

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1.1 Principal activities

Fortum Corporation (the Company) is a Finnish public limited liability company with its domicile in Espoo, Finland. The Company is listed on NASDAQ OMX Helsinki.

Fortum Corporation and its subsidiaries (together the Fortum Group) is a leading energy company focusing on the Nordic countries, Russia and the Baltic Rim area. Fortum's activities cover generation, distribution and sale of electricity and heat, operation and maintenance of power plants as well as energy-related services.

These financial statements were approved by the Board of Directors on 31 January 2012.

1.2 Basis of preparation

The consolidated financial statements of the Fortum Group have been prepared in accordance with International Financial Reporting Standards (IFRS) and IFRIC Interpretations as adopted by the European Union. The financial statements also comply with Finnish accounting principles and corporate legislation.

The consolidated financial statements have been prepared under the historical cost convention except for available for sale financial assets, financial assets and financial liabilities (including derivative instruments) at fair value through profit and loss and items hedged at fair value.

1.2.1 Use of estimates

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting principles. The areas involving higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 2 Critical accounting estimates and judgements on page 50.

1.2.2 New Standards and amendments and interpretations to existing standards

Fortum has adopted the following new or amended standards and interpretations to existing standards on 1 January 2011:

- IFRIC 14 *Prepayments of minimum funding requirements* (Amendment) (effective for annual periods beginning on or after 1 January 2011). The amendment permits an entity to treat prepayments of a minimum funding as an asset. The amendment did not have a material impact on Fortum's financial statements.
- IFRIC 19 *Extinguishing financial liabilities with equity instruments* (effective for annual periods beginning on or after 1 July 2010). The interpretation clarifies the accounting by an entity when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor. The interpretation did not have an impact on Fortum's financial statements.
- *Annual improvements to IFRSs* were issued in May 2010. The improvements primarily remove inconsistencies and clarify wording of standards. There were

separate transitional provisions for each standard. Amendments did not have an impact on Fortum's financial statements.

- Fortum has early adopted IAS 24 *Related party disclosures* (effective for annual periods beginning on or after 1 January 2011) already from 1 January 2010.

Fortum will apply the following new or amended standards and interpretations to existing standards on 1 January 2012 or later and has not early adopted these changes:

- IAS 1 *Presentation of Financial statements* (Amendment) (effective for annual periods beginning on or after 1 July 2012). The amendment relates to presentation of Comprehensive Income and Fortum will apply it latest on annual periods beginning on 1 January 2013. The amendment is still subject to endorsement by EU.
- IAS 12 *Income taxes* (Amendment) (effective for annual periods beginning on or after 1 January 2012). The amendment provides a practical approach for measuring deferred tax assets and liabilities when investment property is fair valued under IAS 40 *Investment property*. The amendment is not expected to have an impact on Fortum, since Fortum currently does not have investment properties. The amendment is still subject to endorsement by EU.
- IFRS 9 *Financial instruments* (effective for annual periods beginning on or after 1 January 2015). The standard has new requirements for the classification and measurement of financial assets and liabilities. New requirements are expected to be added to the standard and it will eventually replace IAS 39 and IFRS 7. Fortum will apply the new standard in due course. The Standard is still subject to endorsement by EU.
- IAS 19 *Employee benefits* (Amendment) (effective for annual periods beginning on or after 1 January 2013). The amendment changes the accounting for defined benefit plans by eliminating the corridor approach. Fortum will apply the amended IAS 19 on the effective date. The amendment is not expected to have a material effect on Fortum's financial statements. The standard is still subject to endorsement by EU.
- IFRS 10 *Consolidated financial statements* (effective for annual periods beginning on or after 1 January 2013). The standard builds on existing principles by identifying the concept of control as the determining factor whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. Fortum still assesses the impact of the standard and will apply it when it is effective and endorsed in the EU.
- IFRS 11 *Joint arrangements* (effective for annual periods beginning on or after 1 January 2013). The standard replaces IAS 31 *Interests in joint ventures*. Joint control under IFRS 11 is defined as the contractual sharing of control of an arrangement, which exists only when the decisions about the relevant activities require unanimous consent of the parties sharing control. Fortum still assesses

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the impact of the standard and will apply it when it is effective and endorsed in the EU.

- IFRS 12 *Disclosures of interests in other entities* (effective for annual periods beginning on or after 1 January 2013). The standard includes disclosure requirements for all forms of investments in other entities. Fortum will apply the new standard when it is effective and endorsed in the EU.
- IFRS 13 *Fair value measurement* (effective for annual periods beginning on or after 1 January 2013). The standard establishes a single framework for measuring fair value where that is required by other standards. Fortum will apply the new standard when it is effective and endorsed in the EU.
- *Annual improvements to IFRSs* were issued in June 2011. The improvements primarily remove inconsistencies and clarify wording of standards. There are separate transitional provisions for each standard. Amendments are not expected to have an impact on Fortum's financial statements. Fortum will apply the amendments when they are effective and endorsed in the EU.

1.2.3 Classification of current and non-current assets and liabilities

An asset or a liability is classified as current when it is expected to be realised in the normal operating cycle or within twelve months after the balance sheet date or it is classified as financial assets or liabilities held at fair value through profit or loss. Liquid funds are classified as current assets.

All other assets and liabilities are classified as non-current assets and liabilities.

