



Skagerak
Energi

2016

ANNUAL REPORT

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CEO Knut Barland

Message from the CEO

Power in a time of change

Skagerak Energi's mission in society is to promote economic growth and social welfare, and safeguard life and health through effective and reliable supplies of energy. In the first weekend in November 2016, the weather gods put us to the test. In just two days, we received 75 mm of precipitation, in the form of heavy, wet snow, which then froze solid. Trees toppled over under the weight of the snow and power lines became encrusted in a thick jacket of ice. This led to a large number of earthing faults and phase interruptions. From one day to the next, we were catapulted into the most serious emergency situation in the company's history. A total of 41,000 customers were affected, most for only a few minutes, but some for considerably longer. It was not until five days later, on Friday, 11 November, that the emergency situation came to an end.

In hindsight, we can conclude that things went well. As far as we know, none of our customers suffered any physical harm. And we succeeded in performing extremely challenging operations in difficult terrain, with 200 people in action, without any personal injuries. At the same time, there are lessons to be learned from the situation, so we can be better equipped next time nature shows her most demanding aspect.

The electrical power market is experiencing a difficult period. The price of electricity came to NOK 0.23/kWh in 2016, around 30 per cent more than in 2015. Nevertheless, the value of green certificates, which provide an additional income for new renewable projects, has fallen, and there is uncertainty surrounding the outlook for the certificates' price. In addition to these demanding market conditions, the economic rent tax, which power companies have to pay, has become a major problem. The way this extra tax is designed means that new facilities, which are highly leveraged, could end up paying more in tax than they make in profit. New hydropower projects are taxed more severely than new oil fields.

Market conditions and the unreasonable economic rent tax means that in 2016 we decided to mothball our largest expansion project, the Sauland Power Plant. It was a difficult decision, after we had worked hard for many years on an environment and climate-friendly expansion project that had been approved by the authorities.

Skagerak Energi is well placed with respect to the "green shift". Our core business, the supply of electricity, is already 100 per cent climate-friendly. 95 per cent of our district heating production is based on woodchips, heat pumps and waste heat from Yara. We only use oil and gas during abnormal demand peaks to ensure our customers have sufficient heat. We are working hard to boost the percentage of renewables even further.

We have quickly become a significant supplier of biogas to the transport sector. It is still a very immature market, but has an enormous potential in Norway. Not everyone can drive an electric vehicle. We supply biogas to refuse collection trucks and buses in Vestfold and Grenland. From the summer of 2017, we will also supply biogas to Nettbuss vehicles from a new filling station in Moss. And Norway Post has signed a deal with us. Biogas is the perfect example of a circular bioeconomy. The plant takes in biogas based on livestock manure and human food waste from Vestfold and Grenland, and out comes biogas and solid residues that can replace inorganic fertiliser, whose production causes emissions of the powerful greenhouse gas nitrous oxide. Combustion of biogas also prevents emissions of another greenhouse gas, methane, which occurs when waste decomposes without oxygen. When buses run on biogas, the waste product is carbon dioxide, which is absorbed by the plants that are eaten by the cattle on the farms. A perfect green circle.

In addition to tackling new environmental requirements, we are entering a period in which widespread digitalisation, the "internet of things" and artificial

intelligence, along with local production and storage of energy, will change the electricity supply industry's business models. No one quite knows what changes will come, but we must analyse today's situation and make strategic decisions that will affect what happens in the time ahead. In 2017, Skagerak Energi is setting up a dedicated corporate development unit to ensure that our business keeps pace with the changes we know will come.

We have previously adjusted our investment level in response to the low prices we have seen in recent years. In 2016, all investments were paid for out of day-to-day earnings. At the same time, we cut our borrowings by NOK 200 million. Our underlying income remains lower than we would like, but the trend is once again positive. Our EBITDA increased by 25 per cent, compared with the year before, and our equity ratio rose to 42 per cent.



Knut Barland
CEO



Skagerak Energi's corporate social responsibility

- Skagerak Energi's mission in society is to ensure the secure and stable provision of the renewable energy that contributes to economic growth and social welfare.
- Renewable energy production contributes to lower greenhouse gas emissions. At the same time, we must impact the natural environment as little as possible and cause no harm to employees or anyone else.
- Skagerak Energi is an engine for value creation in Vestfold and Grenland. Since 2001, it has generated NOK 25 billion for sharing between its stakeholders.

Our mission in society

Skagerak Energi's mission in society is to ensure the secure and stable provision of the renewable energy that contributes to economic growth and social welfare.

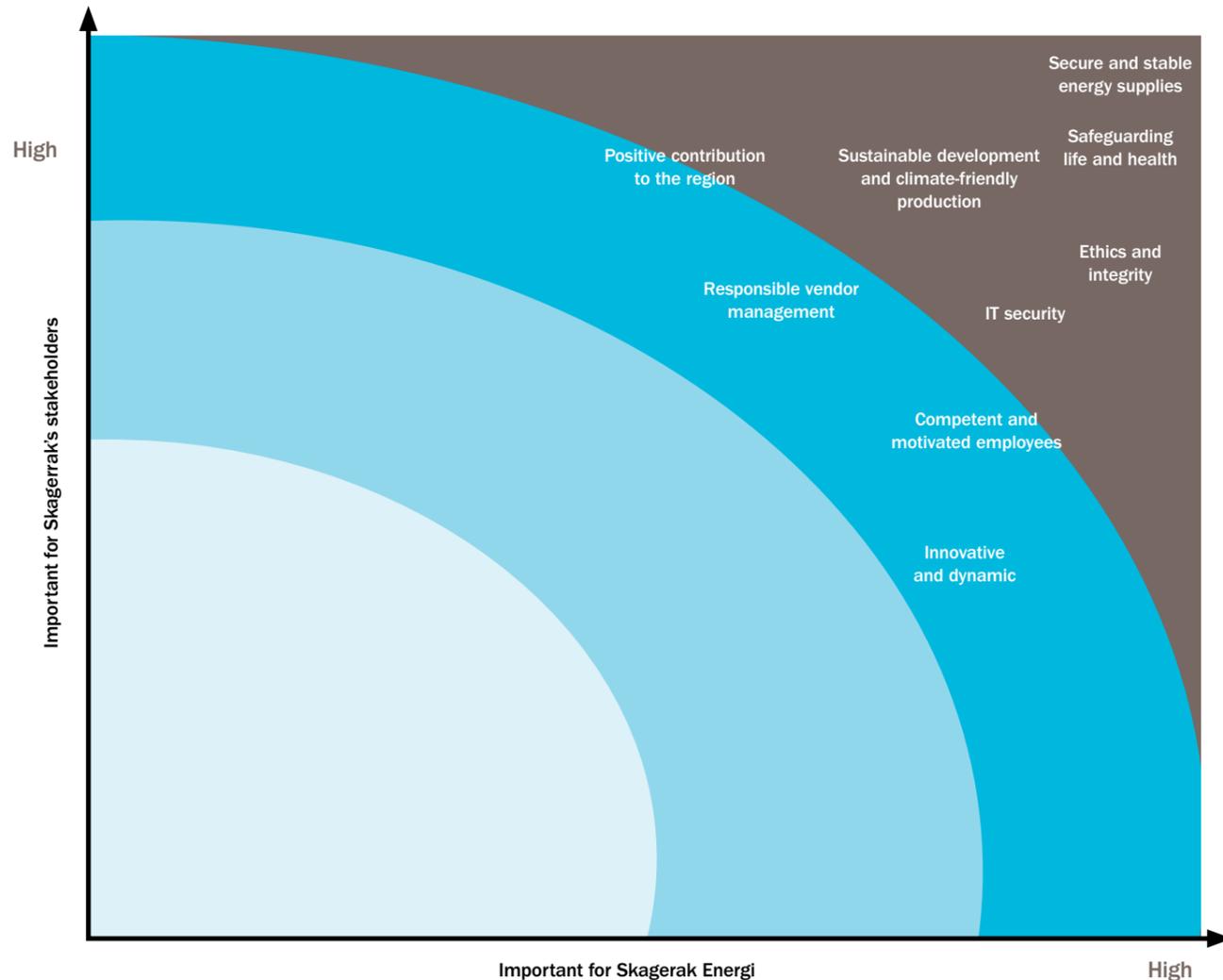
Electrical energy is important for Norway, and the Group builds and manages infrastructures that are critical for society. Power outages or irregularities can have serious consequences, including the loss of human life. Power outages will cause major problems for hospitals, the emergency services, the water supply, and mobile phone and data communications.

For industry, any interruption in the supply of electricity can be very costly, because output must be halted, while electricity is the only form of heating for many private households.

The Group must prioritise its resources in order to fulfil its mission and create long-term value for society and shareholders. All decisions and activities must be taken responsibly and meet our most important stakeholders' needs and expectations. Expertise and good risk management in all areas will safeguard the balance between value creation and the prevention of loss or harm to life, biodiversity or other resources.

