

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
ANNUAL ACCOUNTS
FOR THE YEAR ENDED 31 DECEMBER 2006

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JOINT STOCK COMPANY "LATVIJAS GĀZE"
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DIRECTORS AND AUDITORS

Names and positions of the Council members	Kiril Seleznov (Кирилл Селезнев) – Chairman of the Council Juris Savickis – Deputy Chairman of the Council Stephan Kamphues – Deputy Chairman of the Council Eike Benke – Member of the Council Reiner Lehmann – Member of the Council Uwe Fip – Member of the Council Marcus Anton Söhrich – Member of the Council (from 27.07.2006.) Matthias Keuchel – Member of the Council (till July 26, 2006) Jelena Karpel (Елена Карпель) – Member of the Council Igor Nazarov (Игорь Назаров) – Member of the Council Vlada Rusakova (Влада Русакова) – Member of the Council Aleksandr Krasnenkov (Александр Красненков) – Member of the Council
Names and positions of the Board members	Adrians Dāvis – Chairman of the Board Aleksandrs Mihejevs (Александр Михеев) – Member of the Board, Deputy Chairman of the Board Frank Siebert – Member of the Board (until 15.08.2006.), Deputy Chairman of the Board (until 15.08.2006.) Jörg Tumat – Member of the Board (from 16.08.2006.), Deputy Chairman of the Board (from 16.08.2006.) Anda Ulpe – Member of the Board Gints Freibergs – Member of the Board
Financial year	1 January – 31 December 2006
Name and address of the auditor and responsible certified auditor	PricewaterhouseCoopers SIA Audit company licence No. 5 Kr. Valdemara Street 19 Riga, LV-1010 Latvia Responsible certified auditor: Juris Lapshe Certified auditor Certificate No. 116

Translation from Latvian Original

JOINT STOCK COMPANY “LATVIJAS GĀZE”
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Report of the Board

1. Activities of the Company in the reporting year

During the year 2006, the Joint Stock Company “Latvijas Gāze” (hereinafter – the Company) retained its position in the fuel market. In the reporting year, the Company devoted its major attention to the fulfilment of the Investment program and to safety increase of gas supply network operation, as well as to natural gas supply to the consumers in the amounts and quality as specified in the contracts.

In the reporting period, 1 719.53 mio nm³ of natural gas were delivered to consumers. In comparison to the year 2005, the volume of natural gas sales increased by 3.3% (in 2005 – 1 664.44 mio nm³). The increase of natural gas sales amount is relatively small due to the record-high air temperature in the second half of the reporting year and the rapid growth of natural gas trade tariffs due to increase of gas purchase prices.

In order to speed up the approach of natural gas price to the prices of oil products in Rotterdam market, with effect from January 1, 2005, amendments to the natural gas supply agreement were enforced, according to which the natural gas purchase price was set by a formula taking into account the actual heavy fuel oil quotation. This formula envisaged increase of prices in three years time by up to 60% at a heavy fuel oil quotation of 200 USD/t. As the actual heavy fuel oil quotation in 2005 noticeably exceeded the highest quotation determined in the agreement, in December 2005 new amendments to the natural gas supply agreement were signed, which as from January 1, 2006 cancelled the ceiling of heavy fuel quotation determined in the previous agreement, thus increasing the gas purchase price at the actual heavy fuel oil quotation by an additional 26%. Furthermore, as from January 1, 2007, amendments to the natural gas supply agreement were enforced, according to which the natural gas purchase price in comparison with the price formula of 2006 was increased by about 54% at a heavy fuel oil quotation of 300 USD/t. It is expected that in 2008 natural gas purchase prices will reach the prices of oil products in the Rotterdam market and their changes will depend only on fluctuations of the heavy fuel oil quotation.

On the basis of the changes in the gas purchase price, the Company in 2005 submitted to the Public Utility Commission (hereinafter – PUC) a natural gas tariff project envisaging gradual increase of natural gas transmission, storage, distribution and sales service and natural gas sales end tariffs from the middle of 2005 till 2007. The service and sales end tariffs approved by the PUC resolution No.133 of June 8, 2005 “On natural gas tariffs of the JSC “Latvijas Gāze” in 2006” were enforced as from January 1, 2006 and were applied till May 1, 2006 when they were replaced with the tariffs approved by the PUC resolution No.73 of March 22, 2006 “On natural gas tariffs of the JSC “Latvijas Gāze” in 2006” (depending on the amount of consumption and heavy fuel oil quotation, the actual increase reached 15–31%).

The total revenue from natural gas sales and other basic activities in 2006 amounted to LVL 182.3 mio (EUR 259.5 mio), expenses (excl. administration) – LVL 152.8 mio (EUR 217.4 mio), and gross profit – LVL 29.6 mio (EUR 42.0 mio). The tariff increase provided additional revenues of LVL 18.86 mio (EUR 26.8 mio). In comparison with 2005, net profit of the Company decreased by 11.1% or LVL 2.6 mio (EUR 3.7 mio) and amounted to LVL 21 mio (EUR 29.6 mio), though net rentability of basic activity remained at the level of 2005 – 11.5%. It should be noted that in compliance with the judgment of Stockholm Court of Arbitration and the Swedish Court of Appeal the Company received compensation for losses and interest payment from the state at the total amount of LVL 8.5 mio (EUR 12.1 mio), which basically refers to the previous periods, starting from 2001, which significantly increased the net profit of 2005.

In 2006, much attention was paid by the Company to further expansion of the natural gas distribution system and connection of new users to the existing gas supply system. The total length of natural gas pipelines on January 1, 2007 reached 5 872.3 km, incl. gas transmission pipelines – 1 281.06 km and distribution pipelines – 4 592.25 km. In the reporting year, gas distribution pipelines worth LVL 4.9 mio (EUR 6.96 mio) with a total length of 160 km were commissioned.

The number of individual consumers using gas for heating in 2006 increased by 4.3 thousand and reached 39.4 thousand at the end of the year. The total number of natural gas users came close to 437.2 thousand.

In 2006, good results were achieved by the operation unit “Inčukalns Underground Gas Storage Facility” (hereinafter – IUGS). During the reporting period, 1.95 billion nm³ were injected into the facility, and the total amount of gas reached 4.46 billion nm³, incl. current gas – 2.32 billion nm³.

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Report of the Board (continued)

1. Activities of the Company in the reporting year (continued)

In the reporting period, the value of assets of the Company was increased by revaluation of fixed assets received without reimbursement as on 31.12.2006., due to which assets grew by ~LVL 0.4 mio (~EUR 0.6 mio).

In 2006, the Company invested LVL 25.08 mio (EUR 35.7 mio) in modernization of gas supply system and creation of new fixed assets. Of the total investment, 34.6% were utilized for modernization of the IUGS, 21.7% - for development of gas transmission pipeline system, and 32.3% – for development of the distribution system and attraction of new customers. The most significant projects completed in 2006 were electric supply reconstruction in the IUGS and construction of the new compressor shop KC-1. It is planned that KC-1 will start operating on June 1, 2007.

In the reporting year, internal diagnostics of gas transmission pipeline Izborsk-IUGS was completed, and processing of obtained indications has been commenced. Along with that, pipeline defects found in diagnostics of gas transmission pipelines Pskov-Riga, Vireši-Tallinn and Riga-Daugavpils have been averted. In 2006, a contract has been signed on project development of preparation of gas pipeline Iecava-Liepāja for internal diagnostics, and detail design for construction of pig launcher and receiver units of both lines of gas transmission pipeline Riga-IUGS has been elaborated. For construction of natural gas pipelines in 2006, LVL 6.3 mio (EUR 9 mio) have been utilized. The major commenced projects are construction of gas pipeline on TEC-2 and over Daugava under Dienvidu Bridge in Riga.

The Company's work of the reconstruction of the culture-historical monument – gas reservoir in Vagonu Street 20 has been positively evaluated. The Latvian Constructors' Association has awarded it the title of best construction of 2006 in Latvia in the nomination “Reconstruction”.

2. Research and development activities

In order to provide uninterrupted gas supply to users and secure operation of the gas supply system in long term, the Company has worked out “The program for improvement of safety of gas supply system of the Joint Stock Company “Latvijas Gāze” from 2006 till 2010”. It has been prepared on the basis of judgments by Russian companies “Gazobezopasnostj” and “Lentransgaz”, institutes “VNIIGAZ” and “Giprospepgaz”, as well as German companies “Pipeline Engineering GmbH”, “Untergrundspeicher und Geotechnologie-Systeme GmbH”, “E.ON Engineering GmbH”, “E.ON Ruhrgas International AG” and other partners on the technical condition of equipment and modernization possibilities.