1.2.4 Income statement presentation

In the Consolidated income statement Comparable operating profit is presented to better reflect the Group's business performance when comparing results for the current period with previous periods.

Items affecting comparability are disclosed as a separate line item. The following items are included in "Items affecting comparability":

- non-recurring items, which mainly consist of capital gains and losses;
- effects from fair valuations of derivatives hedging future cash flows which do not obtain hedge accounting status according to IAS 39. The major part of Fortum's cash flow hedges obtain hedge accounting where fair value changes are recorded in equity;
- effects from accounting of Fortum's part of the State Nuclear Waste Management Fund where the assets can not exceed the related liabilities according to IFRIC5.

Comparable operating profit is used for financial target setting, follow up and allocation of resources in the group's performance management.

1.3 Consolidation

1.3.1 Subsidiaries

The consolidated financial statements include the parent company Fortum Corporation and all those companies in which Fortum Corporation has the power to govern the financial and operating policies and generally holds, directly or indirectly, more

than 50% of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the group controls another entity.

✚ *The Fortum Group subsidiaries are disclosed in Note 47 Subsidiaries by segment on 31 December 2011 on page 97.*

The Fortum Group was formed in 1998 by using the pooling-of-interests method for consolidating Fortum Power and Heat Oy and Fortum Oil and Gas Oy (the latter demerged to Fortum Oil Oy and Fortum Heat and Gas Oy 1 May 2004). In 2005 Fortum Oil Oy was separated from Fortum by distributing 85% of its shares to Fortum's shareholders and by selling the remaining 15%. This means that the acquisition cost of Fortum Power and Heat Oy and Fortum Heat and Gas Oy has been eliminated against the share capital of the companies. The difference has been entered as a decrease in shareholders' equity.

The acquisition method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured as the aggregate of fair value of the assets given and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, subsidiaries' accounting policies have been changed to ensure consistency with the policies the Group has adopted.

1.3.2 Associates and joint ventures

Associated companies are entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Joint ventures are entities over which the Group has contractually agreed to share the power to govern the financial and operating policies of that entity with another venturer or venturers. The Group's interests in associated companies and jointly controlled entities are accounted for using the equity method of accounting. Assets acquired and liabilities assumed in the investment in associates or joint ventures are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the associate or joint venture acquired, the difference is recognised directly in the income statement.

The Group's share of its associates or joint ventures post-acquisition profits or losses after tax and the expenses related to the adjustments to the fair values of the assets and liabilities assumed are recognised in the income statement. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. The Group's share of post-acquisition adjustments to associates or joint ventures equity that have not been recognised in the associates or joint ventures income statement, is recognised directly in Group's shareholder's equity and against the carrying amount of the investment.

When the Group's share of losses in an associate or a joint venture equals or exceeds its interest in the associate or joint venture, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate or joint venture.

Unrealised gains on transactions between the Group and its associates or joint ventures are eliminated to the extent of the Group's interest in the associate or joint venture. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates or joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

Fortum owns shareholdings in associated electricity production companies (mainly nuclear and hydro), from which the owners purchase electricity at production cost, including interest costs and production taxes. The share of profit of these companies is mainly IFRS adjustments and depreciations on fair value adjustments from historical acquisitions since the companies are not profit making under local accounting principles.

✚ *For further information regarding the shareholdings in these electricity production companies, see Note 24 Participations in associated companies and joint ventures on page 80 and Note 45 Related party transactions on page 96.*

If more recent information is not available, the share of the profit of certain associated or joint venture companies is included in the consolidated accounts based on the latest available information.

Fortum owns shareholdings in listed associated companies such as Hafslund ASA. The share of profit of these companies is accounted for based on previous quarter information.

Until December 2011 Hafslund ASA owned shares in a listed company Renewable Energy Corporation (REC). Until Q3 2011 Fortum accounted for the fair value changes in REC based on the share price in Oslo stock exchange and the number of shares owned by Hafslund at each closing date since REC is listed in the Oslo stock exchange. When Hafslund publicly announced a divestment of shares in REC, Fortum accounted for any gains or losses of this transaction as soon as information was available. Since Q3 2011 Fortum changed accounting principle for its associated company Hafslund. The share of profits from Hafslund including REC is included in Fortum Group figures based on the previous quarter information since updated interim information is not normally available. If Hafslund divests or impairs its

shareholding in REC, Fortum will account for any occurring sales gains or losses and impairment charges based on Hafslund's previous quarter information.

Regarding Fortum's share of profits in TGC-1, the share of profit is accounted for based on previous quarter information. If TGC-1 reverses impairment losses that have been booked prior to Fortum's ownership in TGC-1, Fortum eliminates such reversals as Fortum assesses the need for impairment is separately.

✚ *Regarding accounting for Fortum's shareholding in Hafslund ASA and TGC-1, see Note 24 Participations in associated companies and joint ventures on page 80.*

1.3.3 Non-controlling interests

Non-controlling interests in subsidiaries are identified separately from the equity of the owners of the parent company. The non-controlling interests are initially measured at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests' share of subsequent changes in equity.

1.4 Segment reporting

Fortum discloses segment information in a manner consistent with internal reporting to Fortum's Board of Directors and to Fortum Management Team led by the President and CEO. Fortum mainly has segments based on type of business operations, combined with one segment based on geographical area.

