HRVATSKA ELEKTROPRIVREDA d.d. Zagreb

Consolidated annual financial statements and

Independent Auditor's Report

for the year 2017

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Responsibility for the consolidated financial statements

The Management Board of the company Hrvatska Elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37, (hereinafter: "the Company") is responsible for ensuring that the consolidated annual financial statements for the year 2017, are prepared in accordance with the Accounting Act (Official Gazette No 78/15, 120/16) and International Financial Reporting Standards, to give a true and fair view of the consolidated financial position, the consolidated results of operations, consolidated changes in equity and consolidated cash flows of the Company for that period.

After making enquiries, the Board has a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, the Board has adopted the going concern basis in preparing the consolidated annual financial statements of the Company.

In preparing the consolidated annual financial statements, the Management is responsible for:

- selection and consistent application of suitable accounting policies in accordance with the applicable financial reporting framework;
- giving reasonable and prudent judgments and estimates; and
- using the going concern basis of accounting, unless it is inappropriate to presume so.

The Management is responsible for keeping the proper accounting records, which at any time with reasonable certainty present the consolidated financial position, the consolidated results of operations, consolidated changes in equity and consolidated cash flows of the Company, and also their compliance with the Accounting Act and the International Financial Reporting Standards. The Management is also responsible for safe keeping the assets of the Company and also for taking reasonable steps for prevention and detection of fraud and other irregularities.

Signed for and on behalf of the Management Board:

Marko Ćosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

HRVATSKA ELEKTROPRIVREDA d.d.
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INDEPENDENT AUDITOR'S REPORT

To the Shareholder of the company Hrvatska elektroprivreda d.d.

Report on the audit of the consolidated annual financial statements

Opinion

We have audited the consolidated annual financial statements of the company Hrvatska elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37 (the "Company" or the „Group") for the year ended 31 December 2017, which comprise the consolidated Statement of financial position (consolidated Balance Sheet) as at 31 December 2017, consolidated Income Statement, consolidated Statement of other comprehensive income, consolidated Statement of changes in equity and consolidated Statement of cash flows of the Company for the year then ended, and Notes to the consolidated financial statements, including a summary of significant accounting policies and other explanations.

In our opinion, the accompanying consolidated annual financial statements give a true and fair view of the financial position of the Company as at 31 December 2017, and of its consolidated financial performance and consolidated cash flows of the Company for the year then ended in accordance with the Accounting Act and the International Financial Reporting Standards (the "IFRS"), determined by the European Commission and published in the Official Journal of the EU.

Basis for Opinion

We conducted our audit in accordance with Accounting Act, Audit Act and International Auditing Standards (ISAs). Our responsibilities under those standards are further described in our Independent Auditor's report under section *Auditor's responsibilities for the audit of the consolidated annual financial statements*. We are independent of the Company in accordance with the Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of matter

As described in the Note 29 to the consolidated financial statements, at 31 December 2017, the Company stated clearing debt liability in the amount of HRK 755,189 thousand (31 December 2016: HRK 863,450 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of Finance for the use of funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the Company and the Ministry of Finance regarding the clearing debt, until the issuance of our Independent Auditor's Report it has not been clearly defined whether it relates to a loan or a some other legal transaction. Our opinion has not been modified in this respect.

As described in the Note 35 to the consolidated financial statements, provisions of the Water Management Act that came into force on 1 January 2010, raised a question on the ownership and legal status of the Company's property - reservoirs and ancillary facilities, used for generation of electricity from hydropower plants. Pursuant to the Water Act those property is defined as "Public water resources in general use as the property in ownership of the Republic of Croatia". The Republic of Croatia initiated several proceedings for registration of title to those properties, part of which were ruled in favour of the Republic of Croatia, part of them were rejected by the relevant courts, and part of them are in still in progress. The Company has filed a motion to the Constitutional Court for review of the constitutionality of Article 23 Paragraph 4 of the Water Act and for the cancelation of the same. During 2015, the Ministry of Agriculture has initiated the procedure for amendment and change of the Water Act, and the Ministry of Economy has also submitted its consent to the initiative of the Company for change and amendment of the Water Act. During 2016 and 2017, the Company continued activities with relevant Ministries and Institutions on the above-mentioned issue. Our opinion has not been modified in this respect.

Other matters

Attention is drawn to Note 35 to the financial statements with a listed web site where, in accordance with point (b), paragraph 8 Article 21a of Labour Act, the separate non-financial statement of the Company will be published no later than 6 months from the date of the consolidated balance sheet. Our opinion has not been modified in this respect.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated annual financial statements for the current period and include the recognized most significant risks of significant misstatement due to error or fraud with the greatest impact on our audit strategy, the allocation of our available resources, and the time spent by the engaged audit team. These matters were addressed in the context of our audit of the consolidated annual financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have determined the matters described below to be the key audit matters to be communicated in our Independent Auditor's report.

Key Audit Matter	How we addressed these key audit matters
Recognition of revenues from electricity sales to customers of universal service (household customers) Revenues from the sale of electricity are recognized on the basis of the best estimate of the delivered energy quantity. As the actual calculation of the delivered volume of energy to customers of the household category is performed twice a year, the Group's electricity sales revenue is based on the total generated and purchased quantities of energy on the distribution network. By doing so, the total generated and purchased amount of energy is corrected for losses on the distribution network based on logarithmic regression. After analysing several different approximation methods (five-year average, linear approximation and similar), the Management Board of the Company selected logarithmic regression as the most suitable one. The correction of household income as at 31 December 2017 was obtained by calculating the logarithmic curve using losses in the network of 7.71%, while for the year ended on 31 December 2016, the percentage of losses used in the calculation was 7.87% . The result is an increase in revenues for 2017 in the amount of HRK 53,177 thousand compared to the previous year, and stated liability for accrued income in the amount of HRK 31,099 thousand. We focused on this area because it involves significant estimates of the recognition of electricity sales revenue at the reporting date. **Related disclosures in the consolidated annual financial statements** See Notes 2, 3, 22 and 33 in the accompanying consolidated annual financial statements.	**Our auditing procedures related to these matters included, among others:** - Obtaining an understanding of key management controls related to estimating electricity sales revenue - Assessing the reasonableness of the key assumptions used in the estimation model, including the quantities of electricity sold and the price - Testing the mathematical accuracy of the model of estimation of electricity sales revenue - Engaging an IT expert to assess system reliability and internally make an independent estimate of unrecorded revenue using data on quantities and prices received by the Group, and we have compared such results with the Group's revenue estimate. We also evaluated the adequacy of the Company's disclosure regarding the recognition of revenues from the sale of electricity to customers of universal service (household customers). The results of our tests were satisfactory.

Key Audit Matter	How we addressed these key audit matters
Leal disputes and continent liabilities Given that the Group is exposed to significant legal claims, we have focused our attention on this area. Any liabilities disclosed or disclosed contingent liabilities, or non-disclosures in the financial statements, are inherently uncertain and depend on a number of significant assumptions and judgments. These are potentially significant amounts in which the determination of the amount for disclosure in the financial statements, if applicable, is subject to a subjective assessment. According to that, Management Board estimates future outcomes and amounts of contingent liabilities that may arise as a result of these claims. **Related disclosures in the consolidated annual financial statements** See Notes 2, 3 and 28 in the accompanying consolidated annual financial statements.	**Our auditing procedures related to these matters included, among others:** - Receiving and analysing the attorneys response to our written inquiries addressed to attorneys and considering certain issues with them; - Critical review of the assumptions used and estimates pertaining to the claims. This includes assessing the probability of unfavourable outcomes of court proceedings and the reliability of the assessment of the related amount of obligation; - Assessing the adequacy of disclosure in the financial statements, taking into account sensitivity and possible prejudice in the disclosure of detailed information. Based on the collected evidence, taking into account inherent uncertainty in legal issues, we agree with the Company's management's assessment of the probability of future significant outflows related to these issues. We have found that issues that are likely to become future outflows are stated as provisions. Furthermore, we assessed the adequacy of the Company's disclosure regarding Contingent liabilities and court disputes. The results of our testing were satisfactory.

Other information in the Annual Report and separate nonfinancial report.

The Management Board is responsible for other information. Other information contain the information included in the Annual Report but does not include the annual consolidated financial statements and our Independent Auditor's Report of those we received prior to the date of this Independent Auditor's Report and the separate non-financial report that we expect will be made available after that date.

Our opinion on the annual consolidated financial statements does not include any other information, except to the extent expressly stated in our Independent Auditor's Report under the heading *Report on Other Legal Requirements*, and we do not express any form of conclusion thereon.

In connection with our audit of annual consolidated financial statements, it is our responsibility to read other information and, in doing so, to consider whether other information is significantly contradictory to annual consolidated financial statements, or our knowledge acquired in the audit or otherwise appears to have been significantly misrepresented, and whether a separate non-financial report presents the non-financial information required by the provisions of paragraph 1 or paragraph 2 of Article 21a of the Accounting Act. If, based on the work we've done, we conclude that there is a significant misstatement of these other information, we are required to report this fact. In that sense, we have nothing to report.

When we read a separate nonfinancial report, if we find that there is a significant misstatement in it, we are required to report it to those in charge of managing the Company.

Responsibilities of the Management and Those Charged with Governance for the consolidated annual financial statements

The Management is responsible for the preparation of consolidated annual financial statements that give a true and fair view in accordance with IFRS, as determined by the European Commission and published in the Official Journal of the EU; and for such internal control as management determines is necessary to enable the preparation of consolidated annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated annual financial statements, the Management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the audit of the consolidated annual financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated annual financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated annual financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the auditin in order to design auditing procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.
- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated annual financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of

our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated annual financial statements, including the disclosures, and whether the consolidated annual financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and that we will communicate with them all relationships and other matters that may reasonably be considered to influence our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated annual financial statements of the current period and are therefore the key audit matters. We describe these matters in our Independent Auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our Independent Auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal requirements

Report based on the requirements of Regulation (EU) No. 537/2014

On 8 June 2017, we were appointed by the General Assembly of the Company to audit the consolidated annual financial statements for 2017.

At the date of this Report, we have been continuously engaged in carrying out the Company's statutory audits of the Company's consolidated annual financial statements from 2012, up to the revision of the Company's annual financial statements for 2017, total of 6 years.

In addition to the issues we have mentioned in our Independent Auditor's Report as Key Audit Issues (Emphasis of Matter), we do not have anything to report in relation with point (c) of Article 10 of Regulation (EU) No. 537/2014.

Through our statutory audit of the Company's consolidated annual financial statements for the year 2017, we are able to detect irregularities, including fraud in accordance with Section 225, Responding to Non-Compliance with Laws and Regulations of the IESBA Code of Conduct, which requires us to, during our audit engagements, see if the Company has complied with laws and regulations which are generally recognized to have a direct impact on the determination of significant amounts and disclosures in annual financial statements, as well as other laws and regulations that do not have a direct effect on the determination of significant amounts and disclosures in the annual financial statements, but compliance with which may be crucial for operational aspects of the Company's business, its ability to continue as a going concern, or to avoid significant penalties.

Except where we encounter or gain knowledge about the non-compliance of any of the aforementioned laws or regulations that is apparently insignificant, in our judgment of its content and its influence, financially or otherwise, for the Company, its stakeholders and the general public, we are obliged to inform the Company and ask it to investigate this case and take appropriate measures to resolve the irregularities and to prevent the reappearance of these irregularities in the future. If the Company, at the audited consolidated balance sheet date, does not correct any irregularities that result in misstatements in the audited consolidated annual financial statements that are cumulatively equal to or greater than the amount of significance for the financial statements as a whole, we are required to modify our opinion in an Independent Auditor's Report.

In the audit of the annual financial statements of the Company for the year 2017, we have determined the significance for the annual financial statements, as a whole, in the amount of HRK 201,861 thousand, which represents about 1.5% of the total sales revenues of the Company, considering sinificant fluctuations of profit before taxation in previous and current period.

Our audit opinion is consistent with the additional report for the Company's auditing board, prepared in accordance with the provisions of Article 11 of Regulation (EU) No. 537/2014.

During the period between the initial date of the audited consolidated annual financial statements of the Company for the year 2017 and the date of this report, we did not provide the Company or its dependent companies, with prohibited non-scheduled services, and in the business year prior to the aforementioned period, did not provide services for the design and implementation of internal control procedures or risk management related to preparation and/or control of financial information or the design and implementation of technological systems for financial information, and we have maintained independence in relation to the Company and its dependent companies during the performance of the audit.

Report pursuant to the requirements of the Accounting Act

The Management is responsible for the preparation of the Management report as part of the Annual report of the Company and we are obliged to express an opinion on the compliance of the Management report as part of the Annual report of the Company with the consolidated annual financial statements of the Company. In our opinion, based on the work that we performed during the audit, information in the Management report for 2017, as part of the Annual report of the Company for the year 2017, are in accordance with the financial information stated in the consolidated annual financial statements of the Company set out on pages 10 to 92 on which we expressed our opinion as stated in the Opinion section above.

In our opinion, based on the work that we performed during the audit, the Company's Management report for 2017, which is an integral part of the Company's Annual report for 2017, is prepared in accordance with the Accounting act.

Based on the knowledge and understanding of the Company and its environment obtained while performing the audit, we have not found that there are material misstatements in the Company's Management report for 2017 which is an integral part of the Company's Annual report for 2017.

In our opinion, based on the work that we performed during the audit, the Statement that the code of corporate governance is applied, included in the Annual report for 2017, is in accordance with the requirements of article 22, paragraph 1, points 3 and 4 of the Accounting Act.

The Statement that the code of corporate governance is applied, included in the Annual report for 2017, includes information from article 22, paragraph 1, points 2, 5 and 6 of the Accounting Act.

The Management is responsible for the preparation of consolidated annual financial statements for the year ended 31 December 2017 in prescribed form based on the Statute of structure and content of annual financial statements (Official Gazette 95/16) and in accordance with other regulations governing the operations of the Company ("Standard consolidated annual financial statements"). Financial information presented in the Company's standard consolidated annual financial statements are in accordance with the information presented in the Company's consolidated annual financial statements given on pages 10 to 92 on which we expressed our opinion as stated in the section Opinion above.

The engagement partner on the audit of consolidated annual financial statements of the Company for 2017, resulting in this Independent auditor's report is Vedrana Stipić, certified auditor.

Zagreb, 27 April 2018

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Jeni Krsticević, President of the Management Board

VStipić

Vedrana Stipić, Certified Auditor

Consolidated Income Statement

For the year ended 31 December 2017

	Notes	2017 In HRK '000	2016 In HRK '000
Revenue from electricity sales	4	11,493,664	10,831,456
Revenue from thermal power sales	4	683,264	699,596
Revenue from sale of gas on wholesale market	4	963,887	1,102,728
Revenue from sale of gas to customers	4	316,576	341,812
Sales revenue		***13,457,391***	***12,975,592***
Other operating income	5	1,511,894	1,424,766
Total operating income		**14,969,285**	**14,400,358**
Electricity purchase cost	6	(2,786,423)	(2,148,249)
Fuel cost	6	(1,903,145)	(1,548,033)
Costs of gas sold	6	(1,130,144)	(1,246,442)
Staff cost	7	(1,946,892)	(1,904,443)
Depreciation and amortization costs	11,12	(1,935,963)	(1,780,269)
Other operating expenses	8	(2,971,895)	(3,049,765)
Total operating expenses		**(12,674,462)**	**(11,677,201)**
Operating profit		**2,294,823**	**2,723,157**
Financial income	9	235,826	232,873
Financial expenses	9	(939,913)	(365,669)
Net loss from financial activities		**(704,087)**	**(132,796)**
Profit before taxation		**1,590,736**	**2,590,361**
Corporate income tax expense	10	(290,437)	(545,359)
Profit for the year		**1,300,299**	**2,045,002**
Attributable to:			
Owners of the Parent Company		1,300,299	2,045,002

The accompanying notes form an integral part of these consolidated financial statements.

Signed on behalf of the Company on 27 April 2018:

Marko Ćosić
Member

Nikola Rukavina
Member

Petar Sprčić
Member

Tomislav Šambić
Member

Saša Dujmić
Member

Frane Barbarić
President

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Consolidated Statement on other comprehensive income

For the year ended 31 December 2017

	2017 In HRK '000	2016 In HRK '000
Profit for the year	**1,300,299**	**2,045,002**
Other comprehensive income		
Exchange differences from translation of foreign operations	(15,609)	(18,984)
Net profit/(loss) from financial assets available for sale	(3,565)	39,457
Reserves	25,514	-
Total other comprehensive income to be reclassified to income/(loss)	6,340	20,473
Other comprehensive income, net	**6,340**	**20,473**
Total comprehensive income for the year, net	**1,306,639**	**2,065,475**
Total comprehensive income attributable to:		
Owners of the Parent Company	1,306,639	2.065,475

The accompanying notes form an integral part of these consolidated financial statements.