The program envisages investment in safety improvement at the amount of LVL 73.8 mio (EUR 105 mio) in total. It basically includes projects necessary for improvement of system operation safety, gasification of new objects and improvement of gas supply stability throughout the region, covering seasonal consumption fluctuations with gas supplies from the IUGS to Estonia and the Western part of Russia, as well as in further perspective – Lithuania.

The greatest investments in the IUGS are intended for installation of new compressors, as well as modernization of wells and gas collection points; in the system of gas transmission pipelines – for completion of diagnostics and aversion of detected defects, replacement of line taps, modernization of GRS Riga-1 and GRS TEC-2.

3. Management of financial risks

Operation of the Company is subjected to various financial risks, including credit risk and foreign currencies exchange rate risks. Management of the Company tries to minimize the negative impact of potential financial risks to the financial standing of the Company.

The Company is not directly subjected to the risk of foreign currencies exchange rate fluctuations, as gas price is set in USD and afterwards recalculated in EUR, while gas sales tariffs are set in lats. Settlements for the supplied gas are made in EUR. Considering that as from January 1, 2005 exchange rate of LVL is pegged to that of the EUR, fluctuations of LVL/EUR rate are limited and no significant influence on further financial results is anticipated. Changes of gas purchase prices in USD depending on heavy fuel oil quotation are covered by the natural gas sales tariffs approved by the PUC. To a certain extent they cover also the fluctuations of EUR/USD rate. The risk of foreign currencies rate fluctuations, which is related to debts to suppliers, is controlled through keeping a significant part of financial resources in deposits of the respective currency.

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Report of the Board (continued)

3. Management of financial risks (continued)

The financial assets subjected to credit risk mostly consist of cash at bank and debtors' liabilities. Cash and cash equivalents of the Company are kept with the major financial institutions of Latvia. Debtors' liabilities are reflected at their recoverable amount. The Company is subjected to concentration of credit risk because a considerable share of the net turnover refers to a limited number of customers. Four customers of the Company make up to 45% (in 2005 – 43%) of sales, one of the debts of these debtors on December 31, 2006 was 20.7% (in 2005 – 19.9%), the second and the third biggest consisted of 8.8% and 6.2% each (in 2005 – 7% and 6%) of the total amount of debtors' debts.

4. Circumstances and activities after the reporting period

Except for the regular revaluation of buildings, gas transportation system and equipment performed by the Company in 2007, between the last day of the reporting year and the day when the Board signs the report there have been no significant or extraordinary circumstances to affect annual results or financial condition of the Company.

Considering the tendencies of the oil products market and the wish of gas suppliers to create conditions for gas supplies to Latvia equal to those of other countries of the European Union, as from January 1, 2007 amendments to natural gas supply agreement are enforced, determining a new formula for setting the gas purchase price. In comparison to the formula of 2006, the gas purchase price is increased by 54% on average at heavy fuel oil quotation 300 USD/t.

After signing the amendments to gas supply agreements, in January 2007 the Company submitted to the PUC a new tariff project. With the PUC resolution No.83 of March 28, 2007 “On natural gas supply tariffs of the JSC “Latvijas Gāze”, the tariffs have been approved and will be enforced as from May 1, 2007. The new tariffs will be pegged to heavy fuel oil quotation in the exchange and will cover the increase of operation costs caused by gas purchase and inflation. Depending on the amount of consumption, the increase of tariffs at heavy fuel oil quotation 260 USD/t will reach 23–32%.

5. Board proposal for the distribution of the profit of 2006

	2006 LVL	2006 EUR
Current year's profit according to statutory financial statements prepared under Latvian accounting regulation	21 007 255	29 890 631
Profit share not available for distribution (unrealized deferred tax income in connection with the revaluation of fixed assets)	(1 175 456)	(1 672 523)
Profit available for distribution	19 831 799	28 218 108
Profit distribution proposed:		
Calculated dividends of shareholders (60.4%)	11 970 000	17 031 776
<i>Dividend per share (LVL/1 share)</i>	0.30	0.427
Transfer to reserves provided for in the Company Articles of Association	7 861 799	11 186 332

Several members of the Company Council and Board own shares and hold managerial positions in several companies registered in the Register of Enterprises of the Republic of Latvia. Except as disclosed in the financial statements, the Company did not have material transactions with those companies during the reporting year.

Information on the shareholdings of the members of the Council and the Board of the Company is available from the Board of the Company.

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Report of the Board (continued)

6. Perspective

Considering the investment made for improvement of system operation safety, expansion of gas pipeline network, attraction of new customers, retrieval of debtors' debts in previous years and in the reporting year, as well as the situation in the fuel market of Latvia, the Board of the Company believes that in 2007 the Company will continue developing successfully and take a stable position in the fuel supply market.

Chairman of the Board



A. Dāvis

Minutes of Board Meeting No. 16 (2007)

Riga, 25 April 2007

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
ANNUAL ACCOUNTS
FOR THE YEAR ENDED 31 DECEMBER 2006

STATEMENT OF DIRECTORS' RESPONSIBILITY

The Board of Directors of JSC "Latvijas Gāze" (hereafter – the Company) is responsible for the preparation of the financial statements of the Company.

The financial statements on pages 11 to 39 are prepared in accordance with the accounting records and source documents and present fairly the financial position of the Company as of 31 December 2006 and the results of its operations and cash flows for the year ended 31 December 2006.

The financial statements are prepared in accordance with International Financial Reporting Standards as adopted in the European Union on a going concern basis. Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgments and estimates have been made by the Board of Directors in the preparation of the financial statements.

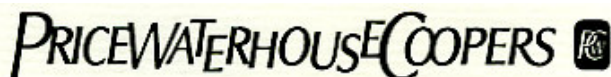
The Board of Directors of JSC "Latvijas Gāze" is responsible for the maintenance of proper accounting records, the safeguarding of the Company's assets and the prevention and detection of fraud and other irregularities in the Company. The Board of Directors is also responsible for operating the Company in compliance with the legislation of the Republic of Latvia.

On behalf of the Board of Directors,



Adriāns Dāvis
Chairman of the Board

April 25, 2007



PricewaterhouseCoopers SIA
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Translation from Latvian original

INDEPENDENT AUDITORS' REPORT

To the Shareholders of JSC "Latvijas Gāze"

Report on the Financial Statements

We have audited the accompanying financial statements on pages 11 to 39 of JSC "Latvijas Gāze" which comprise the balance sheet as of 31 December 2006 and the income statement, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

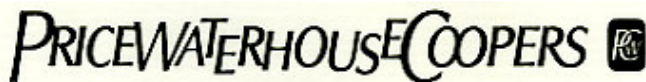
Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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



Basis for qualified opinion

The Company's accounting policy is to account for buildings, gas transmission system and equipment at fair value less subsequent depreciation and impairment. The previous revaluation was performed in 2004. As described in the note 2(u) to the financial statements the Company started preparation for the revaluation in 2006. The revaluation was commenced in early 2007 and has not yet been completed. Preliminary results of the revaluation indicate that the fair value of the buildings, gas transmission system and equipment exceeds the carrying amounts of those assets by a material amount. International Accounting Standard 16, *Property, Plant and Equipment*, provides that the revaluations should be made with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. Considering the general increase in costs of construction, gas pipes and real estate prices in the Latvian market during 2006, as well as the preliminary results of the revaluation being performed in 2007, we consider that the fair value of the buildings, gas transmission system and equipment of the Company is materially different from the carrying amount of those assets as at 31 December 2006. In the absence of valuation of the buildings, gas transmission system and equipment as at 31 December 2006 we were not able to quantify the effect of the required adjustment to the carrying amount of buildings, gas transmission system and equipment as at 31 December 2006.

