# Report from the Board of Directors

In 2012 Hafslund concentrated on further developing its position as a leading energy group, with a primary focus on the core areas of production, networks, heat and markets. The Group is generating organic growth within its core operations, but is also pursuing structural growth. While underlying operations in 2012 were sound, the year was strongly influenced by low power prices and extraordinary write-downs and provisions for some investments in the company's non-core areas.

Hafslund's strategy is to continue to further develop the four core areas of production, heat, networks and markets. Hafslund is well positioned in all its business areas, with a main geographic focus in and around Oslo. The company's power plants are concentrated in lower Glomma. Hafslund Nett is the largest and one of the most efficient grid operators in Norway. Hafslund owns and operates the country's largest district heating network. The Group's power sales business is the largest in Norway, and the Group aims to be a key player in the Nordic region.

Achieving profitable growth in the core areas necessitates a strong operational focus on continual improvement, efficient processes and cost control. Hafslund is continuing its improvement measures in order to be able to utilize the company's competitive advantages even more effectively.

The result for 2012 was strongly impacted by extraordinary write-downs and provisions due to challenging market conditions, and losses at BioWood Norway AS and the Bio-El Fredrikstad waste-to-energy plant, along with a provision for an ongoing tax dispute. In 2012 lower power prices particularly impacted the results from Production and Heat. The achieved power price of 22øre/kWh was 31 percent lower than in 2011, and 44 percent lower than in 2010. After a period in which nearly all produced power was sold in the spot market, Hafslund has altered its strategy to partial price-hedging of expected power production. This change has been made in order to be able to leverage market opportunities more efficiently and to secure earnings and cash flow, in particular in periods of low prices. Hafslund also wishes to reduce its results-related downside risk for Heat, and has decided to price-hedge parts of its sales volume.

The loss after tax for 2012 was NOK 52 million and includes extraordinary write-downs and provisions totalling NOK 586 million. At the end of 2012 total assets amounted to NOK 24.8 billion, and the equity ratio was 31 percent. The Group has a robust financing structure with long-term committed drawdown facilities.

On 21 November the board of BioWood Norway AS decided to cease pellets production at Averøya. Overcapacity and low prices in the pellets market, together with technical challenges at the plant had contributed to the plant running at a loss. The board considered potential options, but could find no long-term basis for profitable operations. The business was closed at the turn of the month February/March.

On 21 March 2012 Finn Bjørn Ruyter took up his position as CEO of Hafslund, having previously served as Acting CEO since 6 January 2012. Ruyter joined Hafslund in 2010, as CFO. He has more than 20 years of experience from the Norwegian energy and power sector.

## Finance

### Result for the year

The Hafslund Group posted sales revenues of NOK 11.5 billion in 2012 (NOK 13.7 billion). The decrease in sales revenues should be viewed in the context of lower power prices. The operating profit for the year came in at NOK 854 million, which represents a year-on-year rise of NOK 511 million. The Group's underlying operational performance was sound. The operating profit includes a charge of NOK 560 million in extraordinary write-downs and provisions as a result of challenging market conditions and losses at BioWood Norway AS and the Bio-El Fredrikstad bioenergy plant. The achieved power price of 22 øre/kWh in 2012 was 10 øre/kWh lower than in 2011, and contributed to a reduced profit for the Production and Heat business areas. The improvement in the operating result compared with the previous year is also partly attributable to the fact that the result for 2011 included a write-down of the former shareholding in REC in the amount of NOK 1,090 million. The return on capital employed in the period was 4.1 percent (1.5 percent).

Financial expenses for the year amounted to NOK 557 million (NOK 584 million). This includes a charge of NOK 48 million (NOK 89 million) due to a rise in the market value of the loan portfolio, which is recognised at fair value as a result of lower interest rates. At 4.0 percent, at the end of 2012 the loan portfolio's coupon rate was down 0.5 percentage points on the previous year. The tax expense of NOK 349 million includes resource rent tax of NOK 111 million (NOK 200 million) relating to power production, and a provision of NOK 183 million in respect of an ongoing tax dispute.
The consolidated net loss for the year of NOK 52 million equates to an earnings per share figure of NOK -0.27 (NOK -3.58).

The board confirms that the company satisfies the conditions to continue as a going Group, and that the 2012 annual financial statements have been prepared on this basis.

