the Riga Railway Junction section Sarkandaugava – Mangaļi – Ziemeļblāzma”, co-financed by the Cohesion Fund, for the construction of which the contract was concluded in 2019.

At the same time, there have been several developments related to the implementation of new projects with the support of the Cohesion Fund.

At the Cabinet meeting held on 19 May 2020, the Information Report on the redistributions of the European Union structural funds and the Cohesion Fund and solutions aimed at minimising the consequences of Covid-19 was reviewed, deciding that the proposal to reallocate Cohesion Fund financing to alternative transport projects would be supported in the light of the discontinued rail infrastructure projects. As for the projects of the railway sector, through the necessary amendments to the Cabinet Regulation, the Ministry of Transport should address the issue of co-financing of the State budget of 19.3 million EUR (15% of the total eligible costs of the projects) for the budgeted alternative projects in the railway sector.

At present, work on the preparation of documentation for the projects “Modernisation of the railway passenger infrastructure”, “Modernisation of railway infrastructure for increasing speed of trains” and “Building of fencing and pedestrian crossings in railway infrastructure facilities” is underway.

Under the project “Modernisation of railway passenger infrastructure” procurement for the construction in four railway lines has been announced, i.e., Riga-Jelgava, Riga-Tukums II line, Riga-Krustpils and Zemitani-Skulte line, where a total of 48 railway passenger stations will be upgraded, including the construction of elevated platforms. On 5 January 2021, the tenders submitted by seven bidders were opened on parts 1-5 of the procurement (construction). An assessment of the tenders is expected to be completed in the first quarter of 2021, considering the time to receive answers to the clarifying questions about the qualifications and tenders of applicants. A complaint has been received for Part 6 of the procurement (the introduction of notification and video surveillance systems) and the procurement procedure was terminated. The procurement “Implementation of the common notification and video surveillance systems” was announced repeatedly at the end of February.

Ongoing work is being carried out in the implementation of the Action Plan for the reduction of noise on railway lines with a traffic intensity of more than 30 000 trains per year for the period from 2019 to 2023, which was developed in accordance with the Law *On Environmental Pollution* and the requirements of Cabinet Regulation No. 16 *Noise Assessment and Management Procedure* of 7 January 2014.

Latvijas dzelzceļš and the entire transport and logistics sector of the country are in direct competition with the nearest neighbouring countries – Lithuania and Estonia – for connecting transport to the transit corridor of Latvia. The efficiency of infrastructure services will be one of the decisive factors in the competition for freight transport by rail.

The difficulties in maintaining financial stability resulting from the decline in freight transport and the lack of funding for the maintenance of passenger transport infrastructure are to be addressed in the manner laid down in the Multi-Annual Agreement.

In 2021, the main priorities and objectives of the *Group* and the *Company* will be related to a significant increase in the operational efficiency of the companies and the recovery and strengthening of the financial position, as well as the implementation and stabilisation of newly developed organizational and technological processes.

To facilitate the implementation of the *Group's* new business model, the largest subsidiaries – SIA “LDZ CARGO”, SIA “LDZ Loģistika” and SIA “LDZ ritošā sastāva serviss” have developed business plans until 2025 and action plans for 2021.

At the same time as reviewing the *Group's* businesses and promoting efficiency in 2021, great attention will be paid to diversifying target markets and cargo segments, winning cargo traffic in new markets, developing new services, etc.

In addition to these goals, the *Group* will actively work to develop comfortable and efficient infrastructure necessary to meet passengers' needs, and constantly work to promote safety on and around routes.

Considering the intense change processes in 2021, the *Group's* management team will ensure effective financial and human resources management, as well as implement comprehensive and transparent communication both within the *Company* and with customers, business partners, stakeholders and the public.

For SIA "LDZ CARGO" it is essential to maintain and strengthen the existing position in cargo transportation and pay special attention to attracting new cargoes from new markets and increasing the profitability of International Passenger Transportation, to ensure the development and competitiveness of business directions and constantly improve the quality, efficiency and productivity of services, to ensure the constant modernization and progress of offered services.

Rail freight in the Republic of Latvia is transported from the eastern borders of the country to the three largest ports of Latvia - Riga, Ventspils and Liepaja - via the major railway hubs of the eastern part of Latvia in Daugavpils and Rezekne, which form the East-West transit corridor connected to the railway line between the northern and southern borders of the country and linked to regional lines.

One of the development directions of SIA "LDZ CARGO" is to improve the quality of customer service and the level of customer satisfaction. To ensure the competitiveness of SIA "LDZ CARGO" under the existing market circumstances, it is necessary to maintain the existing customers and improve the process of customer acquisition, which ensures, among other things, better awareness of customer needs and the use of modern information exchange channels.

So, to achieve a faster and more convenient exchange of information between the carrier and the customer, SIA "LDZ CARGO" is constantly looking for solutions for this purpose.

SIA "LDZ CARGO" is actively involved in expanding the functionality of the developed Cargo Movement Management Information System. The functionality of the system provides for notification of customers, submission and use of the electronic consignment note, prior notification of customs authorities in electronic form of imported goods, preparation and submission of information on shipments in electronic form.

To ensure the efficient use of rolling stock and improve work technology, SIA "LDZ CARGO" budgeted funds for equipping locomotives with a video surveillance system and digital locomotive radio stations for purchase and installation, and in 2021 is planned to purchase freight cars.

In 2021, SIA "LDZ ritošā sastāva serviss" will continue to introduce more efficient and safe technologies for diesel locomotive operations. There are plans to equip the 2TE116 series diesel locomotives with a telemechanical system for driver supervision (TSKBM), which will enable diesel locomotives to be operated "in one person" without a driver assistant. In addition, there are plans to equip the diesel compartments of the locomotives of this series with an internal video monitoring system to ensure constant control and the possibility of monitoring the technical condition of the diesel compartment, the engine and the equipment.

In the beginning of 2021, SIA "LDZ ritošā sastāva serviss" developed and implemented a technical project to equip 2TE116 series diesel locomotive diesel engines with autonomous heating system WEBASTO. There are plans to develop such a project to equip diesel engines of the CHME3 series with the autonomous heating system WEBASTO.

In the first half of 2021, in cooperation with CZ LOKO AS work on the elimination of defects detected by the main generators of diesel locomotives of the 2M62UM series will continue. The necessary measures are being taken to speed up the fault elimination process, and the main generator bearings could be replaced in Daugavpils locomotive repair centre without the generators being transported to the Czech Republic.

On the site Daugavpils Wagon Repair Centre of SIA "LDZ ritošā sastāva serviss" the started project will be continued to be able to carry out the repair of the wheel sets of freight wagons of Western European (1435 mm width) with the replacement of the elements. In 2021, the wheel processing machine will be modernized. For modernisation, the wheel machining machine was delivered to OOO "Stankozavod TBS", Russia. After completion of the upgrading, the wheel processing machine is planned to be put into operation in the first half of 2021.

To participate in the procurement for locomotive repairs and to prove the qualification of SIA “LDZ ritošā sastāva serviss” to the requirements of the laws and regulations on the execution of repairs of diesel locomotives of Russian Federation, efforts have been made to expand the reference range of the deemed number issued to SIA “LDZ ritošā sastāva serviss” as well as the data in the register of international railway companies "С ЖА".

In the first half of 2021, SIA “LDZ ritošā sastāva serviss” will seek to obtain a safety certificate of a new model that meets all the requirements of the European Union.

A 2TE10 series diesel locomotive re-motorization project is planned for 2021, under which 2TE10 series diesel locomotives will be equipped with D49 diesel engines previously used on TEP70 series passenger diesel locomotives.

Ten 2M62U series diesel locomotives and seven 2TE10 series diesel locomotives would be leased to Latvian or foreign customers in 2021.

The goals of SIA “LDZ Loģistika” are to increase transport volumes by developing intermodal and multimodal logistics services, creating strategic partnerships, acquiring existing and new markets, attracting new customers to the Latvian transit industry, developing marketing and sales of logistics services. It also aims to promote domestic rail freight transport, support the use of rail infrastructure for public use and create development opportunities to support the Latvian economy. Achieving these goals also requires the accumulation and application of logistics excellence in educational programmes and technological development.

The business plan of SIA “LDZ Loģistika” until 2025 is based on the company's vision of being a strong player in the logistics industry. The top priorities for the period until 2025 are to promote cooperation with ports, terminals and road carriers, increase freight volumes, develop the 3PL service basket and develop freight corridors, both for the provision of interstate transportation (Europe-Russia, Kazakhstan and Central Asia) and for the provision of regional or domestic freight transportation (Baltics, Ukraine, Belarus).

4. RESEARCH AND DEVELOPMENT ACTIVITIES

Aware of the challenges of the coming years in the field of attracting skilled workers, *Latvijas dzelzceļš* is not only developing the training opportunities that it offers at the *Company's* Training Centre, but in recent years, in cooperation with Riga Technical University, has introduced several new specialisations in the training programmes of Railway Electrical Systems and railway telecommunications. The mastery of these programmes allows not only the development of the technological capacities of the company and the *Group*, but also the provision of skilled workers necessary for the provision of maintenance services for the electrified railway infrastructure in the future.

5. FOREIGN BRANCHES AND REPRESENTATIVE OFFICES

Since 2012, there is a representative office of *Latvijas dzelzceļš* in the capital of Russia Moscow.

Since 2017, there is a representative office of *Latvijas dzelzceļš* in the capital of Belarus Minsk.

The *Group* has no foreign branches.

6. EVENTS AFTER THE DATE OF PREPARATION OF THE ANNUAL REPORT FOR 2020 AND GOING CONCERN CONSIDERATIONS

Freight traffic trends to be observed in 2020 and 2021, as well as current potentially turbulent global and regional developments, including the coronavirus COVID-19 pandemic, suggest that freight traffic volumes will not improve significantly.

However, despite the difficulties, the management of Latvijas dzelzceļš concludes that the going concern principle is applicable for the preparation of the financial statements due to the implementation of the Group's new business model, the implementation of the crisis plan and the review of organizational and technological processes aimed at reducing costs in the future, as well as due to the receipt of the necessary public funding under the Multi-Annual Agreement "On the planning and financing of the maintenance and development of railway infrastructure of public use under the management of VAS *Latvijas dzelzceļš*, concluded between VAS *Latvijas dzelzceļš* and the Ministry of Transport. In addition, in 2021 the work on the implementation of the *Group's* new business model and the Company's medium-term operational strategy until 2025 will be continued.

The main task of the *Company* is to ensure the operation of the publicly used railway infrastructure and to provide safe, high-quality, and effective railway and logistics services in the best interests of the Latvian state and national economy. To fulfil this task, a Multi-Annual Agreement has been concluded with the Ministry of Transport, which provides for the procedure to ensure financial equilibrium/balance.

In 2020, the *Company* received an advance payment to ensure financial balance. The prepayment in the year and the additional funding required to achieve financial stability in 2020 has been recognised as part of other income in accordance with the recognition principles set out in IAS 20 *Accounting for government grants*. These principles determine the recognition of government grants at the time when there is reasonable assurance that the conditions attached to the receipt of the grant will be met. In addition, grants relating to the payment of costs should be recognised in the period in which the costs are incurred, provided there is reasonable assurance that the grant will be received in the future.

The criteria for the *Company* to receive the financial settlement payment are failure to meet the financial settlement conditions provided in the Multi-Annual Agreement. As the *Company* did not meet the financial settlement conditions provided for in the Multi-Annual Agreement in 2020, the criteria for receiving the financial settlement payments provided for in the Multi-Annual Agreement were accordingly met, and the receipt of an advance from the Department of Transportation provided reasonable assurance of the other party's intent and ability to comply with the conditions of the Multi-Annual Agreement, the financial settlement payments were recognised as revenue in 2020. A portion of the required financial settlement payment of EUR 9 503 295 to be received in 2021 has been recognised in the balance sheet under accrued income based on the liabilities and obligations set out in Multi-Annual Agreement.

Although the full amount of the financial settlement payment is recorded in revenue, there is uncertainty regarding the timing of receipt of the additional funds required by the Company. This uncertainty relates both to the funds to compensate for the costs of maintenance and restoration of railway infrastructure in full for the provision of public transport services throughout 2021 in accordance with the requirements of the concluded Multi-Annual Agreement and to the funding to ensure the financial stability of Latvijas dzelzceļš as part of the Multi-Annual Agreement.

7. STATEMENT OF RESPONSIBILITY OF THE MANAGEMENT BOARD

The Management Board of the parent company of the *Group* (hereinafter “*Management”*) is responsible for preparing the consolidated financial statements of the *Group*.

Consolidated financial statements on pages 15 to 56 are prepared based on the accounting records and supporting documents and gives a true view of the *Group's* financial position at 31 December 2020, its performance and cash flows for 2020.

The consolidated financial statements mentioned above are prepared in accordance with International Financial Reporting Standards (IFRS) adopted in the EU, based on the going concern principle. During the preparation of the consolidated financial statements, the decisions and assessments made by *the Management* have been prudent and reasonable.

The Group’s M*anagement* is responsible for ensuring the appropriate accounting system, maintaining the *Group's* assets, as well as for detecting and preventing fraud and other violations by the *Group*. The *Management* is responsible for compliance with the laws of the Republic of Latvia.

Chairman of the Management Board	M. Kleinbergs
Member of the Management Board	V. Balode-Andrūsa
Member of the Management Board	Ē.Šmuksts

This document is signed electronically with secure digital signature and contains time stamp

INDEPENDENT AUDITOR'S REPORT

To the Shareholder of State joint stock company “Latvijas dzelzceļš”

Our opinion

In our opinion, the accompanying consolidated financial statements set out on pages 15 to 56 of the accompanying consolidated annual report give a true and fair view of the financial position of SJSC “Latvijas dzelzceļš” (the “Company”) and its subsidiaries (together the “Group”) as at 31 December 2020, and the Group’s consolidated financial performance and consolidated cash flows for the year ended 31 December 2020 in accordance with the International Financial Reporting Standards as adopted by the European Union.

What we have audited

The Group’s consolidated financial statements comprise:

- the consolidated income statement for the year ended 31 December 2020,
- the consolidated statement of comprehensive income for the year ended 31 December 2020,
- the consolidated statement of financial position as at 31 December 2020,
- the consolidated statement of changes in equity for the year ended 31 December 2020,
- the consolidated statement of cash flows for the year ended 31 December 2020, and
- the notes to the consolidated financial statements which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

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

Independence

We are independent of the Group in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code) and the ethical requirements of the Law on Audit Services that are relevant to our audit of the consolidated financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the Law on Audit Services.