Skagerak Energi has assessed which areas must be prioritised so that it can carry out its mission in a responsible fashion.

All the areas in the diagram are important. The prioritisation has been done on the basis of the Group's strategy and stakeholder analysis. Some areas are discussed in more detail in the report. Emphasis has been placed on describing why the areas are considered important and how the Group is working with them, and presenting the most important results. The report has been prepared in accordance with the Global Reporting Initiative's framework for reporting on corporate social responsibility.



Collaboration and dialogue with stakeholders

Our ties to the region are important for Skagerak Energi. Three of the region's local authorities own shares in the Group, and Skagerak Energi is one of its major employers.

In addition, the Group is a major customer of local businesses. Skagerak Energi's operations depend on a variety of resources that are valuable for society, and a number of socially important functions depend on the Group.

Developments in society mean that people are increasingly dependent on electricity, and patterns of consumption are changing towards higher demand peaks and more local, consumer-produced power.

The production and distribution of

renewable energy helps to limit global climate change. At the same time, the Group's activities will involve some localised changes to the landscape and affect recreational areas. Increased value creation and long-term growth must be achieved through sustainable management of natural resources and a constructive collaboration with stakeholders.

Stakeholders' need for information is growing in response to an increasingly complex world. In 2016, Skagerak Energi has continued working to enhance

its collaboration and dialogue with stakeholders. External reporting has been prepared with the aim of increasing stakeholders' insight and providing a basis for discussion. And moving forward, communication and dialogue with our stakeholders will be given even greater priority.

STAKEHOLDER GROUP	WHAT THEY ARE CONCERNED ABOUT	ARENA FOR DIALOGUE
Shareholders (Statkraft and the municipalities Skien, Porsgrunn and Bamble)	Safe, efficient, profitable and responsible production and distribution of climate-friendly and renewable energy.	Shareholder meetings, board meetings and other formal meetings. Financial and other status reports. Day-to-day communication with the Statkraft Group.
Employees	Safety in the workplace Co-determination Job security Skills development Reputation	Employee representatives on the board Various corporate committees and collective bargaining arrangements Internal staff meetings Employee surveys and annual employee appraisals Day-to-day operations
Customers (industrial, commercial and private customers)	Capacity, quality and secure energy supplies, Price Environmental impact Quick customer service	The Group's website and Facebook page Work on site Information letters, adverts Conferences, trade fairs Meetings and adhoc, case-by-case dialogue Customer service centre
Host municipalities	Safe, efficient and responsible operations, Sensitivity in altering the environment and protection of biodiversity Financial and other positive contributions	Systematised in connection with audits and new permits Meetings and adhoc, case-by-case dialogue
Local population	Safe facilities and access to the landscape Sensitivity in altering the environment and protection of biodiversity Safe and secure jobs Financial and other positive contributions	Systematised in connection with audits and new permits Meetings and ad-hoc, case-by-case dialogue
Environmental interests and organisations	Safe facilities Sensitivity in altering the environment and protection of biodiversity	Dialogue in connection with audits and new permits Meetings and adhoc, case-by-case dialogue
Public authorities	Capacity, quality and secure energy supplies Safe facilities Safe and responsible operations and expansion in compliance with regulations and permits	Inspections Meetings and communication in connection with audits and new permits Meetings and ad-hoc, case-by-case dialogue
Vendors	Solvency Competence and prestige projects Ethical procurement practices	Procurement processes Meetings and adhoc dialogue for follow-up during contractual periods Conferences, trade fairs, courses

Safe and healthy working environment

Skagerak Energi's most important resource is its workforce. Its objective is therefore to provide a safe and healthy working environment with a high level of job satisfaction, and thereby ensure the Group's effective operation.

It is fundamental to Skagerak Energi that the Group's decisions and activities are based on co-determination and involvement, as well as responsibility and consideration for all concerned.

Skagerak Energi's goal is zero harm to life and health, a low sickness absence rate and a high level of job satisfaction. The Group aims to provide a good psychosocial and physical working environment, in which employees enjoy and feel competent to do their work, with no risk to their health.

The Group works systematically to develop its corporate culture, to foster trust, openness, regulatory compliance, an understanding of risk and a thirst for improvement. Skagerak Energi has been an inclusive working environment (IA) company since 2002, and emphasis is placed on early dialogue to prevent and avoid sickness absence, as well as on work-related adaptation and follow-up, so that those off sick can return to work as quickly as possible.

LOWER SICKNESS ABSENCE RATE

The Group had a sickness absence rate of 3.1 per cent in 2016, compared with 3.8 per cent the year before. The industry average was 4.0 in 2015, and the average sickness absence rate in the Norwegian workplace over the past three years has been 6.3 per cent. The results of employee surveys are used as a basis for working environment-related initiatives in all business units. In 2016, the implementation rate for approved initiatives was 97 per cent.

Skagerak Energi offers a varied employee welfare programme. Employees can choose to be physically active, participate in various social events or make use of company-owned holiday houses by the sea and in the mountains. To help employees achieve a good work-life balance, flexitime is also offered.

The Group has an agreement with an approved company health service, and annual occupational health examinations are undertaken, along with other surveys of the health and physical working environment. Action plans are drawn up and followed up by

AREA	RESULTS		
	2016	2015	2014
Sickness absence rate	3,1 %	3,8 %	3,7 %
LTIs/medical treatment	4	7	3
H2 (LTIs per million hours worked)	4,2	6,8	2,9
Occupational health examinations	213	205	235
No. of participants on safety courses (FSE)	375	524	464
No. of contractors on safety courses (FSE)	250	215	—
No. of participants on first aid courses	408	474	472

working environment committees at both the corporate and company level. The company health service attends relevant meetings of the working environment committees, and provides the companies with specialist assistance as required.

INTENSE FOCUS ON RISK PREVENTION

The Group's most important risk areas with regard to life and health have been identified, and underpin the choice of working methods, training requirements and use of personal protection and safety equipment. Examples of hazardous work undertaken at Skagerak Energi include work on or near electrical installations, work at height, work on or near dams and regulated watercourses, and in remote locations.

The Group had four personal injuries among its workforce in 2016. Skagerak Energi demands the same level of safety of its contractors as for its own staff, and employment conditions must comply with applicable legislation for everyone performing work for the Group.

Several of the Group's facilities are located in areas used for recreation and outdoor pursuits. These must be properly secured.

LINE RESPONSIBILITY

HSE is a line responsibility. HSE risk assessments are carried out at many levels, and these form the basis for risk-mitigation and preventive measures. Updated and dynamic procedures for working methods and the use of protective and safety equipment

are important for reducing risk. Important preventive measures include training, non-conformance and improvement work, and inspections focusing on behaviour-based safety observations. Skagerak Energi complies with Norwegian HSE legislation and performs regular internal control inspections in addition to more comprehensive group audits and inspections by the authorities. Serious incidents and near-misses are investigated thoroughly. It is expected that all employees support the policy of openness by reporting HSE-related non-conformances and making improvement suggestions. The number of incoming reports and suggestions is monitored by the Group. This ensures a high level of activity and swift remedy of unwanted situations.



Competent and motivated employees

Growing competition and rapid technological advances are driving the need for change. In response, Skagerak Energi needs competent and motivated employees.

Skagerak Energi's human resource (HR) management policies focus on the three key areas of strategic competence management, management and organisational development, and culture, the working environment and cooperation.

COMPETENCE MANAGEMENT

For Skagerak Energi, employee training and skills development is an important tool for motivating, developing and retaining competent staff. In connection with their annual appraisal, each employee agrees a training plan. The Group focuses on strategic competence planning and the managed transfer of skills based on the companies' business plans. The Group's management and HR policies were revised in 2016, and will be included in all individual employee appraisals with effect from 2017. These appraisals provide a systematic evaluation of both performance and behaviours. All employees at Skagerak Energi must have a good understanding of the behaviours and attitudes expected of them.

The Group supports relevant further training for its employees. This includes financial support to enable employees to take external master or bachelor programmes. Both internal and external training activities are coordinated largely through Skagerak. Important expertise

is also acquired through the companies' R&D projects.

SUBSTANTIAL RECRUITMENT REQUIREMENT

In some parts of the Group, the average age of workers is relatively high. More than 100 employees are older than 60, while more than 200 are more than 50 years of age. Many of those approaching retirement possess important expertise, and the transfer of knowledge is imperative. At a time of rapid technological development, this also provides an opportunity to recruit vital new competence.

Opportunities within the Group for employment, competence development, promotion and other terms and conditions are independent of gender and social, ethnic and cultural background. Measures intended to achieve a better gender balance at management level have been identified and initiated. In recent years, around 15 employees have completed the Female Future programme organised by the Confederation of Norwegian Enterprise (NHO). This programme aims to encourage women to take on management and board roles.

