



**HRVATSKA ELEKTROPRIVREDA d.d., ZAGREB**

Non-consolidated annual financial statements  
and Independent Auditor's Report  
for the year 2017

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## Responsibility for the non-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 non-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 financial position, the results of operations, changes in equity and 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 non-consolidated annual financial statements of the Company.


In preparing the non-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 in preparation of annual financial statements, 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 financial position, the results of operations, changes in equity and 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 Cosić



Member

Nikola Rukavina



Member

Petar Sprčić



Member

Tomislav Šambić



Member

Saša Dujmić



Member

Frane Barbarić



President

HRVATSKA ELEKTROPRIVREDA D.D.  
ZAGREB 32  
Ulica grada Vukovara 37

Hrvatska elektroprivreda d.d.

Ulica grada Vukovara 37

10000 Zagreb

Republic of Croatia

27 April 2018

## INDEPENDENT AUDITOR'S REPORT

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

Report on the audit of the non-consolidated annual financial statements

### Opinion

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

In our opinion, the accompanying non-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 financial performance and 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 non-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 25 to the non-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 based on 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 29 to the non-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, 2017 and 2018, the Company continued activities with relevant Ministries and Institutions on the above-mentioned issue. Our opinion has not been modified in this respect.

The Company's accompanying non-consolidated annual financial statements are prepared in accordance with International Financial Reporting Standards and the requirements of Croatian laws and regulations, and the Company's investments in subsidiaries and associates are stated at cost. The Company has also prepared consolidated financial statements for the Company and its subsidiaries compiled on 27 April 2018. For a better understanding of the Company and the Group as a whole, users should read the annual consolidated financial statements together with these non-consolidated annual financial statements.

### **Other matters**

Attention is drawn to Note 29 to the financial statements, where is, in accordance with point (b) of paragraph 8 Article 21a of the Labour Act, listed a web page where the separate non-financial report of the Company will be published no later than 6 months from the date of the Statement of financial position (Balance Sheet). Our opinion has not been modified in this respect.

### **Key Audit Matters**

Key audit matters are those that, in our professional judgment, were of most significance in our audit of the non-consolidated annual financial statements for the current period, and include the most significant recognized 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 non-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
<p><b>Valuation of investments in subsidiaries and joint ventures</b></p> <p>As at 31 December 2017 the Company reported investments in subsidiaries were determined in the amount of HRK 9,465,828 thousand. Impairment of investments in subsidiaries is defined as key audit matter. As there are some impairment indicators for individual companies, the Company's Management Board was required to assess the value of said investments in subsidiaries. Determining the value of individual investments in subsidiaries requires the Company's Management to make significant estimates of future cash flows and associated discount rates and growth rates based on estimates of future business of the companies.</p> <p><b>Related disclosures in the non-consolidated annual financial statements</b></p> <p>See Notes 3,9,14 and 15 in the accompanying non-consolidated annual financial statements.</p>	<p>Our auditing procedures, related to this area included, among others:</p> <ul style="list-style-type: none"> <li>- The assessment of the reasonableness of the key assumptions used in the valuation model for valuation of investments in subsidiaries and joint ventures, and in particular the projections of operating cash flows, discount rates and long-term growth rates estimates.</li> <li>- The comparison of the key assumptions with external information and the estimates, made by ourselves.</li> <li>- The test of the mathematical accuracy of the valuation model for valuation of investments in subsidiaries and joint ventures.</li> <li>- The test of the sensitivity of the valuation model for valuation of investments in subsidiaries and joint ventures regarding the change of key assumptions.</li> </ul> <p>We have also assessed the adequacy of the Company's disclosure of investments in subsidiaries and joint ventures.</p> <p>The results of our tests were satisfactory and we agree that the assumptions used in the valuation model, are appropriate.</p>
<p><b>Contingent liabilities and court disputes</b></p> <p>Since the Company 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 of which the determination of the amount for disclosure and disclosure in the financial statements, if applicable, is subject to a subjective assessment.</p> <p>According to that, the Management Board estimates future outcomes and amounts of contingent liabilities that may arise as a result of these claims.</p> <p><b>Related disclosures in the non-consolidated annual financial statements</b></p> <p>See Notes 2, 3 and 26 in the accompanying non-consolidated annual financial statements.</p>	<p>Our auditing procedures, related to this area included, among others:</p> <ul style="list-style-type: none"> <li>- Receiving and analysing the attorneys' responses to our written inquiries and considering certain issues with them;</li> <li>- Critical review of the used assumptions and estimates pertaining to the claims. This includes assessing the likelihood of unfavourable outcomes of court proceedings and the reliability of the assessment of the related amount of obligation;</li> <li>- Assessment of the adequacy of disclosure in the financial statements, taking into account sensitivity and possible prejudice in the disclosure of detailed information, to obtain and analyse the statements of all external legal representatives for all material proceedings.</li> </ul> <p>Based on the collected evidence, taking into account inherent uncertainty in legal issues, we agree with the Company's management's assessment of the likelihood of future significant outflows related to these issues. We have found that issues that are likely to become future outflows are stated as provisions.</p> <p>Furthermore, we assessed the adequacy of the Company's disclosure regarding Contingent liabilities and court disputes. The results of our tests were satisfactory.</p>