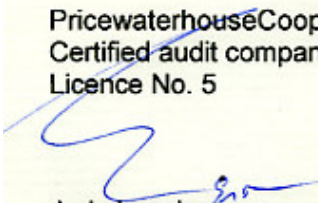
Opinion

In our opinion, except for the effects of the matter referred to above in paragraph *Basis for qualification*, the accompanying financial statements give a true and fair view of the financial position of the Company as of 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

Report on Other Legal and Regulatory Requirements

We have read the Management Report set out on pages 4 to 7 and did not identify material inconsistencies between the financial information contained in the Management Report and that contained in the financial statements for 2006.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5



Juris Lapshe
Certified auditor in charge
Certificate No. 116

Member of the Board

Riga, Latvia
26 April 2007

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

BALANCE SHEET AS AT 31 DECEMBER 2006

	Note	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Assets					
<u>Non-current assets</u>					
Property, plant and equipment	3	225 771	214 323	321 244	304 954
Intangible assets	4	1 795	1 414	2 554	2 012
Trade receivables	5	94	220	134	313
		<u>227 660</u>	<u>215 957</u>	<u>323 932</u>	<u>307 279</u>
<u>Current assets</u>					
Inventories	6	70 312	43 602	100 045	62 040
Trade receivables	5	13 959	13 020	19 861	18 526
Current income tax receivable	21	1 116	669	1 588	952
Other current assets	7	8 416	1 340	11 974	1 907
Cash and cash equivalents	8	11 048	23 868	15 720	33 961
		<u>104 851</u>	<u>82 499</u>	<u>149 188</u>	<u>117 386</u>
Total assets		<u>332 511</u>	<u>298 456</u>	<u>473 120</u>	<u>424 665</u>
Equity and liabilities					
<u>Equity</u>					
Share capital	9	39 900	39 900	56 773	56 773
Share premium		14 320	14 320	20 376	20 376
Revaluation reserve		119 264	119 150	169 697	169 534
Other reserves		47 554	39 061	67 664	55 579
Retained earnings		15 294	16 745	21 760	23 825
Total equity		<u>236 332</u>	<u>229 176</u>	<u>336 270</u>	<u>326 087</u>
<u>Liabilities</u>					
<u>Non-current liabilities</u>					
Borrowings	10	-	18	-	26
Deferred income tax liabilities	21	19 550	19 897	27 817	28 311
Deferred income	11	8 425	6 675	11 988	9 498
		<u>27 975</u>	<u>26 590</u>	<u>39 805</u>	<u>37 835</u>
<u>Current liabilities</u>					
Trade payables		54 967	32 337	78 211	46 012
Borrowings	10	16	35	23	50
Deferred income	11	315	244	448	347
Other current liabilities	12	12 906	10 074	18 363	14 334
		<u>68 204</u>	<u>42 690</u>	<u>97 045</u>	<u>60 743</u>
Total liabilities		<u>96 179</u>	<u>69 280</u>	<u>136 850</u>	<u>98 578</u>
Total equity and liabilities		<u>332 511</u>	<u>298 456</u>	<u>473 120</u>	<u>424 665</u>

The notes on pages 16 to 39 are an integral part of these financial statements.

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JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006

	Note	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Sales		182 344	133 386	259 452	189 791
Cost of sales	14	(152 794)	(110 318)	(217 406)	(156 968)
Gross profit		29 550	23 068	42 046	32 823
Administrative expenses	15	(7 042)	(7 375)	(10 020)	(10 494)
Other income	16	2 255	11 831	3 209	16 834
Other expenses	17	(1 730)	(1 287)	(2 462)	(1 831)
Finance income, net	19	972	635	1 383	903
Profit before income tax		24 005	26 872	34 156	38 235
Income tax expense	21	(3 216)	(3 325)	(4 576)	(4 731)
Profit for the year		20 789	23 547	29 580	33 504
Earnings per share		LVL	LVL	EUR	EUR
- Basic	22	0.521	0.590	0.741	0.840
- Diluted	22	0.521	0.590	0.741	0.840

The notes on pages 16 to 39 are an integral part of these financial statements.

The financial statements on pages 11 to 39 were approved by the Board of Directors and were signed on its behalf by:

Adrians Dāvis
Chairman of the Board

Anda Ulpe
Board Member

April 25, 2007

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JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2006

	Share capital LVL'000	Share premium LVL'000	Revaluation reserve LVL'000	Other reserves LVL'000	Retained earnings LVL'000	Total LVL'000
Balance as at 31 December 2004	39 900	14 320	117 816	33 237	10 898	216 171
Revaluation of property, plant and equipment	-	-	1 680	-	-	1 680
Deferred income tax liability arising on the revaluation of property, plant and equipment	-	-	(252)	-	-	(252)
Disposal of revalued property, plant and equipment	-	-	(111)	-	111	-
Deferred income tax on disposal of revalued property, plant and equipment	-	-	17	-	(17)	-
<i>Net income recognized directly in equity</i>	-	-	<i>1 334</i>	-	<i>94</i>	<i>1 428</i>
Profit for the year	-	-	-	-	23 547	23 547
Total recognized income for 2005	-	-	1 334	-	23 641	24 975
Transfers to reserves	-	-	-	5 824	(5 824)	-
Dividends for 2004	-	-	-	-	(11 970)	(11 970)
Balance as at 31 December 2005	39 900	14 320	119 150	39 061	16 745	229 176
Revaluation of property, plant and equipment	-	-	391	-	-	391
Deferred income tax liability arising on the revaluation of property, plant and equipment	-	-	(59)	-	-	(59)
Disposal of revalued property, plant and equipment	-	-	(256)	-	256	-
Deferred income tax on disposal of revalued property, plant and equipment	-	-	38	-	(38)	-
<i>Net income recognized directly in equity</i>	-	-	<i>114</i>	-	<i>218</i>	<i>332</i>
Profit for the year	-	-	-	-	20 789	20 789
Total recognized income for 2006	-	-	114	-	21 007	21 121
Transfers to reserves	-	-	-	8 493	(8 493)	-
Dividends for 2005	-	-	-	-	(13 965)	(13 965)
Balance as at 31 December 2006	39 900	14 320	119 264	47 554	15 294	236 332

The notes on pages 16 to 39 are an integral part of these financial statements.

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JOINT STOCK COMPANY "LATVIJAS GĀZE"
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STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2006
(CONTINUED)

	Share capital EUR'000	Share premium EUR'000	Revaluation reserve EUR'000	Other reserves EUR'000	Retained earnings EUR'000	Total EUR'000
Balance as at 31 December 2004	56 773	20 376	167 637	47 292	15 506	307 584
Revaluation of property, plant and equipment	-	-	2 390	-	-	2 390
Deferred income tax liability arising on the revaluation of property, plant and equipment	-	-	(359)	-	-	(359)
Disposal of revalued property, plant and equipment	-	-	(158)	-	158	-
Deferred income tax on disposal of revalued property, plant and equipment	-	-	24	-	(24)	-
<i>Net income recognized directly in equity</i>	-	-	1 897	-	134	2 031
Profit for the year	-	-	-	-	33 504	33 504
Total recognized income for 2005	-	-	1 897	-	33 638	35 535
Transfers to reserves	-	-	-	8 287	(8 287)	-
Dividends for 2004	-	-	-	-	(17 032)	(17 032)
Balance as at 31 December 2005	56 773	20 376	169 534	55 579	23 825	326 087
Revaluation of property, plant and equipment	-	-	556	-	-	556
Deferred income tax liability arising on the revaluation of property, plant and equipment	-	-	(83)	-	-	(83)
Disposal of revalued property, plant and equipment	-	-	(365)	-	365	-
Deferred income tax on disposal of revalued property, plant and equipment	-	-	55	-	(55)	-
<i>Net income recognized directly in equity</i>	-	-	163	-	310	473
Profit for the year	-	-	-	-	29 580	29 580
Total recognized income for 2006	-	-	163	-	29 890	30 053
Transfers to reserves	-	-	-	12 085	(12 085)	-
Dividends for 2005	-	-	-	-	(19 870)	(19 870)
Balance as at 31 December 2006	56 773	20 376	169 697	67 664	21 760	336 270

Dividends are distributed and transfers to reserves are made based upon profits and retained earnings as per statutory financial statements prepared under Latvian accounting regulations. Changes in other reserves can be made only with shareholders' approval. Revaluation reserve and share premium cannot be distributed as dividends to shareholders.

The notes on pages 16 to 39 are an integral part of these financial statements.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2005

	Note	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Cash flows from operating activities					
Cash generated from operations	24	28 868	51 932	41 073	73 893
Interest received		1 392	1 191	1 981	1 694
Income tax paid	21	(4 031)	(5 257)	(5 734)	(7 480)
Net cash generated from operating activities		26 229	47 866	37 320	68 107
Cash flows from investing activities					
Purchases of property, plant and equipment		(24 386)	(23 658)	(34 698)	(33 662)
Proceeds from sale of property, plant and equipment		28	17	40	24
Purchases of intangible assets		(692)	(569)	(985)	(810)
Proceeds from sales of securities		-	6	-	9
Net cash used in investing activities		(25 050)	(24 204)	(35 643)	(34 439)
Cash flows from financing activities					
Repayment of long term borrowings		(33)	(24)	(47)	(34)
Interest paid		(1)	(2)	(1)	(3)
Dividends paid		(13 965)	(11 970)	(19 870)	(17 032)
Net cash used in financing activities		(13 999)	(11 996)	(19 918)	(17 069)
Net (decrease) / increase in cash and cash equivalents		(12 820)	11 666	(18 241)	16 599
Cash and cash equivalents at the beginning of the year		23 868	12 202	33 961	17 362
Cash and cash equivalents at the end of the year	8	11 048	23 868	15 720	33 961

The notes on pages 16 to 39 are an integral part of these financial statements.