Signed on behalf of the Company on 27 April 2018:

Marko Ćosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

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ASSETS	Note	31 Dec 2017	31 Dec 2016
		In HRK '000	In HRK '000
Non-current assets			
Property, plant and equipment	11	28,590,553	28,093,856
Assets under construction	11	2,442,559	2,677,233
Intangible assets	12	210,502	157,586
Investment property	13	305,630	231,491
Prepayments for property, plant and equipment	14	15,252	36,707
Long-term loans and deposits	17	36,107	28,973
Available-for-sale and other investments	18	284,443	295,938
Other non-current assets	19	42,918	46,941
Deferred tax assets	10	610,389	555,461
Total non-current assets		**32,538,353**	**32,124,186**
Current assets			
Inventories	20	1,257,292	1,405,368
Trade receivables	21	2,081,000	1,953,592
Other short-term receivables	22	957,817	730,917
Cash and cash equivalents	23	2,017,095	3,018,846
Total current assets		**6,313,204**	**7,108,723**
TOTAL ASSETS		**38,851,557**	**39,232,909**

EQUITY AND LIABILITIES	Note	31 Dec 2017 In HRK '000	31 Dec 2016 In HRK '000
Share capital	24	19,792,159	19,792,159
Reserves	24	162,242	140,293
Retained earnings	24	6,041,625	5,551,226
Total equity		**25,996,026**	**25,483,678**
Liabilities under issued bonds	25	3,595,828	3,606,173
Long-term loan liabilities	26	265,895	664,764
Long-term liabilities to the State	27	13,065	15,901
Long-term provisions	28	1,018,467	930,700
Other long-term liabilities	29	4,356,607	4,190,347
Deferred tax liabilities		24,305	26,007
Total non-current liabilities		**9,274,167**	**9,433,892**
Trade payables	30	1,643,033	1,787,338
Current portion of long-term bonds issued	25	-	586,601
Current portion of long-term loans	26	408,481	411,832
Taxes and contributions	31	80,202	157,750
Interests payable		35,593	42,569
Liabilities to employees	32	274,173	155,269
Other non-current liabilities	33	1,139,882	1,173,980
Total non-current liabilities		**3,581,364**	**4,315,339**
TOTAL EQUITY AND LIABILITIES		**38,851,557**	**39,232,909**

The accompanying notes form an integral part of these consolidated financial statements.

Signed on behalf of the Company on 27 April 2018:

Marko Ćosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

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	Share capital	Reserves	Retained earnings / (Transferred loss)	Total equity
	In HRK '000	In HRK '000	In HRK '000	In HRK '000
Balance at 1 January 2016	**19,792,159**	**100,836**	**4,132,208**	**24,025,203**
Profit for the year	-	-	2,045,002	2,045,002
Other comprehensive income	-	39,457	(18,984)	20,473
Total comprehensive income	-	*39,457*	*2,026,018*	*2,065,475*
Pay-out of the dividends to the Owner	-	-	(607,000)	(607,000)
Balance at 31 December 2016	**19,792,159**	**140,293**	**5,551,226**	**25,483,678**
Profit for the year	-	-	1,300,299	1,300,299
Other comprehensive income	-	21,949	(15,609)	6,340
Total comprehensive income	-	*21,949*	*1,284,690*	*1,306,639*
Pay-out of the dividends to the Owner	-	-	(794,291)	(794,291)
Balance at 31 December 2017	**19,792,159**	**162,242**	**6,041,625**	**25,996,026**

The accompanying notes form an integral part of these consolidated financial statements.

Signed on behalf of the Company on 27 April 2018:

Marko Ćosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

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	2017	2016
	In HRK '000	In HRK '000
OPERATING ACTIVITIES		
Profit for the year	1,590,736	2,590,361
Net losses of financial activities	213,512	235,218
Fair value of property investment	(7,654)	5,287
Impairment of tangible assets	277,534	108,256
Depreciation of property, plant and equipment and intangible assets	1,935,733	1,780,269
Value adjustment of receivables	(60,756)	(149,202)
Value adjustment of inventories	7,217	13,353
Income from reversal of asset impairment	(199,207)	-
Impairment of tangible fixed assets	39,630	-
Increase/(Decrease in provisions	87,767	(38,801)
Cash flow from operating activities before chanes in working capital	*3,884,512*	*4,544,741*
(Increase)/Decrease in trade receivables	(66,652)	42,673
Decrease in inventories	140,859	70,568
DEcrease/(Increase) in other fixed assets	32,998	(105,717)
(Increase) / decrease in other short-term assets	(226,900)	163,636
(Decrease) / increase in trade payables	(144,305)	46,428
Increase in other short-term liabilities	13,461	258,817
Increase / (decrease) in other long-term liabilities	143,013	(224,969)
Cash generated from operations	**3,776,986**	**4,796,177**
Corporate income tax payed	(386,170)	(553,691)
Interest paid	(230,788)	(244,612)
NET CASH FROM OPERATING ACTIVITIES	**3,160,028**	**3,997,874**
INVESTING ACTIVITIES		
Interest received	44,902	49,335
Expenses for purchase of property, plant and equipment	(2,431,933)	(2,589,126)
Disposal of property, plant and equipment	-	2,392
NET CASH FROM INVESTING ACTIVITIES	**(2,387,031)**	**(2,537,399)**

	2017 In HRK '000	2016 In HRK '000
FINANCING ACTIVITIES		
Long-term loans received	12,149	147,623
Repayment of long-term loans	(408,099)	(382,038)
Repayment of issued bonds	(584,507)	(93,380)
Dividends paid	(794,291)	(607,000)
NET CASH FROM FINANCING ACTIVITIES	**(1,774,748)**	**(934,795)**
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	**(1,001,751)**	**525,680**
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	**3,018,846**	**2,493,166**
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	**2,017,095**	**3,018,846**

The accompanying notes form an integral part of these consolidated financial statements.

Signed on behalf of the Company on 27 April 2018:

Marko Čosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

HRVATSKA ELEKTROPRIVREDA d.d.
ZAGREB 3.2
Ulica grada Vukovara 37

1. GENERAL

Hrvatska elektroprivreda Group, Zagreb (hereinafter: the "Group") consists of the parent company Hrvatska elektroprivreda d.d., Zagreb (hereinafter: "HEP d.d." or the "Company") and the subsidiaries listed in the Note 36.

HEP d.d. is registered in Zagreb, Ulica grada Vukovara 37. The principal activities of the Group are generation, transmission and distribution of electricity, and the control of the electric power systems. In addition to main activities, HEP Group also produces and distributes thermal power through the district heating systems in Zagreb and Osijek, sale of gas on the wholesale market, and the distribution of gas in Osijek and Đakovo. All of the Group's activities are governed by applicable laws, regulations and decisions issued by the Croatian Government. As at 31 December 2017 the Group employed 11,894 employees (2016: 11,832), excluding Krško Nuclear Power Plant which employed 608 employees (2016: 617).

These consolidated financial statements are presented in Croatian Kuna as the Company's functional currency.

Laws regulating the energy sector

On 19 October 2012, the Croatian Parliament passed the Energy Act and the Law on Regulation of Energy Activities and on 8 February 2013 the Electricity Market Act. The Gas Market Act was passed on February 22, 2013, and the Heat Market Act on June 21, 2013. On October 17, 2014, the Croatian Parliament passed the Energy Efficiency Act, on September 10, 2015, the Law on Renewable Energy Sources and Highly Effective Cogeneration, and on September 18, 2015, the Law on Amendments to the Electricity Market Act. On February 17, 2017, the Croatian Parliament passed the Law on Amendments to the Gas Market Law.

The new laws and accompanying by-laws, in line with EU directives and directives, have been further restructured and are aligned the Group's operations. According to the provisions of the Electricity Market Act and the Act on Amendments to the Electricity Market Act, the Company and its subsidiaries continue to perform electricity activities carried out as public electricity services in the Republic of Croatia: electricity transmission, distribution of electricity and electricity supply which is performed as a universal service and as a guaranteed service. Electricity generation, electricity supply and electricity trade are performed as market activities as defined in the laws regulating energy activities and trading on the energy market.

Pursuant to the Electricity Market Act, each customer has the right to a free choice of supplier, and household category customers have the right to supply of electricity as a universal service. Customers who have not exercised the right to choose a supplier or are left without suppliers are using a guaranteed supply service. Electricity supply is conducted according to the rules regulating market relations and energy companies are free to contract the amount and price of electricity delivered. Electricity supply that is performed as a guaranteed service is performed as a public service under regulated conditions to non-household customers, who under certain conditions remain without the supplier.

1. GENERAL (continued)

Electricity supply that is performed as a universal service is performed as a public service to household customers who are entitled to such supply and are free to choose or use it automatically. Parts of household customers have used the right to choose suppliers.

The Company and its subsidiaries align the Group's organization in accordance with the amended laws and deadlines prescribed by these laws.

In September 2015, the Croatian Energy Regulatory Agency (HERA) adopted the methodology for determining the amount of tariff items for electricity distribution and the methodology for determining the amount of tariff items for electricity transmission, and in December 2015, had determined the amount of tariff items for electricity distribution and determined the amount of tariffs for electricity transfers to be applied from 1 January 2016.

Since the Act on Amendments to the Electricity Market Act is in force, the decision on the amount of tariff items for the supply of electricity within the universal service is made by HEP Operator Distribucijskog Sustava d.o.o. or HEP Elektra d.o.o. from 2 November 2016. In accordance with the provisions of the Electricity Market Act, on December 17, 2013, HERA adopted a Methodology for determining the amount of tariff items for guaranteed electricity supply. Customers who are supplied with electricity in a guaranteed supply from 1 July 2014 pay the supply b the tariff items in accordance with the HERA decisions on the amount of tariff items for guaranteed electricity supply.

1. GENERAL (continued)

General Assembly

The General assembly consists of the members representing the interests of one shareholder – the Republic of Croatia:

Tomislav Panenić	Member	Member from 4 March 2016 to 25 January 2017
Zdravko Marić	Member	Member from 26 January 2017 to 14 February 2018
Tomislav Ćorić	Member	Member from 15 February 2018

Supervisory Board

Members of Supervisory Board in 2017

Nikola Bruketa	President	President from 23 February 2012 to 6 December 2017
Goran Granić	President	President since 1 January 2018
Žarko Primorac	Member	Member from 23 February 2012 to 6 December 2017
Ivo Uglešić	Member	Member from 23 February 2012 to 6 December 2017
Igor Džajić	Member	Member from 19 September 2012 to 6 December 2017
Mirko Žužić	Member	Member from 19 September 2012 to 6 December 2017
Juraj Bukša	Member	Member from 5 June 2014 to 6 December 2017
Dubravka Kolundžić	Member	Member from 1 July 2015 to 11 January 2018
Goran Granić	Member	Member from 7 December 2017 to 31 December 2017
Marko Primorac	Member	Member from 7 December 2017
Jelena Zrinski Berger	Member	Member from 7 December 2017
Višnja Komnenić	Member	Member from 11 January 2018

Members of Supervisory Board in 2016

Nikola Bruketa	President	President from 23 February 2012
Žarko Primorac	Member	Member from 23 February 2012
Ivo Uglešić	Member	Member from 23 February 2012
Igor Džajić	Member	Member from 19 September 2012
Mirko Žužić	Member	Member from 19 September 2012
Juraj Bukša	Member	Member from 5 July 2014
Dubravka Kolundžić	Member	Member from 1 June 2015

1. GENERAL (continued)

Management Board

Management Board in 2017

Perica Jukić	President	President from 12 September 2014 to 31 December 2017
Zvonko Ercegovac	Member	Member from 23 February 2012 to 31 December 2017
Tomislav Rosandić	Member	Member from 2 January 2015 to 31 December 2017
Saša Dujmić	Member	Member from 4 December 2014 to 31 December 2017
Frane Barbarić	President	President since 1 January 2018
Nikola Rukavina	Member	Member since 1 January 2018
Marko Ćosić	Member	Member since 1 January 2018
Petar Sprčić	Member	Member since 1 January 2018
Tomislav Šambić	Member	Member since 1 January 2018
Saša Dujmić	Member	Member since 1 January 2018

Management Board in 2016

Perica Jukić	President	President from 12 September 2014
Zvonko Ercegovac	Member	Member from 23 February 2012
Tomislav Rosandić	Member	Member from 2 January 2015
Saša Dujmić	Member	Member from 4 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the Group's significant accounting policies which have been applied consistently in the current and previous years is set out below.

Presentation of the consolidated financial statements

The consolidated financial statements for 2017 have been prepared in accordance with the Accounting Act (Official Gazette 78/15, 120/16), the International Financial Reporting Standards (''IFRS''), as well as in accordance with the Ordinance on the structure and content of annual financial statements (Official Gazette 95/16).

The consolidated financial statements have been prepared on the historical cost basis, except for certain non-current assets and certain financial instruments that are presented in revalued amounts. The consolidated financial statements are presented in thousands of Croatian Kuna (HRK '000) as the Group's functional currency.

Basis of accounting

The Group maintains its accounting records in the Croatian language, in Croatian Kuna and in accordance with Croatian legislation and the accounting principles and practices observed by enterprises in Croatia.

Adoption of new and revised International Financial Reporting Standards ("IFRS")
Standards and Interpretations effective in the current period

The following new standards, revised existing standards and interpretations issued by the International Accounting Standards Board adopted by the European Union are effective for the current period:

- **Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealized Losses**
  Amendments shall be effective for annual periods beginning on or after 1 January 2017, subject to prior application being permitted. The purpose of the amendment is to clarify the application for the recognition of deferred tax assets to unrealized losses in order to address the differences in practice related to the application of the provisions of IAS 12 Income Tax. Certain issues related to differences in practice in the treatment of temporary tax differences on the basis of fair value reduction, asset sale for an amount higher than book value and probable future taxable profits and consideration of a combined or separate impact assessment.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- **Amendments to IAS 7: Disclosure Initiative**
  Amendments shall be effective for annual periods beginning on or after 1 January 2017, or, where applicable, prior application may be granted. The purpose of the amendment is to provide disclosures that allow users of financial statements to assess the impact of changes in liabilities from financial activities, including cash and non-cash changes. Amendments state that one way of meeting disclosure requirements is to align the spreadsheet between initial and closing positions in the statement of financial position for liabilities arising from financial activities, including changes in cash flows from financing, changes that result from loss or gain of control over subsidiaries or other affairs, the effect of exchange rate fluctuations, changes in fair value and other changes.

The adoption of these amended standards did not significantly affect the financial statements of the Company.

Standards and Interpretations issued by the Standards Board that have not yet been effective and which the Company has not previously adopted.

At the date of issuance of these financial statements, the following standards, amendments and interpretations issued by the International Standards Board have not been adopted by the European Union:

- ***IFRS 9 Financial Instruments: Classification and Measurement***
  The Standard is effective for annual periods beginning on or after January 1, 2018, with earlier application being allowed. Final version of IFRS 9 *Financial Instruments* refers to all phases of a financial instruments project and modifies IAS 39 Financial Instruments: Recognition and Measurement as well as all prior versions of IFRS 9. The Standard introduces new classification and measurement requirements, impairment and hedge accounting.

- **IFRS 15 *Revenue from Contracts with Customers***
  The Standard is effective for annual periods beginning on or after 1 January 2018. The standard introduces a 5-step model applicable to customer-based revenue (with limited exceptions), regardless of the type of revenue transaction or industry. Standard requirements will also apply to the recognition and measurement of profits and losses from sales of some non-financial assets which is not a part of the Company's regular activities (for example, the sale of property, plant and equipment or intangible assets). Extensive disclosures will be required, including disaggregation of total revenue; information on execution obligations; changes in amounts of contracted assets and liabilities between periods and key estimates and judgments.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- **IFRS 15 Revenue from Contracts with Customers (Explanation)**
  Explanations are effective for annual periods beginning on or after 1 January 2018, or earlier, with prior application being allowed. The purpose of the explanation is to clarify the purpose of the Board when defining the requirements of IFRS 15 Revenue from Contracts with Customers, in particular accounting treatment of identified execution obligations by supplementing the definition of a "separately recognizable" principle, consideration of the relationship between the principal and the agent including an assessment of whether the subject is the principal or the agent in the transaction, as well as the application of access control and licensing by providing additional guidance for the accounting treatment of intellectual property and royalties. Explanations also provide additional practical tools for entities subject to IFRS 15 using a full retroactive approach or for those who opt to use a modified retroactive approach. These clarifications are still not adopted in the EU.

- **IFRS 16 Leases**
  The Standard is effective for annual periods beginning on or after January 1, 2019. IFRS 16 defines the rules for recognition, measurement, presentation and disclosure for the leases of both contractual parties, i.e. the buyer (the "lessee") and the supplier (the "lessor"). In accordance with the new standard the lessees should recognize most leases in their financial statements. A single accounting model will be applied to all leases, with certain exceptions. Accounting treatment of leases at the lessor will not be significantly altered.