Reporting on Other Information Including the Management Report

Management is responsible for the other information. The other information comprises the Management Report, as set out on pages 5 to 11 of the accompanying consolidated annual report, but does not include the consolidated financial statements and our auditor’s report thereon.

Our opinion on the consolidated financial statements does not cover the other information.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

With respect to the Management Report, we also performed the procedures required by the Law on Audit Services. Those procedures include considering whether the Management Report is prepared in accordance with the requirements of the Law on Annual Reports and Consolidated Annual Reports.

Based on the work undertaken in the course of our audit, in our opinion, in all material respects:

- the information given in the Management Report for the financial year for which the consolidated financial statements are prepared is consistent with the consolidated financial statements; and
- the Management Report has been prepared in accordance with requirements of the Law on Annual Reports and Consolidated Annual Reports.

In addition, in light of the knowledge and understanding of the entity and its environment obtained in the course of our audit, we are required to report if we have identified material misstatements in the other information. We have nothing to report in this respect.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ilandra Lejiņa
Certified auditor in charge
Certificate No.168

Member of the Board

Riga, Latvia
15 March 2021

Independent Auditor's Report is signed electronically with a secure electronic signature and contains a time stamp.

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

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT
FOR 2020

(EUR' 000)

	NOTES	2020	2019
Revenue	4	253 866	337 645
Cost of goods sold	5	(285 933)	(339 494)
Gross loss		**(32 067)**	**(1 849)**
Administration costs	6	(19 239)	(25 480)
Other operating income	7	31 774	26 062
Other operating expenses	8	(14 366)	(5 142)
Income from long-term investments		1	330
Financial income	9	-	2
Financial costs	9	(2 227)	(2 237)
Loss before corporate income tax		**(36 124)**	**(8 314)**
Corporate income tax	10	609	(1 014)
Loss for the reporting year		**(35 515)**	**(9 328)**

The notes on pages 22 to 56 form an integral part of these consolidated financial statements.

Chairman of the Management Board M. Kleinbergs

Member of the Management Board V. Balode-Andrūsa

Member of the Management Board Ē.Šmuksts

The annual report was prepared by the Finance Directorate of VAS *Latvijas dzelzceļš*:
Head of Finance Division T. Labzova-Ceicāne

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR 2020

(EUR' 000)

	NOTES	2020	2019
Loss for the reporting year		**(35 515)**	**(9 328)**
Items that will not be reclassified in the income statement:		(9 576)	(494)
Write-off of revalued fixed assets	*20*	*(9 576)*	*(494)*
Other profit or loss for the reporting year		**(9 576)**	**(494)**
Total income or loss for the reporting year		**(45 091)**	**(9 822)**
Loss and comprehensive income for the reporting year attributable to the shareholders of the Group's parent company		**(45 091)**	**(9 822)**

The notes on pages 22 to 56 form an integral part of these consolidated financial statements.

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CONSOLIDATED STATEMENT OF FINANCIAL POSITION AT 31 DECEMBER 2020

(EUR' 000)

ASSETS	NOTES	31.12.2020	31.12.2019
Long-term investments			
Property, plant and equipment	12	756 894	824 486
Intangible assets	11	2 054	1 622
Right-of-use assets	13	10 339	10 249
Advance payments for property, plant and equipment		5 693	52
Long-term financial investments		84	84
Total long-term investments		**775 064**	**836 493**
Current assets			
Inventories	14	16 499	25 693
Long-term investments held for sale	15	1 141	-
Trade and other receivables	16	13 725	16 304
Accrued income	17	9 503	-
Corporate income tax	10	44	51
Cash and cash equivalents	18	87 260	67 471
Total current assets		**128 172**	**109 519**
Total assets		**903 236**	**946 012**

(continued on the next page)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AT 31 DECEMBER 2020 (CONTINUED)

(EUR' 000)

EQUITY AND LIABILITIES	NOTES	31.12.2020	RESTATED 31.12.2019
Equity and liabilities			
Equity			
Attributable to shareholders of the parent company of the *Group*:			
Share capital	19	289 142	256 720
Long-term investment revaluation reserve	20	36 086	45 662
Reserves and retained earnings	20	68 691	94 656
Total equity		**393 919**	**397 038**
Liabilities			
Non-current liabilities			
Deferred tax liability	10	466	1 759
Provisions	21	5 821	127
Borrowings from credit institutions	22	120 615	94 290
Taxes and national social insurance mandatory contributions	23	19 423	-
Trade payables		828	486
Lease liabilities		7 803	8 636
Deferred revenue	24	261 329	274 390
Total non-current liabilities		**416 285**	**379 688**
Current liabilities			
Borrowings from credit institutions	22	38 213	94 897
Provisions	21	264	2 159
Trade and other payables		26 457	36 537
Taxes and national social insurance mandatory contributions	23	4 630	10 174
Lease liabilities		2 601	2 168
Deferred revenue	24	20 867	23 351
Total current liabilities		**93 032**	**169 286**
Total liabilities		**509 317**	**548 974**
Total equity and liabilities		**903 236**	**946 012**

The notes on pages 22 to 56 form an integral part of these consolidated financial statements.

Chairman of the Management Board	M. Kleinbergs
Member of the Management Board	V. Balode-Andrūsa
Member of the Management Board	Ē.Šmuksts

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(EUR' 000)

	ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT COMPANY OF THE *GROUP*				
	SHARE CAPITAL	LONG-TERM INVESTMENT REVALUATION RESERVE	RESERVES AND RETAINED EARNINGS B/F	RETAINED EARNINGS OR UNCOVERED LOSSES	TOTAL EQUITY
		2019			
At 01.01.2019	**256 720**	**46 156**	**89 082**	**14 408**	**406 366**
2018 profit transferred to retained earnings b/f	-	-	14 408	(14 408)	**-**
Transactions with the shareholder of the Group	-	-	*14 408*	*(14 408)*	**-**
Write-off of revalued fixed assets		(494)	494	-	**-**
Loss for the reporting year	-	-	-	(9 328)	**(9 328)**
Total losses for the reporting year	-	*(494)*	*494*	*(9 328)*	***(9 328)***
At 31.12.2019	**256 720**	**45 662**	**103 984**	**(9 328)**	**397 038**
		2020			
At 01.01.2020	**256 720**	**45 662**	**103 984**	**(9 328)**	**397 038**
2019 loss transferred to retained earnings b/f	-	-	(9 328)	9 328	**-**
Payments for the use of state capital from the 2019 profit	-	-	(26)	-	**(26)**
Increase in share capital	32 422	-	-	-	**32 422**
Transactions with the shareholder of the group	*32 422*	-	*(9 328)*	*9 328*	***32 396***
Write-off of revalued fixed assets	-	(9 576)	9 576	-	**-**
Loss for the reporting year	-	-	-	(35 515)	**(35 515)**
Total losses for the reporting year	-	*(9 576)*	*9 576*	*(35 515)*	***(35 515)***
At 31.12.2020	**289 142**	**36 086**	**104 206**	**(35 515)**	**393 919**

The notes on pages 22 to 56 form an integral part of these consolidated financial statements.

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CONSOLIDATED STATEMENT OF CASH FLOWS FOR 2020

(prepared under the indirect method)

(EUR' 000)

	NOTES	2020	2019
Cash flow from operating activity			
Loss before tax		**(36 124)**	**(8 314)**
Adjustments:			
Depreciation of fixed assets and other impairment adjustments		65 174	46 104
Amortisation of intangible assets and other impairment adjustments	11	613	577
Provisions created	21	3 799	(2 397)
Foreign currency exchange loss	8	87	13
Income from investments in associates and other companies		(1)	(330)
Other interest and similar income	9	-	(2)
Interest and similar expenses	9	2 227	2 237
Profit before adjustments in the working capital		**35 775**	**37 888**
Adjustments:			
(Increase)/decrease of receivables		(7 121)	3 419
Decrease/(increase) in inventories		8 028	(7 151)
Increase/(decrease) in trade and other payables		3 219	(15 749)
Gross cash flow from operating activity		**39 901**	**18 407**
Interest expense		(2 234)	(2 258)
Corporate income tax expense	10	(726)	(33)
Net cash flow from operating activity		***36 941***	***16 116***
Cash flow from investing activity			
Acquisition of property, plant and equipment and intangible assets		(22 731)	(29 868)
Proceeds from sale of property, plant and equipment and intangible assets		1 434	179
Subsidies or grants received		4 715	4 676
Interest received		-	2
Dividends received		1	622
Net cash flow from investing activity		***(16 581)***	***(24 389)***

(continued on the next page)

CONSOLIDATED STATEMENT OF CASH FLOWS FOR 2020 (CONTINUED)

(EUR' 000)

	NOTES	2020	2019
Cash flow from financing activity			
Increase in share capital		32 422	-
Loans received		10 001	23 778
Loans repaid		(40 360)	(36 121)
Lease payments		(2 608)	(1 834)
Dividends paid		(26)	-
Net cash flow from financing activity		***(571)***	***(14 177)***
Foreign currency exchange rate fluctuations		**-**	**17**
Increase/(decrease) of cash and cash equivalents in the reporting year		**19 789**	**(22 433)**
Cash and cash equivalents at the beginning of the reporting year		67 471	89 904
Cash and cash equivalents at the end of the reporting year	16	**87 260**	**67 471**

The notes on pages 22 to 56 form an integral part of these consolidated financial statements.

Chairman of the Management Board	M. Kleinbergs
Member of the Management Board	V. Balode-Andrūsa
Member of the Management Board	Ē.Šmuksts

The annual report was prepared by the Finance Directorate of *VAS Latvijas dzelzceļš*:
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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL INFORMATION

The *Group* operates the publicly used railway infrastructure and provides railway transport services and related services.

The *Group's* parent company is the state joint stock company *Latvijas dzelzceļš*; it is the holding company of the *Group* that performs the functions of the public railway infrastructure manager.

The *Group's* parent company is registered in the Commercial Register of the Enterprise register of the Republic of Latvia as a state joint-stock company and is 100% owned by the Republic of Latvia. The registered office of the parent company of the *Group* is at Gogoļa iela 3, Riga, LV-1547, Latvia.

All companies included in the *Group* are registered in the Republic of Latvia and the *Group's* parent company has a direct or indirect decisive influence on them. The *Group* includes:

NAME	TYPE OF ACTIVITY
SIA "LDZ CARGO"	cargo transportation
SIA "LDZ ritošā sastāva serviss"	maintenance and repair of rolling stock
SIA "LDZ infrastruktūra"	repair of railway machinery and equipment, track welding work
SIA "LDZ apsardze"	security services
SIA "LDZ Loģistika"	transport forwarding and logistics services
AS "LatRailNet"	performance of essential functions of the infrastructure manager
SIA "Rīgas Vagonbūves uzņēmums "Baltija""	established with the aim of building wagon cars in Latvia

Financial statements were approved for publication by the Management Board of the *Group's* parent company on 15 March 2021. The consolidated financial statements are approved by the meeting of shareholders, convened by the Board of the state Joint Stock Company "Latvijas dzelzceļš" after receiving the auditor's opinion and the council's report.

2. ACCOUNTING AND MEASUREMENT PRINCIPLES

These financial statements have been prepared based on the accounting and measurement principles described below. Unless otherwise stated, these principles have been applied to all comparatives accordingly.

2.1. ACCOUNTING AND MEASUREMENT PRINCIPLES

These consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) adopted in the EU.

The consolidated financial statements have been prepared under the historical cost convention, in addition to applying the revaluation method for freight wagons for freight transport (included in fixed assets), applying the principle of continuation of activity.

The consolidated financial statements cover the period from 1 January 2020 to 31 December 2020.

In preparing financial statements in accordance with IFRS, management relies on known estimates and assumptions that affect the balances of items reported in the individual financial statements and the amounts of contingent liabilities. Future events may affect the assumptions on which the relevant estimates were based. The effects of changes in estimates are reflected in the financial statements at the time they are determined. Although these estimates have been prepared on the basis of comprehensive information available to management about current events and activities, actual results may differ from these estimates. Significant assumptions and judgements are described in section 3.

During the reporting period there have not been International Financial Reporting Standards, the amendments thereto and amendments to their interpretations, the implementation of which had a material effect on the Company's business activities. In the reporting year, the following amendments to the standards came into force as of 1 January 2020 and have been approved for use in the EU:

- Amendments to the Financial reporting conceptual framework;
- Amendments to IFRS 3 regarding business definition;
- Amendments to IAS 39 and IFRS 8 regarding the materiality definition;
- Amendments to IFRS 9, IAS 39 and IFRS 7 regarding the interest rate reform;
- Amendments to IFRS 16 for reporting Covid-19 concessions in lessee accounts.

The *management* of the *Group* has performed an impact assessment of other standards and interpretations that will be effective on or after 1 January 2021 and does not expect them to have a material impact on the *Company's* financial statements.

2.2. FOREIGN CURRENCY REVALUATION

Functional and presentation currency

Items in the *Group's* financial statements are measured using the currency of the primary economic environment in which the *Group* operates (accounting currency). Items in the financial statements are presented in the official currency of the Republic of Latvia, euro (EUR), which is the *Group's* functional currency. The functional and presentation currency of all the *Group's* companies is EUR.

Transactions and balances in foreign currencies

All transactions in foreign currencies are translated into EUR at the EUR exchange rate published by European Central Bank at the beginning of the date of the transaction. Monetary assets and liabilities denominated in foreign currency on the last day of the reporting year are translated into EUR in the financial statements at the exchange rate to be used in the books as published by European Central Bank at the end of the last day of the reporting year. Exchange rate differences arising from settlements in currencies are recognised in the profit or loss.

FOREIGN CURRENCY	EUR 31.12.2020	EUR 31.12.2019
USD	1.22710	1.12340
CHF	1.08020	1.08540
RUB	91.46710	69.95630

2.3. INTANGIBLE ASSETS

Intangible assets mainly consist of software licences. Initially, they are recognised at cost. Intangible assets have a finite and limited period of use. Subsequently, intangible assets are measured at cost, less accumulated amortisation, and impairment loss.