The Group's businesses are divided into the following reporting segments:

- Power – comprises power generation (exclusive Russia), physical operation and trading as well as expert services for power producers in the Nordic market and selected international markets. Power sells its power mainly to the Nordic power exchange Nord Pool Spot;
- Heat – comprises heat generation and sales in the Nordic countries and other parts of the Baltic Rim. The segment also generates power in the combined heat and power plants (CHP) and sells it to end-customers mainly by long-term contracts, as well as to Nord Pool Spot;
- Distribution – owns and operates distribution and regional networks and distributes electricity to customers in Sweden, Finland, Norway and Estonia;
- Electricity Sales – focuses on the retail sale of electricity to private and business customers as well as to other electricity retailers in Sweden, Finland and Norway. Electricity Sales segment buys its electricity through Nord Pool Spot;
- Russia – comprises power and heat generation and sales in Russia. It includes mainly the Russian subsidiary OAO Fortum and the shareholding in the associated company TGC-1;
- Other – mainly the shareholding in the associated company Hafslund ASA and corporate center including the Fortum Group shared service centers. The shared service centers charge the companies according to service level agreements.

✚ *For further information about the reporting segments, see Note 5 Segment reporting on page 60.*

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1.5 Discontinued operations and assets held for sale

Discontinued operations represent a separate major line of business that either has been disposed of or is classified as held for sale. Assets and liabilities attributable to the discontinued operations must be clearly distinguishable from the other consolidated entities in terms of their operations and cash flows. In addition, the reporting entity must not have any significant continuing involvement in the operations classified as a discontinued operation.

Non-current assets (or disposal groups) classified as held for sale are valued at the lower of their carrying amount and fair value less costs to sell if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. These classification criteria do not include non-current assets to be abandoned or those that have been temporarily taken out of use. An impairment loss (or subsequent gain) reduces (or increases) the carrying amount of the non-current assets or disposal groups. The assets are not depreciated or amortised. Interest or other expenses related to these assets are recognised as before the classification as held for sale.

Neste Oil was included in Fortum Group up until 31 March 2005, when the Annual General Meeting took the final decision to separate the oil operations by distributing approximately 85% of Neste Oil Corporation shares as dividend. The remaining approximately 15% of shares were sold to investors in April 2005.

✚ *Oil operations have been presented as discontinued operations for 2004 and 2005, see Financial key figures on page 99.*

1.6 Foreign currency transactions and translation

1.6.1 Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in euros, which is the Company's functional and presentation currency.

1.6.2 Transactions and balances

Transactions denominated in foreign currencies are translated using the exchange rate at the date of the transaction. Receivables and liabilities denominated in foreign currencies outstanding on the closing date are translated using the exchange rate quoted on the closing date. Exchange rate differences have been entered in the income statement. Net conversion differences relating to financing are entered under financial income or expenses, except when deferred in equity as qualifying cash flow hedges. Translation differences on available for sale financial assets are included in Other equity components section of the equity.

1.6.3 Group companies

The income statements of subsidiaries, whose measurement and reporting currencies are not euros, are translated into the Group reporting currency using the average exchange rates for the year based on the month-end exchange rates,

whereas the balance sheets of such subsidiaries are translated using the exchange rates on the balance sheet date. On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale. Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. The Group deems all cumulative translation differences for all foreign operations to be zero at the date of transition to IFRS, i.e. 1 January 2004.

✚ *Exchange rates used to translate reporting currencies into euros are disclosed in Note 10 Exchange rates on page 67.*

1.6.4 Associates and joint ventures

The Group's interests in associated companies and jointly controlled entities are accounted for by the equity method. Associates and joint ventures, whose measurement and reporting currencies are not euro, are translated into the Group reporting currency using the same principles as for subsidiaries, see 1.6.3 Group companies.

1.7 Revenue recognition

Revenue comprises the fair value consideration received or receivable at the time of delivery of products and/or upon fulfilment of services. Revenue is shown, net of rebates, discounts, value-added tax and selective taxes such as electricity tax. Revenue is recognised as follows:

1.7.1 Sale of electricity, heat, cooling and distribution of electricity

Sale of electricity, heat, cooling and distribution of electricity is recognised at the time of delivery. The sale to industrial and commercial customers and to end-customers is recognised based on the value of the volume supplied, including an estimated value of the volume supplied to customers between the date of their last meter reading and year-end.

Physical energy sales and purchase contracts are accounted for on accrual basis as they are contracted with the Group's expected purchase, sale or usage requirements.

Electricity tax is levied on electricity delivered to retail customers by domestic utilities in Sweden. The tax is calculated on the basis of a fixed tax rate per kWh. The rate varies between different classes of customers. Sale of electricity in the income statement is shown net of electricity tax.

Physical electricity sales and purchases are done through Nord Pool Spot. The sales and purchases are netted on Group level on an hourly basis and posted either as revenue or cost, according to whether Fortum is a net seller or a net buyer during any particular hour.

The prices charged of customers for the sale of distribution of electricity are regulated. The regulatory mechanism differs from country to country. Any over or under income decided by the regulatory body is regarded as regulatory assets

or liabilities that do not qualify for balance sheet recognition due to the fact that no contract defining the regulatory aspect has been entered into with a specific customer and thus the receivable is contingent on future delivery. The over or under income is normally credited or charged over a number of years in the future to the customer using the electricity connection at that time. No retroactive credit or charge can be made.