A BALANCED WORKING LIFE

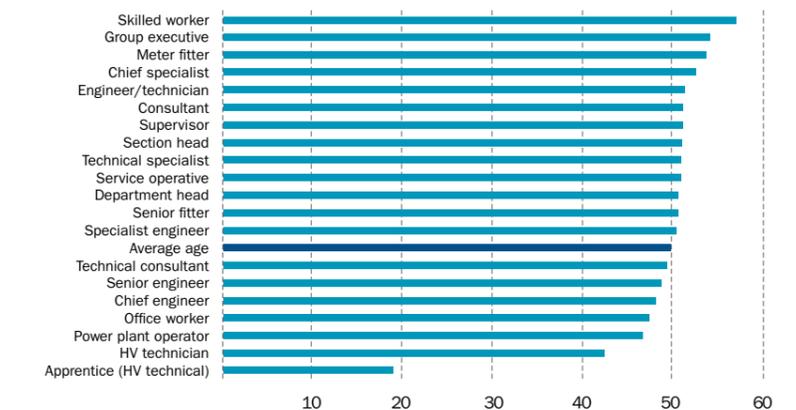
In general, the Group emphasises measures to accommodate employees in all phases

of their lives. Flexible working hours are available, so that employees can adapt their working hours to their own situations. The Group places particular emphasis on providing work adaptations for staff with health issues. This is one of several important factors behind the steady fall in the sickness absence rate. Work experience places have also been made available for non-employees who need workplace training or the opportunity to test their capacity for work.

At the close of 2016, Skagerak Energi had 610 employees, of whom 451 were men and 159 women (26 per cent). Of the Group's 69 managers, 17 are women (25 per cent). Of the Group's board of directors' nine members, two of the shareholder-elected and two of the employee-elected directors are women. In 2016, the Group hosted two trainees in collaboration with Trainee Telemark.



AVERAGE AGE FOR VARIOUS POSITIONS



Secure and stable supplies of renewable energy

In addition to the inconvenience caused to customers, power outages can have major consequences for life and health, as well as businesses' profitability. Skagerak Energi takes its responsibility for providing secure and stable supplies of electricity very seriously.

Skagerak Energi develops and manages infrastructures that are critical for society. Power outages or interruptions can have serious consequences:

- Power outages to important service providers like hospitals, emergency services, water utilities and mobile phone and data communications can, at worst, result in loss of human life.
- Power outages or poor-quality electricity supplies to industry can be costly because production must be halted.
- Electricity is the only form of heating for many households.

Developments in society mean that people are increasingly dependent on electrical power. Rapid technological advances lead to changed needs and expectations, and to more potential solutions. Skagerak Energi meets these challenges through the development of and investment in modern infrastructure and a high level of competence.

RAPID CHANGE REQUIRES HIGH COMPETENCE

The industry is subject to strict regulation and Skagerak Energi maintains a good dialogue with the authorities to ensure regulatory compliance. The environment and resources are expected to be managed responsibly and expertly. Effective planning and operation of the Group's facilities is necessary to achieve secure and stable production and distribution of renewable energy. The Group has a highly skilled workforce, which ensures effective production planning, stable operations and good decisions with respect to the upgrading of existing facilities or the construction of new ones. Analytical methods and competence are developed through the organisation's own R&D projects and in collaboration with well-reputed companies and institutions

When choosing where to route transmission cables, both environmental and climate-related challenges are taken into account. Skagerak Nett has reduced the total length of its overhead cables (high voltage and low

voltage) by almost 500 km in the past five years, and increased the length of buried cables and undersea cables by 620 km in the same period.

GOOD POWER OUTAGE STATISTICS

Secure electricity supplies mean that Skagerak Nett's approx. 190,000 end users should experience as few power outages as possible. Any faults must be identified quickly and repaired safely and rapidly. The number and duration of outages is used actively for performance management. The average number of outages lasting more than three minutes experienced by Skagerak Nett's customers has remained stable and is considerably lower than the national average. Skagerak Nett's average number of outages rose slightly from 2015 to 2016. However, this was primarily due to the severe snow fall and cold weather in early November. (See separate section.)

WELL THOUGHT-OUT MAINTENANCE

Although Skagerak Nett's regional distribution network is in generally good condition throughout the area, constant development and improvement measures are implemented to provide a better grid structure and higher capacity. One example is the project "Solum Switching Station", which will supply the new double-track railway line between Porsgrunn and Larvik from 2018. Several measures will be implemented in the company's power distribution network to improve the standard.

Skagerak Nett makes use of updated building and maintenance standards. In recent years, particular attention has been paid to inspections and the correction of non-conformances. In 2016, two major projects focusing on signage and technical non-conformances were completed. Maintenance activities have been made more systematic, and the intervals between inspections and deadlines for correction have been changed. The changes are well established and are followed up on a regular basis.

The Norwegian Directorate for Civil Protection (DSB) carries out annual inspections.

Any findings are systematically addressed within the DSB's deadlines. Following the DSB's autumn 2016 inspection, Skagerak Nett received good feedback on the standard of the facilities audited.

ICT – AN IMPORTANT TOOL

The choice and development of ICT systems is an important factor for the secure and stable production and distribution of energy. The Group depends on an ICT infrastructure and safety solutions that function optimally and are adapted to the future. Specifications change rapidly, and the companies' ICT platform must support this dynamic development. The industry is increasingly exposed to hacking, and the Group gives priority to resources that can prevent this through the creation of robust barriers. In addition to sound technical expertise and effective technical solutions, employee vigilance, good access-control routines and security clearances are also important. ICT is a resource-intensive activity that is changing constantly and rapidly, and is considered fundamental for the Group's ability to develop itself and continue being a forward-looking energy provider.

ALWAYS PREPARED FOR AN EMERGENCY

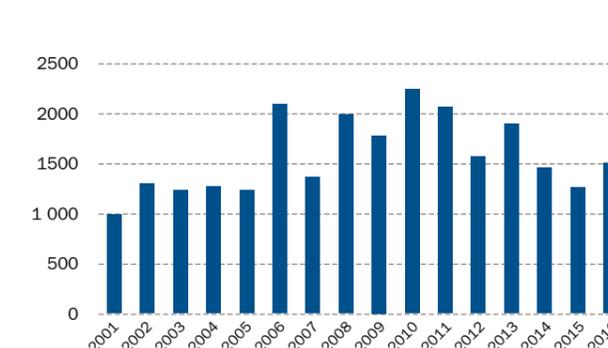
In addition to working preventively in all areas, Skagerak Energi must also be prepared to handle acute situations. Skagerak Nett and Skagerak Kraft have control centres that constantly monitor their installations and implement and coordinate any necessary countermeasures. The Group has an overall quality system comprising work processes and instructions. There is also a strong focus on compliance and safe working, as well as the competence and safety of all those working at or near our facilities. Emergency situations are coordinated from the control centres and associated coordination rooms. Regular training exercises are carried out to ensure that the plans are updated and widely known, and that the emergency response leadership and on-duty crews are well prepared to handle any situations that may arise.

KEY FIGURES, SKAGERAK ENERGI AS

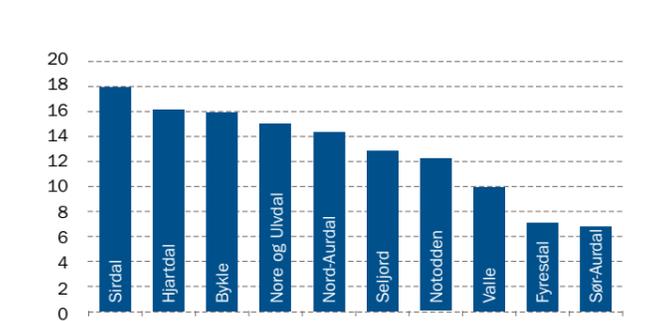
SOCIAL RESPONSIBILITY	UNIT	2012	2013	2014	2015	2016
SICKNESS ABSENCE AND PERSONAL INJURIES						
Sickness absence	%	4,6	3,6	3,7	3,8	3,1
Personal injuries resulting in lost time or medical treatment	No.	14	5	7	8	4
H2 (personal injuries per million hours worked)	#	10,4	3,7	5,7	6,8	4,2
DISTRICT HEATING						
Non-renewable district heating	GWh	27,5	8,1	5,2	4,2	9,0
Renewable district heating	%	85	87	86	85	95
District heating delivery network	km	32	34	33	44	46
District heating water consumption	tonnes	922	5 107	1 089	31 136*	1 850
ENERGY CONSUMPTION						
Electricity						
Pump power	GWh	24,6	21,4	27,1	31,2	21,6
Electrical boilers for district heating	GWh	3,9	3,9	1,4	1,5	1,6
Office buildings	GWh	6,3	4,6	4,04	4,1	4,6
Power stations	GWh				4,5	4,3
Transformer substations	GWh					3,3
Fuel						
Natural gas for district heating	tonnes	947	348	92	83	78
Fuel oil	tonnes	301	59	54,1	41,2	28
Fuel for vehicles, machines and generators	tonnes	436	680	719	754	550
Energy loss						
Energy loss from transformers and power lines	GWh	417	451	456	458	445
BIODIVERSITY						
Release of fish/smolt	No.	75 720	75 720	70 759	70 010	70 136
Red-listed species in watercourses (eels & river mussels)	No.	2	2	2	2	2
LENGTH OF POWER LINES AND CABLES						
High-voltage power lines	km	2 736	2 723	2 710	2 593	2 615
Low-voltage power lines	km	4 078	3 708	3 684	3 638	3 584
Buried cables and undersea cables	km	10 436	10 179	10 338	10 541	10 734
EMISSIONS AND WASTE						
Carbon emissions						
District heating facilities	tonnes	5023	1648	585	338,7	231
Business travel air	tonnes	52	39	54	45	39
Business travel cars & other vehicles, machines & generators	tonnes	1 138	1 774	1 876	1 966	1 435
Emissions of other gases						
SF ₆	tonn CO ₂ e	128	187	404	542	97
Waste						
Total waste	tonnes	973	1 237	1 512	1 237	973
Hazardous waste	tonnes	154	60	381	60	62
Residual waste	tonnes	279	240	217	436	151
Material and energy recycling	tonnes	540	937	732	741	760
REGULATORY NON-COMPLIANCE						
Violation of licence terms or serious environ. non-comp.	No.	0	0	0	0	0
Fines	NOK	0	0	0	0	0