Subsequent costs are capitalised as an increase in the value of the existing intangible asset or recognised as a separate intangible asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the *Company* and the cost of the item can be measured reliably. The remaining costs are charged off to the profit and loss at the time when incurred.

For intangible assets, amortisation shall be calculated on a straight-line basis to write off their cost during the useful life period and shall be charged off to profit or loss for that period. Generally, intangible assets are amortised over five years.

2.4. PROPERTY, PLANT AND EQUIPMENT (PPE)

Property, plant, and equipment (PPE) are recognised using the historical cost method or revaluation method as described below, less accumulated depreciation and accumulated impairment, if any.

Freight wagons used for transport are accounted for using the revaluation method and regularly revalued to ensure that their book value does not differ significantly from their fair value at the end of the accounting year. The increase in the book value resulting from the revaluation shall be recognised under Other income and as a revaluation reserve as part of equity. Impairment related to fixed assets for which an increase in value was previously recognised is recognised under other income and reduces the amount of revaluation reserve under equity. In other cases, impairment resulting from revaluation is recognised in the consolidated profit or loss account. In the case of the sale or write-off of a property, plant and equipment item, the revaluation reserve that was included under equity is reclassified to retained earnings.

On the revaluation date, accumulated depreciation is excluded from the cost of the asset, the net amount is included in the revaluation so that the book value of the property, plant and equipment after revaluation is equal to its revaluation value.

Other categories of property, plant and equipment are accounted for using the cost method, under which property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses, if any. The cost includes the costs directly attributable to the acquisition. The cost of assets constructed by the *Group* consists of the price of materials and the direct cost of labour and any other costs directly attributable to bringing the property, plant and equipment item into working condition for its intended use, and the cost of demolishing and removing the asset and restoring the site on which the property, plant and equipment item is to be located. The cost of acquiring computer software that is closely related to and cannot be separated from the functionality of the equipment is capitalised as part of that equipment.

The *Group* capitalises assets with the value exceeding 300 EUR and the useful life of which exceeds one year. Investments in leased assets are capitalised and reported as property, plant and equipment.

If the useful lives of individual components of an asset differ, they are accounted for as separate components. Estimated residual values and useful lives of property, plant, and equipment are reviewed and adjusted, if necessary, at each date of the reporting year.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the *Group*, and the cost of the item can be measured reliably. The remaining costs of current repair and maintenance of fixed assets are charged off to profit or loss account in the period when incurred.

The gain or loss on disposal of property, plant, and equipment is calculated as the difference between the book value of the asset and the proceeds from the sale and is charged off to profit or loss in the period when incurred.

Where the book value of a property, plant, and equipment item is higher than its recoverable amount, its book value is written down to its recoverable amount (Note 3).

Depreciation

Depreciation on property, plant and equipment is calculated using the straight-line method. Depreciation is charged off to the profit and loss account.

Investments in leased property, plant and equipment are depreciated over the shorter of the lease term or the useful life of a comparable item of property, plant and equipment at the rates applicable to the category to which the leased property, plant and equipment belongs. Land is not depreciated.

For the *Group's* property, plant and equipment, the depreciation expense for the period is calculated from the carrying amount of each item of property, plant and equipment using the useful life established for that item of property, plant and equipment.

PROPERTY, PLANT AND EQUIPMENT (PPE)	USEFUL LIFE
Buildings and structures	10-130 years
Perennial plantings	40 years
Railway rolling stock - wagons for technological purposes and freight transport	22-40 years
Railway rolling stock - locomotives, diesel trains and technological equipment	5-40 years
Track equipment	30 years
Computing equipment, communications equipment, copiers and their equipment	3-10 years
Other property, plant and equipment	5-28 years

Unfinished construction

Assets that are not ready for their intended use at the time of purchase or are in the process of installation are classified under *Unfinished construction*. The historical cost of unfinished construction is increased during the period for borrowing costs and other direct costs associated with the relevant object until its commissioning into operation. The initial value of the relevant item of property, plant, and equipment is not increased by borrowing costs in periods when active work on the development of the unfinished construction object is not carried out.

At the time unfinished construction is completed and ready for its intended use, it is reclassified to the appropriate category of property, plant, and equipment and the calculation of depreciation is begun. Unfinished construction properties are regularly measured to determine whether they show any signs of impairment.

2.5. IMPAIRMENT OF TANGIBLE AND INTANGIBLE ASSETS

All tangible and intangible assets of the *Group* have a finite useful life (except land and the museum inventory). Depreciable assets are reviewed for impairment whenever events and circumstances indicate that their carrying amount may not be recoverable.

An impairment loss is recognised as the difference between the asset's carrying amount and its recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use. To determine impairment, assets are grouped at the lowest level for which a cash flow can be determined (cash-generating units). The impairment loss is recognised in profit or loss.

An impairment loss recognised in prior periods is reviewed at each balance sheet date to determine whether there is any indication that the loss may have decreased or may no longer exist. An impairment loss is reversed if there has been a change in the estimates used to determine the amount to be recovered. An impairment loss may be reversed only to the extent that the carrying amount of the asset does not exceed its carrying amount, less the depreciation that would have been determined had the impairment loss not been recognised.

2.6. FINANCIAL INSTRUMENTS

Classification of financial instruments

The *Group's* financial instruments consist of financial assets (financial assets at amortised cost and financial assets at fair value through profit or loss) and financial liabilities (financial liabilities at amortised cost).

The classification of debt instruments depends on the business model implemented by the *Group's* financial asset management, as well as on whether the contractual cash flows consist solely of principal and interest payments (SPPI). If the debt instrument is held to collect cash flows, it can be accounted for at amortised cost if it meets the SPPI requirements. Financial assets whose cash flows do not meet the SPPI requirements must be measured using the FVPL method (e.g., financial derivatives). Embedded derivatives are not separated from financial assets, but when they are included under financial assets, the SPPI requirements are considered.

Equity instruments are always measured at fair value. However, the *Management* has the option to make the irrevocable choice of showing a change in fair value in other income if the instrument is not held for trading purposes. If the equity instrument is held for trading, changes in fair value must be charged off to consolidated profit or loss account.

Recognition and derecognition

Financial assets are recognised at the moment when the *Group* has become a party to a transaction and has fulfilled the conditions of the transaction, i.e., on the trading date.

Financial assets are derecognised when the *Group's* contractual obligations to receive cash flows from the financial asset expire or when the *Group* transfers the financial asset to another party or transfers the significant risks and rewards of ownership of the asset. Purchases and sales of financial assets in the ordinary course of business are accounted for on the trade date, i.e., the date on which the *Group* takes the decision to buy or sell the asset.

A financial liability is derecognised when the obligation underlying the liability is withdrawn, cancelled or expires.

Measurement

At the time of initial recognition, financial instruments are measured at their fair value. For financial assets and financial liabilities at amortised cost, at the time of initial recognition, fair value shall be adjusted for transaction costs directly attributable to the relevant financial instrument.

Financial assets at fair value through profit or loss

This category includes equity instruments owned by the *Group*, which constitute Other securities and investments. These investments are reported under Long-term assets, unless the *Management* intends to sell them within 12 months from the closing date of the reporting year. The fair value of these financial assets is determined on the basis of estimates made by the *management* of the *Group* based on the financial information of these investments. Changes in fair value are charged to consolidated profit or loss account.

Dividends from investments are recognised in the consolidated profit or loss account at the moment when the *Group* has legal rights to them.

Financial assets at amortised cost

Financial assets at amortised cost are debt instruments with a fixed or determinable payment schedule that are not held for trading and whose future cash flows consist solely of principal and interest payments. Financial assets at amortised cost include trade and other receivables, and cash and cash equivalents. Financial assets at amortised cost are classified as short-term assets if the fall due in less than one year. If they fall due in more than one year, then they are presented as long-term assets. Short-term receivables are not discounted.

Financial assets at amortised cost are initially recognised at fair value and are subsequently reported at amortised cost using the effective interest rate method, net of provisions for impairment.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, current account balances and short-term deposits with an initial maturity of less than 90 days and short-term highly liquid investments that can be easily converted into cash if necessary and are not subject to significant risk of value changes.

Impairment of financial assets at amortised cost

Impairment is recognised in accordance with the expected credit loss (ECL) model. The model has a three-step approach, which is based on a change in the credit quality of the financial asset compared to that at the initial recognition. At the time of initial recognition of a financial asset, the *Group* recognises immediate loss which is equal to the 12-month ECL, even if the financial asset is not impaired (for trade and other receivables lifetime ECL is recognised). In the event of a significant increase in credit risk, the impairment is measured using the lifetime ECL of the asset instead of the 12-month ECL. The model includes operational simplifications for trade receivables.

The *Group* has applied the operational relief allowed by IFRS 9 regarding the valuation of trade receivables – trade receivables are grouped according to their credit quality and maturity date, applying the ECL percentage to each relevant group. ECL rates are estimated considering the payment history of the last three years, adjusting this indicator with the aim of considering information on present and future forecasts.

Receivables due from affiliated parties, as well as the loans issued to the related parties, are grouped separately, with ECL being calculated, considering not only past experience, but also the credit rating of their ultimate owner – the Republic of Latvia – and future development forecasts. Loans granted to subsidiaries are considered assets with a credit risk that has not increased significantly since the date of their initial recognition, therefore the ECL calculation includes the credit losses expected within the next 12 months.

Impairment provisions are included in a separate provision account and losses are recognised in the consolidated profit or loss account. If the loss amount decreases in the next period following the recognition of impairment and this decrease may be objectively related to the event following the recognition of impairment (for example, the debtor's credit rating improves), the reversal of previously recognised impairment losses shall be recognised in the consolidated profit or loss account.

Financial liabilities at amortised cost

Financial liabilities at amortised cost consist of Borrowings from credit institutions, Other borrowings, Trade payables and Other payables.

Financial liabilities at amortised cost are initially recognised at fair value. In subsequent periods, financial liabilities at amortised cost are reported at amortised cost using the effective interest rate. Financial liabilities at amortised cost are classified as current liabilities if they fall due in one year or less. If they fall due in more than one year, then they are presented as non-current liabilities.

Borrowings

Initially borrowings are recognised at fair value less the costs associated with the receipt of the borrowings. Subsequently, borrowings are carried at amortised cost using the effective interest rate. The difference between the amount of cash received, less the costs associated with the receipt of borrowings and the cost of the repayment of the borrowing, is gradually charged to profit or loss account using the effective interest rate on the borrowing. This difference is recognised under financial costs.

Borrowings are classified as short-term liabilities, except in cases where the *Group* has an irrevocable right to defer settlement of liabilities for at least 12 months after the balance sheet date.

Offsetting financial assets and financial liabilities

Financial assets and financial liabilities are offset and reported in the balance sheet at net values if there is a legal right to offset them and if the intention is to settle at net values or to settle the liability and to transfer the asset simultaneously.

2.7. INVENTORIES

Inventories are measured at the lower of cost or net realisable value. Net realisable value is the estimated selling price in the normal course of business, less the estimated costs of completion and selling expenses. The cost is determined using the weighted average stock valuation method for fuel and oil and the FIFO (first in, first out) method for the other inventory components.

If necessary, provisions for impairment loss are created for obsolete, slow-moving, or damaged inventory when necessary. A 100% provision is made for inventories that have not been used for more than one year. The amount of the provisions is recognised in profit or loss.

2.8. NON-CURRENT ASSETS HELD FOR SALE (DISPOSAL GROUPS)

Non-current assets (disposal groups) are classified as held for sale if their carrying value is recovered as a result of the sale transaction and not as a result of long-term use. This condition will be considered fulfilled only if the probability of a sale transaction is high and the relevant asset (or disposal group) is available for immediate sale in its current state. Non-current assets held for sale (or disposal groups) at the time of their reclassification are valued at the lower of their carrying value and at fair value less cost to sell.

Impairment is recognised if, at initial recognition or subsequent measurement of the asset (disposal group), the value is reduced from the initial carrying value to the fair value less cost to sell. The impairment can be reversed and recognised in revenue if the fair value of the asset (disposal group) less cost to sell increases. However, such a reversal can only be recognised to the extent that it compensates for the previously recognised impairment of that asset (or disposal group).

Upon disposal of non-current assets (disposal groups) held for sale, net profit or loss from their derecognition and sale is recognised.

Non-current assets held for sale (or disposal groups) are not used or depreciated as long as they are classified as held for sale.

Non-current assets held for sale and assets that are part of the disposal group are presented separately from other assets in the balance sheet. Liabilities that are part of the disposal group are presented separately from other liabilities in the balance sheet.

2.9. SHARE CAPITAL AND PAYMENTS FOR THE USE OF STATE CAPITAL SHARES (DIVIDENDS)

The share capital of the *Group's* parent consists of ordinary shares. All shares of the *Group's* parent company of the *Group* are dematerialised shares. The nominal value of the share is one euro.

Dividends paid to the shareholder of the *Group's* parent company or payments for the use of state capital shares are carried as liabilities in the *Group's* financial statements during the period when the shareholder of the parent company of the *Group* approves the amount of dividends.

2.10. RESERVES

After approval of each annual report, the shareholder meeting decides on the distribution of profit for the reporting year. A part of the after-tax profit of the *Group's* parent company may be credited to the reserve capital based on the decision of the shareholder meeting of the *Group's* parent company. For this purpose, *Reserves* have been created under equity. The use and distribution of reserves is within the competence of the shareholder meeting.

2.11. ACCRUALS FOR UNUSED ANNUAL LEAVE

Accruals for unused annual leave are calculated for each employee by multiplying the number of unused vacation days at the end of the reporting year by the average daily salary in the last six months of the reporting year and adding the employer's share of national social insurance mandatory contributions.

2.12. PROVISIONS

Provisions are recognised when the *Group* has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

If the *Group* expects to reverse some or all of its provisions, the reversal should be recognised as a separate asset only if it is virtually certain that the expense will be recovered. Expenses relating to the creation of provisions are recognised in profit or loss after deduction of the amounts recovered.

2.13. CORPORATE INCOME TAX FOR THE REPORTING YEAR

Corporate income tax shall be reported in the consolidated profit or loss account.

Corporate income tax is calculated in accordance with the legislation in force at the end of the reporting period. The current legislation lays down a tax rate of 20 percent of the calculated taxable base, which before the application of the tax rate was adjusted by dividing the value of the object subject to corporate income tax by a coefficient of 0.8.