Translation from Latvian Original

**JOINT STOCK COMPANY “LATVIJAS GĀZE”
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006**

NOTES TO THE FINANCIAL STATEMENTS

1 INCORPORATION AND ACTIVITIES

JSC Latvijas Gāze was re-organised on January 31, 1994 as a joint stock company wholly owned by the Government of the Republic of Latvia. The Company was formerly a state enterprise which had its assets transferred to and obligations assumed by the joint stock company in accordance with the law. Since 15 February 1999 the shares of the Company are quoted on Riga Stock Exchange. The registered office of the Company is 6 A. Briāna Street, Riga, Latvia.

The Company is involved in import and sales of natural gas in territory of Latvia as well as supply of gas transmission and storage services to foreign companies. The Company is the sole supplier of natural gas in Latvia. The service territory of the Company has a population of approximately 2,3 million.

The tariffs of gas sold to corporate and retail customers are set by the Public Utilities Commission (PUC) of the Republic of Latvia. Changes to tariffs are considered by PUC based on applications of the Company and in accordance with the methodology approved by PUC.

During 2006 the average number of persons employed by the Company was 1 328 (2005: 1 306).

These financial statements have been approved by the Board of Directors on April 25, 2007.

2 ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

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

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of property, plant and equipment as disclosed in the Accounting policies Note (d) below.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. Significant accounting estimates are described in Note (u).

(a) Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Company

The following standards and amendments to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 March 2006 or later periods that the Company has not early adopted:

IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007).

IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 32, Financial Instruments: Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Company assessed the impact of IFRS 7 and the amendments to IAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Company will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

IFRS 8, Operating Segments (effective from 1 January 2009).

IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131 Disclosures about Segments of an Enterprise and Related Information. The Company assessed the impact of IFRS 8 and concluded that there are no additional disclosures to be made in the financial statements.

Translation from Latvian Original

**JOINT STOCK COMPANY “LATVIJAS GĀZE”
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006**

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(a) Basis of preparation (continued)

(b) Standards, amendments and interpretations that are mandatory for accounting periods beginning on or after 1 January 2006, but are not relevant to the Company's operations:

IAS 19	(Amendment)	Employee benefits
IAS 21	(Amendment)	Net Investment in a Foreign Operation
IAS 39	(Amendment)	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
IAS 39	(Amendment)	The Fair Value Option
IAS 39 and IFRS 4	(Amendment)	Financial Guarantee Contracts
IFRS 1	(Amendment)	First-time Adoption of International Financial Reporting Standards and IFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources
IFRS 6		Exploration for and Evaluation of Mineral Resources
IFRIC 4		Determining whether an Arrangement contains a Lease
IFRIC 5		Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
IFRIC 6		Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment

(c) Standards, amendments and interpretations to existing standards that are not yet effective and not relevant for the Company's operations

The following standards, amendments and interpretations to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 March 2006 or later periods but are not relevant to the Company's operations or according to the management estimates will have no impact on the financial statements:

IAS 23 (amendment), Borrowing Costs, revised (effective from 1 January 2009)

IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies (effective for annual period beginning on or after 1 March 2006).

IFRIC 8, Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006).

IFRIC 9, Reassessment of embedded derivatives (effective for annual periods beginning on or after 1 June 2006).

IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006).

IFRIC 11, IFRS 2 – Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007)

IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008)

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JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(a) Basis of preparation (continued)

(c) Standards and interpretations to existing standards that are not yet effective and not relevant for the Company's operations (continued):

IFRIC 10, 11, 12, IFRS 8 and amendments to IAS 23 have not been yet endorsed by EU.

Accounting policies have been consistent with those used in the previous reporting period.

(b) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

(c) Foreign currency translation

Functional and presentation currency

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the Company operates ('the functional currency'). The financial statements are presented in Latvian Lats (LVL), which is the Company's functional and presentation currency. In accordance with the requirements of the Riga Stock Exchange all balances are also presented in Euro (EUR). For disclosure purposes the translation into EUR is based on the official exchange rate as set by the Bank of Latvia during period from 1 January 2005 to 31 December 2006 – EUR/LVL (1 EUR = LVL 0.702804).

Transactions and balances

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

(d) Property, plant and equipment

Buildings, gas transmission system and equipment are stated at fair value, based on periodic valuation less subsequent depreciation or impairment charge. All other property, plant and equipment are stated at historical cost, less accumulated depreciation and impairment charge. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Assets purchased, but not yet ready for intended use or under installation process are included in Assets under construction.

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

Any accumulated depreciation at the date of revaluation is restated proportionately with the charge in gross carrying amount of the asset. Increases in the carrying amount arising on revaluation of building, gas transmission system and equipment are credited to Revaluation reserve in shareholders' equity. Decreases that offset previous increases of the same asset are charged against revaluation reserve directly in equity; any further decreases are charged to the income statement. The revaluation surplus is transferred to retained earnings on the retirement or disposal of the asset.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(d) Property, plant and equipment (continued)

Land, buffer gas, advances for property, plant and equipment and assets under construction are not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives starting from the date when the asset is available for use, using the following rates:

	years
Buildings	60 - 100
Gas transmission system	40 - 50
Machinery and equipment	5 - 20
Furniture and fittings	5 - 10
Computers and equipment	3.33

The Company's policy is to capitalize property, plant and equipment with cost exceeding LVL 50 and useful life exceeding 1 year.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note (f)).

Costs of borrowing to finance assets under construction and other direct charges related to the particular asset under construction are capitalised, during the time that is required to complete and prepare the asset for its intended use, as part of the cost of the asset. Capitalisation of the borrowing costs is suspended during extended periods in which active developments are interrupted.

Gains or losses on disposals are determined by comparing carrying amount with proceeds and are charged to the income statement during the period in which they are incurred. When revalued assets are sold, the amounts included in Revaluation reserve are transferred to retained earnings.

(e) Intangible assets

Intangible assets primarily consist of software licences and patents. Intangible assets have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated from the date when the asset is available for use. Amortisation is calculated using the straight-line method to allocate the cost of intangible assets over their useful lives. Generally intangible assets are amortised over a period of 5 years.

(f) Impairment of non-financial assets

All Company's non-financial assets have a finite useful life (except land). Assets that are subject to amortization or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Non-financial assets are reviewed for possible reversal of the impairment at each reporting date.

(g) Financial assets

The Company classifies all its financial assets as loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for assets with maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as 'trade receivables' in the balance sheet (Note 5 and (i)).

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(h) Inventories

The cost of natural gas is determined using the first-in first-out (FIFO) method. The natural gas that is permanently at storages (i.e. technological buffer gas) is a part of property, plant and equipment and measured accordingly. Materials, spare parts, gas meters and other inventories cost is determined using the weighted average method. The cost of natural gas comprises cost of gas purchased. Direct labour, other direct costs and related production overheads are recognised on an accruals basis and charged to the income statement in the period when incurred.

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

(i) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of trade receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivables are impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

(j) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, balances of current accounts with banks and deposits held at call with banks with original term less than 90 days and other short-term highly liquid investments, which can be easily converted to cash and are not subject of significant change in value.

(k) Share capital and dividend authorised

Ordinary shares are classified as equity. Incremental external costs directly attributable to the issues of new shares, other than in connection with business combination, are shown in equity as a deduction, net of tax, from the proceeds.

Dividend distribution to the Company's shareholders is recognized as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

(l) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

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

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(m) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss, it is not accounted for. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the temporary differences will reverse.

The principal temporary differences arise from different intangible asset amortization and property, plant and equipment depreciation rates, as well as provisions for slow-moving inventory, accrued expenses for unused annual leave and bonuses and provisions for bad and doubtful debts where the management is of the opinion that they will meet the criteria stated in Article 9 of the law "On Corporate Income Tax". Deferred income tax asset is recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Increase in deferred income tax liability that results from revaluation of property, plant and equipment is charged to equity as deduction from respective increase in the Revaluation reserve.

Decrease in deferred income tax liability that results from depreciation of revalued property, plant and equipment is charged to the income statement.

(n) Income tax

Income tax is assessed for the period in accordance with Latvian tax legislation. The tax rate stated by Latvian tax legislation is 15 percent.

(o) Accrued unused annual leave expenses

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

(p) Employee benefits

Bonus plans

The Company recognizes a liability and expense for bonuses, based on formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Company recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

Social security and pension contribution

The Company pays social security contributions to the state Social Security Fund (the Fund) on behalf of its employees based on the defined contribution plan in accordance with the local legal requirements. The Company also makes contributions to an external defined contribution pension plan (the Plan). A defined contribution plan is a plan under which the Company pays fixed contributions into the Fund or the Plan and will have no legal or constructive obligations to pay further contributions if the Fund or the Plan do not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior period. The social security and pension contributions are recognised as an expense on an accrual basis and are included within staff costs.

(q) Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(r) Revenue recognition

Sales of natural gas

Sales are recognised upon delivery of gas, net of value added tax and discounts. Sales of natural gas are recorded on the basis of meter readings reported by customers. Where relevant, this includes an estimate of the sales value of gas supplied between the date of the last meter reading and the year-end. Natural gas sales to corporate customers are recognized based on invoice issued according to meter reading of customers.