## Cash flow and capital

The Group's cash flow from operations before changes in working capital was NOK 1,184 million (NOK 1,254 million). Working capital was NOK 587 million at the end of 2012, an increase of NOK 835 million during the year. The increase in working capital is attributable to particularly low working capital at the end of 2011, as a result of low power prices and low power consumption due to the mild weather towards the end of 2011. This resulted in a net cash flow from operations of NOK 236 million in 2012.

The operating profit before depreciation and amortisation of NOK 2,113 million was NOK 929 million higher than the net cash flow from operations before changes in working capital. The difference is attributable to payment of interest and tax of NOK 839 million, and result effects of non-cash items in the amount of NOK 90 million relating to items including market value changes of shares and derivatives.

Total investments in operations and expansions in 2012 amounted to NOK 1,084 million (NOK 1,176 million), of which NOK 497 million related to networks and NOK 326 million to district heating. Future investments will primarily relate to ongoing reinvestments in the networks business, the gradual phasing-in of AMS and further development of the district heating business in Oslo.

In 2012 a dividend of NOK 2.50 (NOK 2.50) per share was paid, corresponding to NOK 487 million in total. The above resulted in a cash outflow of NOK 1,299 million for 2012, which in turn increased net interest-bearing liabilities to NOK 10.6 billion at the end of 2012.

The Group has a robust financing structure with long-term committed drawdown facilities. At the end of 2012 Hafslund had unused drawdown facilities of NOK 3.9 billion. None of Hafslund's loan agreements impose any covenants.

## The business areas

Hafslund is a leading energy group and one of the few energy groups in the Nordic region to be publicly listed. The company has produced clean hydropower since 1898, and is now focusing on renewable energy production to meet tomorrow's energy requirements. Hafslund is Norway's largest power grid owner and largest power sales company and a major producer of renewable energy. The Group's core business comprises the business areas Production, Heat, Networks and Markets. Operations mainly take place in Norway and Sweden, and the Group is headquartered in Oslo.

### Production

The Production business area comprises hydropower production, which has a normal annual production of 3,100 GWh, and a central power trading unit. Production is responsible for ensuring outstanding management of the plants in Glomma, and pursuing growth within renewable energy production. The business area posted sales revenues of NOK 755 million (NOK 1,024 million) and an operating profit of NOK 442 million in 2012 (NOK 724 million). At the reporting date the Production business area had capital employed of NOK 4.8 billion.

In 2012 the Production business posted sales revenues of NOK 722 million, which were down 28 percent on 2011. The lower sales are primarily attributable to a 31 percent drop in achieved power prices in 2012 against 2011, despite a positive contribution from higher production. The operating profit of NOK 435 million (NOK 743 million) reflects an achieved power price of  22 øre/kWh (32 øre/kWh) and a production volume of 3,273 GWh (3,135 GWh). Despite gradually rising levels of price-hedging, hydropower production's results will to a large extent be driven by day-to-day fluctuations in the price of electricity. At 3,273 GWh, power production for the year was around six percent higher than normal production.

The year was impacted by production downtime as a result of faults at two of the company's largest generators in the summer floods, involving a total water loss of just under 200 GWh. A final insurance settlement for the above is expected in 2013.

In the year under review Production established routines for rolling advance sales of expected power production. The total gain on hedging recognised in the income statement amounted to NOK 37 million, and is reflected in a higher achieved power price compared with the (volume-weighted) spot price for the year. As of 31 December 2012 the hedged volume for the next six months equated to 39 percent of normal production.

The Group's central power trading unit is responsible for trading on the spot market and in el certificates, financial hedging and power trading. The power trading business posted an operating profit of NOK 7 million (loss of NOK 19 million) in the year under review.

### Heat

The Heat business area is responsible for district heating activities in Oslo and Akershus, and the production of heat and steam to industry in Østfold. Sales revenues for the district heating business totalled NOK 1,107 million (NOK 1,120 million). An operating profit before depreciation and amortisation of NOK 312 million represents an increase of 20 percent against 2011. The operating loss came in at NOK 83 million (profit of NOK 102 million). The operating loss reflects a contribution per volume sold of 28 øre/kWh, an increase of 1 øre/kWh against 2011. A higher percentage of renewable energy sources and cheaper peak loads are pushing up the contribution margins despite lower power prices compared with 2011. The total energy supply of 1,994 GWh represents an increase of 166 GWh against the previous year. The total contribution margin amounted to NOK 597 million (NOK 522 million). The operating loss also reflects an extraordinary write-down relating to the waste-to-energy plant Bio-El Fredrikstad in the amount of NOK 240 million. The plant's profitability has been strongly impacted by waste prices, which represent the facility's revenues. Waste prices fell further in 2012 with few signs of an imminent recovery. The decrease in waste prices is attributable to overcapacity caused by significant new capacity in both Norway and Sweden. The Heat business area had capital employed of NOK 5.6 billion at the end of 2012.

