IFRS-compliant accounting principles

Since 1 January 2005, Uponor Corporation has prepared its consolidated financial statements in compliance with the following accounting principles:

Main functions

Uponor is an international industrial Group providing housing and municipal infrastructure solutions. The Group's primary reporting segment consists of the following four geographical regions: Central Europe, Nordic, Europe – East, West, South, and North America. The secondary reporting segment comprises the housing solutions and the infrastructure and environment businesses.

Accounting principles

Uponor Group's consolidated financial statements are prepared in compliance with the International Financial Reporting Standards (IFRS), including International Accounting Standards (IAS) and the IFRIC interpretations valid on 31 December 2004. The financial statements are based on the historical cost convention unless otherwise specified in the accounting principles section below.

Until 31 December 2004, Uponor's consolidated financial statements were prepared in compliance with the Finnish Accounting Standards (FAS). Since FAS differs from IFRS in some respects, certain accounting, valuation and consolidation principles under FAS were adjusted for IFRS. Comparative data for 2004 were adjusted to reflect these changes.

Use of estimates

The preparation of consolidated financial statements under IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities on the date of financial statements, as well as the reported amounts of income and expenses during the report period. Although these estimates are based on the management's best knowledge of current events and actions, actual results may ultimately differ from those estimates.

Group accounting

The consolidated financial statements include the parent company, Uponor Corporation, and all companies in which the parent company holds more than half of the voting rights, either directly or through its subsidiaries. Subsidiaries acquired or established during the year are included as of the date of acquisition or establishment. Divested companies are included in the income statement until the date of divestment.

Subsidiaries include those companies in which Uponor Corporation has direct or indirect control of over 50 per cent of the voting rights or otherwise has power to govern the financial and operating policies. Intra-Group shareholdings are eliminated using the acquisition cost method. Accordingly, the assets and liabilities of an acquired company are measured at fair value on the date of acquisition, and the remaining difference between the acquisition cost and the equity capital constitutes goodwill. Based on the First-Time-Adoption of IFRS 1, any company acquisitions made prior to the IFRS transition date are not adjusted for IFRS, but the related amounts stated apply FAS. Whenever necessary, the accounting principles applied to the subsidiaries' financial statements are adjusted to correspond to those applied to consolidated financial statements. Intra-Group transactions, receivables, liabilities, unrealised gains and dividends between Group companies are eliminated in the consolidated financial statements.

Associated companies are entities over which the Group has 20–50 per cent of the voting rights, or over which the Group otherwise exercises significant influence. Joint ventures are entities in which the Group has contractually agreed to share the power to govern the financial and operating policies with another party or parties. Holdings in associated companies are included in the consolidated financial statements using the equity method. Accordingly, the share of the post-acquisition profits and losses of associated companies is recognised in the income statement to the extent of the Group's holding in the associated companies. Material differences in accounting conventions between the Uponor Group and its associated companies are eliminated before consolidation using the equity method. When the Group's share of losses of an associated company exceeds the carrying amount, it is reduced to nil and any recognition of further losses ceases, unless the Group has an obligation to satisfy the associated company's liabilities.

Minority interest is stated separately from Group shareholders' equity in the balance sheet and is also shown as a separate item in the consolidated income statement.

Foreign currency translations

Each company translates their foreign currency transactions into the local currency using the exchange rate on the transaction date. Outstanding receivables and payables in foreign currencies are stated using the exchange rates on the balance sheet date. Exchange rate gains and losses on actual business operations are treated as sales adjustment items or adjustment items to materials and services. Exchange rate gains and losses on financing are entered as financial income and expenses.

In the consolidated financial statements, the income statements of the Group's foreign subsidiaries are converted into euros using average exchange rates quoted for the report period. All balance sheet items are converted into euros using exchange rates quoted on the balance sheet date. The resulting conversion difference and other conversion differences resulting from the conversion of subsidiaries' equity are shown as increases and decreases in unrestricted equity. In addition, exchange rate differences in the loans granted by the parent company to foreign subsidiaries to replace their equity are treated as conversion differences in the consolidated financial statements. Realised conversion differences in connection with the redemption of material shares in subsidiaries are recognised as income in exchange-rate differences in the income statement.

Financial instruments

With respect to financial instruments, the Group applies the First-time Adoption of IFRS, which permits certain exceptions and exemptions to individual rules during the transition period. Financial instruments have been measured at fair value since 1 January 2005.

Financial assets and liabilities

Investments in debt and equity securities and in non-listed shares are classified as financial assets held for trading, held-to-maturity assets or available-for-sale assets, under IAS 39.

Changes in the fair value of trading assets and unrealised and realised gains and losses are included in the income statement in the period in which they occur. Changes in the fair value of available-for-sale assets are recognised in the fair value reserve under shareholders' equity. Changes in the fair value will be re-

entered from shareholders' equity to the income statement, when the asset is disposed of or it has lost its value to the extent that an impairment loss must be recognised for the asset.