Corporate income tax, calculated from the distribution of profits in dividends, is recorded in the consolidated profit or loss account separately, while in other cases – included into other operating expenses.

2.14. REVENUE RECOGNITION

Revenue is the consideration received for the performance of principal activities. Revenue is measured at the contractual transaction price. The transaction price is the amount that the *Group* expects to receive after control of the goods or services has been transferred, net of the amounts collected on behalf of third parties (e.g., value added tax). The transaction price is reduced by any rebates or other incentives received by the customer. Specific criteria for recognising *the Group's* revenue by type of revenue are set out below.

The *Group* does not have any customer contracts with a settlement period of more than one year. Therefore, the *Group* does not adjust account for changes in the value of money over time. In addition, the settlements do not provide for variable consideration.

Revenue from the sale of goods is recognised when control of the goods has been transferred, i.e., when the *Group* has delivered the goods to the customer and the goods have been accepted by the customer and it is probable that the receivable will be collected.

Revenue from the rendering of services is recognised in the period in which the services are rendered, considering the ratio of the total service rendered to the total contractual service, if applicable.

The *Group* provides the following services (which are mostly recognised under IFRS 15):

- **Cargo traffic**:
  - from the dispatch station to reception station (in the territory of Latvia) for domestic transport;
  - from border station to the station nearby the port or land border station in transit;
  - from the border station to the receiving station or in the opposite direction (for import and export transport).

  Revenue for cargo traffic (freight) services consist of a tariff charge and an additional charge that is not included in the tariff and is determined by contract. Freight charges are established in accordance with the Transportation Tariff - Tariff System, which includes information on transportation distances, the procedure for calculating the charge, and the transportation charge, which consists of transportation fees, charges for additional operations, and other transportation-related services. In order to effectively ensure the utilisation of the waggon fleet, some of the waggons are leased to other customers. Revenue from waggon hire is a part of freight revenue. Revenue is recognised on the basis of the distance covered and the estimated freight costs for the respective reporting period.
- **Public usage rail infrastructure services** – Access to the railway infrastructure provided by the infrastructure manager on a non-discriminatory basis to all carriers. *Latvijas dzelzceļš* provides a minimum package of services for access to the public use railway infrastructure connecting the railway infrastructure with service facilities (minimum access complex), as well as a service for maintenance of the service location. The services of the minimum access package are provided from 1 July 2019 in accordance with the Commission Implementing Regulation (EU) 2015/909 on the modalities for the calculation of the cost that is directly incurred as a result of operating the train service of 12 June 2015. *The Company* was granted state budget funds to ensure financial compensation for the operator of the railway infrastructure used by the public. The amount of the grant received is recognised as revenue in the period in which the services are provided.
- **Service point maintenance services** – Maintenance of passenger stations and stops. The Company has been granted state budget funds for the maintenance of unused service points. The amount of the grant received (excluding VAT) is recognised as revenue in the period in which the services are performed, capped at the amount of the funds received.
- **Additional services of the infrastructure operator** – Handling of freight train compositions by means of or without train formation, maintenance, and inspection of wagons. Revenue is recognised in the period in which the services are provided.
- **Specific services related to infrastructure maintenance and repair** – Construction and repair of tracks and bridges, replacement of switchgear, repair of railway machinery, tools and mechanisms and modernisation of wagons, welding of tracks and long gauge transportation, installation and repair of water drainage systems, preparation of ground cover. Revenue is recognised when providing service works, or when repair works are completed.
- **International passenger transport** – Transportation of passengers in international traffic on routes Riga-Moscow; Riga-St. Petersburg; Riga-Minsk, Riga-Vilnius-Minsk-Kiev (train of the Ukrainian entity formation). Revenue is recognised in the period when the proceeds from the sale of tickets are received.
- **Forwarding services** – Development of freight transport routes, organisation of rail freight transport, including preparation of transport documents, customs formalities, shipment/receipt of cargo. Revenue is recognised in the period when services are provided.
- **Rental services** – the *Group* leases buildings, structures, land and other fixed assets that are not necessary for the performance of its activities, first of all, to carriers and other companies and institutions related to the operation of the railway system. Renting out

unused areas located in railway infrastructure facilities to external customers reduces the cost price of the basic service. As a result, the competitiveness of the basic service increases, as well as the efficiency of the use of objects increases. Revenue is recognised in the period when services are provided. Revenue from rental services is recognised in accordance with IFRS 16.

- **Electricity sales services** - Distribution and sale of electricity to individuals, corporations and dependent subsidiaries and purchase of electric energy for electric traction of passenger trains. Electricity distribution (traction substations and contact network) required for traction of passenger trains is included in the cost of infrastructure and is excluded from electricity distribution services. Latvijas dzelzceļš provides electricity sales services to electricity consumers, fulfilling its obligations set out in the Electricity Market Law, the Law on Regulatory Authorities Public Services and Cabinet Regulation No. 50 on the sale and use of electricity. Latvijas dzelzceļš acts as the main provider of services, therefore revenues and related costs are recognised on a gross basis. Revenue is calculated depending on tariffs and actual kilowatt hours consumed in the consumption period.
- **Services of a principal** include the submission of a summary return, execution of the customs procedure – transit, and temporary storage. Revenue is recognised in the period when services are provided.
- **Repair and maintenance of rolling stock** – Revenue is recognised when providing maintenance services or when repairs are completed.
- **Traction services** - Services of locomotive brigades to other carriers for which there are not enough locomotive brigades to carry out transportation. Revenue is recognized in the period when services are provided based on the use of brigades in the relevant reporting period.
- **Electronic communications services** – Data and electronic message transmission services, leased line services, access to electronic communications network infrastructure services, public fixed electronic communications network voice telephony services and interconnection services. Revenue is recognised after the actual use of the network during the relevant reporting period.
- **Information technology services** – Includes services related to freight and passenger transport information systems, train movement, as well as business support, Control and Management Information Systems. Revenue is recognised in the period when services are provided.
- **Other services** – These services include management services to dependent companies, sales of self-produced heat, management services and various other minor services to corporate and individual customers. Revenue is recognized in the period in which the services are rendered.

Interest income

Interest income is recognised by the accrual method, applying the effective interest rate. Interest income from cash and cash equivalents is classified as financial income.

Income from fines

Using the prudence principle, contractual penalties, including late payment interest past the due date are recognised in revenue only upon receipt.

Dividend income

Dividend income is recognised when legal rights to them arise.

2.15. LEASE AGREEMENTS

Classification

When entering contracts, the *Group* considers whether the contract is a lease or contains a lease. A contract is a lease or contains a lease if the contract confers the right to control the use of an identifiable asset for a specified period in exchange for consideration. To assess whether an arrangement is, or contains, a lease, the *Group* shall assess whether:

- The contract provides for the use of an identifiable asset – the asset may be directly or indirectly designated and must be physically separable or represent the total capacity of the asset from the physically separable asset. If the supplier has significant rights to substitute the asset, the asset is not identifiable;
- The *Group* may derive all economic benefits from the use of the identifiable asset for the entire period of its use;
- The *Group* has the right to determine the use of the identifiable asset. The *Company* has the right to determine the manner of use if it can decide how and for what purpose the asset will be used. In cases where it has been decided in advance how and for what purpose the asset is to be used, the entity shall determine whether it has the right to dispose of the asset or to determine that the asset is to be used in a particular way, or whether the *Group* intends to use the asset in the way that determines in advance how and for what purpose the asset is to be used.

When initially measuring or remeasuring a contract that contains one or more lease components, the *Group* attributes to each lease component its relative stand-alone price.

Lessee

A lease is recognised as rights to use the asset and the corresponding lease liability on the date the leased asset is available for use by the *Group*. The cost of the right-of-use assets consists of:

- amounts of initial assessment of lease liabilities;
- any lease payments made on or before the start date, net of rental incentive payments received;
- any initial direct costs.

Right-of-use assets are amortised on a straight-line basis from the beginning to the end of the useful life of the underlying asset. Right-of-use assets are amortised on a straight-line basis from the inception of the lease to the end of the lease term unless there is a plan to redeem the asset. The right-of-use asset is periodically reduced for any impairment losses and adjusted for the revaluation of the lease liability.

Lease assets and lease obligations are measured at the present value of the remaining lease payments at the date of initial application, discounted at the e *Group's* reference interest rate on the date of their initial application. The lease liability shall include the current value of the following lease payments:

- fixed lease payments (including essentially fixed lease payments), net of rental incentive payments;
- variable lease payments that depend on the index or rate;
- payments to be made to the lessee under residual value guarantees;
- where there are reasonable grounds to believe that the lessee will use the option, and
- payment of fines for termination of the lease, if the term of the lease reflects the fact that the lessee uses the opportunity to terminate the lease.

Lease liabilities are reassessed if there is a change in future lease payments due to a change in the index or rate used to determine those payments, if there is a change in the *Group's* estimate of expected payments, or if the *Group* changes its assessment of the option to purchase or extend the lease. termination. When the lease liability is reassessed, an appropriate adjustment is made to the book value of the right to use asset or recognised in the income statement if the book value of the right to use asset decreases to zero.

Each lease payment is split into lease liability and the interest expense on the lease liability. The interest expense of the lease liability is recognised in the income statement during the lease period to form a constant periodic interest rate on the remaining lease obligation during each period.

Short-term leases and leases with a low value of the underlying asset

Leases related to short-term leases or leases with a low value of the underlying asset are recognised as expenses according to the linear method in the income statement. A short-term lease is a lease the lease term of which on the starting date is 12 months or less.

Accounting for sublease transactions (the *Group* is the lessor)

If the company is the lessor under the contract, but part of the leased property is leased, it is a sublease. Each sublease is assessed to determine whether it meets the definition of a finance lease or an operating lease in relation to the right-of-use asset. It is accounted for in accordance with the specified type of sublease - the Company is a lessor under the terms of an operating lease, or the *Group* is a lessor under the terms of a finance lease. If the sublease is a finance lease, it is accounted for separately as a lease receivable. Offsetting is not performed.

Accounting for sublease transactions:

- The *Group*, as an intermediate lessor, reduces the right-of-use asset by creating a "finance lease receivable" for that portion without recognising lease income from the sublease, but calculates interest income from the “finance lease receivable";
- During the term of the sublease, the *Group*, as an intermediate lessor, recognises depreciation expense on the “right-of-use asset” to the extent of the portion of the “right-of-use asset” that is not subleased, but recognises interest expense on the lease in full.

2.16. STATE BUDGET CO-FINANCING AND EU FINANCING

State co-financing and EU funds are recognised at their fair value at the moment when there is sufficient confidence in their receipt and it can be reliably asserted that the *Group* will be able to comply with all the rules relating to the receipt of these funds.

State co-financing of assets (fixed assets) and EU funds are reported under the balance sheet item *Deferred revenue* and periodically recognised in the Consolidated profit and loss account in proportion to the depreciation of the relevant assets (fixed assets) over their useful life.

2.17. RELATED PARTIES

Related parties are considered to be the state, members of the Management Board and Council of the *Group’s* companies, their close family members and companies in which these persons have control or significant influence.

2.18. EVENTS AFTER THE BALANCE SHEET DATE

The financial statement reflects such events after the end of the reporting year, which provide additional information on the *Group's* financial position at the balance sheet date (adjusting events). If events after the balance sheet date are not adjusting events, they are disclosed in the notes to the financial statements, only if material.

2.19. EMPLOYEE BENEFITS

Social security contributions and pension plan contributions

The *Group* makes social insurance contributions to the State pension insurance scheme in accordance with Latvian law. The State pension insurance scheme is a defined contribution pension plan, under which the *Group* must make payments in the statutory amount. The *Company* has no additional legal or constructive obligation to make further payments if the State pension insurance scheme is unable to meet its obligations to employees. Social security contributions are charged off to expenses on an accrual basis and form a part of staff costs. Pursuant to the Cabinet Regulation No. 786 *Regulation on the Distribution of the Rates of National Social Insurance Contribution Rates by*

Type of National Social Insurance dated 19 December 2017, in 2020, 69.82% of the national social insurance mandatory contributions were paid to finance the State defined contribution pension system.

2.20. GENERAL PRINCIPLES OF CONSOLIDATION

A subsidiary whose financial or operating activities are controlled by the *Group's* parent company is considered a subsidiary of the *Group*. Control is presumed to exist when the *Group's* parent company owns more than 50% of the shares of a subsidiary and has the power to direct all operating decisions of the subsidiary.

The financial statements of the *Group's* subsidiaries are consolidated from the date on which control is transferred to the parent company and are no longer consolidated from the date on which control ceases.

The financial statements of companies are prepared using uniform accounting and financial policies for similar transactions and other events in similar circumstances. If necessary, the accounting policies of the *Group's* subsidiaries may be changed to ensure consistency with the accounting policies used by the *Group*. The consolidated financial statements include the annual accounts of the parent company and daughter companies for 2020.year. The annual reporting periods of the *Group* companies are the same and coincide with the calendar year.

Intercompany transactions, balances and unrealised gains and losses on transactions between *Group* companies are eliminated.

Associates are those entities in which the *Group* has a significant interest (directly or indirectly), but does not control, generally from 20 to 50 percent of the voting rights. Investments in associated companies are accounted for in the financial statements under the equity method and initially recognised at their acquisition costs. Associates shall include goodwill arising from acquisitions in their book value. Dividends received from the associated company reduce the book value of the Associated company. Other post-acquisition changes in the *Group's* share of the net assets of the associate are recognised as follows: (i) the *Group's* share of the associate's profit or loss is recognised in the consolidated income statement as a gain or loss on its investment in the associate; the associate's other income is recognised in a separate line in other comprehensive income. When the *Group's* share of losses in an associate equal or exceeds its interest in the associate, including any unsecured receivables, the *Group* does not recognise further losses unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the *Group* and its associates are eliminated to the extent of the *Group's* interest in the associate. Unrealised losses are also excluded unless the transaction provides evidence that the transferred asset has been impaired.

3. SIGNIFICANT ASSUMPTIONS AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires the making of significant assumptions. It also requires management to make its assumptions and judgments using the accounting policies adopted by the *Group*.

The preparation of financial statements using IFRS requires the use of estimates and assumptions that affect the values of assets and liabilities reported in the financial statements and the information presented in the annexes at the financial reporting date, as well as revenue and expenditure recognised during the reporting period. Actual results may differ from these estimates. Areas that may be more affected by assumptions are management's assumptions and calculations in determining the recoverable amount of assets and the amount of provisions.