Income of transmission and storage on natural gas

Income of performance of services is recognised upon performance of services, net of value added tax and discounts. Income on natural gas transmission and storage is recognized based on actual amount of transmitted and stored gas, which are determined by meter readings.

The Company as well as the Regulator of the Public Utilities Commission have the right during the tariff period (which is 3 years long) to apply for the revision of the tariffs if any of the price factors (like foreign exchange rate, natural gas purchase price etc.) has changed more than by 5% compared to the approved.

Interest income

Interest income is recognized on a time-proportion basis using the effective interest method. Interest income on term deposits over 90 days is classified as Other income and interest on cash balances is classified as Finance income.

Penalties income

Penalties income is recognised as it accrues unless its collectability is in doubt.

Income from contribution to financing of construction works

The income from residents and enterprises contribution to financing of construction works of gas pipelines is accounted for as deferred income and recognized in the income statement over the expected period of the customer relationship of 30 to 40 years.

(s) Earnings per share

Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the reporting year.

(t) Related parties

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

(u) Critical estimates and judgements

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies.

IFRS requires that in preparing the financial statements, management of the Company make estimates and assumptions that affect the reported amounts of assets and liabilities and required disclosure at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The areas involving a higher degree of judgement are revaluation of property, plant and equipment, determination of frequency of revaluations, the management assumptions and estimates in determination of useful lives of property, plant and equipment, recoverable amount of accounts receivable and inventories as described in respective notes.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 ACCOUNTING POLICIES (continued)

(u) Critical estimates and judgments (continued)

Valuation of Property, Plant and Equipment

The management determines fair value and the remaining useful life of buildings, gas transmission system and equipment based on valuations performed by independent certified valuers in accordance with real estate valuation standards and based on the on the average construction costs relevant for the reporting year. The Company's internal policy is to perform the revaluations when there are indications that average construction costs and/or purchase prices related to the buildings, gas transmission system and equipment have increased by cumulative 25%. The management performed an assessment in 2005 and concluded that the said average costs have not increased above 25%. During 2006 there was a considerable and unexpected increase in construction costs and/or purchase prices related to the buildings, gas transmission system and equipment. Accordingly, the management started preparation of the revaluation in 2006 and commenced it in early 2007. At the date of issuing these financial statements the revaluation has not been completed. The preliminary results of the revaluation indicate that the fair value of buildings, gas transmission system and equipment exceeds the carrying amount of those assets as at 31 December 2006 by material amount.

Recoverable amount of trade receivables

The estimated collectibility of accounts receivable is assessed on an individual basis for each customer. In case individual assessment is not possible due to the large number of individual balances, only the significant debtors are assessed individually. Receivables that are not individually assessed for impairment are classified into groups of receivables with similar credit risk characteristics and are collectively assessed for impairment, using historical loss experience. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Inventory valuation

Upon valuation of inventories, the management will rely on its best knowledge taking into consideration historical experience, general background information and potential assumptions and conditions of future events. In determining the impairment of inventories, the sales potential as well as the net realisable value of inventory.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

3 PROPERTY, PLANT AND EQUIPMENT

	Land, buildings and gas transmission system LVL'000	Equipment and machinery LVL'000	Other assets LVL'000	Advances LVL'000	Assets under construction LVL'000	Total LVL'000
<u>Cost or revaluation</u>						
At December 31, 2004	310 236	40 363	3 904	405	19 185	374 093
Additions	-	-	257	2 578	20 636	23 471
Reclassified	13 665	4 479	483	(2 743)	(15 884)	-
Revaluation	2 394	195	-	-	-	2 589
Disposals	(245)	(332)	(207)	-	(21)	(805)
At December 31, 2005	326 050	44 705	4 437	240	23 916	399 348
<u>Depreciation</u>						
At December 31, 2004	150 760	20 182	2 433	-	-	173 375
Charged for 2005	7 405	3 466	524	-	-	11 395
Reclassified	-	(1)	1	-	-	-
Revaluation	895	14	-	-	-	909
Disposals	(141)	(306)	(207)	-	-	(654)
At December 31, 2005	158 919	23 355	2 751	-	-	185 025
Net book value at December 31, 2005	167 131	21 350	1 686	240	23 916	214 323
Net book value at December 31, 2004	159 476	20 181	1 471	405	19 185	200 718

	Land, buildings and gas transmission system LVL'000	Equipment and machinery LVL'000	Other assets LVL'000	Advances LVL'000	Assets under construc- tion LVL'000	Total LVL'000
<u>Cost or revaluation</u>						
At December 31, 2005	326 050	44 705	4 437	240	23 916	399 348
Additions	-	-	-	2 865	21 206	24 071
Reclassified	8 619	5 727	668	(2 808)	(12 202)	4
Revaluation	339	53	-	-	-	392
Disposals	(254)	(959)	(267)	-	(27)	(1 507)
Transferred to intangible assets	-	(1)	(228)	-	-	(229)
At December 31, 2006	334 754	49 525	4 610	297	32 893	422 079
<u>Depreciation</u>						
At December 31, 2005	158 919	23 355	2 751	-	-	185 025
Charged for 2006	7 954	3 995	624	-	-	12 573
Disposals	(145)	(832)	(266)	-	-	(1 243)
Transferred to intangible assets	-	(1)	(46)	-	-	(47)
At December 31, 2006	166 728	26 517	3 063	-	-	196 308
Net book value at December 31, 2006	168 026	23 008	1 547	297	32 893	225 771
Net book value at December 31, 2005	167 131	21 350	1 686	240	23 916	214 323

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

3 PROPERTY, PLANT AND EQUIPMENT (continued)

	Land, buildings and gas transmission system EUR'000	Equipment and machinery EUR'000	Other assets EUR'000	Advances EUR'000	Assets under construction EUR'000	Total EUR'000
<u>Cost or revaluation</u>						
At December 31, 2004	441 426	57 431	5 555	576	27 298	532 286
Additions	-	-	366	3 668	29 362	33 396
Reclassified	19 444	6 373	687	(3 903)	(22 601)	-
Revaluation	3 406	277	-	-	-	3 683
Disposals	(349)	(472)	(295)	-	(30)	(1 146)
At December 31, 2005	463 927	63 609	6 313	341	34 029	568 219
<u>Depreciation</u>						
At December 31, 2004	214 512	28 716	3 462	-	-	246 690
Charged for 2005	10 535	4 930	746	-	-	16 211
Reclassified	-	(1)	1	-	-	-
Revaluation	1 276	20	-	-	-	1 296
Disposals	(201)	(436)	(295)	-	-	(932)
At December 31, 2005	226 122	33 229	3 914	-	-	263 265
Net book value at December 31, 2005	237 805	30 380	2 399	341	34 029	304 954
Net book value at December 31, 2004	226 914	28 715	2 093	576	27 298	285 596

	Land, buildings and gas transmission system EUR'000	Equipment and machinery EUR'000	Other assets EUR'000	Advances EUR'000	Assets under construction EUR'000	Total EUR'000
<u>Cost or revaluation</u>						
At December 31, 2005	463 927	63 609	6 313	341	34 029	568 219
Additions	-	-	-	4 077	30 173	34 250
Reclassified	12 264	8 149	950	(3 995)	(17 362)	6
Revaluation	482	76	-	-	-	558
Disposals	(361)	(1 365)	(380)	-	(37)	(2 143)
Transferred to intangible assets	-	(1)	(323)	-	-	(324)
At December 31, 2006	476 312	70 468	6 560	423	46 803	600 566
<u>Depreciation</u>						
At December 31, 2005	226 122	33 229	3 914	-	-	263 265
Charged for 2006	11 317	5 686	887	-	-	17 890
Disposals	(206)	(1 183)	(377)	-	-	(1 766)
Transferred to intangible assets	-	(1)	(66)	-	-	(67)
At December 31, 2006	237 233	37 731	4 358	-	-	279 322
Net book value at December 31, 2006	239 079	32 737	2 202	423	46 803	321 244
Net book value at December 31, 2005	237 805	30 380	2 399	341	34 029	304 954

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NOTES TO THE FINANCIAL STATEMENTS (continued)

3 PROPERTY, PLANT AND EQUIPMENT (continued)

During 2003 and 2004 buildings, gas transmission system and equipment were revalued using amortised replacement cost method. The amortised replacement cost was determined by a certified assessor JSC BDO "Invest Riga". Where the amortised cost of the asset replacement amount was lower than their carrying amount the decrease in value was charged to 2003 and 2004 income statements. Increase in value resulting from the revaluation is recognised as increase in the Revaluation reserve, according to the decisions of the Board on February 13, 2004 and February 15, 2005. During 2005 and 2006 the management of the Company revalued the assets which were received for gratis in respective years using the same basis as in revaluation performed during 2003 and 2004. Increase in value resulting from the revaluation is recognised as increase in the Revaluation reserve, according to the decisions of the Board. During 2007 the Company is performing subsequent revaluation of all asset groups mentioned above using amortised replacement cost method. See Note 2(u).