1.7.2 Connection fees

Fees paid by the customer when connected to the electricity, gas, heat or cooling network are recognised as income to the extent that the fee does not cover future commitments. If the connection fee is linked to the contractual agreement with the customer, the income is recognised over the period of the agreement with the customer.

Connection fees paid by customers when connected to the electricity network before 2003 are refundable in Finland if the customer would ever disconnect the initial connection. Also fees paid by the customer when connected to the district heating network in Finland are refundable. These connection fees have not been recognised in the income statement and are included in other liabilities in the balance sheet.

1.7.3 Contract revenue

Contract revenue is recognised under the percentage of completion method to determine the appropriate amount to recognise as revenue and expenses in a given period. The stage of completion is measured by reference to the contract costs incurred up to the closing date as a percentage of total estimated costs for each contract. Costs incurred in the year in connection with future activity on a contract are excluded from contract costs in determining the stage of completion. They are presented as inventories, prepayments or other assets, depending on their nature.

The Group presents as an asset the amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceed progress billings. Progress billings not yet paid by customers and retention are included within 'trade and other receivables'. The Group presents as a liability the amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses).

1.7.4 Other income

Revenue from activities outside normal operations is reported in other income. This includes recurring items such as rental income.

1.8 Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions. Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with

the costs that they are intended to compensate. Government grants relating to the purchase of property, plant and equipment are deducted from the acquisition cost of the asset and are recognised as income by reducing the depreciation charge of the asset they relate to.

1.9 Emission allowances

The Group accounts for emission allowances based on currently valid IFRS standards where purchased emission allowances are accounted for as intangible assets at cost, whereas emission allowances received free of charge are accounted for at nominal value. A provision is recognised to cover the obligation to return emission allowances. To the extent that the Group already holds allowances to meet the obligation the provision is measured at the carrying amount of those allowances. Any shortfall of allowances held over the obligation is valued at the current market value of allowances. The cost of the provision is recognised in the income statement within materials and services. Gains from sales of emission rights are reported in other income.

1.10 Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

1.11 Research and development costs

Research and development costs are recognised as expense as incurred and included in other expenses in the income statement. If development costs will generate future income, they are capitalised as intangible assets and depreciated over the period of the income streams.

1.12 Property, plant and equipment

Property, plant and equipment comprise mainly power and heat producing buildings and machinery, transmission lines, tunnels, waterfall rights and district heating network. Property, plant and equipment are stated at historical cost less accumulated depreciation and accumulated impairment losses as applicable in the consolidated balance sheet. Historical cost includes expenditure that is directly attributable to the acquisition of an item and borrowing costs capitalised in accordance with the Groups accounting policy. Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment. Acquired assets on the acquisition of a new subsidiary are stated at their fair values at the date of acquisition.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic

benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Additionally the cost of an item of property, plant and equipment includes the estimated cost of its dismantlement, removal or restoration.

➔ See also section 1.24.2 Asset retirement obligations on page 48.

Land, water areas, waterfall rights and tunnels are not depreciated since they have indefinite useful lives. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

Hydro power plant buildings, structures and machinery	40–50 years
Thermal power plant buildings, structures and machinery	25 years
Nuclear power plant buildings, structures and machinery	25 years
CHP power plant buildings, structures and machinery (each CHP plant has an individual depreciation period)	15–25 years
Substation buildings, structures and machinery	30–40 years
Distribution network	15–40 years
District heating network	30–40 years
Other buildings and structures	20–40 years
Other tangible assets	20–40 years
Other machinery and equipment	3–20 years
Other non-current investments	5–10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each closing date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

1.12.1 Jointly controlled assets

Fortum owns, through its subsidiary Fortum Power and Heat Oy, the coal condensing power plant Meri-Pori in Finland. Teollisuuden Voima Oyj (TVO) has the contractual right to participate in the plant with 45.45%. The capacity and production can be divided between Fortum and TVO. Each owner can decide when and how much capacity to produce. Both Fortum and TVO purchase fuel and emission rights independently. Since both Fortum and TVO have control, including related risks and rewards, of their share of the power plant, Meri-Pori is accounted for as a jointly controlled asset.

Fortum is accounting for the part of the investment that corresponds to the investment Fortum has made, i.e. 54.55%.

Fortum is also entitled to part of the electricity TVO produces in Meri-Pori through the shareholding of 26.58% of TVO C-series shares.

➔ For further information regarding Fortum's shareholding in TVO, see Note 24 Participations in associated companies and joint ventures on page 80.

1.13 Intangible assets

Intangible assets, except goodwill, are stated at the historical cost less accumulated amortisation and impairment losses if applicable and amortised on a straight-line method over their expected useful lives.

1.13.1 Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to the acquirer when bringing the software into use. These costs are amortised over their estimated useful lives (three to five years). Costs associated with developing or maintaining computer software are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the software development employee costs and an appropriate portion of relevant overheads. Computer software development costs recognised as assets are amortised over their estimated useful lives.

1.13.2 Trademarks and licences

Trademarks and licences are shown at historical cost less accumulated amortisation and impairment losses, as applicable. Amortisation is calculated using the straight-line method to allocate the cost of trademarks and licences over their estimated useful lives (15–20 years).

1.13.3 Contractual customer relationships

Contractual customer relationships acquired in a business combination are recognised at fair value on acquisition date. The contractual customer relations have a finite useful life and are carried at costs less accumulated amortisation. Amortisation is calculated using the straight-line method over the expected duration of the customer relationship.