In 2012 the share of electricity and renewable energy sources used in district heating rose to 93 percent, a rise of 9 percentage points against 2011. The increase is attributable to a higher percentage of waste used as the base load delivered by the City of Oslo's Waste-to-Energy Agency (EGE) at Klemetsrud. The percentage of renewable heat will increase further with the commissioning of the new pellets boiler at Haraldrud heating plant, and a new peak load centre at Rodeløkka. Both plants are due to enter ordinary operations in the first quarter of 2013.

In 2012 investments in Heat totalled NOK 326 million, compared with NOK 463 million in 2011. The investments primarily relate to increased renewable production capacity for the district heating business in Oslo, and organic growth in customer connections. The waste-to-energy plants at Borregaard industrial area in Sarpsborg and Bio-El Fredrikstad were in operation throughout the year. Both plants' performance was affected by a challenging waste market.

Overall operations in 2012 were sound, with the exception of two incidents. On 28 November there was a leak in the district heating pipe in Ljabruveien at Bjørndalen due to rust. Around 1,000 district heating customers were affected. The repair work was completed on Friday morning of 30 November, and supply of district heating to the area was resumed shortly afterwards.

On Wednesday 19 December there was a leak when refilling heating oil at Hafslund's heating plant inside the hospital grounds at Ullevål. Around 19 m3 of heating oil leaked out from the plant and into the public sewage system, some of which reached Akerselva.

Hafslund regards both incidents as extremely serious, and implementation of measures to prevent similar incidents in the future have been accorded high priority.

### Networks

The Networks business unit comprises the companies Hafslund Nett AS and Hafslund Driftssentral AS. Hafslund Nett is Norway's largest grid company. In the year under review operating revenues for the Networks business totalled NOK 3,992 million (NOK 4,202 million). The operating profit before depreciation and amortisation amounted to NOK 1,019 million (NOK 983 million), an increase of 4 per cent from 2011. This reflects a regulated contribution of NOK 1,926 million (NOK 1,916 million) and an income surplus of NOK 268 million (NOK 212 million). At the end of 2012 Networks had capital employed of NOK 9.2 billion.

The business area has improved its operating performance and experienced fewer grid outages in recent years. The company is one of the grid companies in Norway with the lowest percentage grid losses and fewest outages. This trend continued in 2012. On average Hafslund's customers were without power for 0.75 hours during 2012, compared with 1.9 hours in the previous year. 2011 featured lengthy outages for the average customer due to the storm "Dagmar", which hit the company's operating area around Christmas 2011. The figure for 2012 was on a par with in 2010. Networks will continue to work systematically to ensure its power transmission grids offer a stable, robust and safe service, with a high security of supply throughout its area of coverage.

In recent years investments in the regional distribution grid, in particular in Oslo's central areas, have been prioritised. In the period 2013–2015 planned investments in the Group's distribution and regional grid, excluding AMS, are expected to be on a par with ongoing depreciation. Future investment levels will be impacted by further strengthening of the grid, introduction of AMS, and significant population growth in the Hafslund Nett's licence area. Investments and maintenance are included in the annual revenue ceiling which the Norwegian Water Resources and Energy Directorate sets for the business. Hafslund Nett is amongst the companies in Norway with the lowest grid rental charges. At the end of 2012 the company had a total of 562,500 grid customers (552,000).

NVE has adopted a new model for establishing the NVE interest-rate with effect from 2013. This will result in a higher NVE interest-rate than in the past. It is estimated that the NVE interest-rate will rise by around 3.0 percentage points in 2013 compared with 2012. This is an important change in order to secure the networks sector access to the capital required to implement the necessary reinvestments and future investments in AMS. A one percent increase in the NVE interest-rate will result in an around NOK 60 million rise in Hafslund Nett's revenue ceiling. However, a high income surplus as a result of a high transmission volume in the fourth quarter of 2012 will reduce the bottom-line impact of the rise the NVE rate in 2013. At the end of 2012 Networks had a cumulative income surplus of NOK 425 million (NOK 155 million). Based on planned transmission tariffs and maintenance, the operating result is expected to rise by around 15 percent in 2013 against the previous year.