The Management Board of the Company estimates that the application of these standards, amendments and interpretations will not have a material impact on the Company's financial statements for the period of their first application.

The basis for preparation of the Company's consolidated financial statements

The Company’s consolidated financial statements represent aggregate amounts of assets, liabilities and equity, and the results of the Group’s operations for the year ended.

Principles and methods of consolidation

The consolidated financial statements incorporate the financial statements of HEP d.d. (the Parent company) and entities controlled by HEP d.d. (it’s subsidiaries). The list of Group’s subsidiaries is provided in the Note 36. HEP d.d. has control over the entity if based on its participation is exposed to variable yield, i.e. has a right to it and ability to influence the yield with its prevalence in the entity. Considering that HEP has a 100% share in the capital of its subsidiaries and represents the only member resulting in the ability to manage and appoint Members of the Board, all mentioned companies are included in the consolidated financial statements as subsidiaries.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles and methods of consolidation (continued)

Subsidiaries are included in the consolidated financial statements from the date the Company gains control until the date when the Company ceases to control the subsidiary.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with those used by other members of the Group.

All significant intergroup transactions, balances, income and expenses are eliminated in consolidation. Non-controlling interest in the net assets of consolidated subsidiaries in these consolidated financial statements are identified separately from the Group's equity therein. Non-controlling interest consist of the amount of those interests at the date of the original business combination and the non-controlling share of changes in equity since the date of the combination. Profit or loss and every part of other comprehensive income are attributable to Owners of the parent and non-controlling interest, even if it results in a negative amount of non-controlling interest.

Changes in a parent's ownership interest in a subsidiary that do not result in the parent losing control of the subsidiary are accounted as equity transactions. If the parent loses control over the subsidiary, it derecognises related assets (including goodwill) and liabilities, non-controlling interest and other components of equity in former subsidiary, and recognises the gain or loss associated with the loss of control attributable to the former controlling interest. Any remaining interest is recognized at fair value.

Reporting currency

The consolidated financial statements of the Company are presented in Croatian Kuna (HRK '000).

Investments in joint arrangements

In accordance with IFRS 11, Joint arrangements are classified as:

- joint operations - whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement
- joint venture - whereby the parties that have joint control of the arrangement have rights to the net assets of the joint arrangement.

In classification of investments in joint operations, the Group considers:

- The structure of joint operation,
- Legal form of the joint operation structured through separate legal entities,
- Contracting conditions of joint operations,
- All other facts and circumstances (including any other contractual arrangements).

Interest in joint ventures is measured using equity method.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments in joint arrangements (continued)

The Group recognizes its interest in joint operation through its share of assets, liabilities, income and expenses in accordance with its contractual rights and obligations.

The Group identified its investment in Krško Nuclear Power Plant as joint operation (Note 15).

Employee benefits

The Company has no defined post-retirement benefits for its employees or Management. Accordingly, no provision for these costs has been included. Legal pension and health insurance contributions are paid on behalf of the Company's employees. This obligation applies to all employees hired on the basis of employment contract. The contributions are paid at a certain percentage determined on the basis of gross salary.

	2017 and 2016
Pension insurance contributions	20%
Health insurance contributions	15%
Employment Fund contribution	1.7%
Occupational injury	0.5%

The Company has the obligation to withhold the contributions from the employees' gross salaries.
Contributions on behalf of the employer and the employees are recognized as cost in the period in which they incurred (Note 7).

The Group pays employees jubilee awards and one-time severance payments upon retirement. The liabilities and expenses for these payments are determined with the application of the projected unit credit method. By using projected unit credit method, each period of seniority is observed as the basis for additional units of eligibility to allowances and each unit is measured separately until the realization of final liabilities. This liability is determined at the present value of projected future cash outflow with the application of the discount rate which is similar to the interest rate of State bonds in Croatia released on the market where the currency and maturity is in accordance with the currency and estimated duration of liabilities for the payment of these allowances. Liabilities and the costs of these allowances were calculated by a certified actuary.

Jubilee awards
The Group provides long-service benefits (jubilee awards) and retirement benefits to its employees. The long-service benefits range from HRK 1,500 to HRK 5,500, net, and are provided for tenure from 10 to 45 years of continuous employment with the employer.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits (continued)

Severance payments

A new Collective Agreement was adopted as of 1 July 2016 (which covers all of the HEP Group companies), under which the employees are entitled to a severance payment in the extent of 1/8 of the average gross monthly salary earned in the period of three months prior to termination of the employment contract, for each completed year of continuous employment at the employer. The effective date of the Collective contract is until 31 December 2017.

Property, plant and equipment (hereinafter: PPE)

Property, plant and equipment are measured at cost less accumulated depreciation and any impairment losses, except for land, which is carried at cost. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis. PPE in use are depreciated using the straight-line method on the following bases:

Buildings	**2017 and 2016**
Hydroelectric power plants (flood gates and dams, buildings and other buildings as well as accompanying objects)	20 – 50 years
Thermal power plants (buildings and other structures)	33 – 50 years
Electricity transmission and distribution plants and facilities (transmission lines and buildings of transformer stations, switch-yard, dispatch centres and others)	20 – 40 years
Water and steam pipelines and other thermal power generation and transmission objects	33 years
Gas pipelines until 2014	20 – 25 years
Gas pipelines from 2014	40 years
Administrative buildings	50 years
Plant and equipment	
Hydroelectric power plants	10 – 33 years
Thermal power plants	6 – 25 years
Electricity transmission plants and facilities (electric parts of transformer stations and transformers; and electric parts of transmission lines)	15 – 40 years
Electricity distribution plants and facilities (electric parts of transformer stations and transformers, electric parts of distribution lines, measuring instruments, meters and other equipment)	8 – 40 years
Thermal power stations, hot-water pipelines and other equipment	15 – 30 years
Gas meters and other gas network equipment	5 – 20 years
Other equipment and vehicles	
IT equipment	5 – 20 years
Software licenses	5 years
Telecommunications equipment	5 – 20 years
Motor vehicles	5 – 8 years
Office furniture	10 years

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment (continued)

The cost of PPE comprises its purchase price, including import duties and non-refundable taxes and any directly attributable costs of bringing an asset to its working condition and location necessary for it to be capable of operating as intended by Management. Expenditures incurred after PPE have been put into operation are normally charged to profit or loss in the period in which the costs are incurred.

In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item of PPE beyond its originally assessed standard performance, the expenditures are capitalized as an additional cost of PPE. Costs eligible for capitalization include costs of periodic, planned significant inspections and overhauls necessary for further operation.

Any gains or losses arising from the disposal or retirement of any item of PPE are determined as the difference between the sale proceeds and the carrying amount of the asset and are recognized and is recognized as an expense or income in the consolidated income statement.

Impairment of PPE and intangible assets

At each reporting date, the Group reviews the carrying amounts of its PPE and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

The recoverable amount is higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to that asset.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment (continued)

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately as expenditure, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, in a way that the increased carrying amount does not exceed the carrying amount that would have been determined, if no impairment loss would have been recognized for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognized as income, unless the relevant asset is carried at estimated value, in which case the reversal of the impairment loss is treated as a revaluation increase.

Intangible assets

Non-current intangible assets include patents and licenses and are carried at cost less accumulated amortization. Non-current intangible assets are amortized on a straight-line basis over their useful life of 5 years.

Investment property

Investment properties are properties held for the purposes of earning rentals and/or capital appreciation, including property under construction for such purposes. Investment properties are measured initially at cost, including transaction costs. Subsequently, investment properties are measured at fair value. Gains and losses arising from changes in the fair value of investment properties are included in profit or loss for the period in which they arise.

An investment property is derecognized upon sale or retirement and when no future economic benefits are expected from its disposal. Any gain or loss arising on derecognition of the property (calculated as the difference between the net sale proceeds and the carrying amount of the asset) is included in profit or loss in the period in which the property is derecognized.

Finance and operating leases

The Group as lessee

The Group has no significant finance lease arrangements and there were no new significant operating lease arrangements concluded during 2017 and 2016. Operating lease payments are recognized as an expense in on a straight-line basis over the lease term.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Trade receivables and prepayments

Trade receivables are carried at cost less any impairment for bad and doubtful receivables.

The Management carries out impairment of bad and doubtful receivables based on review of the aging structure of all receivables as well as a review of significant individual amounts included in the receivables.

Given the uncertainty that some of receivables will be collected over a longer period, the Group carries out impairment of unrecoverable amounts, based on a reasonable estimate and past experience as follows:

	2017 and 2016
Receivables aging structure	Impairment percentage
31 - 60 days	1.5%
61 - 90 days	3%
91 - 180 days	9%
181 - 365 days	30%
Over one year	90%

Receivables for which legal proceedings have been initiated and receivables from entities in bankruptcy and pre-bankruptcy settlement proceedings (principal and interests) are impaired in their full amount by debiting expenses, regardless of the overdue period.

Inventories

Inventories comprise material and small inventory and are carried at lower of cost and net realisable value. The Management carries out inventories write-off based on review of the ageing structure of all inventories as well as a review of significant individual amounts of inventories.

Since 2013, inventories include CO_2 emission rights. After Croatia joined to the European system for greenhouse gas emissions trading (EU ETS), Hrvatska elektroprivreda as an electricity and thermal energy generator, is obligated to purchase greenhouse gas emission units in the amount corresponding to verified emissions of CO_2 generated from the fossil fuel combustion in thermal power plants, as a result of which CO_2 is emitted.

Companies are obligated to have defined quantities of CO_2 emission rights at 30 April (yearly cycle). Due to withdrawal of IFRIC 3 *Emission Rights* and insufficient provisions of IFRS, the Group has analysed different accounting models for CO_2 emission rights, and among other EFRAG discussion papers. Occasionally, the Group trades with CO_2 emission rights. Due to that the Group recognize these emission rights as inventory.
From April 2014, inventories include gas stock held for trading on the wholesale market and are stated at lower of cost and net realizable value. The Company measures inventories based on the weighted average price (Note 20).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories (continued)

Inventory costs for quantities of gas for direct delivery to customers are calculated using the method of specific identification. Costs comprise invoiced amount as well as all other costs directly attributable to bringing inventories to their present location and condition.

Cash and cash equivalents

Cash and cash equivalents comprise of petty cash, demand deposits and other short-term liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognized as an expense in the period in which they incurred. Interest expense is recognized on an accrual basis.

Foreign currencies

Separate financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group entity are presented in Croatian Kuna (HRK), as the Group's functional and presentation currency.

In the financial statements of individual Group entities, transactions in foreign currencies are translated to the functional currency of the entity at the applicable exchange rates prevailing on the dates of transactions. At each reporting date, monetary balances, denominated in foreign currencies are retranslated to the functional currency of the entity at the applicable exchange rates prevailing at the end of the year. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the applicable exchange rates prevailing on the date when the fair value was determined. Non-monetary items that are carried at historical cost in foreign currency are not retranslated. Exchange differences arising on the settlement of monetary items, and on their retranslation, are stated in the consolidated income statement in the period in which they incurred. Exchange differences arising on retranslation of non-monetary assets carried at fair value are stated in the consolidated income statement as financial cost, except for exchange differences arising on the retranslation of non-monetary assets available for sale, for which gains and losses are recognized directly in equity. For such non-monetary items, any exchange gains or losses arising from retranslations are also recognized directly in equity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies (continued)

For the purpose of presenting consolidated financial statements, assets and liabilities of the Group's foreign entities are presented in Croatian Kuna at the applicable exchange rate on the date of the consolidated statement of financial position. Those assets and liabilities are originally denominated in EUR. As the main goal of the CNB monetary policy is to maintain stability of the currency which is secured through maintenance of the stable HRK rate against EUR, income and expense items (together with comparatives) are translated at the annual average exchange rate. However, if exchange rate fluctuates significantly (over 10%), the Group use the exchange rates at the dates of transactions. Exchange differences arising from year-end translation, are classified as reserves and recognized as profit or loss for the period in the period when the foreign entity is sold.

Taxation

Corporate income tax expense represents the sum of the current tax liability and deferred taxes.

Current tax

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

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit and are accounted for using the statement of financial position liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences, and deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary differences arise from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in transactions that affect neither the taxable profit nor the accounting profit. The carrying amount of deferred tax assets is reviewed at the end of each reporting period and adjusted to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the tax asset to be recovered. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability will be settled or asset realized, based on tax laws that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxation (continued)

Current and deferred tax for the period

Deferred tax is recognized as an expense or income in the consolidated income statement, except when it is related to items credited or debited directly to equity, in which case the deferred tax is also recognized directly in equity, or when the tax is arising from initial recognition of accounting for a business combination.

In case of a business combination, tax effect is taken into account in the measurement of goodwill or in determining the excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities over cost.

Financial assets

Investments are recognized and derecognized on the date of transaction. Financial assets are initially measured at fair value, increased by transaction costs, except for those financial assets classified at fair value through profit or loss.

Financial assets are classified as Available-for-sale, at fair value through profit or loss and Loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortized cost of financial asset and of allocation interest income over the relevant period. The effective interest rate is the rate that discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest basis for debt instruments.

Available-for-sale financial assets (AFS)

Shares held by the Group that are traded in an active market are classified as Available-for-sale financial assets and are measured at fair value. Gains and losses arising from changes in fair value are recognised in revaluation reserve through other comprehensive income, except for impairment losses, interests calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss for the period. Where the investment is disposed or impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is recognized in profit for the period.

Dividends i.e. profit shares on equity instruments are recognized as profit or loss when the Group's right to receive the dividends have been established.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

The fair value of available-for-sale financial assets denominated in a foreign currency are determined in that foreign currency and translated at the exchange rate prevailing at the end of the reporting period.

Loans and receivables

Trade receivables, loans, and other receivables with fixed or determinable payments and that are not quoted in an active market, are classified as loans and receivables. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected. For financial assets carried at amortized cost, the amount of the impairment is the difference between the assets carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced for the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the impairment account. When a trade receivable is considered uncollectible, it is written off through the impairment account. Subsequent recoveries of amounts previously written-off are credited to impairment account. Changes in the carrying amount of the impairment account are recognized in profit or loss.

With the exception of AFS equity instruments, if in a subsequent period, the amount of the impairment loss decreases and the decrease can be objectively related to an event occurring after the impairment was recognized, previously recognized impairment losses are reversed through the profit or loss to the extent that the carrying amount of the investment, at the date when the impairment is reversed, does not exceed what the amortized cost would have been if the impairment has not been recognized.
In respect of AFS equity instruments, any increase in fair value subsequent to an impairment loss is recognized directly in revaluation reserve.

Investments

Investments in immaterial non-consolidated companies are generally recorded at cost less any impairment.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities

Financial liabilities, including loans and borrowings, are subsequently measured at amortized cost by applying the effective interest method.

The effective interest method is a method of calculating the amortized cost of financial liability and of allocating interest expense over the relevant period. Effective interest rate is the rate that discounts estimated future cash payments (including all fees and points paid and received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Derecognition of financial liabilities

The Group derecognizes financial liabilities only when the Group's liabilities are settled, cancelled or they expire. The difference between the carrying amount of derecognized financial liability and consideration paid and payable is recognized in profit or loss.

Derivative financial instruments

The Company entered into a cross currency swap agreement in order to manage its exposure to exchange rate risk. Further details on derivative financial instruments are disclosed in the Note 25.

Derivatives are initially measured at fair value at the date the derivative contracts are entered into and are subsequently re-measured to their fair value at the end of each reporting period. Profit or loss arising from fair value measurement is recognized in profit and loss.

The Company brought Decision on measurement of the fair value of the cross-currency swap in accordance with the calculation of Mark-to-market ("MTM") value prepared by business banks. Profit or loss arising from fair value measurement is recognized in profit and loss.

Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of obligation. Provisions are reviewed at the end of each reporting period and adjusted to reflect the present best estimate. Where the effect of discounting is materially significant, the amount of the provision is the present value of the expenses expected to be required to settle the obligation. When discounting is used, increase in provisions that reflects the passage of time is recognized as interest expense (Note 28).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of estimates in preparation of the consolidated financial statements

Preparation of the consolidated financial statements in conformity with International Financial Reporting Standards, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent liabilities. Estimates used in preparation of these consolidated financial statements relate to employee benefits, impairment of assets, determination of fair values of assets and liabilities and estimated decommissioning costs. Future events may occur which could cause changes in the assumptions used for making these estimates. The effect of any changes in estimates will be recorded in the consolidated financial statements, when determinable.

Revenue recognition

Revenue is realized primarily from the sale of electricity to households, industrial and other customers within the Republic of Croatia. These activities constitute the main source of the Group's operating income.