Available-for-sale assets are measured at fair value based on market prices on the balance sheet date, or using the net present value method of cash flows, or another revaluation model. If an asset's fair value cannot be measured reliably, it will be measured at the lower of cost or net realisable value, if its value has been permanently impaired. Sales and purchases of assets are recognised on their trading date.

Held-to-maturity assets are measured, on an accrual basis, at cost using the effective interest rate method. Other financial assets and liabilities are measured at cost.

Derivative contracts

The Group companies use derivative contracts to decrease interest rate, currency or raw-material price risks. Derivative contracts are initially recognised in the balance sheet at cost and are subsequently re-measured at fair value on each balance sheet date. The fair value of forward rate agreements, interest-rate options, interest-rate swaps and forward exchange contracts is based on their market value on the balance sheet date or the present value of estimated future cash flows. The unrealised and realised gains and losses attributable to the changes in fair value are recognised in the income statement for the period in which they occur.

Segment information

The Group's primary reporting segment is based on geographical segments, in accordance with the Group's organisation. The risks and profits related to products and services by geographical segment differ from segment to segment because of different economic and operating environments. A secondary segment constitutes the housing solutions and infrastructure and environment businesses, whose products and services and related risks and profitability differ from each other.

Discontinued operation

A discontinued operation is formed once the company, according to a single co-ordinated plan, decides to dispose of a separate significant business unit, whose net assets, liabilities and financial results can be separated operationally and for financial reporting purposes. Profit/loss for the period by a discontinued operation and gains/losses on its disposal are shown separately in the consolidated income statement.

Income recognition

Sales of products are recognised as income once the risks and benefits related to ownership of the sold products have been transferred to the buyer, according to the agreed delivery terms, and the Group no longer has possession of, or control over, the products. Sales of services are recognised as income once the service has been rendered. Net sales comprise the invoiced value for the sale of goods and services net of indirect taxes, sales adjustment and exchange rate differences.

For long-term projects, income and expenses are recognised using the percentage of completion method provided that the percentage of completion and related income and expenses can be reliably estimated. When the Group is not able to meet those conditions, the policy is to recognise revenues only equal to costs incurred to date, to the extent of expected recoverable costs.

Research and development

Research costs are expensed as incurred. These are included in the consolidated income statement under other operating expenses. Development costs are capitalised as intangible assets for cases in which the IAS 38 capitalisation requirements are fulfilled. There were no capitalised development costs in the consolidated balance sheet on the transition date.

Pensions

The Group's pension schemes comply with each country's local rules and regulations. Pensions are based on actuarial calculations or actual payments to insurance companies. The Group applies defined contribution and defined benefit pension plans.

Within the defined contribution plan, pension contributions are paid directly to insurance companies and once the contributions have been paid, the Group has no further payment obligations. These contributions are recognised in the income statement for the accounting period during which such contributions are made.

Under the defined benefit plan, the pension obligation is the present value of future pension liabilities on the balance sheet date. The present value of future pension liabilities is the present value of current pension obligations less the fair value of the plan assets and any non-booked actuarial profits or losses. The pension liability is defined using the projected unit credit method. Costs resulting from the defined benefit pension plans are recognised as expenses for the remaining average period of employment, based on annual actuarial calculations.

Income taxes

Income taxes in the consolidated income statement comprise taxes based on taxable income recognised for the period by each Group company on an accrual basis, according to local tax regulations, including tax adjustments from the previous periods and changes in deferred tax. Deferred tax assets or liabilities are calculated using the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, using the tax rate effective on the balance sheet date. Deferred tax assets are recognised to the extent that it appears probable that future taxable profit will be available against which the temporary differences can be utilised.

Intangible assets

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the net assets of the acquired company on the date of acquisition. Goodwill is allocated to the cash generating units and is tested annually for any impairment. If a business' estimated future cash flow is lower than its goodwill on the balance sheet, the resulting impairment loss will be recognised as an expense in the income statement.

Other intangible assets

Other intangible assets, including trademarks, patents, copyrights and software licenses, are capitalised and amortised on a straight-line basis over their estimated useful lives.

Property, plant and equipment

Group companies' property, plant and equipment are stated at historical cost less straight-line depreciation and any impairment losses. Interest costs on borrowings to finance the construction of these assets are

capitalised as part of the cost during the period required to complete and prepare the property for its intended use.

Repair and maintenance costs are expensed as incurred.

Gains or losses on disposal, divestment or removal from use of property, plant and equipment are based on the difference between the net gains and the balance sheet value. Gains are shown under other operating income.