## **Other Information in the Annual Report and separate nonfinancial report**

The Management Board is responsible for other information. Other information includes information included in the Annual report, but does not include the non-consolidated annual financial statements and our Independent Auditor's Report on 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 non-consolidated annual financial statements does not include other information, except to the extent explicitly stated in the part of our Independent auditor's report, entitled *Report on compliance with other legal or regulatory requirements*, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the non-consolidated annual financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the non-consolidated annual financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated; as well as whether the 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 have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. In this sense, we do not have anything to report.

When we read a separate non-financial report, if we find that there is a significant misstatement in it, we are required to inform the Management and those charged with governance of the Company.

## **Responsibilities of the Management and Those Charged with Governance for the non-consolidated annual financial statements**

The Management is responsible for the preparation of non-consolidated annual financial statements that give a true and fair view in accordance with IFRS, 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 non-consolidated annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the non-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 non-consolidated annual financial statements**

Our objectives are to obtain reasonable assurance about whether the non-consolidated annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Independent 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 non-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 non-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 audit 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 non-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 non-consolidated annual financial statements, including the disclosures, and whether the non-consolidated annual financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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 non-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 Compliance with Other Legal or Regulatory 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, based on the suggestion of the Supervisory Board, to audit the non-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 114,704 thousand, which represents about 1.5% of the total sales revenues of the Company for 2017, considering significant 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 9 to 94 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, 6 and 7 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 9 to 94 on which we expressed our opinion as stated in the section Opinion above.

The engagement partner on the audit of non-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

BDO Croatia d.o.o.  
Trg J. F. Kennedy 6b  
10000 Zagreb

  
Jeni Krstičević, President of the  
Management Board**BDO**

BDO Croatia d.o.o.  
za pružanje revizorskih, konzalting  
i računovodstvenih usluga  
Zagreb, J.F. Kennedy 6/b









Vedrana Stipić, Certified Auditor

Income statement – HEP d.d.  
For the year ended 31 December 2017

	Note	2017 in HRK'000	2016 in HRK'000
Revenue from electricity sales	4	3,317,347	3,242,537
Revenue from electricity sales-related companies	28	2,921,350	2,897,038
Revenue from sale of gas	4	967,937	1,106,876
Revenue from sale of gas to HEP- Plin – related company	4,28	132,384	128,938
Operating income – related companies	28	307,939	319,829
<b>Income from sale</b>		<b>7,646,957</b>	<b>7,695,218</b>
Other operating income	5	86,622	172,705
<b>Total operating income</b>		<b>7,733,579</b>	<b>7,867,923</b>
Electricity purchase cost	6	(2,578,790)	(1,957,758)
Electricity supplies – related companies	28	(209,780)	(584,920)
Costs of gas sold	29	(1,124,593)	(1,244,014)
Staff cost	7	(91,177)	(86,110)
Depreciation and amortization costs	11,12	(49,113)	(63,125)
Costs of fees and services - related companies	28	(2,775,469)	(2,598,170)
Other operating expenses	8	(768,551)	(468,529)
<b>Total operating expenses</b>		<b>(7,597,473)</b>	<b>(7,002,626)</b>
<b>Operating profit</b>		<b>136,106</b>	<b>865,297</b>
Financial income		1,090,266	974,254
Financial expenses		(934,010)	(334,068)
<b>Net profit from financial activities</b>	9	<b>156,256</b>	<b>640,186</b>
<b>Profit before taxation</b>		<b>292,362</b>	<b>1,505,483</b>
Corporate income tax expense	10	71,661	(181,664)
<b>Profit for the year</b>		<b>364,023</b>	<b>1,323,819</b>