Revenue from the sale of electricity is recognized based on best estimate on the quantities of energy delivered. As the actual calculation of the quantities of energy delivered to customers is performed twice a year, the Group recognized revenue from sales of electricity based on the total generated and purchased energy quantities on the distribution network corrected for losses on the distribution network based on logarithmic regression. The price of electricity is regulated by the Croatian Energy Regulatory Agency until entry into force of the Law on Amendments to the Electricity Market Act (Official Gazette 102/2015.), when price regulation for public service electricity supply of households in the context of universal service and amounts of tariff items for electricity supply provided by the supplier who has the obligation to provide public service, ceases to exist. The Group does not have a separate accounting model for recognizing any deferral that would result from regulated tariffs. Accordingly, the Group recognizes revenue based on the prices determined by tariffs approved by the regulatory agency, or by decision of the company that has obligation to provide the public service. Alternatively, the Group provides the option for their customers to choose the market price model, in which case revenue is recognized in accordance with free market prices (HEPI tariff model).

Revenue from sale of heating energy to households, industrial and other customers in the Republic of Croatia is recognized when the heating energy is delivered to the customers and is probable that future economic benefits related to transaction will inflow into the Group.

Revenues from gas sale are recognized in the period when the gas is delivered to the customers and is probable that future economic benefits related to transaction will inflow into the Group. The price of gas is regulated by the Croatian Energy Regulatory Agency. The Group does not have a separate accounting model for recognizing any deferral that would result from regulated tariffs.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue from connection fees

As of 1 July 2009, the Group adopted IFRIC 18 "Transfers of Assets from Customers''.

IFRIC 18 clarifies the IFRS requirements regarding accounting of contracts in which an entity receives an asset (item or property, plant and equipment or cash) from the customer for their construction, which the entity, in return, must use either to connect the customer to a network or to provide the customer with the ongoing access to a supply of goods or services. When the item of property, plant and equipment transferred from a customer meets the definition of an asset, the Group must recognize the asset in its consolidated financial statements.

Since 1 July 2009, connection fees received from customers have been recognized as income in the amount of cash received from the customer, either the moment customer is connected to the network/grid or in a moment the customer is enabled continuous access to services.

Segment analysis

The Group has adopted IFRS 8 ''Operating Segments'' and disclosed information about their operating segments, given that the Group has debt instruments, which are traded in public market (Note 4).

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

Critical judgments when applying accounting policies

When applying accounting policies described in the Note 2, the Management made certain judgments that had a significant impact on the amounts stated in the consolidated financial statements. These judgments are provided in detail in the accompanying notes and the most significant relate to the following:

Useful lives of property, plant and equipment

As described in the Note 2, the Group reviews the estimated useful lives of property, plant and equipment at the end of each annual reporting period.

Fair value of financial assets

As described in the Note 21, Management uses judgment to estimate whether trade and other receivables have suffered an impairment loss.

Provisions for power plant decommissioning

The Management Board estimates the cost of the Disposal of NE Krško and TPPs of the Group based on the applicable laws and regulations and their own experiences. The provision also includes activities related to environmental protection to be carried out during the decommissioning of production facilities.

Disposal of NE Krško is provisioned in accordance with the Regulation on Amount, Deadline and Method of Payment of Funds for Financing Disposal and Disposal of Radioactive Waste and Used Nuclear Fuel of NE Krško (OG 155/08) (Note 15).

The amount of provisions for the decommissioning of thermal power plants represents the discounted value of the estimated cost of decommissioning of the Group's thermal power plants (note 28).

Recognition of revenues from sale of electricity - households

As the collection is conducted through prepayments with actual calculation twice a year, the Group is estimating revenues from the sale of electricity. The estimate is based on the total generated and purchased energy quantities, which are corrected for losses in the distribution network based on logarithmic regression. After analysing a number of different methods of approximation (five-year average, a linear approximation, etc.), the Management chosen method of logarithmic regression as the most appropriate.

The difference between initially estimated revenues and actual prepayments is recognized in the consolidated statement of financial position as other short-term liabilities or other short-term receivables.

Impairment of non-current assets

The impairment calculation requires the estimate of value in use of the cash generating units. That value is measured using the discounted cash flow projections. The most significant variables in determining cash flows are discount rates, time values, the period of cash flow projections, as well as assumptions and judgments used in determining cash inflows and outflows.

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Availability of taxable profits for which deferred tax assets could be recognized

Deferred tax assets are recognized for unused tax losses to the extent that it is probable that the related tax benefit will be realised against future taxable profits. Measurement of the amount of deferred taxes that can be recognised, requires a significant level of judgement which is based on the probable quantification of the time and level of future taxable profits, together with the future tax planning strategy (Note 10).

Actuarial estimates used in determining severance payments and jubilee awards

The cost of defined benefits is determined using actuarial estimates. Actuarial estimates involve assumptions about discount rates, future salary increases and the mortality or fluctuation rates. Because of the long-term nature of those plans, there is uncertainty regarding those estimates (Note 28).

Consequences of certain court disputes

The Group is a subject to number of court disputes arising from operating activities. Provisions are made if there is a present obligation as a result of a past event (taking into account all available evidence, including the opinion of law experts) for which is probable that outflow of resources will be required to settle the obligation and if a reliable estimate can be made of the amount of the obligation (Note 28).

4. SEGMENT INFORMATION

The Group generates most income from its operations in a single geographical area – the Republic of Croatia. The Group's reportable segments are defined as follows: electricity (generation, transmission, distribution and sale of electricity), heating (generation, distribution and sale of heating power), and gas (distribution and sale of gas). Each segment's operating profit or loss includes all revenue and expenses directly attributable to the reportable segment. Information about financial income, expense and income tax is not provided on a segment level, as the segments are disclosed based on the operating profit.

	Electricity		Heating		Gas		Group	
	2017	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK
Operating revenue	11,493,664	10,831,456	683,264	699,596	1,280,463	1,444,540	13,457,391	12,975,592
Other segment income	1,409,955	1,350,081	70,016	51,868	31,923	22,817	1,511,894	1,424,766
Operating profit/loss	**2,692,154**	**2,867,744**	**(65,908)**	**(162,625)**	**(22,402)**	**18,038**	**2,294,823**	**2,723,157**
Net financial expense							(704,087)	(132,796)
Corporate income tax							(290,437)	(545,359)
Net profit							**1,300,299**	**2,045,002**

Segment assets consist primarily of property, plant and equipment, receivables, cash and inventories. Segment liabilities consist of trade and other payables. Non-segment assets and liabilities consist of assets and liabilities that cannot be reasonably attributed to the reportable business segments. Total unallocated assets include investments in NEK a part of property, plant and equipment, and unallocated financial assets. Total unallocated liabilities include long-term loans, short-term loans and various other liabilities.

	Total segment assets		Total segment liabilities	
	2017	**2016**	**2017**	**2016**
	in 000 HRK	in 000 HRK	in 000 HRK	in 000 HRK
Electricity	31,664,518	30,179,137	6,067,132	6,227,856
Heating	1,205,007	1,226,459	167,969	170,255
Gas	365,519	370,917	93,308	99,960
Unallocated	5,615,513	7,456,396	6,527,122	7,251,160
Total Group	**38,851,557**	**39,232,909**	**12,855,531**	**13,749,231**

4. SEGMENT INFORMATION (continued)

Customer information

In 2017 electricity sales amounted to HRK 11,493,664 thousand (2016: HRK 10,831,456 thousand).

Heating energy sales for the year 2017 amounted to HRK 683,264 thousand (2016: HRK 699,596 thousand).

In 2017 gas sales in wholesale market amounted to HRK 963,887 thousand and gas sales to customers in the amount of HRK 316,576 thousand (2016 wholesale market: HRK 1,102,728 thousand; gas sales to customers HRK 341,812 thousand).

Geographical information

The Group operates in Europe, with countries that are members of the European Union and other countries that are not members of the European Union.

Presented below is the territorial analysis of the revenue that the Group realized from continuing operations with external buyers of electricity:

	2017 In HRK '000	**2016** In HRK '000
Croatia	10,302,678	9,937,036
EU member states	1,038,870	789,423
Non - EU member states	152,116	104,997
	11,493,664	**10,831,456**

5. OTHER OPERATING INCOME

	2017 In HRK '000	**2016** In HRK '000
Network/grid connection services	372,088	449,450
Income from assets financed by network/grid connection fee	224,404	231,909
Reversal of impaired receivables (Note 21)	79,971	84,807
Services rendered	94,233	97,441
Capitalized assets	90,844	99,916
Penalty interest	38,961	40,592
Income from sale of materials	32,728	28,735
Income from sale of cross – border transmission capacity	130,169	60,616
Revenues from inter-compensation (HOPS) - cross-border	5,513	22,570
Income from reversal of provisions for impairment of fixed assets	199,207	-
Reversal of long-term provisions – vacation accrual	15,348	-
Reversal of long-term provisions for retirement benefits and jubilee awards	187	72,847
Reversal of long-term provisions – court costs	66,928	55,117
Reversal of other provisions	-	5,039
Recovery of receivables from pre-bankruptcy proceedings	11,640	5,433
Income in respect of the electricity payments reminders	1,345	3,538
Income in respect of court costs on claims	7,385	9,382
Income from sale of tangible assets	18,043	30,778
Recovery of written-off receivables	1,829	2,190
Income from subsidies, grants, reimbursements and	2,803	11,930
Overcharged fee in previous year on CO2 emissions for electricity generation	13,109	9,486
Other income - NE Krško	5,409	5,813
Other	99,750	97,177
	1,511,894	**1.424,766**

6. PURCHASE COSTS

	2017 In HRK '000	2016 In HRK '000
Cost of electricity	2,786,423	2,148,249
Gas cost	1,903,145	1,548,033
Fuel cost for sale on the wholesale market	1,130,144	1,246,442
	5,819,712	**4,942,724**

Cost of electricity and gas refers to purchases outside the wholesale sales system and to final customers.

Fuel supply (coal, liquid fuels and gas) refers to purchases outside the power generation system in thermal power plants.

7. STAFF COSTS

	2017 In HRK '000	2016 In HRK '000
Net salaries	1,112,785	1,069,123
Net salaries NE Krško	93,171	92,807
Taxes and contributions	703,795	704,001
Taxes and contributions NE Krško	37,141	38,512
	1,946,892	**1,904,443**

Total staff costs

	2017 In HRK '000	2016 In HRK '000
Gross salaries	1,816,580	1,773,123
Gross salaries NE Krško	130,312	131,319
Reimbursement of costs to employees (Note 8)	120,018	119,205
Employee benefits (Note 8)	99,520	65,498
Unused vacation (Note 8)	5,077	9,800
	2,171,507	**2,098,945**

7. STAFF COSTS (continued)

Remuneration for members of the Management Board and executive directors of the Group:

	2017 In HRK '000	**2016** In HRK '000
Gross salaries	28,881	28,523
Pension contributions	6,430	6,370
Other benefits	3,508	3,329
	38,819	**38,222**

Remuneration for members of the Supervisory Board:

	2017. godina In HRK '000	**2016. godina** In HRK '000
Fees	189	192
Taxes and contributions	120	194
Other costs	4	18
	313	**404**

Reimbursement of costs to employees for 2017 includes commuting costs in the amount of HRK 73,602 thousand (2016: HRK 72,711 thousand), daily allowances and travelling expenses for 2017 in the amount of HRK 22,679 thousand (2016: HRK 21,150 thousand), additional health insurance for 2017 amounting to HRK 8,697 thousand (2016: HRK 8,548 thousand) and other similar expenses for 2017 in the amount of HRK 15,040 thousand (2016: HRK 16,790 thousand).

Employee benefit costs mostly include benefits under the Collective Agreement which amounts to HRK 49,202 thousand, and to a minor extent to solidarity support, family separation allowances, child benefits and other.

In 2017 there were no other payments to the Management Board members in addition to regular salaries and benefits in kind in the amount of HRK 3,508 thousand (2016: HRK 3,329 thousand).

8. OTHER OPERATING EXPENSES

	2017 In HRK '000	2016 In HRK '000
Maintenance costs	566,004	636,610
Impairment of trade receivables (Note 21)	151,143	107,276
Gas costs	116,673	126,178
Cost of services	305,588	296,732
Chargeable services and supplies	179,522	142,643
Cost of material	82,498	86,236
Compensation gas purchased	6,690	12,745
CO2 emission allowances cost	120,163	137,315
Write-off of fixed assets	223,128	18,369
Value adjustment of inventory	7,216	13,209
Value adjustment of non-current tangible assets	39,630	108,256
Value adjustment of non-current intangible assets	72,680	-
Employee benefits (Note 7)	120,018	119,205
Other employees benefits (Note 7)	99,520	65,498
NE Krško – decommissioning expense	106,386	107,197
Taxes and contributions	96,027	90,980
Litigation provisions	18,471	25,244
Contributions and concession for water fees	65,079	64,785
Provision for unused vacation (Note 7)	5.077	9.800
Fee for the usage of power plant facilities	75,138	73,223
Compensation for water-purification and drainage	12,447	10,528
Cost of materials sold	19,806	15,049
Calculation and collection costs	24,807	29,111
Provisions for retirement benefits and jubilee awards	101,164	27,101
Provisions for severance payments based on the termination	-	342,964
Insurance premiums	11,835	12,612
Environmental protection fees	835	732
Compensation for damages	21,311	16,141
Bed debts write off	14,936	20,528
Provisions for decommissioning of fossil fuelled power plants	8,711	8,141
Other	299,392	325,357
	2,971,895	**3,049,765**

9. FINANCIAL INCOME AND EXPENSES

	2017	2016
Financial income	In HRK '000	In HRK '000
Foreign exchange gains	215,803	138,034
Interest	9,275	11,939
Fair value of cross currency swap	-	74,921
Dividend income	8,935	7,176
Other financial income	701	5
NE Krško – other financial income	1,112	798
Total financial income	**235,826**	**232,873**
Financial expenses		
Interest	(222,787)	(246,857)
Foreign exchange losses	(95,090)	(110,727)
Fair value of cross currency swap	(569,172)	-
Fair valuation of shares	(548)	-
NE Krško – other expenses	(556)	(1,781)
Fair valuation of tangible assets	(46,777)	(6,304)
Value adjustment of financial assets	(6,000)	-
Total financial expenses	**(940,930)**	**(365,669)**
Capitalised cost of borrowings	1,017	-
Financial expenses recognized in the income statement	**(939,913)**	**(365,669)**
Net loss from financial activities	**(704,087)**	**(132,796)**

10. CORPORATE INCOME TAX

	2017 In HRK '000	2016 In HRK '000
Current tax	345,365	450,226
Deferred tax expense / (income) relating to the origination and reversal of temporary differences	(54,928)	95,133
Corporate income tax	**290,437**	**545,359**

Adjustments of deferred tax assets are shown as follows:

	2017 In HRK '000	2016 In HRK '000
Balance at 1 January	555,461	650,681
Reversal of deferred tax assets	(124,329)	(112,497)
Recognition of deferred tax assets	179,257	17,277
Balance at 31 December	**610,389**	**555,461**

Deferred tax assets have arisen from tax unrecognized provisions for jubilee awards and regular severance payments, value adjustments and other provisions.

The reconciliation between income tax and profit reported in the income statement is set out below:

	2017 In HRK '000	2016 In HRK '000
Profit before taxation	1,590,736	2,590,361
Income tax at the applicable rate in the Republic of Croatia of (18%/20%)	**286,332**	**518,072**
Tax unrecognized income	57,369	(73,090)
Tax effect on permanent differences	(54,928)	95,133
Unrecognized deferred tax assets from companies operating with loss	1,664	5,244
Tax expense for the year	**290,437**	**545,359**
Effective tax rate	18%	21%

Reduction of the profit tax rate in Croatia from 20% to 18% came into effect from 1 January 2017. As a result of the change in the tax rate, the relevant positions of deferred taxes have been re-calculated.

10. CORPORATE INCOME TAX (continued)

The Group and its subsidiaries are subject to corporate income tax, according to the tax laws and regulations of the Republic of Croatia. Subsidiaries in the Group stated total tax losses in the amount of HRK 479,834 thousand (2016: HRK 1,035,951 thousand), while the Group stated total corporate income tax expense in the amount of HRK 345,365 thousand (2016: HRK 450,266 thousand) and deferred tax assets in the amount of HRK 54,928 thousand (2016: HRK 95,133 thousand).

Tax losses are available for carrying forward and offsetting against the tax base in future tax periods until their expiration as prescribed by the law, which is 5 years following the year in which the tax losses were incurred.