Investment property

Investment property is defined as property the Group holds for long-term rental yields or capital appreciation. Investment property is measured at cost, such as other tangible assets, less depreciation and any impairment losses. The balance sheet values of investment property are continuously reviewed for any impairment. Investment property's fair value is presented in the notes to the balance sheet.

Depreciation on property, plant and equipment

Property, plant and equipment are shown at planned residual value in the balance sheet. Residual values are based on the acquisition cost less accrued depreciation. Planned depreciation is calculated on a straight-line basis on the acquisition cost over the asset's expected useful life as follows:

	Years
Buildings	20–40
Production machinery and equipment	8–12
Other machinery and equipment	5–15
Office and outlet furniture and fittings	5–10
Transport equipment	5–7
Non-current assets	5–10

Government grants

Any grants received for the acquisition of intangible or tangible assets are deducted from the asset's acquisition cost and recorded on the income statement to reduce the asset's depreciation. Other grants are recognised as income for the periods during which the related expenses are incurred.

Impairment

The balance sheet values of assets are assessed for impairment on a regular basis. Should any indication of an impaired asset exist, the asset's recoverable amount is the asset's net selling price or its value in use, whichever is higher. In determining the value in use, the estimated future cash flows are discounted at their present day value, based on such interest rates corresponding to the cash generating unit's average return on investment. Whenever the asset's carrying amount exceeds its recoverable amount, it is impaired, and the resulting impairment loss is recognised in the income statement. An impairment reversal of property, plant and equipment and other intangible assets, excluding goodwill, will be recognised, if circumstances give rise to the reversal, or the recoverable amount has changed from the date the impairment loss was recognised. Impairment is not reversed over the balance sheet value that existed before the recognition of impairment losses in the previous financial periods. Any impairment loss on goodwill is not reversed.

Impairment tests required by the transition-period standards were conducted for goodwill on the IFRS transition date of 1 January 2004.

Leases

Lease liabilities, which expose the Group to risks and rewards inherent in holding such leased assets, are classified as finance leases. These are recognised under tangible assets on the balance sheet and measured at the lesser of the fair value of the leased property at the inception of the lease or the present value of the minimum lease payments. Similarly, lease obligations, from which financing expenses are deducted, are included in interest bearing liabilities. Financing interests are recognised in the income statement during the lease period. An asset acquired under finance lease is depreciated over its useful life or within the shorter lease term.

Leases, which expose the lessor to risks and rewards inherent in holding such leases, are classified as other leases. These rents are recognised as expenses during the lease period.

The assets leased by the Group, where the lessee bears the risks and rewards inherent in holding such leases, are treated as finance leases and recognised as receivables on the balance sheet at their present value.

Inventories

Inventories are stated at the lower of cost or net likely realisable value, based on the FIFO principle . The likely realisable value is the price received on the date of sale, less expenses. In addition to the cost of materials and direct labour, an appropriate proportion of production overheads are included in the inventory value of finished products and work in progress.

Accounts receivable

Accounts receivable are carried at original invoice amount less provision made for impairment of these receivables. A provision for impairment of accounts receivable is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

Liquid assets

Liquid assets comprise cash and cash equivalents and other short-term investments, whose maturity does not exceed three months. Cheque account overdrafts are included in the short-term interest-bearing liabilities on the balance sheet.

Liabilities

Direct transaction expenses due to loans, clearly linked to a specific loan, are included in the loan's original cost on an accrual basis and recognised as interest expenses using the effective interest method.

Provisions

Provisions are recognised when the Group has a present legal obligation as a result of past practice or events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Provisions can include warranty provisions, closure or restructuring costs and onerous contracts. Changes in provisions are included in relevant expenses on the income statement.

Management incentive scheme

In May 2004, Uponor Corporation's Board of Directors approved a new incentive scheme, whereby the Executive Committee can receive a share-based reward in 2007. The reward is based on the fulfilment of a set cumulative operating profit target for 2004–2006. The maximum net value of the reward amounts to

the value of 80,000 Uponor shares. According to IFRS 2, the portion given as shares is measured at the share price quoted on the day of granting. Fair value is recognised as a cost on an accrual basis for the expected revenue period similar to an amount paid out in cash. Any changes in the value after the date of granting are recognised as income using the closing price of each calendar month.

Treasury shares

The parent company held treasury shares during the financial year and the comparative period. These are eliminated from the parent company's and the Group's shareholders' equity and hold no balance sheet value. Treasury shares are not taken into account in calculating key figures and ratios.

Earnings per share

Earnings per share are calculated by dividing the profit for the period by the average number of shares for each period. The average number of bought-back shares is deducted from the average number of outstanding shares. The weighted average number of shares used to calculate the diluted earnings per share takes into account the diluting effect of outstanding stock options during the period.

Dividends

Dividends paid by the Group are recognised for the period during which their payment is approved by the Group's shareholders.