1.13.4 Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates and is tested for impairment as part of the overall balance. Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on disposal of an entity include the carrying amount of goodwill relating to the entity sold.

1.14 Impairment of non-financial assets

The individual assets' carrying values are reviewed at each closing date to determine whether there is any indication of impairment. An asset's carrying amount

is written down immediately to its recoverable amount if it is greater than the estimated recoverable amount.

When considering the need for impairment the Group assesses if events or changes in circumstances indicate that the carrying amount may not be recoverable. This assessment is documented once a year in connection with the Business Plan process. Indications for impairment are analysed separately by each division as they are different for each business and include risks such as changes in electricity and fuel prices, regulatory/political changes relating to energy taxes and price regulations etc. Impairment testing needs to be performed if any of the impairment indications exists. Assets that have an indefinite useful life, such as goodwill, are not subject to amortisation and are tested annually for impairment.

An impairment loss is recognised in the income statement for the amount by which the assets' carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

Value in use is determined by discounting the future cash flows expected to be derived from an asset or cash-generating unit. Cash flow projections are based on the most recent business plan that has been approved by management. Cash flows arising from future investments such as new plants are excluded unless projects have been started. The cash outflow needed to complete the assets is included.

The period covered by cash flows is related to the useful lives of the assets reviewed for impairment. Normally projections should cover a maximum period of five years but as the useful lives of power plants and other major assets are over 20 years, the projection period is longer. Cash flow projections beyond the period covered by the most recent Business Plan are estimated by extrapolating the projections using a steady or declining growth rate for subsequent years.

Non-financial assets other than goodwill that suffered an impairment charge are reviewed for possible reversal of the impairment at each reporting date.

1.15 Financial assets

The Group classifies its investments in the following categories: financial assets at fair value through profit or loss, loans and receivables and available for sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

1.15.1 Financial assets at fair value through profit or loss

A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current

assets if they are either held for trading or are expected to be realised within 12 months of the closing date.

1.15.2 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor. They are included in non-current assets, except for maturities under 12 months after the closing date. These are classified as current assets.

1.15.3 Available for sale financial assets

Available for sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless there is an intention to dispose of the investment within 12 months of the closing date.

Purchases and sales of investments are recognised on the trade-date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

Available for sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of securities classified as available for sale are recognised in equity. When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments are included in the income statement.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

The Group assesses at each closing date whether there is objective evidence that a financial asset or a group of financial assets is impaired. If any such evidence exists for available for sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement.

1.16 Trade receivables

Trade receivables are recorded at their fair value. A provision for impairment of trade receivables is established when there is evidence that the Group will not be able to collect all amounts due according to the original terms of the receivable. Significant financial difficulties of the debtor, probability that the debtor will enter into bankruptcy or financial reorganisation, and default or delinquency in payments are considered as indicators that the receivable is impaired. The amount of the impairment charge is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows.

Trade receivables include revenue based on an estimate of electricity, heat, cooling and distribution of electricity already delivered but not yet measured and not yet invoiced.

1.17 Liquid funds

Cash and cash equivalents in Liquid funds include cash in hand, deposits held at call with banks and other short-term, highly liquid investments with maturities of three months or less. Bank overdrafts are shown within borrowings in current liabilities in the balance sheet.

1.18 Treasury shares

Where any group company purchases the Company's shares (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Company's equity holders until cancelled or reissued. When such shares are subsequently sold or reissued, any consideration received is included in equity.

1.19 Borrowings

Borrowings are recognised initially at fair value less transaction costs incurred. In subsequent periods, they are stated at amortised cost; any difference between proceeds (net of transaction costs) and the redemption value is recognised as interest cost over the period of the borrowing using the effective interest method. Borrowings or portion of borrowings being hedged with a fair value hedge is recognised at fair value.

1.20 Leases

1.20.1 Finance leases

Leases of property, plant and equipment, where the Group has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalised at the commencement of the lease term at the lower of the fair value of the leased property and the present value of the minimum lease payments determined at the inception of the lease. Each lease payment is allocated between the reduction of the outstanding liability and the finance charges. The corresponding rental obligations, net of finance charges, are included in the long-term or short-term interest-bearing liabilities according to their maturities. The interest element

of the finance cost is charged to the income statement over the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

Sale and leaseback transactions resulting in a finance lease agreement are recognised according to the principles described above. The difference between the selling price and the carrying amount of the asset sold is deferred and amortised over the lease period.

The property, plant and equipment leased out under a finance lease are presented as interest-bearing receivables at an amount equal to the net investment in the lease. Each lease payment receivable is allocated between the repayment of the principal and the finance income. Finance income is recognised in the income statement over the lease term so as to produce a constant periodic rate of return on the remaining balance of the receivable for each period.

1.20.2 Operating leases

Leases of property, plant and equipment, where the Group does not have substantially all of the risks and rewards of ownership are classified as operating leases. Payments made under operating leases are recognised in the income statement as costs on a straight-line basis over the lease term.

Payments received under operating leases where the Group leases out fixed assets are recognised as other income in the income statement.

1.21 Inventories

Inventories in Fortum mainly consist of fuels consumed in the production process or in the rendering of services. Inventories are stated at the lower of cost and net realisable value being the estimated selling price for the end product, less applicable variable selling expenses and other production costs. Cost is determined using the first-in, first-out (FIFO) method.