Tax losses stated by the Group and their expirations are presented below:

Year of tax loss origination	Total tax loss stated by the Group	Year of expiry
	In HRK '000	In HRK '000
2013	207,334	2018
2014	168,027	2019
2015	69,009	2020
2016	26,221	2021
2017	9,243	2022
	479,834	

Group companies which are continuously stating losses in their financial statements, are not recognizing deferred tax assets. HEP d.d. is realizing profit and has no tax losses carried forward to be utilized. According to the Croatian legislation, it is not possible to utilize tax losses at the Group level. Each individual company determines its tax liability. As of 31 December 2017, the Group could not recognize deferred tax assets arising from tax losses carried forward in the amount of HRK 479,834 thousand.
In accordance with the tax regulations, the Tax Administration may at any time review the books and records of the Company and its subsidiaries for a period of three years after the expiration of the year in which the tax liability is reported and may impose additional tax liabilities and penalties. The Management Board of the Company is not aware of any circumstances that could lead to potential significant obligations in this respect.

In 2017, the Tax Administration conducted tax supervision for 2015 in the subsidiary HEP Proizvodnja d.o.o.

10. CORPORATE INCOME TAX (continued)

The following table summarizes movements in deferred tax assets during the year:

In HRK '000	Inventories write-off	Provisions for jubilee awards and retirement benefits	Depreciation over prescribed rates	Provisions for MTM bonds	PPE impairment	Tax losses carried forward	Other	Total
As at 1 January 2016	**45,075**	**93,205**	**9,013**	**16,375**	**451,199**	**3,242**	**32,572**	**650,681**
Transfers	-	(105)	-	-	-	-	18	(87)
Credited to profit and loss for the year	(2,399)	(17,788)	476	(10,570)	(56,621)	(1,902)	(6,329)	(95,133)
As at 31 December 2016	**42,676**	**75,312**	**9,489**	**5,805**	**394,578**	**1,340**	**26,261**	**555,461**
Credited to profit and loss for the year	1,087	17,585	1,776	85,136	(56,753)	(1,341)	7,438	54,928
As at 31 December 2017	**43,763**	**92,897**	**11,265**	**90,941**	**337,825**	**(1)**	**33,699**	**610,389**

11. PROPERTY, PLANT AND EQUIPMENT

In HRK '000	Land and buildings	Fixtures and equipment	Assets under construction	Total
COST				
As at 1 January 2016	**38,082,228**	**45,463,879**	**4,386.574**	**87,932,681**
Transfers to another account	298,204	(303,614)	-	(5,410)
Additions	5,602	261,579	2,091,299	2,358,480
Additions NEK	-	-	208,761	208,761
Transfer from assets under construction	749,456	2,966,971	(3,767,586)	(51,159)
Transfer from assets under construction NEK	112,456	127,405	(239,861)	-
Inventory surpluses	8,155	8,666	-	16,821
Disposals	(92,360)	(437,549)	(1,954)	(531,863)
As at 31 December 2016	**39,163,741**	**48,087,337**	**2,677,233**	**89,928,311**
Transfers to another account	97,261	(45,316)	(51,397)	548
Additions	14,173	238,886	1,964,703	2,217,762
Additions NEK	-	-	195,306	195,306
Transfer from assets under construction	623,767	1,254,726	(1,938,594)	(60,101)
Transfer from assets under construction NEK	12,878	114,280	(127,158)	-
Disposals	(74,532)	(386,870)	(277,534)	(738,936)
Transfer to investment property	(97,431)	-	-	(97,431)
As at 31 December 2017	**39,739,857**	**49,263,043**	**2,442,559**	**91,445,459**
ACCUMULATED DEPRECIATION				
As at 1 January 2016	**26,344,621**	**31,479,031**	-	**57,823,652**
Depreciation for the year	672,049	1,043,998	-	1,716,047
Depreciation for the year - NEK	25,179	104,703	-	129,882
Transfers to another account	49,912	(49,881)	-	31
Disposals	(62,047)	(437,798)	-	(499,845)
Inventory surpluses	4,743	(17,288)	-	(12,545)
As at 31 December 2016	**27,034,457**	**32,122,765**	**-**	**59,157,222**
Depreciation for the year	674,478	1,087,016	-	1,761,494
Depreciation for the year - NEK	26,072	100,763	-	126,835
Assessment of Assets IAS 36 / i /	(10,357)	(188,850)		(199,207)
Write-off of investment IAS 36	14,070	25,560		39,630
Transfers to another account	13,115	(12,662)	-	453
Disposals	(80,851)	(383,442)	-	(464,293)
Transfer to investment property	(9,787)	-	-	(9,787)
As at 31 December 2017	**27,661,197**	**32,751,150**	**-**	**60,412,347**
CARRYING AMOUNT				
At 31 December 2017	**12,078,660**	**16,511,893**	**2,442.559**	**31,033,112**
At 31 December 2016	**12,129,284**	**15,964,572**	**2,677.233**	**30,771,089**

11. PROPERTY, PLANT AND EQUIPMENT (continued)

The Group owns a large number of properties, however titles to individual properties has not been fully resolved. The Group is in process of registering ownership over properties. Due to a large number of properties, there is a possibility that all properties of the Group are not registered in the Group's business ledgers. There is also a possibility that the Group's business ledgers include records of properties to which the Group has no title. The Management Board of the parent company adopted the Decision on measures and activities related to resolving the ownership status of properties of HEP d.d. and subsidiaries dated 27 June 2013. The Decision contains tasks and deadlines for the purpose of submitting proposals to the Land Registry Courts in order to register ownership rights. Activities on land-registry will be continued in 2018.

/ i / Based on the established indicators of impairment of assets and the calculation of the required impairment losses in accordance with IAS 36, the carrying value of thermal power plants was corrected during 2014. The key indicators of impairment were the significantly higher costs of electricity generation in thermal power plants compared to the market price of electricity.

In July 2016, Block L of TE TO Zagreb was granted the status of eligible producer on the basis of the Decision on the Acquisition of the Privileged Electricity Producer Status issued by the Croatian Energy Regulatory Agency (HERA) according to which it entered the system of incentives and sales of electricity at a preferential price a period of twenty-five years. This circumstance, after establishing the sustainability of the financing model in which it is based in 2017, has been recognized as an indication of changes in the value of assets and, in accordance with the same revaluation was made by an independent consultant, which showed the need to abolish the recognized impairment loss on Block L in TE TO Zagreb in the amount of HRK 199,207 thousand. This is resulted in an increase in the present value of the property as well as an increase in the income from the abolition of the property decrease. Calculation of the recoverable amount is based on five-year plans for electricity and heat production. The calculation of the recoverable amount implies a terminal growth rate after a five-year period of 0%. Cash flow projections are discounted using a discount rate reflecting the risk of the asset in question, which is approximated at the average weighted capital cost for capital impairment testing of 7.58%.

12. INTANGIBLE ASSETS

	In HRK '000
COST	**Licences**
Balance at 31 December 2015	**726,616**
Transfers to another account	5,410
Additions	21,885
Transfer from assets under construction	51,159
Disposals	(7,295)
Balance at 31 December 2016	**797,775**
Transfers to another account	(548)
Additions	40,320
Transfer from assets under construction	60,101
Disposals	(38,532)
Balance at 31 December 2017	**859,116**
ACCUMULATED AMORTIZATION	
Balance at 31 December 2015	**605,179**
Transfers to another account	(31)
Amortization for the year	42,337
Disposals	(7,296)
Balance at 31 December 2016	**640,189**
Transfers to another account	(453)
Amortization for the year	47,404
Disposals	(38,526)
Balance at 31 December 2017	**648,614**
CARRYING AMOUNT	
At 31 December 2017	**210,502**
At 31 December 2016	**157,586**

13. INVESTMENT PROPERTY

As at 31 December 2017 and 2016, investment property includes real estate held for the purpose of earning income from the lease and / or capital appreciation, and is stated at fair value based on the best estimate of the Management Board. Fair value includes the estimated market price at the end of the reporting period. All investment property is owned by the Company.

Fair valuation was conducted by internal departments of the Group. The estimate is based on data available on the real estate market price in the appropriate locations. These prices are collected from different sources, including available data from Central Bureau of Statistics, Agency for Transactions and Mediation in Immovable Properties, CCE and others. These average values are adjusted to the characteristics and peculiarities of individual properties.

At fair value	**31 Dec 2017** In HRK '000	**31 Dec 2016** In HRK '000
Fair value	**231,491**	**236,778**
Net fair value adjustment	7,654	(5,914)
Transfer from property	66,485	-
Closing balance at fair value	**305,630**	**230,864**
Investment in properties of NE Krško	-	627
	305,630	**231,491**

14. PREPAYMENTS FOR PROPERTY, PLANT AND EQUIPMENT

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Alstom Hrvatska d.o.o.	-	8,066
Arvos Ljungstroem GMBH	-	1,600
Đuro Đaković Holding d.d.	1,325	2,754
General Electrics Hrvatska	3,764	-
JSC Tehnopromexport –TE Sisak	-	58
Končar GIM	-	1,527
Končar inženjering Zagreb	3,043	350
Končar KET	2,208	6,482
Litostroj Slovenija	-	85
Siemens	336	4,282
Spegra Inženjering	-	1,046
TPK Orometal d.d.	1,445	3,101
VOITH Siemens Austrija	-	16
Other	3,131	7,340
	15,252	**36,707**

Prepayments for PPE relate to construction of production facilities.

15. INVESTMENT IN THE NUCLEAR POWER PLANT KRŠKO

Investment background

In late 2001, the Governments of the Republic of Croatia and the Republic of Slovenia signed an Agreement governing the status and other legal relations in connection with their respective investment in NE Krško, usage and decommissioning, as well as a partnership agreement between HEP d.d. and ELES GEN d.o.o. This agreement was ratified by the Croatian parliament during 2002, and it became effective at 11 March 2003, following the ratification by the Slovenian parliament on 25 February 2003.

The Agreement acknowledges the ownership rights of HEP d.d. in the newly formed company, Ne Krško in respect to its 50% holding. Which were previously denied. Both parties have agreed to extend the useful life of the power plant at least to the year 2023. The Agreement also regulates that the produced electricity is supplied 50:50 to both contracting parties, and that the price of the electricity supplied is determined based on real production cost.

The Agreement was also clearly defined obligation towards the Croatian half of disposal of radioactive waste and used nuclear fuel from NE Krško. Each country/government has an obligation to provide half of the funds necessary to prepare the decommissioning plan and cost of the program. Each side will allocate fund for this purpose into a separate fund in the amounts estimated by the decommissioning program. According to the current program of decommissioning and disposal of radioactive waste and spent nuclear fuel, HEP d.d. is a contributor to the Fund in the amount of EUR 14,250 thousand per year.

Current status

Payments to the Fund for Decommissioning of NEK

Based on the Regulation on the amount, time and manner of payment of funds for the decommissioning and disposal of radioactive waste and used nuclear fuel of NE Krško, adopted by the Croatian Government on 24 December 2008, in the period from 2006 to 2017 HEP d.d. made payments to the Fund for Decommissioning of NE Krško in the amount of HRK 1,481,915 thousand. The amount of payment is determined by the Program of decommissioning from 2004. Actual annual liability in the amount of EUR 14,250 thousand is payable quarterly.

Extension of useful life of NEK

After NE Krško has obtained from the Slovenian nuclear safety administration a safety license to operate without any limitations in 2012, at the end of 2016 HEP and GEN Energija d.o.o. adopted a decision to extend the operational life of the plant until 2043. The decision to extend the operating life of NE Krško for 20 years was preceded with an investment feasibility study of long-term investments in the power plant.

15. INVESTMENT IN THE NE KRŠKO (continued)

Accounting of Joint operation in NE Krško

The joint operation in NE Krško is recognized in the Company's financial statements using the equity method. The application required by IFRS 11 has resulted in numerous issues and ambiguities, as well as failure to recognize by part of the users of financial statements.

With the aim of eliminating the possible doubts of certain state bodies (FINA, Ministry of Finance, Central Bureau of Statistics, etc.) on information in separate financial statements of the Company, in accordance with the provisions of IAS 1, item 19 and item 20, the Company's Management has adopted the decision to change this policy.

In the consolidated financial statements, the Company applies the method of joint asset management and liabilities and discloses the Company's share of each asset and each liability, income and expense in accordance with IFRS 11.

In table below is shown an extract from financial statements of NE Krško in full (100%) amounts at 31 December 2017 and 2016:

	31 Dec 2017	**31 Dec 2017**
	In HRK ‘000	In HRK ‘000
Property, plant and equipment	2,522,384	2,400,731
Capital and reserves	3,308,725	3,339,824
Gross sales	1,181,749	1,229,413
Cash flow from operating activities	317,624	137,363
Profit for the year	-	3,396

16. INVESTMENT IN TE POMIN

In November 1996, HEP d.d. entered into a Joint Venture Agreement with RWE Energie Aktiengesellschaft, Germany ('RWE') regarding the completion and operation of TE Plomin II. Consequently, a joint venture, TE Plomin d.o.o. ('TE Plomin') was formed in December 1996, with each partner holding 50% of the equity of the new entity. Agreement between HEP d.d. and RWE expired in May 2015 in accordance with its provisions since HEP decided to exercise its right related to the possibility that 15 years after start of production, HEP can takeover RWE's shares in TE Plomin d.o.o..

The Company paid all liabilities to RWE.

On 1 August 2017 TE PLOMIN d.o.o. was merged with the Company.

Balance sheet at the date of merger

	31 July 2017
	In HRK '000
Fixed assets	349,729
Current assets	25,609
	375,338
Share capital	100
Reserves and retained earnings	181,033
Long-term liabilities	70,887
Short-term liabilities	123,318
	375,338

17. LONG TERM LOANS AND DEPOSITS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Loans given	61,879	57,373
Current portion of long-term loans given	(25,772)	(28,400)
Long-term portion	**36,107**	**28,973**

Loans given to non-related parties

	Year of loan approval	Repayment period	Loan amount	31 Dec 2017	31 Dec 2016
				In HRK '000	In HRK '000
City of Dubrovnik	2013.	5 years	5,707	-	2,512
City of Pregrada	2006.	10 years	1,358	-	136
Did d.o.o.	2007.	4 years	1,010	-	129
Total				-	**2,777**
Current maturity				-	(2,648)
Long-term portion				-	**129**

Loans given to related parties

	Year of loan approval	Repayment period	Loan amount	31 Dec 2017	31 Dec 2016
				In HRK '000	In HRK '000
LNG Hrvatska	2015	5 years	63.600	61,879	54,596
Current maturity				(25,772)	(25,752)
Long-term portion				**36,107**	**28,844**

18. AVAILABLE FOR SALE AND OTHER INVESTMENTS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Available-for-sale investments	282,998	288,493
Other investments	1,445	7,445
	284,443	**295,938**

Changes in available-for-sale investments are presented below:

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Opening balance	**288,493**	**244,845**
Changes in fair value of assets	(5,495)	43,648
Closing balance	**282,998**	**288,493**

18. AVAILABLE FOR SALE AND OTHER INVESTMENTS (continued)

Changes in fair value of available-for-sale investments shown in the table above are presented in the gross amount. In the consolidated income statement within other comprehensive income is presented amount of changes in fair value of available-for-sale investments net of corporate income tax under Net gain/(loss) on AFS financial assets.

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	31 Dec 2017 In HRK '000	**31 Dec 2016** In HRK '000
Investments in securities		
Jadranski Naftovod d.d.	280,701	286,099
Viktor Lenac d.d.	305	177
Đuro Đaković d.d.	5	5
Kraš d.d.	3	4
Pevec d.d.	547	555
Jadran d.d.	364	364
Elektrometal d.d.	41	-
Industrogradnja grupa d.d.	-	490
Optima Telekom d.d.,	298	296
Institut IGH d.d.,	191	172
Međimurje beton d.d.	153	153
HTP Korčula d.d.	61	71
Lanište d.o.o.	61	72
Pominvest d.d.	35	35
Konstruktor Inženjering d.d. u stečaju	233	-
Total	**282,998**	**288,493**

	31 Dec 2017 In HRK '000	**31 Dec 2016** In HRK '000
Other investments		
Geopodravina d.o.o.	200	200
LNG Hrvatska d.o.o.	865	865
Novenerg d.o.o.	380	380
Cropex	-	6,000
	1,445	**7,445**
	284,443	**295,938**

18. AVAILABLE FOR SALE AND OTHER INVESTMENTS (continued)

In December 2008, HEP d.d. acquired 53,981 shares of Jadranski Naftovod d.d. under a Decision of the Croatian Government, with a nominal value of HRK 2,700 per share i.e. the total nominal value of HRK 145,748,700. By the decision of the Management Board, shares of Jadranski Naftovod were classified as available for sale. Transfer of shares was registered at Central Depository Agency on 19 March 2009.

In 2017 and 2016 fair value was determined by a market value from Zagreb Stock Exchange as of 31 December. The market price of one share of Jadranski Naftovod as of 31 December 2017 was HRK 5,200 and as of 31 December 2016 was HRK 5,300. By fair valuation of the investment in Jadranski Naftovod as of 31 December 2016 total amount of investment was decreased by HRK 5,398 thousand (2015: increased by HRK 43,184 thousand). The fair valuation in 2017 and 2016 was recognised through equity (revaluation reserves).