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

Signed on behalf of the Company on 27 April 2018:

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







HRVATSKA ELEKTROPRIVREDA d.d.  
ZAGREB  
Ulica grada Vukovara 37

Statement of other comprehensive income – HEP d.d.  
For the year ended 31 December 2017

	2017 in HRK'000	2016 in HRK'000
<b>Profit for the year</b>	<b>364,023</b>	<b>1,323,819</b>
<b>Other comprehensive income</b>		
Net gain from AFS financial assets	(3,565)	39,456
Net other comprehensive income to be reclassified to profit/ (loss) in subsequent periods	(3,565)	39,456
<b>Other comprehensive income, net</b>	<b>(3,565)</b>	<b>39,456</b>
<b>Total comprehensive income for the year, net</b>	<b>360,458</b>	<b>1,363,275</b>

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

Signed on behalf of the Company on 27 April 2018:

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

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

Statement of financial position / Balance sheet – HEP d.d.  
As at 31 December 2017

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<b>ASSETS</b>	<b>Note</b>	<b>31 Dec 2017</b> in HRK'000	<b>31 Dec 2016</b> in HRK'000
<b>Non-current assets</b>			
Property, plant and equipment	11	762,226	1,349,042
Intangible assets	12	128,365	57,745
Investments in property	13	33,266	15,433
Investments in stakes and equity	14	9,465,828	9,203,125
Available-for-sale and other investments	15	284,163	289,938
Long term loans	16,28	17,069,042	17,046,947
Other receivables	17	543	666
Deferred tax assets	10	105,279	19,727
<b>Total non-current assets</b>		<b>27,848,712</b>	<b>27,982,623</b>
<b>Current assets</b>			
Inventories	18	467,902	605,412
Trade receivables	19	325,006	320,061
Current portion of long-term receivables	28	1,355,636	1,342,170
Other short-term receivables	20	292,342	201,734
Receivables from related companies	28	3,153,035	2,692,696
Cash and cash equivalents	21	925,174	2,366,100
<b>Total current assets</b>		<b>6,519,095</b>	<b>7,528,173</b>
<b>TOTAL ASSETS</b>		<b>34,367,807</b>	<b>35,510,796</b>

Statement of financial position / Balance sheet – HEP d.d. (continued)  
As at 31 December 2017

<b>EQUITY AND LIABILITIES</b>	<b>Note</b>	<b>31 Dec 2017</b> in HRK'000	<b>31 Dec 2016</b> in HRK'000
Share capital	22	19,792,159	19,792,159
Revaluation reserves	22	136,727	140,292
Retained earnings	22	5,220,987	5,649,310
<b>Total equity</b>		<b>25,149,873</b>	<b>25,581,761</b>
Liabilities under issued bonds	23	3,595,828	3,606,173
Long-term loan liabilities	24	259,119	654,682
Other long-term liabilities	25	1,273,807	909,524
Long-term provisions	26	217,014	212,605
Deferred tax liabilities		24,304	26,007
<b>Total non-current liabilities</b>		<b>5,370,072</b>	<b>5,408,991</b>
Current portion of long-term bonds issued	23,24	405,219	995,312
Liabilities toward related companies	28	2,790,547	2,758,202
Other short-term liabilities	27	652,096	766,530
<b>Total current liabilities</b>		<b>3,847,862</b>	<b>4,520,044</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>34,367,807</b>	<b>35,510,796</b>

The accompanying notes form an integral part of these non-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






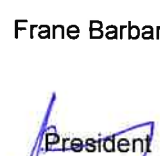
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ZAGREB 3.2  
Ulica grada Vukovara 37