Property, plant and equipment include fully depreciated assets with a total book value of LVL 5 211 thousand or EUR 7 415 thousand (2005: LVL 4 790 thousand or EUR 6 815 thousand).

As at December 31, 2006 the carrying amount in case the property, plant and equipment would be carried under the cost model is LVL 117 810 thousand or EUR 167 629 thousand (December 31, 2005: LVL 98 660 thousand or EUR 140 381).

4 INTANGIBLE ASSETS

	LVL'000	EUR'000
<u>Cost</u>		
As at December 31, 2004	2 371	3 373
Additions	569	810
Disposals	(13)	(18)
As at December 31, 2005	2 927	4 165
 <u>Amortisation</u>		
As at December 31, 2004	1 096	1 559
Charge for the year	425	605
On disposals	(8)	(11)
As at December 31, 2005	1 513	2 153
 Net Book Value as at December 31, 2005	1 414	2 012
Net Book Value as at December 31, 2004	1 275	1 814
	 LVL'000	 EUR'000
<u>Cost</u>		
As at December 31, 2005	2 927	4 165
Additions	687	977
Transferred from property, plant end equipment	229	326
Disposals	(78)	(111)
As at December 31, 2006	3 765	5 357
 <u>Amortisation</u>		
As at December 31, 2005	1 513	2 153
Charge for the year	488	694
On disposals	(78)	(111)
Transferred from property, plant end equipment	47	67
As at December 31, 2006	1 970	2 803
 Net Book Value as at December 31, 2006	1 795	2 554
Net Book Value as at December 31, 2005	1 414	2 012

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NOTES TO THE FINANCIAL STATEMENTS (continued)

4 INTANGIBLE ASSETS (continued)

Intangible assets include fully amortised intangible assets with a total cost value of LVL 822 thousand or EUR 1 169 thousand (2005: LVL 670 thousand or EUR 953 thousand). The major intangible assets are financial accounting software Oracle Applications at carrying amount of LVL 172 thousand (EUR 245 thousand) and remaining useful life of 12 months, and individual customer payment settlement system PUNS 2 at carrying amount of LVL 177 thousand (EUR 252 thousand) and remaining useful life of 18 months as at December 31, 2006.

5 TRADE RECEIVABLES

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
<i>Non-current trade receivables</i>				
Gross value	94	220	134	313
	94	220	134	313
<i>Current trade receivables</i>				
Gross value	15 870	15 106	22 580	21 494
Provisions for impairment of receivables	(1 911)	(2 086)	(2 719)	(2 968)
	13 959	13 020	19 861	18 526
Total trade receivables	14 053	13 240	19 995	18 839

Provisions for impairment of bad and doubtful debts:

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Provisions at the beginning of the year	3 035	3 111	4 318	4 427
Charged to income statement	231	613	329	872
Released to income statement	(510)	(257)	(726)	(366)
Net charge to income statement	(279)	356	(397)	506
Written off	(816)	(432)	(1 161)	(615)
Provisions at the year end	1 940	3 035	2 760	4 318

Of the provisions as at 31 December 2006 LVL 1 911 thousand (EUR 2 719 thousand) relate to current trade receivables and LVL 29 thousand (EUR 41 thousand) relate to current other debtors, but for year 2005 LVL 2 086 thousand (EUR 2 968 thousand) to current trade receivables and LVL 949 thousand (EUR 1 350 thousand) to current other debtors (see Note 7). Provisions were created based on evaluation of the financial position and operations of separate groups of customers. The eventual losses may differ from the current calculations, as the specific amounts required are regularly reviewed and changes are reflected in the income statement.

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NOTES TO THE FINANCIAL STATEMENTS (continued)

6 INVENTORIES

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Materials and spare parts (at net realisable value)	2 365	1 612	3 365	2 294
Gas and fuel (at cost)	67 860	41 898	96 556	59 615
Other (at cost)	87	92	124	131
	70 312	43 602	100 045	62 040

Provisions for impairment of obsolete and slow moving inventories:

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Provisions at the beginning of the year	430	365	612	519
Charged to income statement	71	96	101	136
Released to income statement	(30)	(25)	(43)	(35)
Written off	(88)	(6)	(125)	(8)
Provisions at the year end	383	430	545	612

Provisions of 100% have been created for slow moving materials and spare parts. During 2006 the Company sold inventories amounting to LVL 2 thousand or EUR 2 thousand (2005: LVL 7 thousand or EUR 10 thousand) and used in operations inventories amounting to LVL 11 thousand or EUR 16 thousand (2005: LVL 16 thousand or EUR 23 thousand) that had been written off in previous years.

7 OTHER CURRENT ASSETS

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Term deposits*	7 126	-	10 140	-
Prepayments and deferred expense	427	520	608	740
Value added tax overpaid	201	216	286	307
Natural resource tax overpaid	1	173	1	246
Interest accrued on bank deposits	19	12	27	17
Claims according to court decisions	1	86	1	123
Receivable for services supplied	33	34	47	48
Other debtors	637	1 248	905	1 776
	8 445	2 289	12 015	3 257
Provisions for impairment of bad and doubtful debts**	(29)	(949)	(41)	(1 350)
	8 416	1 340	11 974	1 907

* Term deposits fixed interest rate is from 2.0% to 4.9% per annum.

** Provisions for impairment of bad and doubtful debts relate principally to Other debtors.

8 CASH AND CASH EQUIVALENTS

Cash on hand	2	2	3	3
Current accounts with banks	7 110	8 666	10 117	12 330
Term deposits*	3 936	15 200	5 600	21 628
	11 048	23 868	15 720	33 961

* Term deposits fixed interest rate is from 2.0% to 4.9% per annum (2005: from 2.10% to 4.75% per annum).

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NOTES TO THE FINANCIAL STATEMENTS (continued)

9 SHARE CAPITAL

- (a) Authorised, subscribed and paid-up share capital as at December 31, 2006 consists of 39 900 000 ordinary shares of LVL 1 each. All shares have equal voting rights and rights to dividend.

	31.12.2006.		31.12.2005.	
	% from total share capital	Number of shares	% from total share capital	Number of shares
Registered (closed issues) shares	36.52	14 571 480	36.52	14 571 480
Bearer (public issues) shares	63.48	25 328 520	63.48	25 328 520
	100.00	39 900 000	100.00	39 900 000

- (b) Shareholders

	31.12.2006.		31.12.2005.	
	% from total share capital	Number of shares	% from total share capital	Number of shares
E.ON Ruhrgas International AG <i>(including registered shares of closed issues 7 285 740)</i>	47.23	18 846 385	47.23	18 846 385
Itera Latvija LLC	16.00	6 384 001	16.00	6 384 001
JSC Gazprom <i>(including registered shares of closed issues 7 285 740)</i>	34.00	13 566 701	34.00	13 566 701
Shares owned by the State	0.00	117	0.00	117
Bearer (public issues) shares	2.77	1 102 796	2.77	1 102 796
	100.00	39 900 000	100.00	39 900 000

State owned shares are given for holding to the Ministry of Economy of the Republic of Latvia.

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NOTES TO THE FINANCIAL STATEMENTS (continued)

10 BORROWINGS

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Ministry of Finance, 2007	<u>16</u>	<u>53</u>	<u>23</u>	<u>76</u>

On November 7, 1995 an agreement was concluded between the Company and the Ministry of Finance of the Republic of Latvia. The agreement provided for assignment of a Danish Government interest free loan of DKK 3 493 thousand that should be used to finance the project stipulated in an agreement of May 4, 1995 between Lyngso Energi & Miljo and JSC "Latvijas Gāze" branch "Rīgas gāze". In 1998 the total amount of the agreement was specified and fixed as USD 508 thousand. The repayment of the loan should be made in 17 semi-annual equal payments commencing June 1999.

Maturity of the borrowings:

Current portion of borrowings	16	35	23	50
Non-current portion of borrowings	-	18	-	26
	<u>16</u>	<u>53</u>	<u>23</u>	<u>76</u>

Maturity of non-current borrowings:

between 1 and 2 years	-	18	-	26
	<u>-</u>	<u>18</u>	<u>-</u>	<u>26</u>

11 DEFERRED INCOME

Income from residents and enterprises contribution to financing of construction works of gas pipelines:

Non-current portion	8 425	6 675	11 988	9 498
Current portion	315	244	448	347
	<u>8 740</u>	<u>6 919</u>	<u>12 436</u>	<u>9 845</u>

Movement of deferred income:

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
At the beginning of the year	6 919	4 663	9 845	6 635
Received from residents and enterprises during the reporting year	2 147	2 505	3 055	3 564
Recognized as income in the reporting year (see Note 16)	(326)	(249)	(464)	(354)
Deferred to the following periods	<u>8 740</u>	<u>6 919</u>	<u>12 436</u>	<u>9 845</u>

See also Accounting policies Note (r).