On 1 June 2010, HEP d.d. and Plinacro d.o.o. had concluded the Articles of Incorporation of LNG Hrvatska d.o.o., *a liquefied natural gas company*. Recapitalization was conducted in 2011 and subscribed capital was increased from HRK 20 thousand to HRK 220 thousand and in 2012 to HRK 1,730 thousand. The Company LNG Hrvatska d.o.o. was recapitalized by Plinacro d.o.o. in the amount of HRK 22,600 thousand which was registered at the Commercial Court on 4 February 2013. Share capital of LNG Hrvatska d.o.o. amounts to HRK 24,330 thousand. Consequently, the Company owns a 3.5% stake and Plinacro d.o.o. 96.5% stake, while voting rights are 50%: 50%.

19. OTHER NON-CURRENT ASSETS

	31 Dec 2017	**31 Dec 2016**
	In HRK '000	In HRK '000
Housing loan receivables	13,685	17,590
Energy efficiency receivables – long-term portion	23,610	23,836
Other non-current assets	5,623	5,515
	42,918	**46,941**

Prior to 1996, the Group had sold apartments/flats in its ownership to its employees, the sale of which was regulated by the laws of Republic of Croatia. These flats were usually sold on credit, and the related receivables, which are secured and bear interest at rates below market, are repayable on a monthly basis over periods of 20-35 years. Receivables for sold apartments/flats were transferred to new subsidiaries as of 1 July 2002. The housing loan receivables are stated in the consolidated financial statements at their discounted net present values, determined using an interest rate of 7.0%. The liability to the State, which represents 65% of the value of sold apartments, is included in non-current liabilities to the State (Note 27). The receivables are secured by mortgages over the sold apartments.

20. INVENTORIES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Inventories of fuels and chemicals	109,854	150,627
Electric materials	367,226	330,917
Spare parts	201,458	194,400
Construction material	15,100	24,974
Gas inventory for wholesale	353,600	379,488
CO_2 emission units	106,248	222,957
Other inventories	57,001	74,967
Nuclear fuel and other material - NE Krško (Note 22)	287,097	260,113
	1,497,584	**1,638,443**
Value adjustment of obsolete materials and spare parts	(240,292)	(233,075)
	1,257,292	**1,405,368**

21. TRADE RECEIVABLES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Electricity – Corporate customers	1,449,741	1,422,648
Electricity – Households	521,542	489,270
Export of electricity	155,966	67,886
Heating, gas and services	717,772	791,301
Receivables from NE Krško	15,788	15,057
Other	55,831	63,826
	2,916,640	**2,849,988**
Impairment of bad and doubtful receivables		
	(835,640)	(896,396)
	2,081,000	**1,953,592**

Aging structure of unimpaired trade receivables:

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Undue	1,441,335	1,336,879
Up to 30 days	349,467	333,439
31-60 days	109,038	118,850
61-90 days	62,517	55,159
91-180 days	51,319	56,141
181-365 days	57,504	43,773
More than 365 days	9,820	9,351
	2,081,000	**1,953,592**

21. TRADE RECEIVABLES (continued)

Changes in impairments were as follows:

	2017. In HRK '000	2016. In HRK '000
Balance at 1 January	**896,396**	**1,045,598**
Impairment of trade receivables (Note 8)	151,143	107,276
Derecognition of previously impaired trade receivables	(131,928)	(171,671)
Reversal of impairments (Note 5)	(79,971)	(84,807)
Balance at 31 December	**835,640**	**896,396**

The Management performs review of receivables and recognizes impairment of bad and doubtful receivables based on a review of the overall ageing structure of all receivables and of significant individual receivables amounts.

22. OTHER SHORT-TERM RECEIVABLES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Receivables for corporate income tax	98,093	60,522
Receivables for VAT	10,084	-
Prepayments	54,777	5,863
Receivables from the State for employees	3,642	3,421
Claims for overcharged water management fees	-	5,914
Demand and time deposits for a period longer than 3 months	129,845	111,191
Demand and time deposits for a period longer than 3 months NE Krško	252,244	275,980
Short-term given domestic - reprogram	94,486	-
Receivables from HEP-ESCO d.o.o. for Energy efficiency project	8,145	9,813
Loan receivables from companies with participating interest	28,772	25,752
Receivables for sold flats	6,116	6,464
Receivables from OIE - HROTE	48,766	34,774
Other receivables from HROTE	128,752	-
Receivables for accrued income from el. en. household	31,099	-
Received bills of exchange	-	27,456
Derivative financial instruments (Note 25)	-	96,196
Other receivables NE Krško	2,431	2,369
Other short-term receivables	60,565	65,202
	957,817	**730,917**

23. CASH AND CASH EQUIVALENTS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Current accounts - HRK	1,037,821	938,761
Current accounts – Foreign currency	412,724	216,798
Current accounts for special purposes	69,104	31,686
Petty cash - HRK	186	260
Short term deposits - up to 90 days	160,730	1,314,216
Daily deposits	261,150	441,633
Cash Funds	75,252	75,322
Current account – HRK and foreign currency – NE Krško	128	170
	2,017,095	**3,018,846**

24. EQUITY AND RESERVES

The share capital was first registered on 12 December 1994 in German marks (DEM) and amounted to DEM 5,784,832 thousand. On 19 July 1995, the share capital was reregistered in Croatian Kuna in the amount of HRK 19,792,159 thousand. The share capital consists of 10,995,644 ordinary shares, with a nominal value of HRK 1,800 each.

Capital reserves

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Opening balance	140,293	100,836
Other comprehensive income/(loss)	21,949	39,457
Opening balance		
	162,242	**140,293**

Retained earnings

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Opening balance	5,551,226	4,132,208
Exchange differences from foreign operations	(15,609)	(18,984)
Dividends paid	(794,291)	(607,000)
Profit for the current year	1.300,299	2,045,002
	6,041,625	**5,551,226**

25. LIABILITIES FOR ISSUED BONDS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Nominal value of bonds in the country issued in 2007	93,030	92,946
Discounted value	-	84
Repayment due	(93,030)	
Current maturity on bonds	-	(93,030)
	-	**-**
Value of bonds issued abroad in 2012	493,571	498,617
Repayment due	(491,477)	-
Exchange difference	(2,094)	(5,046)
Current portion of bonds	-	(493,571)
Bonds issued in 2012	**-**	**-**
Nominal value of bonds from 2015 issued abroad	3,626,428	3,656,047
Exchange differences	(21,431)	(37,511)
Discounted value	7,613	7,892
	3,612,610	**3,626,428**
Accrued bond expenses	(16,782)	(20,255)
Bonds issued in 2015	**3,595,828**	**3,606,173**
Total liabilities for issued bonds	**3,595,828**	**3,606,173**

Bonds issued in the country

Bonds issued at the end of 2007 amounting to HRK 700,000 thousand are repayable in 15 semi-annual instalments, commencing three years from the date of issue, and are bearing fixed interest of 6.50%. The bonds are listed on the Zagreb Stock Exchange. In December 2017, the last instalment of outstanding bonds was repaid, i.e. the bonds were repaid in full.

25. LIABILITIES FOR ISSUED BONDS (continued)

Bonds issued abroad

Bonds issued abroad in 2012

In November 2012, the Company has issued bonds in the amount of USD 500,000 thousand. Bonds have maturity of 5 years and are bearing fixed annual interest of 6%. Bonds are listed at Luxembourg stock - exchange and they are actively traded. In November 2017 bonds were repaid in full.

In October 2015, the Company issued new corporate bonds in the amount of USD 550,000 thousand with maturity of 7 years, fixed interest rate of 5.875% per annum and the issue price of 98.594%. Bonds issued in 2015, are mainly used for the repurchase of 83.37% of the bonds issued in 2012 (i.e. the repurchase of USD 416,852 thousand). The remaining issue is intended to finance the Company's business. Bonds are listed at Luxembourg stock - exchange and they are actively traded.

Cross currency swap

In order to reduce exposure to currency risk, i.e. hedge against fluctuations in USD exchange rate, the Company has concluded cross currency swap agreement, by which liability upon issued bonds abroad in USD is converted in EUR for all period of bond duration, respectively until its outermost maturity date at 9 November 2017.

According to the cross-currency swap agreement from 2012, annual interest rate paid by the Company semi-annually is fixed and amounts to 6.53% (including swap cost).

Refinancing

In October 2015, bonds issued in 2012 were refinanced from the new bond issue and repaid 83.37% of the principal respectively USD 416,852 thousand.

Cross currency swap agreement from 2012 is applicable for outstanding principal until its outermost maturity date at 9 November 2017.

The new bond issue

In October 2015, the Company issued new corporate bonds in the amount of USD 550,000 thousand with maturity of 7 years, fixed interest rate of 5.875%.

Bonds issued in 2015, are mainly used for the repurchase of 83.37% of the bonds issued in 2012 (i.e. the repurchase of USD 416,852 thousand). The remaining issue is intended to finance the Company's business. Bonds are listed at Luxembourg stock - exchange and they are actively traded.

Cross currency swap

In order to reduce exposure to currency risk, i.e. hedge against fluctuations in USD exchange rate, the Company has concluded cross currency swap agreement, by which liability upon issued bonds abroad in USD is converted in EUR for all period of bond duration, respectively until its outermost maturity date at 23 October 2022.

25. *LIABILITIES FOR ISSUED BONDS (continued)*

According to the agreement from 2015, annual interest rate paid by the Company semi-annually is fixed and amounts to 4.851% (weighted interest rate include swap cost).

Derivative financial instruments

Cross currency swap

In order to reduce exposure to currency risk, i.e. hedge against fluctuations in USD exchange rate, the Company has concluded cross currency swap agreements, by which liabilities upon issued bonds abroad in 2012 and 2015 in USD are converted in EUR for all period of bond duration, respectively until its outermost maturity date.

The purpose of the cross-currency swap agreement is to reduce currency risk and recommendations of the credit agencies about the importance of strategic management of currency risks to reduce their impact on the business performance of the Company.

According to the agreement from 2012., annual interest rate paid by the Company semi-annually is fixed and amounts to 6.53%, and according to the agreement from 2015 amounts to 4,851% (weighted interest rate).

The Company measures the fair value of the cross-currency swap according to the calculation of Mark-to-market ("MTM") value, according to official banks calculation for the reporting period.

A positive "MTM" value is recorded as a receivable respectively it is formed financial income for the period, and negative "MTM" value is recorded as a liability and it is formed financial expense of the reporting period.
After the maturity of the derivative financial instruments, subject receivables or liabilities will be debited to the expense or credited to the income of the Company.

On 31 December 2017, using this measuring method, the Company stated fair value of liabilities by bonds issued in 2015 in the amount of HRK 505,208 thousand (2016: HRK 32,251 thousand), (Note 29).

26. LONG-TERM LOAN LIABILITIES

	Interest rates	31 Dec 2017	31 Dec 2016
		In HRK '000	In HRK '000
Domestic bank loans	Floating	445,468	827,728
Foreign bank loans	Fixed	219,793	237,817
Finance leases	Fixed	10,038	13,202
Total		**675,299**	**1,078,747**
Deferred loan originated fees		(923)	(2,152)
Total long-term loans		**674,376**	**1,076,595**
Current portion of long-term loans		(405,219)	(408,711)
Current portion of finance lease (Note 33)		(3,262)	(3,120)
Long-term portion		**265,895**	**664,764**

The Company has contracted loans with domestic and foreign banks with applicable floating and fixed interest rates ranging from 0.44% to 2.57% in 2017. Finacial leasing with fixed interest rate of 5.6% was also contracted.

Domestic banks' loans are secured by bills of exchange and indebtedness. As of December 31, 2017, the Group has no debt covered by the guarantee of the Republic of Croatia.

New financing sources

For the financing of the investment plan and the regular operations in 2017 the Group used own funds and funds from loans in use.

Loans in use

During 2017, a long-term loan from KfW Entwicklungsbank of EUR 50 million was still used for the financing of renewable energy projects. Of the contracted loan amount of EUR 50 million as at 30 December 2017 EUR 33,1 million was used. The remaining amount of unused funds of EUR 16,9 million was canceled and on 30 December 2017 the loan started to repay. As of 31 December 2017, the Group no longer has loans in use.

26. LONG-TERM LOAN LIABILITIES (continued)

Annual principal repayment schedule of long-term loans in next five years is stated as follows:

	(In HRK '000)
2018	408,482
2019	116,959
2020	39,962
2021	36,632
2022	36,632
after 2022	36,632
	675,299

Loans from domestic banks are secured by bills of exchange and promissory notes, except for one club loan for which the Group is obliged to meet the required level of financial indicators (covenants) on annual and semi-annual basis: tangible net worth, EBITDA to net finance charges, total net borrowings to tangible net worth. The primary goal related to risks resulting from covenants is to protect the Group from possible defaults, respectively early maturity of loan liabilities. The agreed covenants are monitored and calculated based on the projected Balance sheet and the Income statement.

The Group prepares preliminary calculations of the covenants in the upcoming mid-term period, and is following their trends.

If the projections accounted at the end of the financial year shows that the Company could be in breach of covenants, the Company is obligated to inform the bank regarding the possibility of a breach (event of default) and timely request a waiver from the bank.

In the event that the bank does not approve the "waiver", the possible scenario is an early maturity of the debt, which represents liquidity risk for the Group.

The Management believes that in the case of breach of covenants, the Company can obtain a "waiver" from the creditors, given that timely payment of liabilities to financial institutions represent priority obligation of the Company and the Company has never been late in payment of liabilities to financial institutions.

Therefore, the Management estimates that possibility of early maturity of loan liabilities due to breach of covenant, as well as Group's exposure to credit risk, liquidity risk and market risk, which would result from a possible non-compliance with covenants is minimal.

26. LONG-TERM LOAN LIABILITIES (continued)

As of 31 December 2017 covenants were not breached and the Group has met all contractual financial indicators.

The Group's total exposure to loan liabilities subject to covenant conditions as of 31 December 2017 amounts to EUR 35,294 thousand.

An analysis of long-term loans in foreign currencies is provided below (in '000):

Currency	**31 Dec 2017**	**31 Dec 2016**
	In HRK '000	In HRK '000
EUR	89,876	142,733

For the purpose of providing solvency reserves for the following mid-term period, the Company has negotiated with domestic banks multi-purpose overdraft agreements in the total amount of HRK 1,4 billion. Funds from agreed overdrafts the Company may use as short-term loans, as well as for issuance of guarantees, letters of credit and letters of intention in accordance with the Group needs.

During 2017, due to good liquidity, the Group did not conclude short-term loans from preapproved mid-term multipurpose overdraft agreements.

As of 31 December 2017, the Group has available the amount of up to HRK 1,320 million from short-term financing sources.

27. LONG-TERM LIABILITIES TO THE STATE

Long-term liabilities to the State amounted to HRK 13,065 thousand in 2017 (2016: HRK 15,901 thousand) and relate to the sale of apartments to employees in accordance with the State program that was discontinued in 1996. According to the law regulating housing sales, 65% of the proceeds from the sale of apartments to employees were payable to the State at such time as the proceeds were collected. According to the law, HEP d.d. has no liability to allocate the funds until they are collected from the employee.

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28. LONG-TERM PROVISIONS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Provisions for court disputes	298,504	337,899
Provisions for severance payments	429,489	329,693
Provisions for jubilee awards	46,083	44,986
Provisions for decommissioning of fossil fuelled power plants	170,149	161,438
Provision for electricity purchased from wind power plants	21,631	21,631
Provisions for severance payments, jubilee awards and other – NE Krško	52,611	35,053
	1,018,467	**930,700**

Provisions for decommissioning of fossil fuelled power plants in the amount of HRK 170,149 thousand represent discounted value of the estimated decommissioning costs of the Group's fossil fuel power plants.

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Changes in provisions during the presented period were as follows:

	Legal disputes	Provisions for severance payments	Jubilee awards	Decommission-ing of FFPPs	Other	Total
	In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000
At 1 January 2016	**367,772**	**374,550**	**45,875**	**128,297**	**53,007**	**969,501**
Additional provisions	25,870	29,789	2,031	33,141	3,677	94,508
Decrease in provisions (amounts paid)	(10,650)	(3,856)	(857)	-	-	(15,363)
Decrease in provisions based on estimates	(45,093)	(70,790)	(2,063)	-	-	(117,946)
At 31 December 2016	**337,899**	**329,693**	**44,986**	**161,438**	**56,684**	**930,700**
Additional provisions	27,104	156,516	2,614	8,711	-	194,945
Decrease in provisions (amounts paid)	(13,215)	(4,036)	(600)	-	-	(17,851)
Decrease in provisions based on estimates	(53,284)	(73)	(917)	-	(35,053)	(89,327)
At 31 December 2017	**298,504**	**482,100**	**46,083**	**170,149**	**21,631**	**1,018,467**

28. LONG-TERM PROVISIONS (continued)

Provisions for court disputes

Provisions for court disputes relate to cases where possible outcome has been determined as uncertain or negative. Most significant court disputes are initiated against HEP Proizvodnja d.o.o. and HEP d.d.