Hafslund Nett is going to install AMS-meters (advanced metering services) with all network customers. Regulation 301 on Metering, Settlement and Invoicing stipulates that all electricity customers in Norway shall have AMS in place by 1 January 2017. In its letter of 18 February 2013, the Norwegian Ministry of Petroleum and Energy (OED) communicated that the Settlement Regulation would be changed in such a way that the rollout of AMS would be delayed two years until 1 January 2019. With AMS all households will have "smart meters" installed, which record power consumption on an hourly basis and automatically send data on consumption to the grid company. This will result in more rapid retrieval of meter values and improved information for the customer.

## Markets

The Markets business area comprises the business units Power Sales, Invoicing Services and the Customer Service Centre. Markets is active in Norway, Sweden, Finland and Spain, and aims to consolidate its position as the largest and most efficient power sales operator in Norway. In the longer term the aim is also to achieve a leading position in the Nordic market. Total sales for the year amounted to NOK 5.5 billion, down 1.7 billion against 2011. The decrease in sales is primarily attributable to lower wholesale prices for power purchased on Nord Pool in 2012 compared with 2011. The number of power customers rose by more than 26,000, while the delivered volume was up 0.9 TWh. A total of 16.4 TWh of electricity was sold to customers in 2012, compared to 15.5 TWh in 2011.

Markets posted an operating profit of NOK 364 million in 2012 (NOK 277 million). The increase against 2011 is primarily attributable to a rise in value of power derivatives of NOK 44 million (decrease of NOK 85 million), which are recognised in the income statement at fair value on an ongoing basis. A major portion of the gain relates to the reversal of provisions for hedging and end-user contracts for the period December 2011 to March 2012, which were recognised in the income statement in 2011. There is an inconsistency in the way changes in value of power and end user contracts are officially recognised. In accordance with IFRSs losses on hedging contracts shall always be recognised in the income statement, while the corresponding end user contracts may not be recognised in income. This asymmetry can have a major impact in periods when wholesale prices fluctuate significantly. Markets had capital employed of NOK 1.8 billion at the end of 2012.

The authorities are aiming to establish a joint Nordic end-user market for electricity by the end of 2016. Against this background, in 2010 Hafslund bought a stake in the Swedish power sales companies Göta Energi AB (100 percent) and Energibolaget i Sverige Holding AB (49 percent). In 2012 Hafslund consolidated its presence in the Swedish market through organic growth and the establishment of the company SverigesEnergi AB. SverigesEnergi shall be a clear low-price provider. Hafslund wishes to build on the experiences of NorgesEnergi and try on a low price concept in the Swedish market. Together with the company's strong position in the Norwegian power market, the above means Hafslund is well positioned to participate in a joint Nordic end-user market for electricity. At the end of 2012 Hafslund had a total of 905,000 electricity customers in wholly owned companies and a number of customers in part-owned companies. These include the customer portfolios belonging to Hafslund Strøm, NorgesEnergi, Fredrikstad EnergiSalg, Hallingkraft and Røyken Kraft in Norway, and the portfolios of the Swedish companies Göta Energi, SverigesEnergi and Energibolaget Sverige.

The market situation, which was characterised by relatively low power prices and moderate media focus on power prices in 2012, resulted in a 20 percent fall in enquiries to Hafslund's customer service centres in 2012 against the previous year. The company continually works to improve the customers' possibilities of self-service, programmes to reduce the number of incoming requests, and more efficient work-processes. More long-term plans to reduce incoming enquiries and improve internal processes have also been implemented. Ongoing surveys of a selection of customers contacting Hafslund's customer service centres reveal that customers generally have a positive impression of dealing with the customer service centres.

Hafslund Fakturaservice supplies metering, invoicing and collection services to the Group's companies. This includes ongoing invoicing of more than one million end customers. A major system and organisation development programme project designed to change the company's core systems for invoicing and metering was initiated in 2010. The new system was commissioned on 15 October 2012. Following the initial operating period all operating functions were found to be working normally, the system was functioning well and all activities had been implemented in accordance with plan. The rollout of the system will continue on its way to completion in 2013, when the last of the Group companies will be migrated to the new solution.