Useful life of property, plant, and equipment

At the end of each reporting period, the *Group* reviews the remaining useful life of the asset. Based on the *Group's* most recent assessment Financial Directorate, the current useful life of the *Group's* property, plant and equipment is the same as the actual useful life of the asset.

Provisions

When assessing provisions, management uses estimates of contingent obligations and the period in which the obligations could materialise. If these events do not occur or occur in a different manner, the actual cost may differ from the estimated cost. More detailed information on the assumptions regarding provisions is presented in Note 21.

Impairment of property, plant and equipment

An impairment loss is recognised for property, plant and equipment items that are not economically recoverable and for assets whose future expected economic benefits are significantly less than their carrying amount. The most significant impairment loss is recognised for buildings, structures and rail roads based on the future cash flows from the use of these assets to provide services. The future expected cash flows are determined based on the annual actual results for 2020 and extrapolated over the next ten years. The calculation period of ten years is chosen due to the particular nature of the assets of the infrastructure operator – they are long-term assets that provide income over a long period of time.

A weighted average cost of capital (WACC) of 2.54% is used in discounting the future forecast cash flows, which is the same as that used by the infrastructure manager. WACC is the most significant variable impacting the total impairment charge. WACC of 4.04% (increase of 1.5%) would increase the impairment by EUR 64 million. On the other hand, if the WACC was 2% (a decrease of 0.54%), no impairment would be recognised.

Financial balance payment

The main task of the *Company* is to ensure the operation of railway infrastructure of public use and safe, high-quality, and effective railway and logistics services for the benefit of the Latvian state and national economy. For this task, a Multi-Annual Agreement has been concluded with the Ministry of Transport, which provides for arrangements to ensure financial stability (see Note 4).

4. REVENUE

(EUR' 000)

	2020	2019
Revenue from customer contracts (15.IFRS):		
Cargo transportation	137 556	205 809
Fees for the use of public-use railway infrastructure	16 144	45 440
Forwarding services	15 620	30 400
Electricity sale services	5 792	5 538
Repair and maintenance of rolling stock	4 392	5 326
Additional services of the infrastructure manager	3 513	6 964
Fuel and oil sales	2 357	2 645
Specific services related to infrastructure maintenance and repair	2 075	1 216
Services of a principal	1 570	2 569
Security services	1 530	738
Services at passenger stations	996	-
International passenger transport	750	7 394
Information technology services	483	604
Electronic communications services	421	416
Traction provision services	118	196
Other services	3 431	5 943
Other revenue:		
Revenue for the maintenance of railway infrastructure (state budget funding)	30 276	11 648
Financial balance income*	22 514	-
Rental services	4 079	4 202
Revenue for maintenance of service sites (state budget funding)	249	597
Total	**253 866**	**337 645**

* The financial balance payment received in advance in the reporting year and additionally required to ensure financial stability is recognised as other income in accordance with the recognition principles set out in IAS 20 *Accounting for Government Grants*. A part of the required financial stability payment of EUR 9 503 thousand to be received in 2021, was recognised in the statement of financial

position under *Accrued income* (see Note 17) based on the commitments and obligations stipulated in the Multi-Annual agreement.

5. COST OF GOODS SOLD

(EUR' 000)

	2020	2019
Salaries	97 291	115 528
National social insurance mandatory contributions	23 340	27 683
Depreciation of property, plant and equipment and amortisation of intangible assets	59 599	62 350
Heating and fuel	21 601	36 743
Impairment of fixed assets (Note 12)	19 315	-
Materials	9 798	17 794
Electricity	9 243	9 408
Amortisation of the right-of-use assets	2 284	1 525
Other costs	43 462	68 463
Total	**285 933**	**339 494**

6. ADMINISTRATION COSTS

(EUR' 000)

	2020	2019
Salaries	13 000	16 961
National social insurance mandatory contributions	3 117	4 060
Depreciation of property, plant and equipment and amortisation of intangible assets	787	802
Materials, heating and fuels, electricity	164	390
Amortisation of the right-of-use assets	182	160
Other costs	1 989	3 107
Total	**19 239**	**25 480**
of which remuneration to members of the Management Board and Council of the *Group's* companies	1 374	929
including salary	*1 110*	*747*
national social security mandatory contributions (employer's contributions)	*264*	*182*

7. OTHER OPERATING INCOME

(EUR' 000)

	2020	2019
Deferred revenue (Note 24)	18 763	19 438
Gain on sale of scrap metal	2 203	491
Accrued annual leave liabilities	2 455	301
VAT adjustment for the minimum access to the service for 2019	2 571	-
Reduction of other provisions (Note 21)	1 936	4 263
Gain on sale of property, plant and equipment	1 623	170
Payments from other railway administrations for complex settlements	854	-
Penalties and overdue charges	221	296
State budget grant for compensation of damages	-	75
Gain on disposal of property, plant and equipment	162	-
Other revenue	986	1 028
Total	**31 774**	**26 062**

8. OTHER OPERATING COSTS

(EUR' 000)

	2020	2019
Payments to other railway administrations for complex settlements	4 283	-
Impairment of inventories (Notes 14 and 15)	2 509	195
Increase and use of Other provisions, net (Note 21)	5 736	1 866
Provisions for materials that have not been used for more than a year (Note 14)	421	1
Costs provided for in the collective agreement of the *Latvijas dzelzceļš Group*, etc.	402	1 301
Increase of provisions for doubtful debts	115	34
Foreign currency exchange rate fluctuations	87	13
Currency conversion	69	91
Penalties and overdue charges	38	47
Corporate income tax on deemed profit distribution	19	10
Social infrastructure maintenance costs	15	17
Liquidation costs of fixed assets and construction in progress	-	1 092
Other costs	672	475
Total	**14 366**	**5 142**

9. FINANCIAL COSTS, NET

(EUR' 000)

	2020	2019
Financial income	**-**	**2**
Bank interest	-	2
Financial costs	**(2 227)**	**(2 237)**
Bank interest, including long-term borrowing interest	(2 096)	(2 129)
Interest costs in lease transactions	(131)	(108)
Financial costs, net	**(2 227)**	**(2 235)**

10. CORPORATE INCOME TAX

The *Group's* deferred tax is calculated on the future corporate income tax due from the subsidiaries from the retained earnings of 2020, which are planned to be paid to the parent company in dividends in the following years, based on the amount of dividends from state capital companies established in the country.

Corporate income tax movement table for the reporting year

(EUR' 000)

	2020	2019
Overpaid at 1 January	51	28
Calculated for the reporting year	(702)	(10)
Paid in the reporting year	726	33
Transferred to other taxes	(31)	-
Overpaid at 31 December	**44**	**51**

Overpayment of corporate income tax and liabilities apply to various subsidiaries of the *Group*. The *Group* has no legal right to transfer these amounts to each other.

Current corporate income tax expense

(EUR' 000)

	2020	2019
Deferred corporate tax liability at the beginning of the year	1 759	745
Deferred corporate income tax liability (decrease)/increase	(1 293)	1 014
Deferred corporate tax liabilities at the end of the year	**466**	**1 759**

11. INTANGIBLE ASSETS

(EUR' 000)

LICENSES AND RIGHTS	2020	2019
Historical cost at the beginning of the year	**7 992**	**7 294**
Additions	117	730
Reclassified from property, plant and equipment	1 091	3
Disposals	(573)	(35)
Historical cost at the end of the year	**8 627**	**7 992**
Accumulated amortisation at the beginning of the year	**6 370**	**5 827**
Calculated amortisation	613	577
Reclassified from property, plant and equipment	133	-
Disposals	(543)	(34)
Accumulated amortisation at the end of the year	**6 573**	**6 370**
Residual value at the beginning of the year	**1 622**	**1 467**
Residual value at the end of the year	**2 054**	**1 622**

12. PROPERTY, PLANT AND EQUIPMENT (PPE)

(EUR' 000)

	LAND PLOTS	BUILDINGS, STRUCTURES AND PERRENIAL PLANTATIONS	TRACKS	LONG-TERM INVESTMENTS IN LEASED PPES	TECHNOLOGICAL EQUIPMENT AND DEVICES	WAGONS FOR FREIGHT TRANSPORT	COMPUTING EQUIPMENT, COMMUNICATIONS EQUIPMENT, COPIERS AND THEIR EQUIPMENT	OTHER PPE	COST OF UNFINISHED CONSTRUCTION OBJECTS	TOTAL
Historical cost/ revalued at 01.01.2019	**1 340**	**146 910**	**620 989**	**2 654**	**408 573**	**197 144**	**31 595**	**28 467**	**11 725**	**1 449 397**
Acquisition and creation of PPE	25	4 317	15 243	-	13 077	-	3 562	2 511	(9 663)	29 072
Reclassified	-	(63)	-	(2 417)*	4	-	(3)	59	-	(2 420)
Write-off of PPE	-	(136)	(3 879)	-	(1 688)	(631)	(658)	(617)	(42)	(7 651)
Historical cost/ revalued at 31.12.2019	**1 365**	**151 028**	**632 353**	**237**	**419 966**	**196 513**	**34 496**	**30 420**	**2 020**	**1 468 398**
Accumulated depreciation at 01.01.2019	**-**	**48 969**	**238 089**	**835**	**158 927**	**96 208**	**21 610**	**18 185**	**-**	**582 823**
Calculated depreciation	-	4 072	29 421	9	18 364	5 966	3 245	1 665	-	62 742
Reclassified	-	-	-	(671)*	4	-	-	(4)	-	(671)
On disposals	-	(110)	(2 934)	-	(1 620)	(438)	(653)	(602)	-	(6 357)
Accumulated depreciation at 31.12.2019	**-**	**52 931**	**264 576**	**173**	**175 675**	**101 736**	**24 202**	**19 244**	**-**	**638 537**
Impairment at 01.01.2019	**-**	**-**	**-**	**-**	**(5 375)**	**-**	**-**	**-**	**-**	**(5 375)**
Recognised impairment/ impairment reversal	-	-	-	-	-	-	-	-	-	-
Impairment at 31.12.2019	**-**	**-**	**-**	**-**	**(5 375)**	**-**	**-**	**-**	**-**	**(5 375)**
NBV at 01.01.2019	**1 340**	**97 941**	**382 900**	**1 819**	**244 271**	**100 936**	**9 985**	**10 282**	**11 725**	**861 199**
NBV at 31.12.2019	**1 365**	**98 097**	**367 777**	**64**	**238 916**	**94 777**	**10 294**	**11 176**	**2 020**	**824 486**

* reclassified to the right-of-use assets under IFRS 16 requirements in 2019.

(EUR' 000)

	LAND PLOTS	BUILDINGS, STRUCTURES AND PERRENIAL PLANTATIONS	TRACKS	LONG-TERM INVESTMENTS IN LEASED PPES	TECHNOLOGICAL EQUIPMENT AND DEVICES	WAGONS FOR FREIGHT TRANSPORT	COMPUTING EQUIPMENT, COMMUNICATIONS EQUIPMENT, COPIERS AND THEIR EQUIPMENT	OTHER PPE	COST OF UNFINISHED CONSTRUCTION OBJECTS	TOTAL
Historical cost/ revalued at 01.01.2020	**1 365**	**151 028**	**632 353**	**237**	**419 966**	**196 513**	**34 496**	**30 420**	**2 020**	**1 468 398**
Acquisition and creation of PPE	-	1 224	7 421	-	5 045	-	1 954	924	(573)	15 995
Reclassified	-	26	-	(26)	(26)	(3 343)	(1 091)	26	-	(4 434)
Disposals	-	(215)	(2 759)	(99)	(8 183)	(9 830)	(4 282)	(1 407)	(136)	(26 911)
Historical cost/ revalued at 31.12.2020	**1 365**	**152 063**	**637 015**	**112**	**416 802**	**183 340**	**31 077**	**29 963**	**1 311**	**1 453 048**
Accumulated depreciation at 01.01.2020	**-**	**52 931**	**264 576**	**173**	**175 675**	**101 736**	**24 202**	**19 244**	**-**	**638 537**
Calculated depreciation	-	4 160	28 594	8	16 768	5 412	3 215	1 742	-	59 899
Reclassified		11	-	(11)	(18)	(2 116)	(133)	18	-	(2 249)
On disposals	-	(197)	(2 485)	(99)	(7 660)	(8 774)	(4 139)	(1 369)	-	(24 723)
Accumulated depreciation at 31.12.2020	**-**	**56 905**	**290 685**	**71**	**184 765**	**96 258**	**23 145**	**19 635**	**-**	**671 464**
Impairment at 01.01.2020	**-**	**-**	**-**	**-**	**(5 375)**	**-**	**-**	**-**	**-**	**(5 375)**
Recognised impairment/ impairment reversal	(38)	(2 495)	(15 220)	-	(1 414)	-	-	(148)	-	**(19 315)**
Impairment at 31.12.2020	**(38)**	**(2 495)**	**(15 220)**	**-**	**(6 789)**	**-**	**-**	**(148)**	**-**	**(24 690)**
NBV at 01.01.2020	**1 365**	**98 097**	**367 777**	**64**	**238 916**	**94 777**	**10 294**	**11 176**	**2 020**	**824 486**
NBV at 31.12.2020	**1 327**	**92 663**	**331 110**	**41**	**225 248**	**87 082**	**7 932**	**10 180**	**1 311**	**756 894**

13. RIGHT-OF-USE ASSETS

(EUR' 000)