At HEP d.d. most significant provision relate to the litigation related to HE Peruča (hydropower plant Peruča) which started in 1995, for which a first Instance ruling was issued in 2012 and was ruled in favour of the plaintiff. Litigation case value amounts to HRK 330,000 thousand, and provisions are recorded at 50% of case value, i.e. HRK 165,000 thousand. Other significant provisions relate to Kartner sparkass amounting to HRK 9,903 thousand.

Against HEP Proizvodnja d.o.o. several legal disputes have been conducted for which the company has made a reservation. The most significant of them is Sanac, whose value as of 31 December 2017 amounts to HRK 9,710 thousand.

Provisions for severance payments and jubilee awards

Movements in the present value of the defined employee's benefits during the current period were as follows:

	Severance In HRK '000	**Jubilee awards** In HRK '000	**Total** In HRK '000
At 1 January 2016	**374,550**	**45,875**	**420,425**
Cost of services	12,636	2,393	15,029
Interest expense	8,636	1,161	9,797
Benefits paid	(11,639)	(5,830)	(17,469)
Past service cost	3,267	474	3,741
Actuarial (losses)	(57,757)	913	(56,844)
At 31 December 2016	**329,693**	**44,986**	**374,679**
Cost of services	17,239	2,486	19,725
Interest expense	9,897	1,044	10,941
Benefits paid	(26,330)	(6,438)	(32,768)
Past service cost	25,322	915	26,237
Actuarial (losses)	73,668	3,090	76,758
At 31 December 2017	**429,489**	**46,083**	**475,572**
NE Krško	52,611	-	56,611
Total	**482,100**	**46,083**	**532,183**

28. LONG-TERM PROVISIONS (continued)

The following assumptions were used in preparing the calculations:

- The termination rates ranges from 0% to 5.77% and is based on the statistical fluctuation rates for the Group in the period from 2006 to 2017.
- The probability of death by age and sex is based on 2010 - 2012 Croatian Mortality Tables published by the Croatian Bureau of Statistics. It is assumed that the population of employees of the Group represents average with respect to mortality and health status.
- It is assumed that there will be 2% annual salary growth
- Present value of the obligation was determined using a 3% discount rate for all Group members; except for HEP Proizvodnja d.o.o. i HEP ODS d.o.o. where a discount rate of 2.4% is used.

29. OTHER LONG-TERM LIABILITIES

	31 Dec 2017	**31 Dec 2016**
	In HRK '000	In HRK '000
Deferred income – assets financed by third parties	3,080,826	3,280,668
Long-term liabilities for assets financed from clearing debt	755,189	863,450
Cross currency swap (Note 25)	505,228	32,251
Other long-term liabilities	15,364	13,978
	4,356,607	**4,190,347**

Deferred income relates to income earned from assets received from customers and others without charge or assets financed from connection fee. The income from these assets is recognized over the same period as the related assets are depreciated, which applies to contracts for connection to the network concluded with customers by 30 June 2009. After 1 July 2009 the connection fee is recognized as income in the amount of cash received from the customer in the period when the customer is connected to the grid/network or when the customer is permitted permanent access to the delivery of the service.

At 31 December 2017, the Company stated clearing debt liability in the amount of HRK 755,189 thousand (2016: HRK 863,450 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of Finance for the use of funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the Company and the Ministry of Finance regarding the clearing debt, it has not been clearly defined whether it relates to a loan or a government grant.

30. TRADE PAYABLES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Domestic trade payables	1,407,038	1,490,580
Foreign trade payables	70,504	169,824
Foreign trade payables - EU	93,241	97,937
Trade payables - NE Krško	72,250	28,997
	1,643,033	**1,787,338**

31. TAXES AND CONTRIBUTIONS

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
VAT liability	-	106,110
Utility and other fees	33,636	17,190
Contributions on salaries	21,034	21,527
Contributions and taxes for employees material right	21,772	8,878
Other	3,760	4,045
	80,202	**157,750**

32. LIABILITIES TO EMPLOYEES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Net salaries	80,331	79,092
Contributions	36,099	36,379
Severance payments for retirements	123,487	4,303
Net salaries NE Krško	15,290	15,176
Other	18,966	20,319
	274,173	**155,269**

33. OTHER SHOT-TERM LIABILITIES

	31 Dec 2017	31 Dec 2016
	In HRK '000	In HRK '000
Prepayments received for connection fees	432,357	380,208
Other prepayments	144,013	128,914
Accrued expenses for unused vacations	60,995	71,304
Accrued income from electricity sale to households	-	22,077
Liabilities for calculated solidarity fee	15,064	14,612
Liabilities for fees for renewable energy sources	128,859	46,457
Accrued severance payments to employees	179,820	342,964
Accrued interest expenses	-	2,122
Accrued expenses for CO_2 emissions	120,148	137,289
Other accrued expenses	9,008	3,682
Current portion of liabilities for finance lease (Note 26)	3,262	3,120
NE Krško liabilities	23,822	5,045
Other	22,534	16,186
	1,139,882	**1,173,980**

Calculated revenues from the sale of electricity to households in the amount of HRK 22,077 thousand in 2016 and HRK 31,099 thousand in 2017 (note 22) are based on calculating the correction of income from households obtained by calculating the logarithmic curve. The correction of household income as at 31 December 2017 was obtained by calculating the logarithmic curve using losses in the network of 7.71%, whereas for the year ended 31 December 2016, the percentage of losses used in the calculation was 7,87%. The result is an increase in revenues of HRK 53,177 thousand in 2017 compared to the previous year, and a receivable in the amount of HRK 31,099 thousand.

According to the Air Protection Act (OG 130/2011, 47/14) and related by-laws in the field of greenhouse gas emissions the Company is classified as EU ETS system obligors and nine HEP plants, from 1 January 2013 to the EU-ETS system.

The Group has obtained greenhouse gas emissions permits for all nine HEP plants in the EU-ETS and monitors the emissions from the plant in accordance with the approved monitoring plan and submits verified reports to the Environmental Protection Agency by March 31 each year on total CO2 emissions for the last calendar year.

On the basis of the submitted report, the Group shall, no later than 30 April of the current year, submit the quantity of emission allowances to the Union Registry in the amount corresponding to the verified total greenhouse gas emissions from the plant in the previous calendar year, in accordance with the verified report.

33. OTHER SHOT-TERM LIABILITIES (continued)

HEP's EU-ETS plants have submitted to the EU Emission Unit Registry the quantities of verified emissions for 2013, 2014, 2015 and 2016. The entry of verified CO2 emissions data for 2017 is underway to the EU Greenhouse Gas Register, in accordance with the prescribed deadlines.

In accordance with the stated costs of purchasing greenhouse gas emissions consist of the amount of CO2 emitted and the unit price of emission units that the Group calculates on the accrued expenses and the expense of the period in the year in which the greenhouse gas emissions occurred.

34. RELATED PARTY TRANSACTIONS

The Company holds 50% of shares in NE Krško. Although investment in NE Krško is recognized in the financial statements as joint operation, due to the fact that NE Krško is a separate legal entity, transactions between NE Krško and HEP d.d. are also presented within related party transactions. The electricity generated by NE Krško is delivered to HEP d.d. at 50% of total generated quantities and at prices determined in accordance with the total generation costs.

Receivables and liabilities, and income and expenses arisen from related party transactions are presented in the table below:

	31 Dec 2017	**31 Dec 2016**
	In HRK '000	In HRK '000
NE Krško		
Liabilities for purchased electricity	49,603	52,444
Costs of purchased electricity	585,443	609,026

Management remunerations are explained in the Note 7.

34. RELATED PARTY TRANSACTIONS (continued)

In HRK '000	Sales revenue 2017	Sales revenue 2016	Purchase cost 2017	Purchase cost 2016
Companies partially owned by the State				
Društvo Hrvatske Željeznice	87,282	101,658	439	1,307
INA-Industrija nafte d.d.	143,094	158,780	1,007,305	1,049,732
Prirodni Plin d.o.o.	-	-	-	-
Plinacro d.o.o.	5,302	1,377	156,944	149,952
Croatia osiguranje d.d.	3,622	2,839	8,736	1,775
Hrvatska pošta d.d.	7,148	12,147	34,537	39,331
Hrvatske šume d.o.o.	4,195	3,751	2,852	3,042
Jadrolinija d.o.o.	529	609	554	580
Narodne novine d.d.	2,234	2,346	3,748	3,639
Hrvatska radio televizija	13,135	11,713	1,594	1,514
Plovput d.d.	510	327	155	164
Croatia Airlines d.d.	706	974	4	6
Petrokemija Kutina d.d.	15,020	17,631	374	257
Ministry of Foreign Affairs	5	481	-	-
Ministry of Defence	23,128	21,192	-	-
Ministry of the Interior	24,678	23,236	-	-
Elementary and high schools	48,778	76,890	14	18
Judicial institutions	6,662	9,126	163	126
Colleges and universities	25,258	31,294	1.611	1,201
Legislative, executive and other bodies of Republic of Croatia	18,738	27,836	67,781	4,031
Health institutions and organizations	90,620	100,785	639	193
HROTE d.o.o.	352,181	157,687	690,593	655,880
Others	7,149	9,635	7,067	7,353
TOTAL	**879,974**	**772,314**	**1,985,110**	**1,920,101**

34. RELATED PARTY TRANSACTIONS (continued)

In HRK '000	Receivables 31 Dec 2017	Receivables 31 Dec 2016	Liabilities 31.prosinca 2017.	Liabilities 31.prosinca 2016.
Companies partially owned by the State				
Društvo Hrvatske Željeznice	25,911	27,589	245	177
INA-industrija nafte d.d.	16,053	19,923	45,264	119,264
Plinacro d.o.o.	861	152	20,078	31,228
Croatia osiguranje d.d.	213	242	1,944	427
Hrvatska pošta d.d.	3,446	1,448	6,930	8,120
Hrvatske šume d.o.o.	1,038	1,029	2	13
Jadrolinija d.o.o.	76	123	22	25
Narodne novine d.d.	529	411	897	645
Hrvatska radio televizija	2,514	2,525	50	23
Plovput d.d.	67	58	48	51
Croatia Airlines d.d.	98	109	-	-
Petrokemija Kutina d.d.	3,095	3,176	419	82
Ministry of Defence	3,522	4,356	-	-
Ministry of the Interior	6,030	4,648	-	-
Elementary and high schools	12,037	15,531	-	-
Judicial institutions	1,144	1,495	-	-
Colleges and universities	4,664	5,519	-	-
Legislative, executive and other bodies of Republic of Croatia	3,712	5,404	-	-
Health institutions and organizations	20,218	19,881	-	-
HROTE d.o.o.	281,259	80,128	116,278	127,841
Others	17,998	18,567	6,587	18,892
TOTAL	**404,485**	**212,314**	**198,764**	**306,788**

35. CONTINGENT LIABLILITIES AND COMMITMENTS

Legal disputes

In 2017, the Group has recorded provisions for court disputes for which it considers it is unlikely that they will be ruled in favour of HEP d.d. and their subsidiary companies.

The Group has long-term investments in Bosnia and Herzegovina and Serbia in the amount of HRK 1,243,970 thousand. During the Company's transition in 1994 into a shareholding company, this amount was excluded from the net assets value.

The Company has long-term investments in immovable assets in the territory of Bosnia and Herzegovina and Montenegro in the amount of HRK 722 thousand, which is excluded from the net asset value.

Operating commitments

As part of regular investment activities, at 31 December 2017 the Group had concluded agreements for investments in various facilities and equipment that has commenced but has not been completed. In 2017, the value of the most significant contracted investments in progress amounted to HRK 994,834 thousand (2016: HRK 1,380,746 thousand).

Environmental and nature protection

HEP d.d. and subsidiaries continuously monitors and analyses impact of its business operations to the environment. The most important indicators of that impact are emissions of air pollutants and the quantity of industrial waste and ensures timely and objective reporting to the relevant institutions, local government and the public. HEP d.d. reports on its impact on the environment, economy and society within the framework of non-financial sustainability reports prepared under the GRI-Global Reporting Initiative guidelines and publishes them on its website http://www.hep.hr/o-hep-grupi/publikacije/izvjesca-o-odrzivosti/1401. Employees involved in environmental and nature protection are going through additional trainings, seminars and workshops where they are informed of the obligations and activities resulting from legal regulations in the areas of environmental and nature protection.

HEP d.d. environmental expenditure monitoring system (RETZOK) introduced in 2004, monitors all investments for the environmental and nature protection.

All HEP's thermal power plants with nominal input thermal power greater than 50 MW have obtained Environmental Solution Approvals from the competent Ministry of Environmental Protection and Nature.

The CO_2 emissions trading system was officially set up pursuant to the Decision of the Management Board of HEP d.d. under which, obligations, responsibilities and deadlines for meeting obligations for individual departments and companies within HEP's emission trading system are set. Croatian Environment Agency has opened nine "Accounts" of plant operators in the EU Greenhouse Gas Inventory. HEP successfully fulfilled its legal obligations for submission of emission units to the EU Greenhouse Gas Inventory for 2016 and for 2017 HEP entered information verifying CO_2 emission, which were after confirmation by Croatian officials submitted onto all nine Accounts of plant operators with the relevant quantities that corresponded the verified CO_2 emissions.

35. CONTINGENT LIABLILITIES AND COMMITMENTS (continued)

Environmental and nature protection (continued)

In 2017, a non-financial sustainability report for 2016 for the HEP Group was completed according to the Global Reporting Initiative (GRI 4) guidelines. The Sustainability Report is published on the Company's website in Croatian and English and in a printed version.

Report on the Status of the Nonfinancial Sustainability Report for the Group for 2017

The preparation of a separate non-financial statement on the Group's sustainability for 2017 is underway. The nonfinancial report will be published on HEP's web pages in accordance with the provisions of the Accounting Act (OG 78/15 and 120/16) within 6 months from the date of the consolidated balance sheet until 30 June 2018 at the latest. The report will be published, as well as the three already published nonfinancial sustainability reports available at the following link http://www.hep.hr/o-hep-grupi/publikacije/izvjesca-o-odrzivosti/1401

The HEP Group uses reports using the Global Reporting Initiative (GRI) guidelines and the indicators in the Standard - General and Standard Indicators and Sector Addendum for the Energy Sector.

The general content of the Sustainability Report for 2017 is:

- Editorial from the President of the Board
- HEP's sustainability approach, including goals, sustainability and accountability, as integrated into business policies, a description of sustainability risk
- material themes (description and impact assessment), a framework of sustainability towards the UN's sustainable development goals
- Stakeholder analysis. Involvement of stakeholders. Explanation of the reporting framework
- Business Transparency, includes a management approach, corporate governance principles, ethical business, expertise and accountability, transparency in communication and information (all according to the required GRI indicators). Responsibility in the work environment, data related to employees (and prescribed by GRI indicators), safety and security at work. The chapter also includes representative stories and case studies describing accountability and sustainability.
- Market access. HEP Group in Market Operations. General approach. Business and accountability, especially for HEP Group companies. Description of the most important trends related to market operations, supply chain, according to GRI requirements. The chapter also includes representative stories and case studies describing accountability and sustainability.
- Caring for the environment. Environmental protection, investments, projects, initiatives. The data are given according to the areas of environmental protection (segments of activity). The data is indicated by the GRI indicators.
- The chapter also includes representative stories and case studies describing accountability and sustainability.
- Investing in the community. Various forms of community investment, stakeholder co-operation, dialogue, information and education campaigns, co-operation initiatives and so on are described. The chapter also includes representative stories and case studies describing accountability and sustainability.
- List of indicators

35. CONTINGENT LIABLILITIES AND COMMITMENTS (continued)

Environmental and nature protection (continued)

Integrated environmental and quality management system at HEP-Proizvodnja d.o.o. was introduced on 1 January 2017 and includes all locations (headquarters, production areas and hydro power plants, power plants, thermal power plants and power plants).

TÜV Croatia d.o.o. confirmed and certified the new system in accordance with the new ISO 14001: 2015 and ISO 9001:2015 standards in all facilities and in the headquarters. In HEP-ODS d.o.o. during 2017, the procedures for system certification preparation continued in accordance with the new standards ISO 14001:2015 and ISO 9001:2015.

In 2017, we continued with the upgrading and harmonization of the environmental information system in the HEP Group with the provisions of environmental legislation in order to bring together data related to nature and environment protection. INFOZOK has been upgraded with modules for collecting data on the use and monitoring of water quality and keeping environmental permit data and analyses of environmental legislation.