## Government relations and framework conditions

Hafslund's grid business is regulated by the authorities as a natural monopoly. Revenue ceilings for district heating are established by statute. Revenues for both power production and district heating are directly linked to prices on the power market, a market that to a large extent is impacted by political decisions.

It is vital that Hafslund is able to give the authorities useful input on the effect of framework conditions on its businesses and development opportunities. At the same time Hafslund must contribute to effective political and regulatory decisions by highlighting how decisions affect the important functions the company delivers to modern society. The change in the establishment of the NVE interest-rate is one example of how Hafslund, together with the rest of the power industry and the authorities, has helped to bring about positive change, in this case by helping to raise the NVE interest-rate from a dangerously low level to one that provides a better basis for profitable development of the future electricity grid.

## Corporate Social Responsibility

Hafslund is responsible for the social consequences caused by the Group's operations with regard to impact on the external environment, human rights, working conditions and other social issues. This responsibility permeates Hafslund's entire value chain and business, and also covers Hafslund's procurements and investments. Hafslund adopts the Norwegian government's definition of corporate social responsibility as stated in Report to the Storting no. 10 (2008-2009): "Corporate Social Responsibility in a Global Economy".

During 2012 the Group continued to focus on reinforcing corporate social responsibility across the Group's companies, primarily targeting the external environment and ethical trading. A policy for the external environment and corporate social responsibility, and dedicated procedures for environmental management and ethical trading, are guiding for the Group's work. Hafslund has drawn up ethical guidelines that apply to all the company's suppliers, and whose contents comprise part of relevant contracts.

In recent years Hafslund has been involved in several important sponsorship schemes. As a natural consequence of the change in business in recent years, and a heightened cost focus across the entire Group, the sponsorship portfolio will be significantly scaled back from 2013. Future sponsorships will have to contribute to value creation within the Group and be of benefit to society at large.

## External environment

### Environmental management

Effective environmental management is a natural part of Hafslund's corporate social responsibility, and an important means for securing efficient resource utilisation and operations. The Group has established requirements for all units to adopt a systematic approach to environmental management. The company that is responsible for the majority of energy consumption and emissions in the Group, Hafslund Varme, is certified to the international environmental standard ISO 14001. In addition, the head office at Drammensveien 144 and the conference centre at Hafslund Manor are both certified to the Environmental Beacon standard.

### Hafslund Produksjon

The run-of-river hydroelectric plants produce environmentally friendly power. It is in everyone's interests that the water resources of the Glomma river system be exploited in the most efficient way possible. In 2012 production uptime at Hafslund's electricity generating facilities stood at 93.14 percent, compared with 99.6 percent the previous year. The decrease is attributable to major faults at Kykkelsrud and Vamma.

### Hafslund Varme

The bulk of Hafslund's energy consumption and emissions are associated with the production of heat. A higher percentage of waste and other renewable energy in the input factors means that emissions of greenhouse gases are low in relation to the amount of energy generated. In addition, district heating is increasingly replacing older oil boilers. Emissions of greenhouse gases in 2012 amounted to 73 grams per kWh delivered per customer in Oslo. This represents a significant decrease compared with 2011, when the corresponding figure was 111 grams.

Incineration plants also produce emissions of a more local and regional nature, such as particle emissions, NOx and SOx, while some dioxins and heavy metals are emitted from the waste-to-energy plants. In 2012 these emission levels were generally much lower than the maximum limits set by the authorities, and any emissions exceeding maximum limits were quickly dealt with and reported to the authorities.

Hafslund Varme has specific plans to further increase the proportion of renewable energy used as input factors in the production of heat, including through the use of pellets. The first trials of the new pellets boiler were implemented in December 2012. Hafslund has set itself a long-term target of phasing out all fossil energy sources used in district heating production. Specific situations and lengthy periods of cold weather can result in some use of fossil energy sources to maintain security of supply.

In December 2012 there was a major oil discharge of around 19 m3 from Ullevål heating plant to the public sewage system, some of which reached Akerselva. Notification and contingency services functioned well, and remedial measures were implemented across the Christmas period. The discharge was treated as a non-compliance, and measures to prevent similar incidents have been accorded high priority.