* Water consumption in 2015 was due to technical faults that caused leaks

VALUE CREATION 2001–2016 NOK million



TAX PAID TO THE LARGEST HOST MUNICIPALITIES IN 2016 NOK millioner kroner



Sustainability and climate-friendly production

Developments in society are driving up demand for energy, at the same time as the Paris Agreement requires any developments to be sustainable. The answer is to boost production of renewable energy and cut consumption of fossil energy carriers.

Skagerak Energi's production and distribution of renewable energy is helping to limit global climate change. The Group's overarching goal is for all expansion and operations to comply with the principles of sustainable development. This is achieved by:

- Proper management of water resources and the protection of biodiversity
- Good operating standards, systematic maintenance and infrastructure inspections
- Good working methods and technologies to prevent emissions and other pollution
- Responsible vendor management

No violations of watercourse regulation permits took place in 2016, and no other incidents occurred that had serious consequences for the environment. The total volume of waste has been reduced from 1,237 tonnes in 2015 to 973 tonnes in 2016. Furthermore, while 65 per cent of the waste was sorted at source in 2015, that figure had risen to 85 per cent in 2016. The Group continued to facilitate the private use of electric cars in 2016, and several vehicle-charging stations have been set up.

Skagerak Kraft has kept its ISO 14001 environmental certification, which reflects its active engagement in those areas where the company can affect the environment and shows that it is constantly reducing its environmental impact. The quality of the company's environmental efforts and its compliance with the ISO 14001 standard are verified annually by DNVGL.

Skagerak Kraft emphasises sound management of its watercourses to safeguard effective operations and value creation. This helps to protect communities through anti-flooding measures in connection with periods of substantial precipitation. This is particularly important at a time when extreme weather is becoming a more frequent occurrence. In general, considerable importance attaches to regulatory compliance, as well as self-imposed restrictions which, in some watercourses, are even stricter than those stipulated in the company's operating licences. Examples of remedial measures include the annual release of around 70,000 juvenile fish and the transport of eels past all five power plants on the Kragerø watercourse. This means that eels that have migrated up the watercourse can return to the sea unharmed.

Otherwise, Skagerak Kraft actively participates in and helps finance other environmental and climate-related research projects initiated by the Norwegian Water Resources and Energy Directorate (NVE) and the Norwegian Environment Agency, which are carried out by well-reputed institutions, such as SINTEF, the Norwegian University of Science and Technology (NTNU), the Norwegian Institute for Nature Research (NINA) and the University College of Southeast Norway.

In 2016, Skagerak Kraft maintained its focus on improving the technical barriers to emissions at all its facilities. The upgrade of all generator pits was completed in 2016. The risk of oil and chemical leaks has therefore become substantially smaller. In 2016 as well, the company ran a pilot project involving a skimmer solution for bilge tanks. This is an extra barrier intended to catch any emissions inside a power plant. The project will be evaluated in 2017, and if considered a success the solution will be installed at additional sites.

Skagerak Nett adopted an environmental strategy in 2016. Including dedicated environmental policies and goals, this has helped the company to improve its waste



A lot of rubbish can accumulate near the power plant intakes. Waste caught by screens and containment booms is collected up and transported to waste reception centres, where it is sorted. Several of the watercourses where Skagerak operates power plants drain directly in to the sea. By collecting up the plastic, we are making a small contribution towards preventing more plastic ending up in the ocean. The photo is from the Tinnelva river.

sorting and generally raised the whole workforce's level of environmental awareness. The company makes a holistic assessment with regard to upgrading and developing the distribution grid, and takes account of environmental and climate-related issues. This includes strengthening the grid, choosing optimal routes for power lines and replacing overhead cables with buried cables. One example is the project

"Network Reinforcement Grenland". When this project is completed early in 2017, it will have made a substantial contribution to improving the grid structure and increasing capacity. In addition, more than 50 km of overhead high-voltage cables and masts will have been removed from densely populated areas.

By 2020, Skagerak Nett aims to have installed oil separators or automatic oil meters at all the company's outdoor

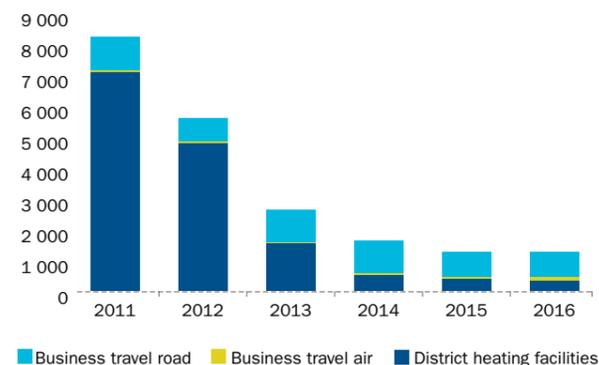
transformer pits. No other energy company in Norway uses surveillance systems for the environmentally safe emptying of rainwater from pits to such an extent. The system guarantees against oil discharges, and allows more effective maintenance.

Skagerak Varne aims to have eliminated all fossil fuels from its district heating production by 2020. In 2016, the company's carbon emissions totalled 231 tonnes, a reduction of 97 per cent since 2011. Renewable energy deliveries from Skagerak Varne's district heating facilities totalled 105 GWh in 2016. Although the heat production facilities also produce nitrous oxide (NO_x) and particulate emissions, Skagerak Varne's emissions are significantly lower than permitted levels. In 2016, the company's NO_x emissions were less than 120 mg/Nm₃, while the limit is 300 mg/Nm₃. Particulate emissions were less than

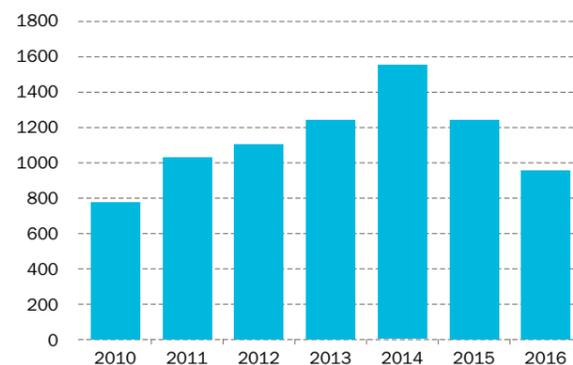
2 mg/Nm₃, compared with a limit of 75 mg/Nm₃.

Skagerak Naturgass contributes to the "green shift" by supplying biogas, which is used primarily to replace diesel in the transport sector. Biogas is a climate-neutral fuel made from organic household and agricultural waste. Use of biogas makes sure the resources contained in the waste are recycled. Compared with diesel, it also produces significantly lower greenhouse gas emissions and reduced emissions of nitrous oxide (NO_x), sulphur dioxide (SO₂) and particulates. In 2016, Skagerak Naturgass delivered around 30 GWh of biogas. The portion supplied to vehicles replaces some 2.6 million litres of diesel, cutting greenhouse gas emissions in the region by around 8,400 tonnes of CO₂.