	RIGHT-OF-USE LAND PLOTS	RIGHT-OF-USE BUILDINGS AND STRUCTURES	RIGHT-OF-USE TRACKS	RIGHT-OF-USE TECHNOLOGICAL EQUIPMENT AND DEVICES	RIGHT-OF-USE COMPUTING EQUIPMENT AND THEIR EQUIPMENT, COMMUNICATIONS EQUIPMENT, COPIERS AND THEIR EQUIPMENT	RIGHT TO USE OTHER FIXED ASSETS	TOTAL
Historical cost at 01.01.2019	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Impact of the implementation of IFRS 16	492	3 334	2 611	-	1 020	901	8 358
Reclassified from PPE	-	2 417	-	-	-	-	2 417
New lease agreements	-	-		636	-	1 426	2 062
Amendments to contracts and termination of contracts	1	(131)	3	(13)	-	113	(27)
Historical cost at 31.12.2019	**493**	**5 620**	**2 614**	**623**	**1 020**	**2 440**	**12 810**
Accumulated amortisation at 01.01.2019	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Calculated amortisation as a result of implementation of IFRS 16	83	547	523	86	240	462	1 941
Reclassified from PPE	-	671	-	-	-	-	671
On disposals	-	-	-	-	-	(51)	(51)
Accumulated amortisation at 31.12.2019	**83**	**1 218**	**523**	**86**	**240**	**411**	**2 561**
NBV at 01.01.2019	**-**	**-**	**-**	**-**	**-**	**-**	**-**
NBV at 31.12.2019	**410**	**4 402**	**2 091**	**537**	**780**	**2 029**	**10 249**

(EUR' 000)

	RIGHT-OF-USE LAND PLOTS	RIGHT-OF- USE BUILDINGS AND STRUCTURES	RIGHT-OF-USE TRACKS	RIGHT-OF-USE TECHNOLOGICAL EQUIPMENT AND DEVICES	RIGHT-OF-USE COMPUTING EQUIPMENT AND THEIR EQUIPMENT, COMMUNICATIONS EQUIPMENT, COPIERS AND THEIR EQUIPMENT	RIGHT-OF-USE OTHER FIXED ASSETS	TOTAL
Historical cost at 01.01.2020	**493**	**5 620**	**2 614**	**623**	**1 020**	**2 440**	**12 810**
Impact of the implementation of IFRS 16							
New lease agreements	35	21	-	-	-	2 945	3 001
Amendments to contracts and termination of contracts	(118)	(2 531)	1 618	5	-	(311)	(1 337)
Historical cost at 31.12.2020	**410**	**3 110**	**4 232**	**628**	**1 020**	**5 074**	**14 474**
Accumulated amortisation at 01.01.2020	**83**	**1 218**	**523**	**86**	**240**	**411**	**2 561**
Calculated amortisation as a result of implementation of IFRS 16	83	546	521	163	246	907	2 466
On disposals	(42)	(818)	-	-	-	(32)	(892)
Accumulated amortisation at 31.12.2020	**124**	**946**	**1 044**	**249**	**486**	**1 286**	**4 135**
NBV at 01.01.2020	**410**	**4 402**	**2 091**	**537**	**780**	**2 029**	**10 249**
NBV at 31.12.2020	**286**	**2 164**	**3 188**	**379**	**534**	**3 788**	**10 339**

During the entire reporting period and comparative periods, 15 thousand hectares of land registered in the name of the Ministry of Transport was transferred to the *Group* for use (mostly it is a strip of railway land that is part of the railway public use infrastructure and is intended for the deployment of railway infrastructure facilities in order to ensure the development and safe operation of the railway infrastructure).

14. INVENTORIES

(EUR' 000)

	31.12.2020	31.12.2019
Road surface materials	6 507	11 453
Spare parts	6 798	8 695
Other materials	5 288	4 785
Heating and fuel	1 641	2 861
Other inventories and work in progress	1 525	870
Gross carrying amount	**21 759**	**28 664**
Provisions for materials that have not been used for more than a year	(3 197)	(2 776)
Impairment of inventories	(2 063)	(195)
NBV	**16 499**	**25 693**

15. ASSETS HELD FOR SALE

(EUR ' 000)

	31.12.2020	31.12.2019
Wagons and locomotives held for sale	1 141	-
Total	**1 141**	**-**

Assets held for sale

In December 2020, the management of SIA "LDZ CARGO" approved a plan to sell at auction 200 freight wagons and 9 diesel locomotives, which are not used in operation by SIA "LDZ CARGO". The sale is expected to be completed by the end of 2021. Under IFRS 5 *Non-current assets held for sale and discontinued operations*, rolling stock intended for sale in the annual financial statements for 2020 was reclassified from the item *Long-term investments – property, plant and equipment* to the item *Current assets –Long-term assets held for sale*.

One-off fair value measurements

Assets held for sale at the time of reclassification were valued at the lowest of their carrying amount and fair value less cost to sell. As a result, an impairment charge in the value of EUR 446 thousand was recognised, which was included in the statement of comprehensive income as *Other operating expenses*. The fair value of assets is determined based on the selling price of other similar assets on the market. This measurement corresponds to Level 2 fair value measurement under the fair value measurement hierarchy described in Note 26.

16. TRADE AND OTHER RECEIVABLES

(EUR' 000)

	31.12.2020	31.12.2019
Trade receivables	7 873	7 236
Overpaid value added tax	3 080	4 309
Doubtful debts	1 247	1 138
Other payables	2 772	4 759
Gross carrying amount	**14 972**	**17 442**
Provisions for impairment of receivables	(1 247)	(1 138)
NBV	**13 725**	**16 304**

Receivable impairment movement table:

(EUR' 000)

	2020	2019
Provisions for impairment of receivables at the beginning of the year	1 138	1 411
Reduction of provisions due to recovery of receivables	(56)	(38)
Reduction of provisions due to write-off of the receivables	(17)	(307)
Additional provisions created	182	72
Provisions for impairment of receivables at the end of the year	**1 247**	**1 138**

To estimate the expected impairment, the receivables were grouped according to their risk characteristics and days outstanding (see detailed information in Note 25). The expected loss rates are based on historical recovery figures, determined as the ratio of bad debts to relevant sales in the last 36 months (counted either from 31 December 2020 or from 1 January 2020). The historical loss ratios have been adjusted to reflect current and forecast information on macroeconomic factors affecting the ability of customers to settle with the *Group*. GDP forecasts are considered the most important factor as they have the most direct impact on bad debts.

In making these calculations as at 31 December 2020 and 1 January 2020, the provisions for such trade receivables that were paid within the terms or were outstanding for less than 6 months were immaterial, therefore they have been recognised at nil in the financial statements.

Similar calculations were made for other debtors and cash and cash equivalents, except that these calculations were based on external credit rating agencies' default rates for similar debtors or groups of debtors rather than historical experience. This approach was adopted as the *Group* does not have historical data on losses on these groups of financial assets. As a result of the calculations as of 31 December 2019 and 31 December 2020, it was determined that the credit quality of the assets was good, therefore the expected credit losses were not material and were set at zero.

In accordance with the *Group's* accounting policy, trade receivables that are more than six months outstanding are generally provided for at 100% for expected credit losses, with adjustments made only to reflect the possible recoverability of such receivables.

17. ACCRUED INCOME

	31.12.2020	31.12.2019
Accrued income	9 503	-
Total	**9 503**	**-**

In the reporting year, the required additional financial stability payment received in advance was recognised under *Other income* in accordance with IAS 20 *Accounting for government grants*. These principles determine the recognition of state grants at the moment when there is reasonable certainty of the fulfilment of the conditions relating to the receipt of the grant. In addition, grants relating to the payment of costs should be recognised during the period when the costs occurred, provided that there is reasonable certainty of receipt of the grant in the future.

The criteria for the *Company* to receive the financial stability compensation is non-compliance with the financial equilibrium conditions set out in the Multi-Annual Agreement. Since the Company did not meet the financial stability conditions provided for in the Multi-Annual Agreement in 2020, the criteria for receiving the financial compensation provided for in the Multi-Annual Agreement were accordingly met, as well as the receipt of an advance from the Ministry of transport provided reasonable assurance of the intention and ability of the other party to fulfil the conditions of the Multi-Annual Agreement, the annual revenue.

Latvijas dzelzceļš has received an advance payment of EUR 13 011 000 from the financial stability payment for the state-owned operator of the publicly used railway infrastructure, the full amount of which has been used to cover losses and recognized as other income as at 31.12.2020. Part of the required financial stability payment of EUR 9 503 295 to be received in 2021 was recognised under Accrued income in the Statement of financial position based on the commitments and obligations laid down in the Multi-Annual Agreement.

18. CASH AND CASH EQUIVALENTS

(EUR' 000)

	31.12.2020	**31.12.2019**
Cash at bank	87 260	67 469
Cash on hand	-	2
Total	**87 260**	**67 471**

19. SHARE CAPITAL

Registered and paid-up share capital of the Group's parent company

The share capital of *Latvijas dzelzceļš* is EUR 289 142 391, consisting of two hundred and eighty-nine million one hundred and forty-two thousand three hundred and ninety-one shares, with a nominal value of EUR 1 (one EUR) per share. Under the Cabinet Regulation No. 392 *On Increasing the Share Capital of the State Joint Stock Company Latvijas Dzelzceļš* of 15.07.2020, share capital was increased by EUR 32 422 016.

The Republic of Latvia is the sole shareholder, the shares have been fully paid-up. The holder of capital shares of the Company is the Ministry of Transport. All shares of the Company carry equal rights to receive dividends, liquidation quota and voting rights at the meeting of shareholders.

Payments for the use of state capital (dividends)

Since the Cabinet had not adopted a resolution in 2020 on the share of profits of VAS Latvijas dzelzceļš to be distributed in the form of dividends for 2019, pursuant to Paragraph 3 of Cabinet Regulation No. 806 *Procedure under which state corporations and public-private corporations in which the state has a shareholding forecast and determine the share of profit to be distributed in the form of dividends and make payments to the state budget for the use of state capital* of 22.12.2015, the minimum predictable share of profit to be distributed in the form of dividends and the share of profit to be distributed in the form of dividends shall be 80% of the profit for the reporting year of the corporation, unless otherwise specified in the medium-term operational strategy. Pursuant to paragraph 9, no later than two months after the approval of the company's annual report, the general meeting of shareholders shall decide on the proportion of profit to be distributed in the form of dividends as a percentage of the corporation's profit.

On 27 August 2020, the shareholder meeting, by resolution No. A1.1./ 4-3, decided to distribute the net profit of EUR 25 944 of VAS *Latvijas dzelzceļš* for the year 2019 in the form of dividends and to retain 20%, i.e., EUR 6 486 as reserves of VAS *Latvijas dzelzceļš* of public-use railway infrastructure for development and reconstruction, including accumulation of reserves that can be used by *the Company*, which will ensure sustainability of maintenance and for use of public-use railway infrastructure for implementation of projects in accordance with the medium-term strategy of the *Company* for the years 2017-2022.

20. LONG-TERM INVESTMENT REVALUATION RESERVE, OTHER RESERVES AND RETAINED EARNINGS

From 1 July 2013, wagons used for the transport of goods, which form part of the railway's rolling stock, are accounted for in the Group using the revaluation method. In 2013, these fixed assets were revalued and the increase in value is recognized as a long-term investment revaluation reserve (net with tax effect). In 2018, SIA “LDZ CARGO” carried out the valuation of its freight wagons using the market method. The commission decided to consider the residual value of fixed assets as fair value and not to revalue the fixed assets as the current market value of freight wagons does not differ significantly from the existing book value. The established market value would be only 0,41% higher than the existing book value.

Reserves consist of retained profits of previous periods which have been transferred to other reserves by decision of the owner in order to ensure the development of the Group. Therefore, reserves and retained earnings of prior periods do not differ in nature and are therefore combined in a single balance sheet item. The procedure for using the *Group* parent company's reserves and retained earnings from previous years is determined by the *Group* parent company's shareholder meeting.

21. PROVISIONS

(EUR' 000)

	31.12.2020	31.12.2019
Provisions for fines imposed by the Competition Council	5 694	-
Other provisions	127	127
Total non-current share	**5 821**	**127**
Other provisions	264	2 159
Total current portion	**264**	**2 159**
Total	**6 085**	**2 286**

Provisions movement table by type of provision in 2020

(EUR' 000)

	01.01.2020.	INCREASE IN PROVISIONS	DECREASE IN PROVISIONS	31.12.2020
Provisions for fines imposed by the Competition Council	-	5 694	-	5 694
Provisions for possible losses from litigation	6	-	-	6
Other provisions	2 280	42	(1 937)	385
Total	**2 286**	**5 736**	**(1 937)**	**6 085**

In 2018, the Competition Council initiated Procedure No. KL\5-5\18\30 *On the violation of the prohibition under Section 13, paragraph one of the Competition Law in the activities of SIA “LDZ CARGO” and SJSC “Latvijas dzelzceļš” on the rail freight market in Latvia*. On 05.01.2021, an extract from the minutes of the Competition Council meeting has been received with the information that on 28.12.2020 a decision was taken on imposing a fine in the amount of EUR 5 694 thousand against SIA “LDZ CARGO” jointly with VAS “Latvijas dzelzceļš”. SIA “LDZ CARGO” believes that the decision was made on the basis of erroneous conclusions based on a misunderstanding of the nature of the carrier's activity. The decision of Competition Council, Case No. KL\ 5-5\18\30 is appealed to the District Administrative Court with the aim to recognise it as unfounded and cancel it altogether. Currently, it is not possible to predict the outcome of the appeal of the decision, as well as additional risks related to the possible assertion of claims by other persons whose rights may be affected if the decision of the Competition Council is not reversed. Due to the said, in 2020 the provisions for contingent losses from fines were increased by EUR 5 694 thousand and amount to EUR 5 694 thousand.

The increase and the use of the provisions are recognized as net amounts as part of other operating income or other operating expenses.

Provisions movement table by type of provision in 2019

(EUR' 000)

	01.01.2019	INCREASE IN PROVISIONS	DECREASE IN PROVISIONS	31.12.2019
Provisions for public use railway infrastructure services	3 461	-	(3 461)	-
Provisions for possible losses from litigation	15	3	(12)	6
Other provisions	1 207	1 863	(790)	2 280
Total	**4 683**	**1 866**	**(4 263)**	**2 286**

22. BORROWINGS FROM CREDIT INSTITUTIONS

(EUR' 000)

	31.12.2020	RESTATED 31.12.2019
Non-current borrowings from credit institutions	120 615	94 290
Short-term borrowings from credit institutions	38 213	94 897
Total borrowings from credit institutions	**158 828**	**189 187**

Borrowings were used from Swedbank AS, Nordea Bank AB, SEB banka AS, Nordic Investment Bank, OP Corporate Bank plc, OP Corporate Bank branch in Latvia and Luminor Bank AS Latvian branch. During the reporting period, loans totalling EUR 10 001 thousand and repaid EUR 40 360 thousand.