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NOTES TO THE FINANCIAL STATEMENTS (continued)

12 OTHER CURRENT LIABILITIES

	31.12.2006.	31.12.2005.	31.12.2006.	31.12.2005.
	LVL'000	LVL'000	EUR'000	EUR'000
Prepayments received	4 748	3 016	6 756	4 291
Social insurance contributions	382	338	544	481
Personal income tax	318	289	452	411
Value added tax	2 549	2 230	3 627	3 173
Real estate tax	13	20	18	29
Salaries	395	314	562	447
Accrued expenses for unused annual leave	653	442	929	629
Accrued expenses for bonuses	1 979	1 965	2 816	2 796
Other current liabilities	1 869	1 460	2 659	2 077
	12 906	10 074	18 369	14 334

13 SEGMENT INFORMATION

As the Company is operating in the single business segment – natural gas, no separate information on segments is presented.

There are no geographical segments of the Company as all principal operations are carried out in Latvia.

14 COST OF SALES

	2006	2005	2006	2005
	LVL'000	LVL'000	EUR'000	EUR'000
Purchase of natural gas	120 478	83 367	171 425	118 621
Salaries	8 238	7 166	11 722	10 196
Social insurance contributions	1 875	1 675	2 668	2 383
Life, health and pension insurance	561	515	798	733
Materials and spare parts	4 293	3 061	6 108	4 355
Depreciation and amortisation	12 406	11 237	17 652	15 989
Other	4 943	3 297	7 033	4 691
	152 794	110 318	217 406	156 968

15 ADMINISTRATIVE EXPENSES

Salaries	2 690	2 737	3 828	3 894
Social insurance contributions	415	332	590	472
Life, health and pension insurance	146	115	208	164
Maintenance and utilities	777	593	1 106	844
Real estate tax	1 328	1 286	1 890	1 830
Depreciation and amortisation	614	564	874	803
Bank charges	173	173	246	246
Provisions for impairment of bad and doubtful debts, net	(279)	356	(397)	506
Other expenses	1 178	1 219	1 675	1 735
	7 042	7 375	10 020	10 494

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16 OTHER INCOME

	2006	2005	2006	2005
	LVL'000	LVL'000	EUR'000	EUR'000
Penalties from customers	274	380	390	541
Income from contribution to financing of construction works (see Note 11)	326	249	464	354
Profit on sale of fixed assets	56	15	80	21
Indemnity of loss	-	6 906	-	9 827
Other income	213	3 516	303	5 003
Net foreign exchange gains	961	278	1 367	395
Interest income	425	487	605	693
	2 255	11 831	3 209	16 834

17 OTHER EXPENSES

Materials	11	11	16	16
Salaries	110	109	157	155
Social insurance contributions	11	8	16	11
Depreciation and amortisation	42	18	60	26
Sponsorship	746	814	1 061	1 158
Provisions for slow moving and obsolete inventories impairment	41	71	58	102
Other expense	769	256	1 094	363
	1 730	1 287	2 462	1 831

18 EXPENSES BY NATURE

Purchase of natural gas	120 478	83 367	171 425	118 621
Depreciation and amortisation	13 062	11 820	18 584	16 816
Employee benefit expense (see Note 26)	14 046	12 657	19 986	18 010
Material and spare parts	4 304	3 072	6 124	4 371
Net provisions for impaired receivables	(279)	356	(397)	506
Other expenses	9 955	7 709	14 164	10 971
	161 566	118 981	229 886	169 295

19 FINANCE INCOME, NET

Finance income

- Interest income	973	637	1 384	906
	973	637	1 384	906

Finance expenses

- Service charge for borrowings	(1)	(2)	(1)	(3)
	(1)	(2)	(1)	(3)

Finance income, net

	972	635	1 383	903
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NOTES TO THE FINANCIAL STATEMENTS (continued)

20 NET FOREIGN EXCHANGE GAINS AND INTEREST INCOME

The exchange differences are credited to the income statement under Other income (see Note 16).

Interest income credited to the income statement is included as follows:

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Other income (see Note 16)	425	487	605	693
Finance income, net (see Note 19)	973	637	1 384	906
	1 398	1 124	1 989	1 599

21 INCOME TAX EXPENSE

Current tax	3 584	3 697	5 098	5 260
Unrealised deferred income tax gain related to revalued property, plant and equipment	(1 176)	(1 183)	(1 672)	(1 682)
Deferred income tax	808	811	1 150	1 153
	3 216	3 325	4 576	4 731

Corporate income tax differs from the theoretically calculated tax amount that would arise applying the 15% rate stipulated by the law to profit before taxation:

Profit before income tax	24 005	26 872	34 156	38 235
Theoretically calculated tax at tax rate of 15%	3 601	4 031	5 124	5 735
<i>Tax effect of:</i>				
Tax non-deductible expenses, net	1 425	1 170	2 026	1 664
Tax relief on donations	(634)	(693)	(902)	(986)
Unrealised deferred income tax gain related to revalued property, plant and equipment	(1 176)	(1 183)	(1 672)	(1 682)
Tax charge	3 216	3 325	4 576	4 731

Deferred income tax is calculated by using the enacted tax rate – 15%.

Reconciliation between actual corporate income tax charge and the amount of corporate income tax payable:

(Receivable) / liabilities as at 1 January	(669)	891	(952)	1 268
Charge for the year	3 584	3 697	5 098	5 260
Paid during the year	(4 031)	(5 257)	(5 734)	(7 480)
(Receivable) as at 31 December	(1 116)	(669)	(1 588)	(952)

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NOTES TO THE FINANCIAL STATEMENTS (continued)

21 INCOME TAX EXPENSE (continued)

Calculation of deferred income tax

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Deferred income tax liabilities at the beginning of the reporting year	19 897	20 034	28 311	28 505
Increase of deferred income tax liabilities (charged to income statement)	808	811	1 150	1 153
Increase in deferred income tax liabilities that results from revaluation of property, plant and equipment (charged to equity)	59	252	83	359
Decrease in deferred income tax liabilities that results from depreciation of revalued property, plant and equipment (charged to income statement)	(1 176)	(1 183)	(1 672)	(1 682)
Deferred income tax that results from disposal of revalued property, plant and equipment (charged to equity)	(38)	(17)	(55)	(24)
Deferred income tax liabilities at the end of the reporting year	19 550	19 897	27 817	28 311

Deferred income tax assets and liabilities are attributable to the following items:

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Temporary difference on depreciation of property, plant and equipment (to be settled within 12 months)	867	960	1 234	1 365
Temporary difference on depreciation of property, plant and equipment (to be settled after more than 12 months)	19 573	19 861	27 850	28 260
Temporary difference on provisions for impairment of bad and doubtful debts (to be settled within 12 months) *	(394)	(492)	(561)	(700)
Temporary difference on accrued expenses for unused annual leave and bonuses (to be settled within 12 months)	(439)	(367)	(625)	(522)
Temporary difference on provisions for impairment of inventories (to be settled within 12 months)	(57)	(65)	(81)	(92)
Deferred income tax liability, net	19 550	19 897	27 817	28 311

* These are provisions for impairment of bad and doubtful debts that are expected to become allowable for corporate income tax purposes in the foreseeable future as relevant debtor companies are in liquidation.

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NOTES TO THE FINANCIAL STATEMENTS (continued)

22 EARNINGS PER SHARE

The Company has no dilutive potential ordinary shares and therefore diluted earnings per share are the same as the basic earnings per share.

Basic earnings per share are calculated by dividing the net profit attributable to the shareholders by the weighted average number of ordinary shares in issue during the year.

	2006	2005	2006	2005
	LVL	LVL	EUR	EUR
Net profit attributable to shareholders (a)	20 789 451	23 546 833	29 580 724	33 504 124
	number	number	number	number
Ordinary shares as at 1 January	39 900 000	39 900 000	39 900 000	39 900 000
Ordinary shares as at 31 December	39 900 000	39 900 000	39 900 000	39 900 000
Weighted average number of ordinary shares outstanding during the year (b)	39 900 000	39 900 000	39 900 000	39 900 000
Basic earnings per share during the year (a/b) in LVL or EUR	0.521	0.590	0.741	0.840

23 DIVIDENDS PER SHARE

Dividends payable are not accounted for until they are declared at the Annual General Meeting. At the meeting, a dividend in respect to 2006 of LVL 0.30 (EUR 0.427) per share (2005 actual dividend LVL 0.35 (EUR 0.50) per share) amounting to LVL 11 970 thousand (EUR 17 032 thousand) (2005 actual LVL 13 965 thousand (EUR 19 870 thousand)) is to be proposed by the management. These financial statements do not reflect these dividends payable, which will be accounted for in the shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2006.