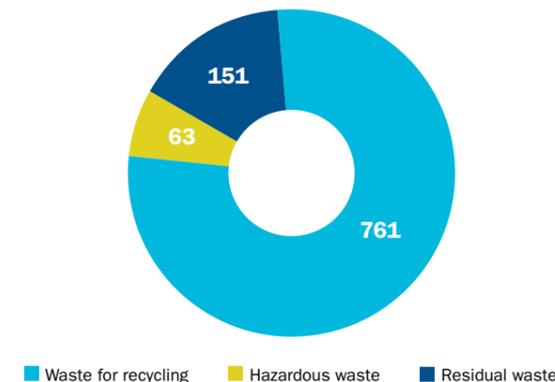
FOCUS ON LOWER CARBON EMISSIONS tonnes



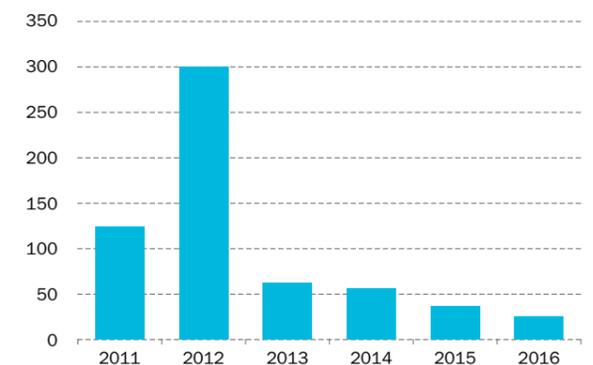
TOTAL VOLUME OF WASTE tonnes



WASTE SORTING tonnes



PHASING OUT OF OIL FOR DISTRICT HEATING tonnes



Board report and financial statements

- Underlying EBITDA totalled NOK 1,308 million, a 25% improvement on the year before.
- Sickness absence fell further to 3.1% (3.8 %) and the number of personal injuries was halved to four.
- The sale of biogas got underway in Tønsberg and Grenland, with a total of 30 GWh sold.

Annual report 2016 Skagerak Energi Group

THE BUSINESS

Skagerak Energi is a regional energy group headquartered in Porsgrunn. The business areas Power, Networks, Heat and Natural Gas undertake the bulk of its commercial activity. Skagerak Energi also owns 48% of Fjordkraft, which sells electricity to consumers, and 33.4% of the electrical installation company Laugstol (formerly Skagerak Elektro).

Skagerak Kraft produces hydropower in Southern Norway. Its 48 wholly or partly owned production facilities have generated an average of 5.7 TWh pa over the past 10 years. Skagerak Nett manages and develops regional and local power distribution grids in Vestfold and Telemark, and has around 190,000 customers. Skagerak Varme operates district heating facilities in Vestfold and Telemark. Skagerak Naturgass's business includes the sale and distribution of natural gas and biogas in Southern Norway. In the following, the figures for 2015 are given in parenthesis.

HIGHLIGHTS FROM 2016

- Profit after tax under IFRS totalled NOK 378 million (NOK 692 million).
- Corrected for unrealised gains on hedging contracts, the Group's underlying EBITDA came to NOK 1,308 million, a 25 per cent improvement on the year before.

- Electricity prices rose from 2015's record low, and Skagerak's achieved average price after hedging rose by 15 per cent.
- Operating costs fell in line with the Group's objectives and improvement plan.
- Fjordkraft's end-user business continued to deliver strong results.
- Receipt and distribution of biogas made extremely good progress in 2016, its first year of operation, with the establishment of biogas filling stations for buses and refuse collection vehicles in Grenland and Tønsberg.
- Sickness absence fell further to 3.1 per cent (3.8 per cent).
- There were four personal injuries (8).

MARKET CONDITIONS

A mild and dry winter and spring characterised the first half-year. Spot prices in Southern Norway remained generally stable through the whole period, with the exception of a brief spell in January, when lower than normal temperatures drove up prices.

Although the autumn began with stable prices, a number of coincidental events caused substantial fluctuations in the power market in the fourth quarter. After a record-dry October, Norway had a hydrological deficit of almost 20 TWh. During the same period, prices for coal, gas and CO₂ rose sharply, while uncertainty attached to nuclear

power production on the continent. This significantly boosted electricity prices in both the spot market and the financial market. The weather picture in the Nordic region reversed in December, from cold and dry to wet and mild, the price of coal and CO₂ peaked and started to fall, and concerns about nuclear power died down. This resulted in a fall in electricity prices which offset most of the rise earlier in the quarter. There were also major restrictions on the flow of electricity both within and in and out of Southern Norway since as far back as May. This resulted in bottlenecks and, periodically, substantial price differences between the price areas in Southern Norway and between Norway and Sweden.

In 2016 as a whole, precipitation in Norway was approx. 90 per cent of normal, while the average temperature was 0.4 degrees hotter than normal. The average spot price in Southern Norway (NO₂) was NOK 0.233/kWh (NOK 0.177/kWh). Power output in Norway was 12 per cent above mean, largely due to high reservoir water levels at the start of 2016.

THE GROUP'S EARNINGS AND FINANCIAL DEVELOPMENT

The Group generated gross operating revenues of NOK 2,489 million (NOK 2,381 million), up 5 per cent on the year before. The increase, which was moderated by the fact

Skagerak Energi's Board of Directors



Steinar Bysveen
Chair



Rolf Erling Andersen
Deputy Chair

that Laugstol was not consolidated in 2016, is attributable in particular to higher electricity prices and slightly higher network revenues. The average volume-weighted price, including realised gains on price hedging, was 15 per cent above the 2015 levels.

The Group made a net profit of NOK 378 million (NOK 692 million). The fact that the recognised result is NOK 314 million lower than in 2015 is due largely to unrealised changes in the value of financial power contracts.

The underlying EBITDA, corrected for unrealised changes in value, was NOK 1,308 million, up 25 per cent on the year before.

Operating costs continued to fall in line with the Group's objectives and improvement programme. Improvement efforts have been further reinforced at the start of 2017, with even greater involvement by the Group's workforce.

Revenues from associates totalled NOK 106 million (NOK 110 million), and remain very good. The high level of profitability achieved by Fjordkraft in the end-user business played an important role here.

The Group's net financial items came to NOK 189 million (NOK 68 million). The change is due primarily to the fact that the 2015 figure included the gain on the sale of Skagerak's shares in Småkraft.

The tax expense for 2016 is NOK 137 million lower than in 2015. This is largely due to the non-recurring impact of NOK 208 million in deferred tax assets relating to economic rent being taken to income.

Corrected for unrealised changes in the value of power contracts, as well as the non-recurring impact of the recognition of deferred tax assets, the underlying net profit came to NOK 342 million (NOK 264 million).

Investments in property, plant and equipment totalled NOK 660 million in 2016 (NOK 645 million). The bulk of the investments have been in Skagerak Nett (71 per cent) and Skagerak Kraft (16 per cent).

The Group's net cash flow from operating activities totalled NOK 986 million (NOK 602 million). This increase enabled the Group to finance all its investments from its current account and reduce net interest-bearing debt from NOK 5.0 billion to NOK 4.8 billion.

At the close of 2016, total capital stood at NOK 11.6 billion (NOK 11.9 billion) and the Group had an equity ratio of 42 per cent (39 per cent). The market value of the production facilities is significantly higher than their book value.

Going concern

The financial statements have been prepared on the assumption that the business is a going concern. The business is financially sound, has adequate liquidity and a market position which, based on existing forecasts, is expected to provide a good foundation for long-term value creation.

Net profit and allocation of funds

The Group's net profit for the year totalled NOK 378 million. The parent company, Skagerak Energi AS, made a net profit for the year of NOK 193 million. The board proposes that Skagerak Energi AS's AGM allocate the net profit for the year as follows:

To other equity: NOK 193 million

Total allocated: NOK 193 million

It is proposed that a dividend of NOK 114 million be paid for 2016. The board has assessed the company's equity and liquidity after the proposed dividend payment and considers that this is an appropriate level, given the business's scale and risk picture.

Following the close of the financial year, no circumstances have arisen that are of material significance for an assessment of the financial statements. The board is of the opinion that the year-end financial statements provide a true and fair picture of Skagerak Energi's assets and liabilities, financial position and results.

THE BUSINESS AREAS' EARNINGS, OPERATIONS AND DEVELOPMENT

Power production (Kraft)

Gross operating revenues from in-house production of electricity rose by 12 per cent to NOK 1,468 million in 2016, largely as a result of higher electricity prices.

Operating costs fell by 7 per cent. In 2015, operating costs were affected by the recognition of pre-project costs.

EBITDA corrected for unrealised changes in the value of power contracts totalled NOK 956 million (NOK 767 million). The business

has invested NOK 104 million (NOK 113 million) in property, plant and equipment.

Major projects Skagerak has worked on in 2016 include preparations for a new generator at Grunnål and a new control facility at Sundsbarm. Several of the partly owned plants are currently busy with the upgrading of dams and control facilities.

In 2016 as a whole, Skagerak produced a total of 5,993 GWh (6,071 GWh). Skagerak's output accounted for 4.0 per cent of Norway's total annual electricity production. At the start of 2017, the water level in Skagerak's reservoirs was slightly lower than normal.

Availability at the power plants has been extremely good in 2016.

The business involves considerable market risk with respect to both volume and price. The Group has clear guidelines for the sale of its own power output, and routines for optimising water consumption in relation to expected market prices.

The exploitation of waterfalls is strictly regulated by the Norwegian Water Resources and Energy Directorate (NVE) through its licensing terms. In coming years, many older licences will be revised. Skagerak Kraft is involved in six such revisions, and is busy preparing the relevant documentation and engaging in on-site inspections of the watercourses concerned along with the NVE.