The loan agreements concluded by *Latvijas dzelzceļš* with the banks specify the respective financial covenants of VAS Latvijas dzelzceļš or the consolidated financial statements, which must be complied with during the term of the credit agreement. At 31 December 2020 and the beginning of 2021, no long-term borrowings had breach of covenants.

One of the business activities of SIA “LDZ ritošā sastāva serviss” is the sale of diesel fuel. According to Section 31 of the law On Excise Tax, in order to carry out operations with excisable goods and use deferred payment of tax, the taxpayer must provide security. In 2020, SIA “LDZ ritošā sastāva serviss” received an insurance policy from AAS “Baltijas apdrošināšanas nams” for EUR 2 200 thousand for the general security of excise duty until 1 June 2021.

In the financial statements for 2020, the classification error made in the previous period was corrected. The error of EUR 54 538 thousand was due to the breach of covenants specified in the borrowing agreements, which led to specified borrowings required to be presented in the financial statements as current borrowings, under the requirements of IAS 1 *Presentation of financial statements*, while they were presented as non-current borrowings. In the financial statements of 2020, the opening balances were restated, reclassifying accordingly the 2019 indicators and correcting errors that arose in the previous period.

Borrowings repayable and interest rates at 31 December 2020

BORROWING CURRENCY	BORROWING, EUR ' 000	INTEREST RATE
EUR	120 284	3M EURIBOR + 0,77% to 3,5%
	38 544	6m EURIBOR + 0,75% to 1,2%
Total	**158 828**	

Borrowings repayable and interest rates at 31 December 2019

BORROWING CURRENCY	BORROWING, EUR ' 000	INTEREST RATE
	13 222	1M EURIBOR + 1.33%
EUR	129 717	3M EURIBOR + 0.69% to 1.61%
	46 248	6m EURIBOR + 1.05% to 1.8%

Total	**189 187**	

Borrowings movement table

(EUR' 000)

	2020	2019
Borrowings at the beginning of the reporting year	**189 187**	**201 519**
Received in the reporting year	10 001	23 778
Paid in the reporting year	(40 360)	(36 121)
Foreign currency exchange rate fluctuations	-	11
Borrowings at the end of the reporting year	**158 828**	**189 187**

Impact of exchange rate fluctuations on foreign currency borrowings

(EUR' 000)

BORROWING CURRENCY: USD	2020	2019
Borrowings at the beginning of the reporting year	**-**	**572**
Paid in the reporting year	-	(583)
Foreign currency exchange rate fluctuations	-	11
Borrowings at the end of the reporting year	**-**	**-**

23. TAXES AND NATIONAL SOCIAL INSURANCE MANDATORY CONTRIBUTIONS

Movement of tax and national state social insurance mandatory contributions in the reporting year

(EUR' 000)

TYPE OF TAX	TAX) LIABILITIES (+) AT 31.12.2019	TAX OVERPAYMENT (-) AT 31.12.2019	TAX) LIABILITIES (+) AT 31.12.2020	TAX OVERPAYMENT (-) AT 31.12.2020
Corporate income tax	-	(51)	-	(44)
National social insurance mandatory contributions	4 124	-	12 903	-
Personal income tax	1 964	-	5 004	-
including Belarus	*1*	-	*1*	-
Excise duty	1 482	-	1 152	-
Natural resources tax	13	-	21	-
Value added tax	2 539	(4 309)	4 937	(3 080)
Stamp duty for storage of safety reserves	48	-	33	-
Business risk duty	4	-	3	-
Total, including	**10 174**	**(4 360)**	**24 053***	**(3 124)**

** Non-current liabilities 19 423 thousand. EUR, current liabilities-4 630 thousand. EUR.*

At 31 December 2020 the Group had no outstanding payments to the budget.

The increase in personal income tax, national social insurance mandatory contributions and value added tax liabilities is related to the fact that in the emergency situation, the State Revenue Service has extended for *Latvijas dzelzceļš* the payment term for the personal income tax, state social insurance mandatory contribution and value added tax for April, May, June, July and December 2020 for three years, because *Latvijas dzelzceļš* complied with the provisions of Section 4, paragraph one of the Covid-19 Infection Consequence Management Law.

24. DEFERRED REVENUE

(EUR' 000)

	31.12.2020	31.12.2019
Non-current portion of deferred revenue (EU funds and State budget funds)	261 262	274 298
Other deferred revenue	67	92
Total non-current portion	**261 329**	**274 390**
Short-term portion of deferred revenue (EU funds and state budget funds)	19 341	20 572
Other deferred revenue	1 526	2 779
Total current portion	**20 867**	**23 351**
Total deferred revenue	**282 196**	**297 741**

Most of the revenue for future periods is from EU funds and State budget funds received for the development of railway infrastructure.

EU project fund movement table for property, plant and equipment financed from EU funds in 2020:

(EUR' 000)

DEFERRED REVENUE	BALANCE AT 01.01.2020.	RECLASSIFIED (MOVED)	RECEIVED STATE BUDGET FUNDS	REFUNDING OF UNUSED FUNDS	REDUCTION DUE TO DEPRECIATION OF PPE	BALANCE AT 31.12.2020
Non-current portion	274 298	(17 751)	4 715	-	-	261 262
Current portion	20 572	17 751	-	(219)	(18 763)	19 341
Total	**294 870**	**-**	**4 715**	**(219)**	**(18 763)**	**280 603**

An advance payment of EUR 4 694 thousand was received from the EU fund for the project *Modernisation of the Riga Railway Junction Section Sarkandaugava-Mangali-Ziemeļblāzma* and received a prepayment of 39 thousand EUR from the European Commission and Innovation and Networks Executive Agency (INEA) as manager of the Connecting Europe Facility (CEF) for the project *Building an Interoperable Railway System in the Baltic States* of which EUR 18 thousand were remitted by *Latvijas dzelzceļš* as the recipient of the financing (beneficiary) to AS *Eesti Raudtee*.

EU project fund movement table for property, plant and equipment financed from EU funds in 2019:

(EUR' 000)

DEFERRED REVENUE	BALANCE AT 01.01.2019.	RECLASSIFIED (MOVED)	ADJUSTMENT	REDUCTION DUE TO DEPRECIATION OF PPE	BALANCE AT 31.12.2019
Non-current portion	290 238	(20 616)	4 676	-	274 298
Current portion	19 394	20 616	-	(19 438)	20 572
Total	**309 632**	**-**	**4 676**	**(19 438)**	**294 870**

In 2019, an advance payment of EUR 4 664 thousand from the EU fund for the project *Modernisation of the Riga Railway Junction Section Sarkandaugava-Mangali-Ziemeļblāzma* and received a prepayment of EUR 21 thousand from the European Commission and Innovation and Networks Executive Agency (INEA) as manager of the Connecting Europe Facility (CEF) for the project *Building an Interoperable Railway System in the Baltic States* of which EUR 9 thousand were remitted by *Latvijas dzelzceļš* as the recipient of the financing (beneficiary) to AS Eesti Raudtee.

25. FINANCIAL RISK MANAGEMENT

The *Group's* most important financial instruments are borrowings from banks, other borrowings, money and deposits with banks, as well as receivables and payables. The main task of these financial instruments is to ensure the financing of the *Group's* business activities. The *Group* also has a number of other financial assets and liabilities, such as buyers 'and customers' debts and debts to suppliers and contractors arising directly from its economic activities.

The *Group* is exposed to market, credit and liquidity risks related to its financial instruments.

Financial risk management is ensured by the *Group's* parent company's Financial Directorate and the *Group's* Financial Committee.

Financial instruments of the *Group* are divided into the following categories:

(EUR' 000)

	31.12.2020	31.12.2019
Financial assets at amortised cost		
Trade and other receivables, excluding advances	17 376	7 236
Cash and cash equivalents	87 260	67 471
Financial assets at fair value through revaluation in profit or loss account		
Long-term financial investments	84	84
Total financial assets	**104 720**	**74 791**
Financial liabilities at amortised cost		
Borrowings from credit institutions	158 828	189 187
Trade and other payables, lease obligations, excluding advances (including non-current portion)	34 890	43 109
Total financial liabilities	**193 718**	**232 296**

Market risk

Market risk is the risk that changes in market factors such as changes in foreign exchange rates, interest rates and commodity prices will affect the *Group's* revenue or the value of its financial instruments. Market risk includes currency risk and interest rate risk.

Interest rate risk

Interest rate risk is the risk of incurring losses due to changes in interest rates on assets and liabilities of the *Group*. The *Group* is exposed to the risk of market interest rate changes in relation to its non-current liabilities subject to variable interest rates.

All the *Group's* borrowings have variable interest rates. For a detailed description of interest rates on borrowings see Note 22. The *Group* manages its interest rate risk by periodically evaluating borrowing rates available in the market. When lower than current interest rates are available, the Company evaluates the financial benefits of debt restructuring.

Group companies do not use financial derivatives to manage interest rate risks.

Interest rate sensitivity

The following table sets out the sensitivity of the *Group's* pre-tax profit to reasonably possible changes in interest rates at the end of each reporting period, provided that all other variables remain unchanged. The *Group's* own funds, equity, except for the result of the reporting year, is not affected.

(EUR' 000)

	2020		2019	
	BASE RATE INCREASE / DECREASE (BASE POINTS)	EFFECT ON PROFIT BEFORE TAX (EUR ' 000)	BASE RATE INCREASE / DECREASE (BASE POINTS)	EFFECT ON PROFIT BEFORE TAX (EUR ' 000)
EURIBOR	(+100)	(1 589)	(+100)	(1 892)
	(-100)	1 589	(-100)	1 892

Currency risk

Currency risk is the risk of incurring losses as a result of unfavourable foreign currency exchange rate changes in relation to assets and liabilities in foreign currencies. The currency risk to which the *Group* is exposed mainly results from its economic activities – revenues and costs are denominated in different currencies from foreign loans. The *Group's* trade payables are mainly denominated in EUR, while loans from banks are denominated in EUR and US dollars. A detailed breakdown of financial instruments by currency is provided in Note 28. The main currency risk management tool used by the *Group* is the identification and use of the currency assets of the *Group's* companies within the *Group* to cover the liabilities of the *Group's* companies in foreign currencies.

Group companies do not use financial derivatives to manage currency risks.

Currency sensitivity

The *Group* did not have significant foreign currency balances during the reporting year; therefore, the potential impact of exchange rate fluctuations was insignificant.

Credit risk

Credit risk is the risk that a counterparty will default on its obligations to the *Company*, causing it significant financial loss. The Company is exposed to credit risk arising directly from its business activities - mainly trade receivables, and credit risk related to the *Company's* financing activities - mainly cash deposits with banks.

Trade receivables

Each company of the *Group* manages trade receivables in accordance with the *Group's* policies. Before concluding contracts, the solvency of buyers and customers is assessed. The *Company* will insure against credit risk by receiving prepayments from its customers.

The *Group* continuously monitors the balances of receivables in order to minimise the possibility of incurring irrecoverable receivables arising. Possible impairment of trade debts is constantly analysed. The *Group* has not received pledges as collateral for the trade receivables.

The *Group* rates its concentration of its trade receivables is medium. At 31 December 2020, the Group had three customers (2019: two customers), who each owed the *Group* more than EUR 700 thousand and accounted for about 70.6% (2019: 41.6%) of total receivables.

The *Group* has not developed an internal credit rating system for assessing trade receivables.

In 2020, there were no significant changes in the expected credit losses in relation to trade receivables. Write-off of trade receivables occurs only if their recovery is not expected. Indicators indicating the impossibility of recovery include, among others, the debtor's inability to agree on a repayment schedule, which is accompanied by the debtor's insolvency, bankruptcy or liquidation.

The *Group* is subject to maximum credit risk as shown in the table below:

(EUR' 000)

	31.12.2020	31.12.2019
Cash and cash equivalents	87 260	67 471
Receivables and other receivables (gross amount), excluding advances and prepayments	18 623	8 374
Total	**105 883**	**75 845**

At 31 December 2020, expected credit losses were determined by applying the following expected credit loss rates:

(EUR' 000)

	CURRENT	OUTSTANDING FOR OVER 30 DAYS	OUTSTANDING FOR OVER 90 DAYS	OUTSTANDING FOR 120 DAYS	TOTAL
Expected credit loss rate	0.3%	2.0%	11.0%	90.0%	
Trade and other receivables (gross amount)	17 195	70	33	1 325	**18 623**
Expected credit loss	(49)	(1)	(4)	(1 193)	**(1 247)**

At 31 December 2019, expected credit losses were determined applying the following expected credit loss rates:

(EUR' 000)

	CURRENT	OUTSTANDING FOR OVER 30 DAYS	OUTSTANDING FOR OVER 90 DAYS	OUTSTANDING FOR 120 DAYS	TOTAL
Expected credit loss rate	0,5%	2.0%	11.0%	95,9%	-
Trade and other receivables (gross amount)	7 193	31	2	1 148	**8 374**
Expected credit loss	(36)	(1)	-	(1 101)	**(1 138)**

Cash deposits

Credit risk arising from the *Group's* cash deposits with banks is managed by the *Group's* Finance Committee in accordance with the *Group's* financial management policy. According to this policy, the *Group's* free resources are allowed to be invested only in deposits or money market funds. Before placing funds in banks (deposits or current accounts), the *Group's* Finance committee evaluates the credit ratings of banks and the interest rates offered.

The *Group's* cash balances with banks in accordance with the bank credit ratings assigned by Moody's:

(EUR' 000)

RATING	31.12.2020	31.12.2019
Aa2	10	15 029
Aa3	5 004	2
A3	74 564	-
Baa1	-	44 345
Unrated*	7 682	8 093
Total	**87 260**	**67 469**

** No ratings assigned to the State Treasury and VAS "Latvijas pasts" (State-owned company).*

Liquidity risk

Liquidity risk is the risk that the *Group* will not be able to meet its financial obligations when they fall due.

The *Group's* Finance Committee manages the liquidity risk by maintaining adequate cash reserves and ensuring sufficient funding through granted loans, lines of credit, financial leases, etc. as well as continuously monitoring projected and actual cash flows and harmonizing the term structure of financial assets and liabilities.

The *Group* prepares a long-term cash flow forecast for the year and an operational cash flow forecast for one week to ensure that the *Group* has sufficient funds at its disposal to finance the expected operating costs, settle financial liabilities and make the necessary investments.