### Hafslund Nett

Ensuring that energy produced actually arrives at its business and private customers' locations without significant interruptions or energy losses, and at the lowest possible cost to society, is also part of Hafslund Nett's corporate social responsibility remit. The ongoing conversion of the main distribution grid in Oslo to 132 kV will thus reduce grid losses relative to the current level.

The establishment of a requirement for an environmental, transport and utilities plan (ETU plan) for all major grid constructions, which are also subject to a subsequent public review, represented a major new development in 2012. This will result in an increased focus on decisions and processes.

### Other operations

The impact on the external environment of Hafslund's other operations largely derives from pellets production at Averøya, BioWood Norway, which was closed at the end of February 2013, and the company's buildings, transport and externally sourced services (transport and construction). The Group collaborates with Norsk Gjennvinning  AS in connection with waste collection and return schemes. Hafslund is also a member of Renas, the collection and treatment scheme for industrial electrical waste.

### Ethics and anti-corruption initiatives

Hafslund is committed to maintaining high ethical standards in all its commercial operations. The Group has been a member of the Initiative for Ethical Trading (IEH) since 2008. Hafslund leverages its membership to continue to place clear ethical demands on its suppliers in order to ensure that these exercise their business operations in line with Norwegian and internationally recognised principles and guidelines on human and employee rights, the environment and corruption. These requirements are incorporated into all contracts entered into by Hafslund.

To prevent the possibility of corruption, bribery or conflicts of interest, Hafslund has also drawn up a code of conduct for its employees, which has been approved by Hafslund ASA's Board of Directors.

## Corporate social responsibility

### Employees

At the end of 2012 Hafslund employed 1,216 staff (1,174 full-time equivalents). 35.8 percent of the Group's staff are women, while 64.2 percent are men. Hafslund strives to achieve a more equal distribution of women and men within all business areas, and focuses on this in the Group's management development programs. 58 percent of participants in the Growth development program which was implemented in 2012 were women. Hafslund's remuneration policy is based on the individual establishment of salaries, and the Group takes steps to ensure that any salary differentials are not based on discriminatory grounds. Remuneration paid to senior executives is discussed in Note 23 to the consolidated financial statements.

Until 1 March 2013 Group management comprised two women and five men. After this date it comprised three women and four men. 25 percent of the management teams at Group companies are women and 75 percent are men. The board of Hafslund ASA comprises eight representatives, three of whom are women and five of whom are men. The company thus complies with statutory requirements regarding board composition.

### Health, safety and the environment

Hafslund shall ensure high standards with regard to health, safety and the environment (HSE), and HSE shall be integrated into all the company's processes and activities. The Group endeavours to be an attractive employer with a progressive and inclusive working environment, and to prevent employees from being injured at work or developing work-related illnesses.

The Group ensures that Group companies adopt a systematic approach to health, safety and the environment, including by carrying out internal audits and inspection rounds. In 2012 HSE audits were carried out at six companies, along with 17 inspection rounds at various plants and projects. The Group also monitors any non-compliances recorded during audits to ensure that these are remedied within a reasonable time.

The Group emphasises the importance of collaboration across all companies, and has established various forums intended to help raise skills levels and ensure exchange of experiences and development of best practice in HSE.

#### Personal injuries

Six personal injuries were recorded involving employees in the Norwegian business during the year. None of the injuries resulted in absence from work. The injuries occurred at BioWood Norway AS and Hafslund Varme AS. A further seven personal lost-time injuries and five non-lost-time injures were recorded among Group suppliers whilst working at Hafslund's facilities. The injuries occurred on assignment for Hafslund Nett AS and Hafslund Varme AS.

No new cases of work-related illnesses were registered in 2012.

### Reported undesired incidents (RUIs)

Reporting of undesired incidents is a particularly effective tool in helping the company to achieve its vision of zero injuries at work. During the year the company adopted a particular focus on reporting and offering training on such incidents at the companies Hafslund Varme AS, Hafslund Nett AS and Hafslund Produksjon AS. The aim is to make all employees aware of the importance of reporting undesired incidents, and in this way help to prevent injuries and to improve operations. A total of 1,355 RUIs were recorded in the Group in 2012.

### Sickness absence

In 2012 the sickness absence rate in the Group was  4.7 percent. This was slightly up on the previous year's figure of 4.35 percent. The short-term sickness absence rate (up to 16 days) was 2.3 percent, while the long-term absence rate was 2.4 percent. The sickness absence rate varies considerably between Group companies, ranging between one and eight percent.