The first period of the Water Directive has now come to a close. The action plans in each individual water region were discussed by the county councils at the end of 2015.

A final decision was made by the sectoral authorities in 2016 and forwarded to Brussels. However, although the decision means that the environmental goals were more moderate than many had initially assumed, it will still be the assessments made during the coming licence revisions that will determine whether there is any loss of output resulting from stricter requirements for minimum water flow and reservoir restrictions.

The NVE also manages the regulations for dam safety. A significant tightening up of the regulations has meant that many older dams must be modified at considerable cost.

Skagerak and its partly owned plants are well underway with the necessary upgrades. This activity will continue up until 2030.

New hydropower projects are actively being assessed and planned. However, the substantial fall in prices experienced in the energy markets has put profitability under increasing pressure. Electricity certificates, which were intended to provide a significant boost to the construction of new renewable energy facilities, have also had a low market price. There is growing uncertainty with respect to future certificate prices.

Tax is a significant cost element for hydropower, through property tax, licence fees, economic rent tax and ordinary corporation tax. Despite low power prices, more economic rent tax was paid in 2016 due to a reduction in the tax-free allowance.

Skagerak also sells certificates of origin. This is a market that is expected to grow as more and more attention is paid to climate issues.

Power distribution (Nett)

The power distribution business generated gross revenues of NOK 855 million (NOK 806 million). Operating costs were NOK 16 million higher in 2016, largely as a result of higher depreciation. In accordance with IFRS, EBITDA came to NOK 396 million (NOK 344 million).

In 2016, NOK 276 million less than the permitted earnings ceiling was billed. This led to a reduction in the accumulated surplus revenue balance with respect to customers.

A total of NOK 470 million was invested in 2016 (NOK 471 million). The networks business's capital base (NVE capital) at the

close of 2016 came to NOK 3,405 million. This is an increase compared with the year before. The NVE capital constitutes the basis for return, which, according to the NVE's income regulation model, is calculated using a reference rate. In both 2015 and 2016, the reference rate was set at 6.32 per cent.

The operational situation was normal through the year, apart from an extremely demanding situation caused by a massive snowfall on 5–6 November. Over the course of a day and a half, upwards of 70 mm precipitation fell in the form of wet snow that blanketed trees and power lines in the supply area. The conditions led to many and lengthy power outages for a large number of end-user customers.

The power distribution business is regulated by the NVE, which imposes a wide range of requirements relating to activities, technical infrastructure, organisation and competence. The business's earnings are determined by the NVE in accordance with a model that rewards efficiency compared with other grid companies. Skagerak Nett is working constantly to reduce its costs and improve the efficiency of its operations.

Skagerak Nett supplied 7,045 GWh in 2016 (6,997 GWh), and had 190,496 network customers at the close of the year.

District heating (Varme)

The district heating business generated net operating revenues of NOK 76 million (NOK 62 million), up 23 per cent on the year before. In 2016, the company achieved good growth

in its sales volume, which ended the year at 114 GWh (88 GWh). Halfway through the year, the subsidiary Skien Fjernvarme (51 per cent) was integrated into Skagerak Varme to form a single organisation under joint management. This led to a reduction in overall payroll costs for the business. EBITDA for the year came to NOK 10 million (NOK 2 million).

The business focused on customer-related activities in 2016, with the aim of increasing volume sales through profitable investment projects. A total of NOK 49 million was invested in 2016 (NOK 39 million), of which NOK 12 million (NOK 14 million) was financed via Enova.

Efforts were made to optimise the waste-water, bioenergy and heat-pump facilities, as well as the overall management of the various heat sources. 95 per cent of the energy used was renewable. In Horten, construction of a 7 GWh new renewable heat system for the Karljohansvern area was completed, with the connection of customers as planned. In Porsgrunn, the company has signed agreements giving greater access to waste heat from Yara, and the connection of the Herøya Industrial Park as a customer. As a result, Skagerak Varme will expand its delivered volume by 1,618 GWh in Porsgrunn. The number of customers in other towns where the company has a licence to operate also increased, enabling it to achieve a more effective utilisation of its facilities and a lower production cost per kWh.

The company is continuing its efforts to increase its customer base in all



Ida Helliesen
Director



Arvid Wisløff
Director



Kristin Steinfeldt-Foss
Director

licensed areas, with particular emphasis on increasing the density of take-up in the existing district heating network.

Natural gas (Naturgass)

Skagerak Naturgass boosted its operating revenues by 7 per cent to NOK 106 million in 2016 (NOK 99 million). The improvement is largely attributable to strong growth in the biogas segment. The volume of natural gas (LNG) sold fell due to low prices on competing products such as electricity and LPG.

The total sales volume came to 16,879 tonnes, the equivalent of 231 GWh, an increase of 5 per cent on the year before. Biogas sales totalled 30 GWh.

EBITDA totalled NOK 14.2 million (NOK 6.5 million). The increase is largely attributable to sales of biogas. The focus on biogas also led to a rise in payroll and operating costs.

The business invested NOK 34 million in 2016 (NOK 18 million). The establishment of biogas filling stations for buses and refuse collection vehicles in Grenland and Tønsberg accounted for a large part of this amount. The focus on biogas continues in 2017, with investments in a filling station for buses in Moss.

Associates

At the close of 2016, Skagerak Energi had shares in Laugstol AS (formerly Skagerak Elektro) (33.4 per cent), Fjordkraft AS (48 per cent), Nape Kraft AS (49 per cent), Steinsvik Kraft AS (20 per cent), Energi og Miljøkapital AS (35 per cent) and Viking Varme AS (50 per cent). In its consolidated financial statements, Skagerak Energi has recognised a combined total of NOK 106 million (NOK 110 million) as its share of the profit/loss from these shareholdings, whose book value in the Group's balance sheet is NOK 164 million.

ORGANISATION AND HSE

Human resources and organisation

Skagerak Energi is organised as a group comprising four business areas and a parent company which, in addition to exercising its role as owner, performs corporate and shared support functions for the business areas.

At the close of 2016, the Group had 610 employees, corresponding to 579 full-time

ORGANISATION

Company	31.12.2016		31.12.2015	
	No. employees	FTE	No. employees	FTE
Skagerak Nett	373	354	376	358
Skagerak Kraft	123	115	116	108
Parent company	91	87	102	97
Skagerak Varme	15	15	15	15
Skien Fjernvarme	1	1	2	2
Skagerak Naturgass	7	7	6	6
Total	610	579	617	586

equivalents (FTE). This is a 1 per cent decrease in the headcount since the previous year.

Skagerak Energi is working systematically to retain and develop the skilled employees it requires to meet its future needs, and implements a variety of measures in the area of employee and management development.

In 2016, the Group's employment and management policies have been revised on the basis of its core values, and work to implement these principles has been given a high priority.

Both the board of directors and the organisation as a whole pay particular attention to ethical behaviour and the Group's code of conduct in order to maintain a high ethical standard through compliance with the governing documents in this area.

To accommodate employees at various phases in their lives, flexitime is offered, so that staff can tailor their working hours to their own situations. The Group places particular emphasis on work adaptations for staff with health issues, one of several important reasons for the steady fall in sickness absence.

Work experience places have also been made available to non-employees who need workplace training or the opportunity to test their capacity for work. In 2016, the Group hosted two trainees in cooperation with Trainee Telemark.

Health and safety

The Group's overall sickness absence rate came to 3.1 per cent (3.8 per cent including Laugstol). Through preventive HSE activities, the Skagerak Group has managed to stabilise its overall sickness absence rate at

under 4 per cent and its short-term absence to a fraction over 1 per cent.

The Group's objective is for no one to suffer injury or work-related illness because of its operations. In 2016, there were four personal injuries, all resulting in lost time. In 2015, there were 8 personal injuries, including Laugstol. This gave H1 and H2 values of 4.2 (H1 equals the total number of lost time injuries per million hours worked, while H2 equals the total number of injuries per million hours worked).

To avoid personal injuries and serious incidents, managers and employees must have a good understanding of risk and how assignments and projects can be performed safely and efficiently. Working methods, equipment, understanding of risk and attitudes must constantly be improved, and all group companies are actively engaged in preventive HSE initiatives involving managers and staff. The most important tools with regard to preventive measures are the performance of risk assessments, dealing with reported incidents and hazardous conditions, and observations of behaviours and attitudes in practice. A large number of behaviour-based on-site safety observation rounds are conducted, and serious incidents and near misses are investigated. Safety training is carried out annually, while other HSE courses are staged as required. The board will continue to pay close attention to the Group's injury prevention and HSE awareness efforts.

Equality

The Group is keen to offer equal opportunities for employment, competence development, promotion and other employment terms irrespective of gender or

social, ethnic or cultural background.

In 2016, 17 of the Group's 69 managers were women, which constitutes 25 per cent (22 per cent). The Group's board of directors comprises 9 members, of whom 4 are women: 2 shareholder-elected and 2 employee-elected.