Inventories which are acquired primarily for the purpose of trading are stated at fair value less selling expenses.

1.22 Income taxes

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, if the deferred tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not accounted for. Deferred tax is determined using

tax rates (and laws) that have been enacted or substantially enacted by the closing date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax assets are set off against deferred tax liabilities if they relate to income taxes levied by the same taxation authority.

Deferred tax is provided on temporary differences arising from investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference is controlled by the Group, and it is probable that the temporary difference will not reverse in the foreseeable future.

1.23 Employee benefits

1.23.1 Pension obligations

The Group companies have various pension schemes in accordance with the local conditions and practises in the countries in which they operate. The schemes are generally funded through payments to insurance companies or Group's pension fund as determined by periodic actuarial calculations. The Group has both defined benefit and defined contribution plans.

The Group's contributions to defined contribution plans are charged to the income statement in the period to which the contributions relate.

For defined benefit plans, pension costs are assessed using the projected unit credit method. The cost of providing pensions is charged to the income statement as to spread the service cost over the service lives of employees. The defined benefit obligation is calculated annually on the balance sheet date and is measured as the present value of the estimated future cash flows using interest rates of high-quality corporate bonds that have terms to maturity approximating to the terms of the related pension liability. In countries where there is no deep market in such bonds, market yields on government bonds are used instead. The plan assets for pensions are valued at market value. The liability recognised in the balance sheet is the defined benefit obligation at the closing date less the fair value of plan assets with adjustments for unrecognized actuarial gains or losses or past service costs. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

Actuarial gains and losses exceeding 10% of total of the present value of defined benefit obligations or the fair value of plan assets (whichever is higher) are recorded in the income statement over the employees' expected average remaining working lives. These limits are calculated and applied separately for each defined benefit plan. Past-service costs are recognised immediately in income statement or amortised on a straight-line basis over the vesting period.

1.23.2 Share-based compensation

The Group operates long-term incentive (LTI) arrangements that are divided into five/six-year share plans. The potential reward is based on the performance of the

Group and its divisions. The reward is recognised as an expense during the vesting period with a corresponding increase in the liabilities and for the transactions settled in shares in the equity.

In the new LTI system (first plan started in 2008) the value of the share participation is defined after the three-year earning period when the participants are paid the earned rights in the form of shares (net of taxes and other employment-related expenses). Shares are placed in lock-up for two/three years during which the shares may not be sold, transferred, pledged or disposed in any other way.

The share plans under the new LTI system are accounted for partly cash- and partly equity-settled arrangements. The portion of the earned reward for which the participants will receive shares is accounted for as an equity settled transaction, and the portion of the earned reward to be settled in cash to cover tax and other charges payable by the participants, is accounted for as cash settled transaction.

Under the previous LTI system (last plan commenced in 2007) the fair value of the potential reward of outstanding share rights is measured based on the market value of the Fortum share initially when the share participation is defined and at each closing date after that. Estimated departures are taken into account when determining the fair value of the potential reward. The changes of the fair value of the potential reward are accrued over the remaining vesting period. A provision is recorded on the social charges related to the arrangement payable by the employer.

In order to hedge the Group against the changes in the fair values of the potential rewards under the previous LTI system the Group has entered into share forward transactions which are settled in cash. The forward transactions do not qualify for hedge accounting and therefore the periodic changes to their fair values are recorded in the income statement.

1.24 Provisions

Provisions for environmental restorations, asset retirement obligations, restructuring costs and legal claims are recognised when the Group has a present legal or constructive obligation as a result of past events to a third party, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

✚ *Regarding provisions for decommissioning and provision for disposal of spent fuel for nuclear production, see 1.25 below.*

1.24.1 Environmental provisions

Environmental provisions are recognised, based on current interpretation of environmental laws and regulations, when it is probable that a present obligation has arisen and the amount of such liability can be reliably estimated. Environmental expenditures resulting from the remediation of an existing condition caused by past

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operations, and which do contribute to current or future revenues, are expensed as incurred.

1.24.2 Asset retirement obligations

Asset retirement obligation is recognised either when there is a contractual obligation towards a third party or a legal obligation and the obligation amount can be estimated reliably. Obligating event is e.g. when a plant is built on a leased land with an obligation to dismantle and remove the asset in the future or when a legal obligation towards Fortum changes. The asset retirement obligation is recognised as part of the cost of an item of property and plant when the asset is put in service or when contamination occurs. The costs will be depreciated over the remainder of the asset's useful life.

1.24.3 Restructuring provisions

A restructuring provision is recognised when the Group has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement the plan or announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring, which are those amounts that are both necessarily entailed by the restructuring and not associated with the ongoing activities of the entity. Restructuring provisions comprise mainly of employee termination payments and lease termination costs.

1.25 Assets and liabilities related to decommissioning of nuclear power plants and the disposal of spent fuel

Fortum owns Loviisa nuclear power plant in Finland. Fortum's nuclear related provisions and the related part of the State Nuclear Waste Management Fund are both presented separately in the balance sheet. Fortum's share in the State Nuclear Waste Management Fund is accounted for according to IFRIC 5, *Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds* which states that the fund assets are measured at the lower of fair value or the value of the related liabilities since Fortum does not have control or joint control over the State Nuclear Waste Management Fund. The related provisions are the provision for decommissioning and the provision for disposal of spent fuel.