The Water Act

With the entry into force of the Water Act on January 1, 2010, the property and property rights of the Company and the Group related to the accumulation lakes and associated facilities, which are used for the production of electricity from hydro power plants, became questionable, since they were defined as Public water good in the owned by the Republic of Croatia. The Company and the Group acquired the said property by toll from their previous owners, merging an exceptionally large number of parcels, which by the construction of the dam were flooded, resulting in accumulation. Several registrations of ownership of the Republic of Croatia on the mentioned real estates are in progress, of which part has been carried out for the benefit of the Republic of Croatia, and a part of the request for registration of the ownership right of the Republic of Croatia has been rejected by the competent courts, and one part is in the process of solving.

At the moment, the final text of the Law on Amendments to the Water Act is being drafted, which at the proposal of the Government of the Republic of Croatia was accepted at the first reading in the Croatian Parliament, according to which the Republic of Croatia establishes the right of construction for the constructed water structures invested by the Company ad its predecessors, other than accumulation, drainage and drainage channels in favour of the Company, without compensation for a period of 99 years. As long as the right of building is exercised, the Company is granted the right to manage public property / land on which constructions of electricity generation, accumulation and supply and drainage channels are built on behalf of the Republic of Croatia.

35. CONTINGENT LIABLILITIES AND COMMITMENTS (continued)

Supply on the wholesale gas market

The Act on Amendments to the Gas Market Act (OG 16/17), which was passed by the Croatian Parliament at its session on 17 February 2017, appointed the Company as a supplier on the wholesale gas market from 1 April 2017 until the selection procedure of suppliers on the wholesale gas market is conducted. Supplier on the wholesale market sells gas to suppliers in public service for household customers at a regulated sales price and is obliged to provide reliable and secure gas supply.

Pursuant to Article 31, paragraph 4 of the Act on Amendments to the Gas Market Act, the Government of the Republic of Croatia adopted at its session held on 28 February 2017 a decision on the price of gas by which the gas wholesale supplier is obliged to sell the gas to the suppliers in the public service supply gas for household customers, which amounts to 0.1809 hrk/kWh.

By the Act on Amendments to the Gas Market Act, as of April 1, 2017, the natural gas producer is no longer obligated to deliver gas as well as the regulated price at which it was obliged to sell the gas to the wholesale gas market for the needs of customers using the public service supply. Pursuant to the Act on Amendments to the Gas Market Act, 60% of the storage capacity of the underground gas storage plant was allocated, i.e. 61 packages. In the period from April 1, 2014 to March 31, 2015, the Company has contracted a lease of 3,600 million kWh; in the period from April 1, 2015 to March 31, 2016, the Company has contracted a lease of 3.550 million kWh, in the period from April 1, 2016 to March 31, 2017, a contracted capacity of 3,500 million kWh, while in the period from April 1, 2017 to March 31, 2018, a capacity of 3.050 million kWh was contracted.

36. SUBSIDIARIES

As at 31 December 2017 the Company had the following subsidiaries in its ownership:

Subsidiary	Country	Ownership interest in %	Principal activity
HEP-Proizvodnja d.o.o.	Croatia	100	Electricity generation and heating
Hrvatski operator prijenosnog sustava d.o.o.	Croatia	100	Electricity transmission
HEP-Operator distribucijskog sustava d.o.o.	Croatia	100	Electricity distribution
HEP ELEKTRA d.o.o.	Croatia	100	Electricity supply
HEP Opskrba d.o.o.	Croatia	100	Electricity supply
HEP-Toplinarstvo d.o.o.	Croatia	100	Thermal power generation and distribution
HEP-Plin d.o.o.	Croatia	100	Gas distribution
TE Plomin d.o.o.	Croatia	100	Electricity generation
HEP ESCO d.o.o.	Croatia	100	Financing of energy efficiency projects
Plomin Holding d.o.o.	Croatia	100	Development of infrastructure in area around Plomin
CS Buško Blato d.o.o.	BiH	100	Maintenance of hydro power plants
HEP-Upravljanje imovinom d.o.o.	Croatia	100	Accommodation and recreation services
HEP NOC Velika	Croatia	100	Accommodation and training
HEP-Trgovina d.o.o.	Croatia	100	Electrical energy trading and optimization of power plants production
HEP Energija d.o.o. Ljubljana	Slovenia	100	Electricity trading
HEP –MagyarorszagEnergiaKft	Hungary	100	Electricity trading
HEP Trade d.o.o. Mostar	BIH	100	Electricity trading
HEP KS sh.p.k. Priština	Kosovo	100	Electricity trading
HEP Trade d.o.o. Beograd	Serbia	100	Electricity trading
Program Sava d.o.o.	Croatia	100	Spatial planning, design, construction and supervision
HEP Opskrba plinom d.o.o.	Croatia	100	Gas distribution
HEP-Telekomunikacije d.o.o.	Croatia	100	Telecommunication services
Hrvatski centar za čistiju proizvodnju (u likvidaciji)	Croatia	100	Teaching and counseling in the field of cleaner production and environmental management systems
Nuklearna elektrana Krško d.o.o.	Slovenia	50	Electircity generation

Most of these subsidiaries were established within the framework of the reorganization and restructuring of core business under the new energy laws that entered into force on 1 January 2002, as noted in Note 1.

Company HEP-Telecommunication d.o.o. was established in 2013, HEP-RVNP d.o.o. in 2014 it changed its name to the Sava d.o.o program, while in 2014 a new HEP Opskrba plinom d.o.o. was established.

In November 2016 HEP Elektra was founded, which was created by the status change of the separation of supply activity from HEP-Operator distribucijskog sustava d.o.o.

In 2017 HEP-Trade Mostar d.o.o. changed its name to HEP Energija d.o.o., HEP-Trade Beograd d.o.o. changed its name to HEP Energija d.o.o., and HEP-KS.sh.p.k. the name changed to HEP Energija sh.pk.

In 2017, the Company was incorporated into TE Plomin d.o.o..

Beginning of the liquidation of the company Hrvatski centar za čistiju proizvodnju started on November 9, 2017.

HEP-Magyarorszag Energia Kft. shall be removed from the Court Registry on March 22, 2018.

37. FINANCIAL RISK MANAGEMENT

Capital risk management

The Group manages its capital to ensure that it will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance. The capital structure of the Group consists of debt, which includes loans and issued bonds disclosed in the Notes 25 and 26, cash and cash equivalents and equity attributable to Owners of the parent, comprising of share capital, legal and other reserves and retained earnings.

Gearing ratio

The Management monitors and reviews the equity structure on a semi-annual basis. As part of this review, the Management considers the cost of equity and the risks associated with each class of equity. The gearing ratio at the year-end can be presented as follows:

	31 Dec 2017	**31 Dec 2016**
	In HRK '000	In HRK '000
Debt	4,270,205	5,269,370
Cash and cash equivalents	(2,017,095)	(3,018,846)
Net debt	2,253,110	2,250,524
Equity	25,996,026	25,483,678
Net debt to equity ratio	**9%**	**9%**

Significant accounting policies

Details on significant accounting policies and methods adopted, including criteria for recognition and basis for measurement of each class of financial assets, financial liabilities and equity instruments are disclosed in the Note 2 to the consolidated financial statements.

37. FINANCIAL RISK MANAGEMENT (continued)

Categories of financial instruments

	31 Dec 2017 In HRK '000	**31 Dec 2016** In HRK '000
Financial assets		
Available-for-sale	284,443	295,938
At fair value through profit or loss	-	96,196
Loans and receivables (including cash and cash equivalents)	4,525,801	5,454,059
Other non-current assets	73,402	70,399
Financial liabilities		
At fair value through profit or loss	505,228	32,251
Non-current liabilities	4,641,233	5,161,943
Other current liabilities	2,078,873	2,844,932

Financial risk management objectives

The Treasury function within the Group provides to the companies support to their business, co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Group companies through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

Market risk

Market risk exposure is monitored and managed through sensitivity analysis. There have been no changes in the Group's exposure to market risks or in the manner in which the Group manages and measures the risk.

Foreign currency risk

The Group undertakes certain transactions denominated in foreign currencies and thus the Group is exposed to foreign currency risk. Foreign currency risk exposure is managed within approved policy parameters utilizing cross currency swap contracts.

The carrying amounts of the Group's foreign currency denominated monetary assets and liabilities at the reporting date are as follows:

	Assets		**Liabilities**	
	31 Dec 2017	**31 Dec 2016**	**31 Dec 2017**	**31 Dec 2016**
	(in 000)	*(in 000)*	*(in 000)*	*(in 000)*
European Union (EUR)	252,468	236,444	678,756	733,424
USD	9,590	10,496	122,572	12,814

37. FINANCIAL RISK MANAGEMENT (continued)

Foreign currency sensitivity analysis

The Group is mainly exposed to the changes of EUR and USD currency. The following table details the Group's sensitivity to a 10% increase and decrease in the Croatian Kuna against the EUR and USD. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents Management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes foreign currency denominated receivables and liabilities and adjustments of their translation at the period end for a 10% change in foreign currency rates. The sensitivity analysis includes external loans where the denomination of the loan is in a currency other than the currency of the lender or the borrower. A positive / negative number below indicates an increase in profit and other equity components where HRK strengthens 10% against the relevant currency. For a 10% weakening of the HRK against the relevant currency, there would be an equal effect, but the balance would be negative.

	2017 In HRK '000	**2016** In HRK '000
EUR change effect		
Gain or loss	320,298	375,606
USD change effect		
Gain or loss	70,836	1,662

Interest rate risk management

The Group is exposed to interest rate risk as it borrows funds at both fixed and floating interest rates. The Group's exposure to interest rates on financial assets and financial liabilities is explained in the liquidity risk management section. The Group manages this risk by maintaining an appropriate mix between fixed and floating interest rate in its loan portfolio.

Interest rate sensitivity analysis

The sensitivity analysis has been determined only for financial instruments with floating interest rate, based on the Group's exposure at the end of the reporting period. For floating interest rates, the analysis is prepared assuming that the amount of outstanding liability at the date of the consolidated statement of financial position, was outstanding for the whole year. A 50 basis-point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents Management's assessment of the reasonably possible change in interest rates.

37. FINANCIAL RISK MANAGEMENT (continued)

Interest rate sensitivity analysis (continued)

If interest rates had been 50 basis points higher/lower and all other variables were held constant:

- Profit for the year ended 31 December 2017 would decrease by HRK 1,918 thousand (2016: HRK 3,866 thousand) based on exposure to interest rate risk. This is mainly attributable to the Group's exposure to interest rates on its floating interest rate loans representing 10.30% of all interest-bearing loans (2016: 15.52%); and
- the Group's sensitivity to interest rates would decrease during current period mainly due to decrease in floating interest rate.

Credit risk management

Credit risk refers to the risk that counterparty will fail to meet its contractual obligations resulting in financial loss to the Group. The Group is the largest provider of electric energy in the Republic of Croatia. As such, it has public responsibility to provide services to all customers, and at all locations within the country, irrespective of credit risk associated with particular customer. Net trade receivables, consist of a large number of customers, spread across diverse industries and geographical areas.

The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The Group defines counterparties as having similar characteristics if they are related entities. Credit risk with respect to trade receivables is primarily related to corporate receivables, specifically those companies that are in difficult financial position. Overdue receivables from households are limited due to Group's ability to disconnect such customers from the power supply network.

Carrying amount of financial assets presented in the consolidated financial statements, less losses arising from impairment, represents the Group's maximum exposure to credit risk without taking into account the value of any collateral obtained.

Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the Management Board, which has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate reserves, loans from banks, and other sources of financing, and by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

Liquidity and interest rate risk tables

The following table details the remaining period to contractual maturity for the Group's non-derivative financial assets. The tables below have been drawn up based on the undiscounted cash flows of the financial assets, including interest to be earned on those assets except where the Group anticipates that the cash flow will occur in a different period.

37. FINANCIAL RISK MANAGEMENT (continued)

Maturity of non-derivative financial assets

	Weighted average effective interest rate	Less than 1 month	1 - 3 months	3 -12 months	1 - 5 years	Over 5 years	Total
		In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000
31 Dec 2017		-	-	-	-	-	-
Interest free		4,069,586	514,463	123,992	111,298	-	4,819,339
Floating interest	0.72%	25,772	-	-	44,685	-	70,457
Fixed interest		-	-	-	-	-	-
Total		**4,095,358**	**514,463**	**123,992**	**155,983**	**-**	**4,889,796**
31 Dec 2016							
Interest free		4,943,768	589,005	250,529	81,441	-	5,864,743
Floating interest	0.45%	25,923	-	-	36,230	-	62,153
Fixed interest		-	-	-	-	-	-
Total		**4,969,691**	**589,005**	**250,529**	**117,671**	**-**	**5,926,896**

37. FINANCIAL RISK MANAGEMENT (continued)

Liquidity risk management

Maturity of non-derivative financial liabilities

The following table details the Group's remaining contractual maturity for its non-derivative financial liabilities. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay

	Weighted average effective interest rate	Less than 1 month	1 - 3 months	3 -12 months	1 - 5 years	Over 5 years	Total
	%	In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000	In HRK '000
31 Dec 2017							
Interest free		1,077,182	531,957	109,911	1,271,673	-	2,990,723
Floating interest	1.95%	68,432	28,762	278,727	77,506	-	453,427
Fixed interest	4.60%	311	622	217,356	4,511,748	36,756	4,766,793
Total		**1,145,925**	**561,341**	**605,994**	**5,860,927**	**36,756**	**8,210,943**
31 Dec 2016							
Interest free		1,144,789	611,756	86,834	875,105	32,251	2,750,735
Floating interest	2.09%	70,981	29,634	297,689	693,488	-	1,091,792
Fixed interest	4.84%	313	626	837,098	963,718	3,850,940	5,652,695
Total		**1,216,083**	**642,016**	**1,221,621**	**2,532,311**	**3,883,191**	**9,495,222**

The Group has access to sources of financing. The total unused amount at the end of the reporting period was HRK 1,319,608 thousand. The Group expects to meet its other obligations from operating cash flows and proceeds from matured financial assets.

Fair value of financial instruments

The fair values of financial assets and financial liabilities are determined as follows:

- The fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets is determined with reference to quoted market prices.
- The fair value of other financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions.

37. FINANCIAL RISK MANAGEMENT (continued)

- The fair value of derivative instruments is calculated by using the quoted prices. Where such prices are not available, an analysis of discounted cash flows is used by the applicable yield curve for the period of non-derivative financial instruments.

Fair value indicators are recognized in the balance sheet

The table analyzes the financial instruments that have been reduced to fair value after the first recognition are classified into three groups in accordance with IFRS 13:

Level 1 - Fair Value Indicators are derived from (non-harmonized) prices quoted on active markets for identical assets and identical liabilities

Level 2 - fair value indicators are derived from other data, not from quoted prices from Level 1, relating to the observed asset or liability (i.e. their prices) or indirectly (derived from the price) and

Level 3 - Indicators derived using valuation methods in which inputs or assets are used as input data, which are not based on available market data (unavailable input data).

Measurement of fair value of currency swap is linked to the value of "Markt To Market" (MTM) "according to the calculation of commercial banks and the value is adjusted to each reporting date through profit or loss.

The fair value levels recognized in the consolidated statement of financial position are :

	Level 1 In HRK '000	**Level 2** In HRK '000	**Level 3** In HRK '000	**Total** In HRK '000
31 December 2017				
Available-for-sale assets	284,443	-	-	**284,443**
Derivative financial assets	-	-	-	**-**
Derivative financial liabilities	-	-	505,228	**505,228**
Investment property	-	305,630	-	**305,630**
31 December 2016				
Available-for-sale assets	295,938	-	-	**295,938**
Derivative financial assets	-	-	96,196	**96,196**
Derivative financial liabilities	-	-	32,251	**32,251**
Investment property	-	231,491	-	**231,491**

38. OTHER DISCLOSURES

The auditors of HEP Group's financial statements provided services in the amount of HRK 730 thousand (in 2016: HRK 730 thousand). Services in 2017 and 2016 mainly relate to audit costs, review of condensed interim financial information and audits of regulatory reports prepared for regulatory needs.

39. EVENTS AFTER THE REPORTING PERIOD

New Management and Supervisory Board

From 1 January 2018, new members of the Management Board and the Supervisory Board of the Company were appointed (Note 1).

After the consolidated statement of financial position date / (consolidated balance sheet) date, there were no events relevant to be published in the consolidated financial statements of the Company for 2017.

40. APPROVAL OF THE FINANCIAL STATEMENTS

These consolidated financial statements were approved by the Management Board and authorized for issue on 27 April 2018.

Signed on behalf of the Company on 27 April 2018:

Marko Ćosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

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