Environment

Skagerak Energi's products make up part of the "Green Shift". Its core business, the production and distribution of energy from renewable sources, contributes to a society with fewer greenhouse emissions.

The Group's corporate social responsibility is to safeguard the supply of energy to people's daily lives and those functions that are critical for society. Developments in society are increasing people's dependence on electrical power, and electricity consumption is rising. At the same time, technology developments and global climate change are opening a wider range of opportunities when choosing solutions.

Skagerak Energi's ability to deal successfully with this situation depends on it having a high level of expertise and good working methods, with high standards for operation, maintenance and expansion. The Group's overarching goal is that all expansion and operations will comply with the principle of sustainable development, and will have as little as possible impact on the environment.

Technical solutions, inspections and maintenance of all facilities will prevent

the discharge of polluting chemicals and other hazardous substances into their surroundings. Good routines for the sorting and treatment of waste, at both fixed locations and temporary building sites, contribute to the recycling of resources.

Skagerak Kraft has maintained its ISO 14001 environmental certification. Sound management of its watercourses is intended to safeguard effective operations and value creation. This helps to protect communities through anti-flooding measures in connection with periods of substantial precipitation. This is particularly important at a time when extreme weather is becoming a more frequent occurrence. No non-conformances relating to the regulation of watercourses occurred in 2016. Skagerak Kraft actively participates in and helps finance other environmental and climate-related research projects initiated by the Norwegian Water Resources and Energy Directorate (NVE) and the Norwegian Environment Agency, which are carried out by well-reputed institutions, such as SINTEF, the Norwegian University of Science and Technology (NTNU), the Norwegian Institute for Nature Research (NINA) and the University College of Southeast Norway. In addition, the company is engaged in several smaller local surveys to learn more about completed and potential measures to safeguard biodiversity.

Skagerak Nett is constantly developing the power distribution network in ways that both safeguard supplies of electricity and cause as little inconvenience as

possible to the local environment and society at large. The company has devoted considerable resources to increasing its level of competence in order to understand future requirements and technological opportunities.

Through its development work, the company aims to gain insight into tomorrow's "smarter" solutions and use of the power grid, as well as its interaction with local production and storage. The company is in the process of concluding the major project "Network Reinforcement Grenland", which has led to a better network structure and higher capacity, as well as the dismantling of 50 km of high-voltage power lines and masts in built-up and recreational areas in the region. In addition, another major project is underway to build a new switching station to supply the new double-track railway line between Porsgrunn and Larvik, in accordance with its scheduled completion in early 2018.

Skagerak Varme aims to achieve fossil-free heat production at all its facilities by 2020. The company's CO₂ emissions totalled 231 tonnes in 2016, a reduction of 97 per cent since 2011. Skagerak Varme's renewable energy meant that total carbon emissions to the environment in 2016 were around 35,000 tonnes less than the equivalent heat production based on oil-fired boilers. This corresponds to the emissions from more than 20,000 private cars.

Skagerak Naturgass contributes to the "green shift" by supplying biogas, so that the



Line Klausen
Director



Gunnar Møane
Director



Kjersti Haugen
Director

transport industry in particular can replace diesel with biogas. Biogas is a climate-neutral fuel made from organic household and agricultural waste. This ensures that resources in the waste are recycled and contributes to a substantial reduction in local pollution from nitrous oxides (NO_x), sulphur dioxide (SO₂) and particulates (dust).

In 2015, the company started supplying biogas to buses and refuse collection vehicles in Grenland and Vestfold. In 2016, Skagerak Naturgass supplied enough biogas to replace approx. 2.6 million litres of diesel. As a result, greenhouse gas emissions in the region were cut by more than 8,400 tonnes of CO₂. It is Skagerak Naturgass's long-term ambition to increase its deliveries at the same rate as developments in the biogas market. The biogas comes primarily from the Greve plant in Tønsberg, but there are also a number of other sources in Norway which could potentially increase the reduction in greenhouse gas emissions many times over.

CORPORATE GOVERNANCE AND RISK

Skagerak Energi has a corporate governance system that includes governing documents which specify both what the business is to do and how it should do it. The system encompasses corporate governance, risk management, internal control, authorisations, principles and guidelines for the Group's business units; the Group's strategy, action plans and a balanced scorecard for the strategy's implementation

and follow-up.

Skagerak does not tolerate corruption in any form. The offering, giving, acceptance or receipt of bribes or other unwarranted benefits for private gain or corporate advantage is completely prohibited.

Skagerak actively communicates its requirements and the conduct it expects in the Group's governing documents.

Particular vigilance is exercised in connection with procurement and the undertaking of projects. All agreements entered into must be documented and must describe actual conditions. The agreed consideration must also be proportional to the services performed.

Skagerak Energi's businesses are exposed to risk in a number of areas and along the entire value chain. Risk management is an integral part of the Group's business operations, and is designed to maintain risk at an acceptable level in order to ensure the achievement of strategic and operational goals. The individual business areas are responsible for risk management and internal control.

Market risk

Skagerak Energi is exposed to market risk largely through its own production of electricity and its power distribution business. In a hydropower-based system, prices and production capacity will fluctuate substantially, and this can have a major impact on Skagerak Energi's financial results. Given the major investments and

considerable uncertainty with respect to power prices moving forward, a portion of power sales have been hedged up until the end of 2018. In addition, there will normally be a certain balancing out of revenues, in that substantial inflows of water and high output come in years with low prices and vice versa. Skagerak Varme and Skagerak Naturgass are exposed to raw materials prices, electricity prices and competing energy solutions.

Regulatory risk

The Group's energy supply activities are subject to licensing requirements and a large degree of public regulation. This applies particularly to the electricity production (Kraft), power distribution (Nett) and district heating (Varme) business areas. The power distribution business is a natural monopoly whose earnings are publicly regulated. Skagerak Nett's earnings framework is determined each year by the NVE, and is affected by changes in the regulation model.

FINANCIAL RISK

Interest and exchange rate risk

Skagerak is indirectly exposed to changes in exchange rates. Generated electricity is sold on the power exchange Nord Pool, where prices are noted in EUR, while settlement is offered in either EUR or NOK. Skagerak has elected to receive

payment in NOK. The Group operates a capital-intensive business and is, with a normal gearing level in relation to its assets, substantially exposed to changes in market rates of interest. Around 75 per cent of the Group's total long-term interest-bearing debt is at fixed interest rates. Furthermore, the Group is exposed to interest rate risk through the rate of interest's impact on the power distribution business's earnings framework, as well as the tax-exempt dividend's effect on the calculation of economic rent tax within the power production segment.

Credit risk

Credit risk in connection with the sale of electricity relates to counterparty risk in respect of Nord Pool. This is considered low. Credit risk associated with power distribution operations is spread across many small counterparties, with good opportunities to limit any losses.

Liquidity risk

The Group has liquid reserves deriving from drawdown agreements with Statkraft. The Group's liquidity risk is considered low.

Operational risk

Skagerak manages its operational risk through its workforce's expertise, operating procedures, controls and emergency

response plans.

A material part of the business encompasses infrastructures that are critical for society in that they help meet the population's fundamental needs. Security of supply is therefore a crucial aspect of Skagerak's planning and operations. Risk relating to security of supply is also part of the overall risk picture at group level, which is subject to assessment by the board of directors.

The Group has set up a system for the registration and reporting of irregularities, unwanted incidents and injuries. All of Skagerak's projects perform risk analyses in order to assess and plan any appropriate measures required.

OUTLOOK

The electricity market improved slightly in 2016, compared with the low point seen in 2015. However, considerable uncertainty attaches to developments moving forward. In the next few years, electricity prices are expected to remain at a relatively low level as a result of the expansion of renewable energy facilities, and thereby output, in the Nordic region and on the continent. At the same time, demand is not expected to change significantly. Nevertheless, as long as power transmission capacity remains limited, major fluctuations in Norwegian prices

may be expected due to weather conditions and precipitation levels in some years. Both Statnett and the NVE have published several analyses indicating higher prices after 2020, largely underpinned by expectations of higher carbon quota prices, increased export capacity to the continent and the UK, as well as the phasing out of nuclear power. The future of electricity certificate prices is also extremely uncertain.

The earnings framework for the power distribution business will continue to rise as a result of substantial investments.

Efforts will continue to be made to expand the sale and distribution of biogas to new customer groups, in a market with interesting development opportunities.

The Group's F20 improvement programme will encourage all employees to redouble their efforts to realise the potential for increased efficiency and improved profitability. A shared structure and methodology in these efforts will increase cooperation and the sharing of knowledge across the Group.

The work of restructuring continues, and Skagerak will seek to exploit opportunities with other companies in order to further promote development and synergies at a time when the power sector expects increased consolidation.