The fair values of the provisions are calculated by discounting the separate future cash flows, which are based on estimated future costs and actions already taken. The initial net present value of the provision for decommissioning (at the time of commissioning the nuclear power plant) has been included in the investment cost and is depreciated over the estimated operating time of the nuclear power plant. Changes in the technical plans et.c, which have an impact on the future cash flow of the estimated costs for decommissioning, are accounted for by discounting the additional costs to the current point in time. The increased asset retirement cost due to the increased provision is added to property, plant and equipment and

depreciated over the remaining estimated operating time of the nuclear power plant.

The provision for spent fuel covers the future disposal costs for fuel used until the end of the accounting period. Costs for disposal of spent fuel are expensed during the operating time based on fuel usage. The impact of the possible changes in the estimated future cash flow for related costs is recognised immediately in the income statement based on the accumulated amount of fuel used until the end of the accounting period. The related interest costs due to unwinding of the provision, for the period during which the spent fuel provision has been accumulated and present point in time, are also recognised immediately in the income statement.

The timing factor is taken into account by recognising the interest expense related to discounting the nuclear provisions. The interest on the State Nuclear Waste Management Fund assets is presented as financial income.

Fortum's actual share of the State Nuclear Waste Management Fund, related to Loviisa nuclear power plant, is higher than the carrying value of the Fund in the balance sheet. The legal nuclear liability should, according to the Finnish Nuclear Energy Act, be fully covered by payments and guarantees to the State Nuclear Waste Management Fund. The legal liability is not discounted while the provisions are, and since the future cash flow is spread over 100 years, the difference between the legal liability and the provisions are material.

The annual fee to the Fund is based on changes in the legal liability, the interest income generated in the State Nuclear Waste Management Fund and incurred costs of taken actions.

Fortum also has minority shareholdings in the associated nuclear power production companies Teollisuuden Voima Oyj (TVO) in Finland and directly and indirectly in OKG AB and Forsmarks Kraftgrupp AB in Sweden. The Group's interests in associated companies are accounted for by the equity method. Accounting policies of the associates regarding nuclear assets and liabilities have been changed where necessary to ensure consistency with the policies adopted by the Group.

✚ *For more information regarding nuclear related assets and liabilities, see Note 35 Nuclear related assets and liabilities on page 89.*

1.26 Contingent liabilities

A contingent liability is disclosed when there is a possible obligation that arises from events and whose existence is only confirmed by one or more doubtful future events or when there is an obligation that is not recognised as a liability or provision because it is not probable that an outflow of resources will be required or the amount of the obligation cannot be reliably estimated.

1.27 Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to the owners of the parent company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Group and held as treasury shares.

Diluted earnings per share is calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. For the warrants and stock options a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Fortum share) based on the monetary value of the subscription rights attached to outstanding stock options.

The number of shares calculated as above is deducted from the number of shares that would have been issued assuming the exercise of the stock options. The incremental shares obtained through the assumed exercise of the options and warrants are added to the weighted average number of shares outstanding.

Options and warrants have a dilutive effect only when the average market price of ordinary shares during the period exceeds the exercise price of the options or warrants. Previously reported earnings per share are not retroactively adjusted to reflect changes in price of ordinary shares.

1.28 Dividends

Dividends proposed by the Board of Directors are not recognised in the financial statements until they have been approved by the Company's shareholders at the Annual General Meeting.

1.29 Accounting for derivative financial instruments and hedging activities

Within the ordinary course of business the Group routinely enters into sale and purchase transactions for commodities. The majority of these transactions take the form of contracts that were entered into and continue to be held for the purpose of receipt or delivery of the commodity in accordance with the Group's expected sale, purchase or usage requirements. Such contracts are not within the scope of IAS 39. All other net-settled commodity contracts are measured at fair value with gains and losses taken to the income statement.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either: (1) hedges of highly probable forecast transactions (cash flow hedges); (2) hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge); or (3) hedges of net investments in foreign operations. The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Derivatives are divided into non-current and current based on maturity. Only for those electricity derivatives, which have cash flows in different years, the fair values are split between non-current and current assets or liabilities.

1.29.1 Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item will affect profit or loss (for instance when the forecast sale that is hedged takes place). However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory) or a liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability. When a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity is recognised in the income statement when the forecast transaction is ultimately also recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately recognised in the income statement.

1.29.2 Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss for the period to maturity.

1.29.3 Net investment hedging in foreign operations

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in equity; the gain or loss relating to the ineffective portion is recognised immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed of.

1.29.4 Derivatives that do not qualify for hedge accounting

Certain derivative instruments hedging future cash flows do not qualify for hedge accounting. Fair value changes of these financial derivative instruments are recognised in items affecting comparability in the income statement.

1.30 Fair value estimation

Fair value measurements are classified using a fair value hierarchy i.e. Level 1, Level 2 and Level 3 that reflects the significance of the inputs used in making the measurements.

✚ *Financial instruments that are measured in the balance sheet at fair value are presented according to fair value measurement hierarchy in the Note 21 Financial assets and liabilities by fair value hierarchy on page 76.*

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1.30.1 Fair values under Level 1 measurement hierarchy

The fair value of some commodity derivatives traded in active markets (such as publicly traded electricity options, coal and oil forwards) are market quotes at the closing date.