Hafslund's target is for a sickness absence rate of no more than four percent. In accordance with the Inclusive Workplace (IA) agreement, all the Group's companies closely monitor employees during sickness absence and implement preventative measures. This involves close collaboration with the company's occupational health service Stamina Helse og Trening, and the Norwegian Labour and Welfare Organisation (NAV).

## Risk

In addition to operational risks, Hafslund's business operations are exposed to regulatory, legal, financial, reputational, political and market risks. Risk assessment is an integral part of all the Group's business activities, and the Group's overall risk is assessed by the board itself. Hafslund has established guidelines and frameworks for active risk management in a number of areas. The Group has long-term committed drawdown facilities in order to secure availability of liquidity, even in periods when it may be difficult to obtain financing in the capital markets.

The market price of electricity is one of several important value drivers affecting the Group's financial performance. This is in particular true for the Production and Heat businesses. During the year Hafslund changed from a strategy of selling produced power in the spot market to partial price-hedging of sales of expected production of power in order to reduce power price risk. Hafslund manages market risk by trading in financial instruments. Authorities and frameworks for the hedging strategy have been established, and these are reported to the board and management on an ongoing basis. The Group can hedge the power volume for up to the next 36 months in the forward market at any one time, where the proportion of hedging is expected to be higher in the first six months than in the remainder of the period. The power sales business seeks to reduce the uncertainty associated with electricity price fluctuations through hedging. Counterparty risk in the power market is minimised through the use of standardised contracts which are cleared and settled via Nasdaq OMX Commodities. Hafslund is also exposed to raw materials used in district heating production and waste incineration. Group management evaluates and adopts strategies with which to manage this kind of risk within the risk profile determined by the board.

The Group's finance department actively manages and hedges foreign currency exposure in order to reduce foreign exchange risk in relation to power trading, purchase of goods and services and foreign currency borrowing. Hafslund is exposed to interest rate risk in the guise of changes in interest rates on its interest-bearing liabilities, and due to the inclusion of five-year government bonds in the income framework established for the distribution grid business for 2012. The Group seeks to reduce its interest rate risk through balanced management of fixed and variable interest rates on its interest rate portfolio. The board has approved the guidelines and frameworks which govern the management of financial risk.

Several of the Group's energy supply businesses are subject to public licences and a large degree of public regulation. This applies in particular to the Production, Heat and Networks businesses. The Networks business is a natural monopoly with publicly-regulated earnings. The grid regulation scheme in force throughout 2012 resulted in some unforeseen negative fluctuations in the revenue ceiling and returns. NVE has made changes to the regulation model from 2013. These are expected to result in more stability, improved returns and increased investment insensitivity, along with improved incentives for mergers and acquisitions. The introduction of advanced metering systems (AMS) in Norway is one of the greatest challenges ever embraced by the energy industry. Hafslund Nett has embarked on work to ensure that the grid company's 562,500 customers receive AMS on time.

The key risk element for the power sales business relates to its customer base. At any given time the business has a substantial volume of accounts receivable due from customers. However, the bulk of these are relatively small receivables from private customers invoiced on a monthly basis, and losses have traditionally been marginal.

### Ownership structure and shareholders

Hafslund ASA has two classes of shares, with A shares granting voting rights at general meetings of the Group's shareholders. The reason for this is historical and deviates from the Norwegian Code of Practice for Corporate Governance. At the end of 2012 the Group's share capital totalled NOK 195,186,264, divided between 115,427,759 A shares and 79,758,505 B shares. As of 28 December 2012 the price of A shares was NOK 45.60 and B shares NOK 45.30. At the end of the year Hafslund's market capitalisation totalled NOK 8.9 billion. The return (change in value + dividend) in 2012 totalled -16.3 percent. By comparison, the Oslo Stock Exchange's main index OSEBX (OSEBX is adjusted for dividends) fell by 14.0 percent.

At the reporting date the City of Oslo was Hafslund ASA's largest shareholder, with 53.7 percent of share capital, comprising 58.5 percent of A shares and 46.8 percent of B shares. Fortum Forvaltning AS was the second-largest shareholder with 34.1 percent of the share capital, comprising 32.8 percent of A shares and 36.0 percent of B shares. At the close of the year Hafslund held 397,361 treasury B shares.