The dividends paid in 2006 for 2005 were LVL 13 965 thousand (LVL 0.35 per share) or EUR 19 870 thousand (EUR 0.50 per share). The dividends paid in 2005 for 2004 were LVL 11 970 thousand (LVL 0.30 per share) or EUR 17 032 thousand (EUR 0.427 per share).

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NOTES TO THE FINANCIAL STATEMENTS (continued)

24 CASH GENERATED FROM OPERATIONS

Reconciliation of profit before tax to cash generated from operations:

	2006 LVL'000	2005 LVL'000	2006 EUR'000	2005 EUR'000
Profit before income tax	24 005	26 872	34 156	38 235
<i>Adjustments for:</i>				
Depreciation (Note 3)	12 573	11 395	17 890	16 211
Amortisation (Note 4)	488	425	694	605
Provision for impairment of slow moving inventories (Note 6)	41	71	58	101
Accrued expenses for bonuses	(14)	(400)	(19)	(569)
Accrued expenses for unused annual leave	(211)	(81)	(300)	(115)
Release of provisions	-	(1 386)	-	(1 972)
Interest income (Note 20)	(1 398)	(1 124)	(1 989)	(1 599)
Interest expense (Note 19)	1	2	1	3
Profit on sale of property plant and equipment (Notes 16)	(56)	(15)	(80)	(21)
<i>Changes in working capital</i>				
- trade and other receivables	(7 762)	4 757	(11 043)	6 769
- inventories	(26 669)	(16 145)	(37 947)	(22 972)
- trade and other payables	27 870	27 561	39 652	39 217
	28 868	51 932	41 073	73 893

25 RELATED PARTY TRANSACTIONS

No entity exercises a control over the Company. Entities disclosed below own or owned more than 20% of the shares that deemed to provide a significant influence over the Company.

(a) Sale of services

JSC “Gazprom”	4 538	4 267	6 457	6 071
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(b) Purchase of natural gas

JSC “Gazprom” and “Itera Latvija” LLC*	104 619	75 766	148 860	107 805
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*“Itera Latvija” LLC was a related party until 28 January 2005.

(c) Purchase of services

E.ON Ruhrgas International AG	-	19	-	27
E.ON Ruhrgas AG	9	17	13	24
	9	36	13	51

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NOTES TO THE FINANCIAL STATEMENTS (continued)

25 RELATED PARTY TRANSACTIONS (continued)

(d) Accounts payable for natural gas and services as at 31 December

	31.12.2006.	31.12.2005.	31.12.2006.	31.12.2005.
	LVL'000	LVL'000	EUR'000	EUR'000
JSC "Gazprom"	10 706	7 575	15 234	10 778
E.ON Ruhrgas International AG	-	19	-	26
	10 706	7 594	15 234	10 804

Payables are payable in cash and are not secured by a pledge or otherwise.

(e) Remuneration to Board of Directors and Council

A listing of the members of the Board of Directors and Council is shown on page 3.

	2006	2005	2006	2005
	LVL'000	LVL'000	EUR'000	EUR'000
Salaries*	1 297	1 393	1 845	1 982
Social insurance contributions*	87	102	124	145
Health and life insurance	11	11	16	16
Contributions to pension funds	70	29	100	41
	1 465	1 535	2 085	2 184

* Salaries and social insurance contributions include accrued bonuses for the reporting year.

26 EMPLOYEE BENEFIT COSTS

Wages and salaries	11 038	10 012	15 706	14 246
Social insurance contributions	2 301	2 015	3 274	2 867
Life, health and pension insurance	707	630	1 006	897
	14 046	12 657	19 986	18 010

In accordance with the rulings of the Cabinet of Ministers of Latvia 74% (2005: 75%) of the social insurance contributions are used to fund the state defined contribution pension system.

27 FINANCIAL RISK MANAGEMENT

The Company's activities expose it mainly to a currency exchange risk and credit risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance.

(a) Credit risk

Cash at bank and receivables are the main financial assets exposed to the credit risk. The Company's cash funds and their equivalents are kept with the largest financial institutions of Latvia. Receivables are shown at their recoverable amount. The Company is exposed to the concentration of the credit risk because considerable part of the net turnover refers to a limited number of customers. Four of the Company's customers form up to 45% of the sales (in 2005 – 43%), the debt of one of these customers on December 31, 2006 was 20.7% (in 2005 – 19.9%) of the total trade receivables, while second and third largest debtor comprised respectively 8.8% and 6.2% each (in 2005 – 7% and 6%) of the total trade receivables.

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NOTES TO THE FINANCIAL STATEMENTS (continued)

27 FINANCIAL RISK MANAGEMENT (continued)

(b) Currency exchange risk

The Company is not directly subjected to the risk of foreign currencies exchange rate fluctuations, as gas price is set in USD and afterwards recalculated in EUR, while gas sales tariffs are set in lats. Settlements for the supplied gas are made in EUR. Considering that as from January 1, 2005 exchange rate of LVL is pegged to that of EUR, fluctuations of LVL/EUR rate are limited and no significant influence on further financial results is anticipated. Changes of gas purchase prices in USD depending on heavy fuel oil quotation are covered by the natural gas sales tariffs approved by the Regulator of the Public Utilities Commission. To a certain extent they cover also the fluctuations of EUR/USD rate. The risk of foreign currencies rate fluctuations, which is related to debts to suppliers, is controlled through keeping a significant part of financial resources in deposits of the respective currency.

	2006		2005	
	USD' 000	EUR' 000	USD' 000	EUR'000
Financial assets	426	6 257	227	1 818
Financial liabilities	(74)	(74 890)	(172)	(43 865)
Balance sheet position in original currency	352	(68 633)	55	(42 047)
Balance sheet position in LVL'000	189	(48 236)	33	(29 551)
Balance sheet position in EUR'000	269	(68 633)	47	(42 047)

(c) Fair value

The carrying value of financial assets and liabilities approximates their fair value.

28 CAPITAL COMMITMENTS

The Company has planned to spend the following amounts for capital expenditures for property, plant and equipment and intangible assets in the subsequent year:

	31.12.2006. LVL'000	31.12.2005. LVL'000	31.12.2006. EUR'000	31.12.2005. EUR'000
Contracted for, but not delivered	16 265	12 065	23 143	17 167
Authorised, but not yet contracted for	16 885	20 455	24 025	29 105
	33 150	32 520	47 168	46 272

29 CONTINGENT LIABILITIES

In 2005 in the Vidzeme Suburb Court of Riga proceedings concerning claim of E.ON Ruhrgas International AG against Joint Stock Company “Latvijas Gaze” regarding resolution of the meeting of shareholders on invalidation of the amendments to the charter, which provides for increase of required quorum for competence of the meeting of the shareholders from 75% to 85%, were started. SIA “Itera Latvia” was invited to participate as the third party. Since the court rejected the claim of E.ON Ruhrgas International AG, the judgment of the court in 2005 was appealed in Regional Court of Riga, which with its judgment of April 10, 2007 satisfied the claim of the E.ON Ruhrgas International AG. The Board of the Joint Stock Company “Latvijas Gaze” decided to appeal in cassation order against the judgment of the Regional Court of Riga in the Supreme Court of the Republic of Latvia. Legal proceedings are continued.

In November 23, 2005 the Administrative Regional Court received an application of the E.ON Ruhrgas International AG regarding cancellation of the decision of the Enterprise Register of the Republic of Latvia of December 20, 2004 concerning re-entering of the Joint Stock Company “Latvijas Gaze” into the Commercial Register. The court suspended the proceedings until the civil claim submitted by E.ON Ruhrgas International AG will be processed by the court of the general jurisdiction.

The management of the Company believes that it is less than probable that any of the above litigations will result in a material outflow of the Company’s resources.

Translation from Latvian Original

JOINT STOCK COMPANY "LATVIJAS GĀZE"
FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

NOTES TO THE FINANCIAL STATEMENTS (continued)

30 TAX CONTINGENT LIABILITIES

The tax authorities have carried out full-scope tax audit at the Company for the years 2002 and 2004. The effect of this audit was not significant to these financial statements.

The tax authorities may at any time inspect the books and records within 3 years subsequent to the reported tax year, and may impose additional tax assessments and penalties. The Company's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

31 SUBSEQUENT EVENTS

There are no subsequent events since the last date of the reporting year, which would have a significant effect on the financial position of the Company as at December 31, 2006.

On January 26, 2007 the Board has passed the resolution to revalue property, plant and equipment using amortised replacement cost method. See Note 2(u).