Porsgrunn 21 March 2017
The Board of Directors



Øystein K. Beyer
Director



Knut Barland
CEO

Steinar Bysveen

Steinar Bysveen
Chair

Rolf Erling Andersen

Rolf Erling Andersen
Deputy Chair

Kristin Steinfeldt-Foss

Kristin Steinfeldt-Foss
Director

Arvid Wisløff

Arvid Wisløff
Director

Øystein Kåre Beyer

Øystein Kåre Beyer
Director

Ida Helliess

Ida Helliess
Director

Gunnar Møane

Gunnar Møane
Director

Kjersti Haugen

Kjersti Haugen
Director

Line Klausen

Line Klausen
Director

Knut Barland

Knut Barland
CEO

Income Statement

(All figures in NOK 1,000)

SKAGERAK ENERGI GROUP			SKAGERAK ENERGI AS		
2016	2015	Note	2016	2015	
OPERATING REVENUES					
1 290 608	1 158 051	3, 4	0	0	Power sales revenues
924 665	841 544	5	0	0	Power distribution revenues
273 830	381 124	6, 28	123 657	139 361	Other operating revenues
2 489 102	2 380 719		123 657	139 361	GROSS OPERATING REVENUES
87 645	85 390		0	0	Transmission costs
-229 694	358 475		0	0	Unrealised changes in value of energy contracts
2 171 762	2 653 803		123 657	139 361	NET OPERATING REVENUES
432 987	507 679	7, 20, 28	97 389	109 319	Salary & payroll costs
132 756	136 894	8	0	0	Property tax & licence fees
527 605	603 849	9, 28	94 956	102 399	Other operating expenses
1 078 414	1 405 382		-68 689	-72 357	EBITDA
510 360	511 227	12, 13	15 078	14 703	Depreciation & impairment
568 054	894 155		-83 767	-87 060	EBIT
106 350	109 857	14	358 624	1 828 658	SHARE OF PROFIT/LOSS FROM SUBSIDIARIES & ASSOCIATES
FINANCIAL ITEMS					
27 179	139 179	10, 28	163 129	115 656	Financial income
204 376	207 336	10, 28	186 856	204 551	Financial expenses
-11 316	306	10	-11 316	306	Unrealised changes in value of interest/currency contracts
-188 513	-67 851		-35 043	-88 589	NET FINANCIAL ITEMS
485 891	936 161		239 814	1 653 009	PROFIT/LOSS BEFORE TAX
107 789	244 392	11	46 876	80 045	Tax expense
378 102	691 769		192 938	1 572 965	NET PROFIT/LOSS
NET PROFIT/LOSS ALLOCATED TO					
-2 292	-3 205				Non-controlling interests
380 394	694 974				Controlling interests
SPECIFICATION OF:					
			88 000	65 000	Dividend paid

Statement of Comprehensive Income

(All figures in NOK 1,000)

SKAGERAK ENERGI GROUP			SKAGERAK ENERGI AS		
2016	2015	Note	2016	2015	
378 102	691 769	19	192 938	1 572 965	NET PROFIT/LOSS
OTHER COMPREHENSIVE INCOME					
ITEMS IN OTHER COMPREHENSIVE INCOME THAT WILL NOT RECYCLE OVER PROFIT/LOSS:					
13 450	336 550		20 459	104 859	Actuarial gains/losses on defined-benefit pension plans
-6 445	836		0	0	Items recognised in associates
-10 752	-119 044		-6 793	-32 077	Tax relating to <i>Other Comprehensive Income</i>
-3 748	218 341	19	13 666	72 781	OTHER COMPREHENSIVE INCOME
374 355	910 110		206 604	1 645 746	TOTAL COMPREHENSIVE INCOME
TOTAL COMPREHENSIVE INCOME ALLOCATED TO					
-1 397	-2 894				Non-controlling interests
375 751	913 004				Controlling interests

Balance Sheet

(All figures in NOK 1,000)

SKAGERAK ENERGI GROUP			SKAGERAK ENERGI AS	
31.12.2016	31.12.2015	Note	31.12.2016	31.12.2015
ASSETS				
NON-CURRENT ASSETS				
378 974	304 586		40 089	48 206
10 125 892	9 983 738	11, 12	171 330	170 626
163 459	149 645	13	5 036 915	5 046 207
33 407	136 493	14	0	0
356 835	300 809	25	5 856 588	6 171 938
		15, 28		
11 058 568	10 875 272		11 104 922	11 436 977
CURRENT ASSETS				
2 904	6 061		0	0
325 426	295 508		20 116	26 728
5 081	16 397	16, 28	5 081	16 397
0	112 401	17	0	0
207 091	639 900	25	14 234	14 202
		18		
540 501	1 070 267		39 431	57 326
11 599 069	11 945 538		11 144 353	11 494 304

Balance Sheet

(All figures in NOK 1,000)

SKAGERAK ENERGI GROUP			SKAGERAK ENERGI AS	
31.12.2016	31.12.2015	Note	31.12.2016	31.12.2015
EQUITY AND LIABILITIES				
EQUITY				
1 695 539	1 695 539		1 695 539	1 695 539
399 211	399 211	19	399 211	399 211
2 094 750	2 094 750		2 094 750	2 094 750
PAID-IN EQUITY				
2 765 922	2 478 171		3 602 821	3 484 217
2 765 922	2 478 171	19	3 602 821	3 484 217
RETAINED EARNINGS				
28 495	29 892		0	0
4 889 167	4 602 813	19	5 697 571	5 578 967
LIABILITIES				
551 891	718 418		48 747	51 408
5 281	25 692	11, 20	0	0
4 581 500	4 469 975	25	4 375 000	4 350 000
5 138 672	5 214 085	21, 24, 28	4 423 747	4 401 408
NON-CURRENT LIABILITIES				
408 800	1 200 000		754 776	1 266 794
465 802	360 742	22, 28	177 606	166 530
38 198	3 580	11	0	0
658 429	564 318	25	90 653	80 605
1 571 229	2 128 640	23, 28	1 023 035	1 513 929
CURRENT LIABILITIES				
6 709 901	7 342 726		5 446 782	5 915 337
11 599 069	11 945 538		11 144 353	11 494 304

Porsgrunn 21 March 2017
The Board of Directors


 Steinar Bysveen
 Chair


 Rolf Erling Andersen
 Deputy Chair


 Kristin Steinfeldt-Foss
 Director


 Arvid Wisløff
 Director


 Øystein Kåre Beyer
 Director


 Ida Helliessen
 Director


 Gunnar Møane
 Director


 Kjersti Haugen
 Director


 Line Klausen
 Director


 Knut Barland
 CEO

Statement of Cash Flow

(All figures in NOK 1,000)

SKAGERAK ENERGI GROUP			SKAGERAK ENERGI AS	
2016	2015		2016	2015
		CASH FLOW FROM OPERATING ACTIVITIES		
485 891	936 161	Profit/loss before tax	239 814	1 653 009
5 383	-114 085	Gains(-)/losses on sale of non-current assets	3 197	6 026
510 360	511 227	Depreciation & impairment	15 078	14 703
241 010	-358 792	Other items with no cash flow effect	11 316	-1 244 847
-229 210	-311 462	Tax paid	-34 475	-70 161
1 013 435	663 049	NET CASH FLOW FROM THE YEAR'S OPERATIONS	234 930	358 731
		CASH FLOW FROM INVESTING ACTIVITIES		
67 351	7 029	Change in inventory, receivables & payables	16 661	-8 264
79 993	57 834	Dividend from associates	79 993	0
-106 350	-109 857	Share of profit/loss from associates	-75 093	0
-68 808	-16 263	Change in other non-current items	332 102	-4 001
985 620	601 792	NET CASH FLOW FROM OPERATING ACTIVITIES	588 593	346 466
		CASH FLOW FROM INVESTING ACTIVITIES		
		Investments in property, plant & equipment:		
-272 992	-280 941	- linked to increased capacity	0	0
-387 089	-364 168	- linked to reinvestments	-16 128	-17 840
1 316	3 958	Sale of property, plant & equipment (sales price)	377	2 699
25	118 116	Payment of loans to other companies	25	25
7 986	346 688	Net receipts/payments re. investments in other companies	2 184	59 726
-650 754	-176 347	NET CASH FLOW FROM INVESTING ACTIVITIES	-13 542	44 610
		CASH FLOW FROM FINANCING ACTIVITIES		
0	7 253	New long-term borrowings	0	0
-679 675	0	Change in short-term/long-term debt	-487 018	-163 870
-88 000	-65 000	Dividend paid	-88 000	-65 000
0	0	Change in non-current receivables and liabilities	0	-154 000
-767 675	-57 747	NET CASH FLOW FROM FINANCING ACTIVITIES	-575 018	-382 870
-432 809	367 698	Net change in cash & cash equivalents	32	8 206
639 900	306 012	Cash & cash equivalents as at 1 Jan	14 202	5 996
0	-33 810	Withdrawal of cash re. disposals	0	0
207 091	639 900	CASH & CASH EQUIVALENTS AS AT 31 DEC	14 234	14 202



**Skagerak
Energi**