### The work of the Board of Directors

Hafslund's Board of Directors has complied with the previously adopted board mandate and guidelines for the board's activities. Updated principles for corporate governance were adopted on 5 December 2012, and are amended on an ongoing basis in line with the Norwegian Code of Practice for Corporate Governance. A description of principles for corporate governance, and non-compliances with the above Code can be viewed at hafslund.no The board's work is based on good corporate governance.

Hafslund meets the statutory requirements relating to gender balance on boards of ASA companies. The board carries out an annual appraisal of its working practices, competence and working relationship with Group management. The board's Compensation Committee advises the board on a number of matters including the remuneration paid by the company to its President and CEO. In 2010 the board established an Audit Committee. The Audit Committee's remit is to assist the board in performing its duties regarding preparation of the financial statements and evaluation of the company's internal controls.

At the Annual General Meeting held on 24 April 2012 Board Chairman Birger Magnus and board members Maria Moræus Hanssen and Ellen Christine Christiansen were elected with a term of office until the 2014 Annual General Meeting.

There is agreement within Hafslund not to establish a Corporate Assembly. Consequently the board reports directly to the general meeting and the shareholders. Disclosures that Hafslund is obliged to make in accordance with § 3-3b of the Norwegian Accounting Act regarding reporting on business management contained in the 2012 annual report are incorporated in the section on Corporate Governance at hafslund.no.

On 26 October 2012 employee representatives were elected to the board of Hafslund ASA. Per Orfjell and Per Luneborg were re-elected for a further two years, while Jane Koppang was elected as a new employee representative.

### Dividend and appropriation of profit

At the Annual General Meeting to be held on 7 May 2013 the board will propose that a dividend of NOK 2.50 per share, a total of NOK 487 million, be paid for the 2012 financial year. The board proposes the following appropriation of Hafslund ASA's net profit for the year of NOK 42 million:

| | |
|---|---|
| Transferred from other equity: | NOK -445 million |
| Proposed dividend: | NOK 487 million |
| Total appropriated: | NOK 42 million |

Less these appropriations the company's distributable reserves stood at NOK 2,709 million as of 31 December 2012.

### Outlook

Hafslund's overarching objective is to consolidate its position as a leading integrated energy company in Norway based on profitable growth. This will be achieved based on the four business areas of Production, Heat, Networks and Markets, primarily through organic, but also through structural growth, as well as through efficient operations and by leveraging synergies.

The Group has a strong market position in all its business areas, and is also well established in areas with expanding populations and thus growing energy needs. By 2030 the population of Oslo is expected to be nearly 800,000, compared with the current figure of 600,000. Consequently, the need for new energy supply capacity both within and into the region is growing. Hafslund is catering for this population growth by modernising and reinforcing Oslo's energy infrastructure.

Hafslund's financial performance is directly affected by fluctuations in the price of electricity. This applies to power generation and district heating, while revenues from the network operations are largely affected by changes in the regulatory framework. The power sales business is subject to extreme competition, where profitability is contingent on Hafslund's ability to maintain customer loyalty and efficiency.

At any one time power prices are impacted by the hydrological situation and financial conditions in the Nordic region and the rest of Europe, along with any regulatory and political initiatives. On 31 December 2012 the listed price for future supply of power for 2013 and 2014 on Nasdaq OMX was NOK/MWh 280. Significant uncertainty attaches to future power price changes. In order to be able to exploit market opportunities and to secure earnings and cash flows, Hafslund has gradually changed from a spot policy for selling produced power to one of partial price-hedging.

In addition to ongoing operational investments in existing business, the Group's future investment needs are being shaped by statutory investments in AMS. In its letter of 18 February 2013, the Norwegian Ministry of Petroleum and Energy (OED) communicated that the Settlement Regulation would be changed in such a way that the rollout of AMS would be delayed two years, until 1 January 2019.

The strategic focus on core business will strengthen Hafslund's role as a leading energy company, and underpin the Group's focus on renewable energy, infrastructure for energy and the power market. The board believes that Hafslund has established a sound commercial and financial platform for satisfactory future development, and to meet the various challenges the Group will face in the future.

The Board of Directors of Hafslund ASA
Oslo, 19 March 2013

Birger Magnus
Chairman of the Board

Maria Moræus Hanssen
Deputy Chairman

Ellen Christine Christiansen

Odd Håkon Hoelsæter

Hans Kristian Rød

Per Orfjell

Per Luneborg

Jane Koppang

Finn Bjørn Ruyter
President and CEO