At 31 December 2020, the *Group's* current assets exceeded current liabilities by EUR 35 140 thousand, resulting in total liquidity-current assets and current liabilities ratio of 1.4. Current liabilities include deferred revenue of EUR 19 341 thousand related to the investment of EU projects and state budget funds in railway public infrastructure, therefore there is a low risk that financial resources will be required to cover these commitments. The total liquidity ratio, excluding deferred revenue related to the investments of EU projects and state budget funds in railway public infrastructure, is 1.7.

The concluded loan agreements with the banks specify financial covenants, which *Latvijas dzelzceļš* must comply with during the term of the agreement. At 31 December 2020 and the beginning of 2021, none of the non-current borrowings had breach of covenants.

In the following tables, the *Group's* financial liabilities are analysed by their maturity based on the amounts of non-discounted financial liabilities, including interest payments, specified in the contracts:

(EUR' 000)

AT 31 DECEMBER 2020	UP TO 3 MONTHS	3 TO 12 MONTHS	1 TO 5 YEARS	MORE THAN 5 YEARS	TOTAL
Borrowings from credit institutions	7 799	32 188	104 986	19 235	164 208
Other liabilities (including other borrowings, trade and other payables)	16 890	9 505	7 316	1 547	35 258
Total	**24 689**	**41 693**	**112 302**	**20 782**	**199 466**

(EUR' 000)

AT 31 DECEMBER 2019	UP TO 3 MONTHS	3 TO 12 MONTHS	1 TO 5 YEARS	MORE THAN 5 YEARS	TOTAL
Borrowings from credit institutions	9 004	90 060	70 930	26 190	196 184
Other liabilities (including other borrowings, trade and other payables)	22 460	11 638	7 134	2 162	43 394
Total	**31 464**	**101 698**	**278 064**	**28 352**	**239 578**

26. FAIR VALUE CONSIDERATIONS

IFRS 13 lays down the value measurement technique hierarchy, based on whether the measurement technique uses observable market data or market data are not observable. Observable market data are obtained from independent sources. If market data are not observable, the value measurement technique reflects *the Company's* assumptions about the market situation.

The said hierarchy requires that observable market data must be used if they are available. In carrying out revaluation, *the Company* takes into consideration the relevant observable market prices, if possible.

The purpose of the fair value measurement, even in inactive markets, is to arrive at the price at which market participants would be willing to sell the asset or assume the liability at the measurement date under current market conditions.

To determine the fair value of a financial instrument, several methods are used: quoted prices or a valuation technique that includes observable market data and is based on internal models. Based on the fair value hierarchy, all measurement techniques are subdivided into Level 1, Level 2, and Level 3.

The fair value hierarchy level of a financial instrument level must be determined as the lowest level if a substantial part of the value is made up of lower level data.

In the fair value hierarchy, financial instruments are grouped into two stages:

1. Group the data of each level to determine the fair value hierarchy;

2. Assets are grouped at the lowest level, based on proportion of observable data used in determination of the fair value.

Quoted market prices - Level 1

Valuation technique at Level 1 uses unadjusted quotation prices in an active market, for identical assets or liabilities are used where the quotation prices are readily available and the price is representative of the actual market situation for transactions under fair competition circumstances. The *Group* does not have financial instruments measured at Level 1.

At Level 2, the valuation technique uses market data

In the models used in valuation technique Level 2, all relevant data, directly or indirectly, are observed on part of assets or liabilities. The model uses market data other than quoted prices included in Level 1 but rather that are observed either directly (i.e., price) or indirectly (i.e., derived from the price). The *Group's* cash and cash equivalents correspond to Level 2 fair value hierarchy.

Valuation technique when market data are used that are not based on observable market data – Level 3.

In the valuation technique, when market data are used that are not based on observable market data (unobservable market data) are classified as Level 3. Data that are not readily available on an active market, because of the complexity of an illiquid market or a financial instrument are observable market data. Level 3 data shall be predominantly determined based on observable market data of a similar nature, historical observations or using analytical approaches.

The following financial assets and liabilities are included in Level 3:

		(EUR' 000)
ACTIVELY:	**31.12.2020**	**31.12.2019**
Net trade receivables	17 376	7 236
Long-term financial investments	84	84
Total	**17 460**	**7 320**

		(EUR' 000)
COMMIT:	**31.12.2020**	**31.12.2019**
Borrowings from credit institutions	158 828	189 187
Trade payables	34 890	43 109
Total	**193 718**	**232 296**

Assets and liabilities for which fair value is disclosed

The carrying value of liquid and short-term (repayment term not exceeding three months) financial instruments, such as cash and cash equivalents, short-term deposits, short-term receivables and payables, approximately corresponds to their fair value.

The fair value of borrowings from credit institutions, financial leases and other non-current liabilities is assessed by discounting future cash flows by applying market interest rates. As the interest rates applied to borrowings from credit institutions, finance lease liabilities and other non-current liabilities are generally variable and do not differ materially from market interest rates, and the risk premium applied to the *Group* has not changed significantly, the fair value of non-current liabilities approximates their carrying amount.

Assets measured at fair value

The evaluation analysis of the economic activity of freight wagon park management has been carried out in accordance with the norms of the Commercial Law of the Republic of Latvia, the definition of the market value of assets formulated in International Valuation Standards and in accordance with International Financial Reporting Standard 13 *Fair Value Measurement*.

27. CAPITAL MANAGEMENT

The Republic of Latvia owns 100% shares in VAS Latvijas dzelzceļš.

The *Groups objectives* in terms of capital management are to ensure the *Group's* ability to continue as a going concern and provide the return on capital set by the shareholder meeting. The Latvian Government has the right to take decisions related to the increase or reduction of the share capital of *the Group*, the payment of dividends or using them for the development of the Group.

For capital management purposes, the *Group* assesses the leverage ratio. The *Group's* financial risk management policy does not set a minimum or maximum amount for this indicator. When preparing the short - term and long-term financial plans and budgets, the *Group* considers the financial conditions set by the banks regarding the leverage ratio.

	31.12.2020	(EUR' 000) 31.12.2019
Loans from credit institutions and other borrowings	158 828	189 187
Liabilities (including taxes)	61 742	58 001
Other liabilities	288 747	301 786
Total liabilities	**509 317**	**548 974**
Equity	393 919	397 038
Total liabilities and equity	**903 236**	**946 012**
Leverage ratio	56%	58%
Equity to total liabilities ratio	77%	72%

28. ANALYSIS OF FINANCIAL ASSETS AND LIABILITIES BY CURRENCY

The table below shows the *Group's* financial instruments by currency at 31 December 2020:

	EUR	USD	OTHER CURRENCIES	TOTAL
	EUR ' 000	EUR ' 000	EUR ' 000	EUR ' 000
Trade and other receivables, excluding advances	17 069	153	154	17 376
Cash and cash equivalents	85 696	63	1 501	87 260
Total financial assets	**102 765**	**216**	**1 655**	**104 636**
Borrowings from credit institutions	158 828	-	-	158 828
Trade and other payables, except advances	32 776	98	2 016	34 890
Total financial liabilities	**191 604**	**98**	**2 016**	**193 718**

The table below shows the *Group's* financial instruments by currency at 31 December 2019:

	EUR	USD	OTHER CURRENCIES	TOTAL
	EUR ' 000	EUR ' 000	EUR ' 000	EUR ' 000
Trade and other receivables, excluding advances	6 626	206	404	7 236
Cash and cash equivalents	66 899	114	458	67 471
Total financial assets	**73 525**	**320**	**862**	**74 707**
Borrowings from credit institutions	189 187	-	-	189 187
Trade and other payables, except advances	40 305	178	2 626	43 109
Total financial liabilities	**229 492**	**178**	**2 626**	**232 296**

29. CAPITAL COMMITMENTS

In the next reporting year, the *Company* expects to make capital expenditure in property, plant and equipment and intangible assets, of which:

- major contracts concluded but not yet completed are:

NAME OF COUNTERPARTY, SUBJECT OF CONTRACT	DATE OF CONTRACT	TERM OF EXECUTION OF THE CONTRACT	CONTRACT AMOUNT EUR '000
Association of entities Belam-Leonhard Weiss *Modernisation of Riga Railway Junction section Sarkandaugava-Mangali - Ziemelblazma*: construction	13.12.2019	15.01.2023	21 950
General partnership *Belam-Belss pilnsabiedrība* Implementation of digital radio communication system	13.08.2020	13.08.2022	6 506

30. CONTINGENT TAX LIABILITIES

At any time within three years after the tax year, the tax authorities may conduct an audit of the accounts and calculate additional liabilities and penalties. The Management of the *Group* is not aware of any such circumstances that could result in a potential material liability in the future.

31. FUTURE LEASE PAYMENTS

In 2020, the *Group's* costs in connection with the concluded operating lease agreements were EUR 1 477 thousand, and EUR 2 354 thousand in 2019, respectively.

32. STAFF COSTS

(EUR' 000)

	2020	2019
Payroll	111 698	134 497
National social security mandatory contributions (employer's contributions)	26 796	32 226

Average number of persons employed in the *Group* in 2020 were 8 539 (in 2019: 10 155).

33. TRANSACTIONS WITH RELATED PARTIES

The *Group* engages in transactions with the Ministry of Transport (100% shareholder of *Latvijas dzelzceļš*) and other commercial companies owned by the State. The largest transactions are carried out with AS “Pasažieru vilciens” (charges for the public use of the railway infrastructure for domestic passenger services, electricity distribution and sales, leasing of premises, subscribers’ tickets): EUR 16 959 thousand (in 2019: EUR 35 577 thousand) and VAS Latvenergo (purchase of electricity) for EUR 10 447 thousand (in 2019: EUR 8 350 thousand). The mutual transactions are related to the main activities of the parties concerned.

34. COVID-19 AND GOING CONCERN

Freight traffic trends in 2020 and 2021, along with current developments that could impact the global and regional economy, including the Covid-19 pandemic, suggest that freight traffic volumes will not improve significantly. There is a significant decline in freight volumes in 2020, plus the Covid-19 pandemic is having an additional negative impact on operations. Due to the virus, face-to-face meetings have had to be kept to a minimum and remote working has been used as much as possible. International passenger traffic has been completely suspended. The restrictions imposed by Covid-19 may have had an additional negative impact on freight volumes.

In response to the changes in freight volumes in the second half of 2019 and in 2020, the *Group's* contingency action plan included several measures that enabled overall costs to be reduced, and they will continue to fall. As a significant part of Latvian Railways' costs is related to employee resources - salary costs, review of organizational and technological processes - optimization of the number of employees will continue in 2021.

In 2020, the *Group* approved the future directions of railway infrastructure development, freight transport and maintenance of rolling stock and ancillary services. The new business model of Latvijas dzelzceļš is based on the assets available to the *Group* – a high-quality infrastructure, a qualified team, and many years of experience, while significantly expanding the *Group's* existing areas of activity, the development of forwarding activities, including sea forwarding, road forwarding, warehousing services, additional finishing services, etc. Future priorities determined by the direction of cargo transportation and logistics business - cargoes to and from Belarus, Ukraine, special cargoes, close cooperation with port authorities and port terminals, unified logistics offer.

Following the completion of work on the *Group's* new business model and in accordance with Resolution No. A 1.1/2-1 of the shareholder meeting of 30 April 2020, *Latvijas dzelzceļš* has developed the *Company's* medium-term operational strategy until 2025, which has been approved by the Ministry of Transport and Trans-Port Coordination Centre. Work is continued to integrate the recommendations of these institutions into the strategy.

The main task of the *Group* is to ensure the management of the publicly used railway infrastructure and safe, high-quality, and effective railway and logistics services in the best interests of the Latvian state and national economy. To ensure this task, a multi-year contract was concluded with the Ministry of Transport, which provides for the procedure of ensuring financial stability.

According to the Multi-Annual Agreement, VAS *Latvijas dzelzceļš* needs additional funds from the state budget in 2021 to ensure the financial stability of Latvijas dzelzceļš. Latvijas dzelzceļš will also need additional funding to fully offset the ineligible costs of providing passenger transport services that it provides in relation to the public service contract throughout 2021.

Although the financial stability payment will be recognised as income in the full amount, there is uncertainty as to the timing of receipt of the additional funds required by the *Group*. This uncertainty relates both to the funds to compensate for the costs of maintenance and restoration of the railway infrastructure in full for the provision of public transport services throughout 2021 in accordance with the requirements of the concluded Multi-Annual Agreement and to the funds to ensure the financial compensation payment to Latvijas dzelzceļš in accordance with the Multi-Annual Agreement.

Despite this uncertainty, the Management of *Latvijas dzelzceļš* believes that the going concern principle is applicable based on the implementation of *the Group's* new business model, the review of the contingency plan and the organisational and technological processes that will lead to cost reduction in the future. The main task of *Latvijas dzelzceļš* is to ensure the management of the state public railway infrastructure and safe, high-quality, and efficient railway and logistics services in the interests of the State, population, and the Latvian economy. Consequently, the financial statements have been prepared on a going concern basis, and no adjustments, including revaluations of assets and liabilities, have been made that would be required if the going concern principle had not been applied in preparing the financial statements.

35. EVENTS AFTER THE END OF THE REPORTING YEAR

In February 2021, an application was filed to the Administrative District Court regarding the decision No. KL\5-5\18\30 *On violation of the prohibition in the activities of SIA "LDZ CARGO" and VAS "Latvijas dzelzceļš" laid down in Section 102 of the Treaty on the functioning of the European Union and Section 13, Paragraph one of the Law on Competition.* In the financial statement for 2020 SIA "LDZ CARGO" recognised the provisions on fines in a full amount.

Under the plan approved by the management and Council of VAS "Latvijas dzelzceļš" in 2021, SIA "LDZ infrastruktūra" would be liquidated. In order to start liquidation of SIA "LDZ infrastruktūra", the consent of the shareholder and the approval of the Cabinet of Ministers to carry out these activities is required.

With the exception of the above, since the last day of the reporting year until the date of approval of this financial statement, there are no other significant events that need to be reported in these financial statements.

Chairman of the Management Board	M. Kleinbergs
Member of the Management Board	V. Balode-Andrūsa
Member of the Management Board	Ē.Šmuksts

The annual report was prepared by the Finance Directorate of VAS *Latvijas dzelzceļš*:

Head of Finance Division	T. Labzova-Ceicāne

This document is signed electronically with secure digital signature and contains time stamp