1.30.2 Fair values under Level 2 measurement hierarchy

The fair value of financial instruments including electricity derivatives traded in active markets (such as publicly traded derivatives, and trading and available for sale securities) is based on quoted market prices at the closing date. Known calculation techniques, such as estimated discounted cash flows, are used to determine fair value of interest rate and currency financial instruments. The fair value of interest-rate swaps is calculated as the present value of the estimated future cash flows.

The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the closing date. Fair values of options are determined by using option valuation models. The fair value of financial liabilities is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments. In fair valuation, credit spread has not been adjusted, as quoted market prices of the instruments used are believed to be consistent with the objective of a fair value measurement.

The Group bases the calculation on existing market conditions at each closing date. Financial instruments used in Fortum are standardised products that are either cleared via exchanges or widely traded in the market. Commodity derivatives are generally cleared through exchanges such as for example NASDAQ OMX Commodities Europe and financial derivatives done with creditworthy financial institutions with investment grade ratings.

1.30.3 Fair values under Level 3 measurement hierarchy

Fair valuation of electricity derivatives maturing over six years which are not standard NASDAQ OMX Commodities Europe products are based on prices collected from reliable market participants.

1.30.4 Other measurements

The nominal value less estimated credit adjustments of trade receivables and payables are assumed to approximate their fair values.

2 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results and timing may differ from these estimates. Below are areas where management's accounting estimates and judgements are most critical to reported results and financial position.

2.1 Intangible assets and property, plant and equipment acquired in a business combination

In an acquisition acquired intangible and tangible assets are fair valued and their remaining useful lives are determined. Management believes that the assigned values and useful lives, as well as the underlying assumptions, are reasonable, though different assumptions and assigned lives could have a significant impact on the reported amounts.

2.2 Impairment of property, plant and equipment and intangible assets

The Group has significant carrying values in property, plant and equipment as well as goodwill which are tested for impairment according to the accounting policy stated in Note 1 Accounting policies. The recoverable amounts of cash-generating units have been determined based on value in use calculations. These calculations are based on estimated future cash flows. Preparation of these estimates requires management to make assumptions relating to future expectations. Assumptions vary depending on the business the tested assets are in. For power and heat generation business the main assumptions relate to the estimated future operating cash flows and the discount rates used to present value them. The distribution business is regulated and supervised by national authorities. Estimated future cash flows include assumptions relating to the development of the future regulatory framework.

⊕ *Key assumptions used in goodwill impairment testing are discussed in Note 22 Intangible assets on page 77.*

The Group has not recognised any impairment losses in 2011 based on impairment testing done in late 2011.

⊕ *Impairment losses recognised during 2011 relating to specific items are presented in Note 5 Segment reporting on page 60, in Note 22 Intangible assets on page 77 and in Note 23 Property, plant and equipment on page 78.*

The Group has considered the sensitivity of the testing to changes in key assumptions. When doing this any consequential effect of the change on the other variables has also been considered. The calculations are most sensitive to changes in estimated future operating profit levels and discount rate. If the revised estimated operating profit before depreciation on 31 December 2011 was 10% lower than management's estimates or pre-tax discount rate applied to the discounted cash flows was 10% higher than management's estimates, the Group would not have recognised impairment losses for property plant and equipment or goodwill.

2.3 Deferred and income taxes

Fortum has deferred tax assets and liabilities which are expected to be realised through the income statement over the extended periods of time in the future. In calculating the deferred tax items, Fortum is required to make certain assumptions and estimates regarding the future tax consequences attributable to differences between the carrying amounts of assets and liabilities as recorded in the financial statements and their tax basis.

Assumptions made include the expectation that future operating performance for subsidiaries will be consistent with historical levels of operating results, recoverability periods for tax loss carry-forwards will not change, and that existing tax laws and rates will remain unchanged into foreseeable future. Fortum believes that it has prudent assumptions in developing its deferred tax balances.

The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

If the actual final outcome (regarding tax audits) would differ negatively from management's estimates with 10%, the Group would need to increase the income tax liability by EUR 8 million.

Most critical assumptions used by management relate to acquisitions, impairment testing of non-current assets and provisions

2.4 Liabilities related to nuclear production

The provision for future obligations for nuclear waste management including decommissioning of Fortum's nuclear power plant and related spent fuel is based on long-term cash flow forecasts of estimated future costs. The main assumptions are technical plans, timing, cost estimates and discount rate. The technical plans, timing and cost estimates are approved by governmental authorities.

Any changes in the assumed discount rate would affect the provision. If the discount rate used would be lowered, the provision would increase. Fortum has contributed cash to the State Nuclear Waste Management Fund based on a non-discounted legal liability, which leads to that the increase in provision would be offset by an increase in the recorded share of Fortum's part of the State Nuclear Waste Management Fund in the balance sheet. The total effect on the income statement would be positive since the decommissioning part of the provision is treated as an asset retirement obligation. This situation will prevail as long as the legal obligation to contribute cash to the State Nuclear Waste Management Fund is based on a non-discounted liability and IFRS is limiting the carrying value of the assets to the amount of the provision since Fortum does not have control or joint control over the fund.

➔ See Note 35 Nuclear related assets and liabilities on page 89.

2.5 Pension obligations

The present value of the pension obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. Any changes in these assumptions will impact the carrying amount of pension obligations.

➔ Assumptions used and sensitivity analysis for changes in major assumptions is presented in Note 37 Pension obligations on page 91.