Statement of changes in equity – HEP d.d.  
For the year ended 31 December 2017

	Share capital in HRK'000	Revaluation reserves in HRK'000	Retained earnings in HRK'000	Total in HRK'000
<b>Balance at 1 January 2016</b>	<b>19,792,159</b>	<b>100,836</b>	<b>4,932,491</b>	<b>24,825,486</b>
Profit for the year	-	-	1,323,819	1,323,819
Other comprehensive income	-	39,456	-	39,456
<i>Total comprehensive income</i>	-	39,456	1,323,819	1,363,275
Dividends paid	-	-	(607,000)	(607,000)
<b>Balance at 31 December 2016</b>	<b>19,792,159</b>	<b>140,292</b>	<b>5,649,310</b>	<b>25,581,761</b>
Profit for the year	-	-	364,023	364,023
Other comprehensive income	-	(3,565)	-	(3,565)
<i>Total comprehensive income</i>	-	(3,565)	364,023	360,458
Merger effects	-	-	1,945	1,945
Dividends paid	-	-	(794,291)	(794,291)
<b>Balance at 31 December 2017</b>	<b>19,792,159</b>	<b>136,727</b>	<b>5,220,987</b>	<b>25,149,873</b>

The accompanying notes form an integral part of these non-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.  
Z A G R E B 3.2  
Ulica grada Vukovara 37

Statement of cash flow – HEP d.d.  
For the year ended 31 December 2017

	2017	2016
	in HRK'000	in HRK'000
<b>OPERATING ACTIVITIES</b>		
Profit before tax	292,362	1,505,483
Net profit /(loss) from financial activities	81,718	(640,186)
Depreciation of property, plant and equipment and intangible assets	49,113	63,125
Increase in provisions	4,409	1,016
Fair value of property investment	4,025	(946)
Impairment of receivables	811	5,283
Impairment of tangible assets	274,100	0
<i>Operating cash flows before movements in working capital</i>	<i>706,538</i>	<i>933,775</i>
(Increase) in trade receivables	(5,756)	(15,381)
(Increase)/decrease in receivables from related companies	(445,656)	916,214
Decrease in inventories	137,510	148,212
(Increase) in other current assets	(99,543)	(44,472)
(Decrease) in trade payables	(136,067)	(51,577)
Increase/(decrease) in other liabilities	193,709	(5,856)
(Decrease) in liabilities to subsidiaries	32,345	179,629
(Decrease) in other long-term liabilities	345,575	-
<b>Cash from operations</b>	<b>728,655</b>	<b>2,060,544</b>
Corporate income tax paid	(179,155)	(223,413)
Interest paid	(227,692)	(244,604)
<b>NET CASH FROM OPERATING ACTIVITIES</b>	<b>321,808</b>	<b>1,592,527</b>









Statement of cash flow – HEP d.d. (continued)  
For the year ended 31 December 2017

	2017 in HRK'000	2016 in HRK'000
<b>INVESTING ACTIVITIES</b>		
Interest receipts	139,162	161,631
Dividends from related companies	11,837	431,710
Sale of tangible assets to related companies	0	(79,324)
Increase in the share capital of the subsidiary	0	(70,000)
Acquisition of property, plant and equipment	(114,843)	(360,114)
Cost of acquisition of other non-current assets	(3,999)	92,275
Collection of loan receivables from related companies	(23,307)	(422,547)
<b>NET CASH FROM INVESTING ACTIVITIES</b>	<b>8,850</b>	<b>(246,369)</b>
<b>FINANCING ACTIVITIES</b>		
Dividend payment	(794,291)	(607,000)
Repayments of bonds issued	(584,507)	(93,380)
Long-term loans received	12,149	147,623
Repayments of long-term loans	(404,935)	(379,174)
<b>NET CASH FROM INVESTING ACTIVITIES</b>	<b>(1,771,584)</b>	<b>(931,931)</b>
<b>NET INCREASE /(DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>(1,440,926)</b>	<b>414,227</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR</b>	<b>2,366,100</b>	<b>1,951,873</b>
<b>CASH AND CASH EQUIVALENTS AT END OF THE YEAR</b>	<b>925,174</b>	<b>2,366,100</b>

The accompanying notes form an integral part of these non-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

HRVATSKA ELEKTROPRIVREDA d.d.  
ZAGREB  
Ulica grada Vukovara 37

## 1. GENERAL

### *Foundation and development*

Hrvatska elektroprivreda d.d. Zagreb (hereinafter: HEP d.d. or the Company) is registered in Zagreb with its headquarters at Ulica Grada Vukovara 37. The Company's principal activities are the generation, transmission and distribution of electricity. Since 1 July 2002 it began operating with subsidiary companies as the sole owner of companies that are engaged in the generation, transmission, distribution, supply and trade of electricity, and the distribution and supply of thermal power through the district heating systems in Zagreb, Osijek and Sisak as well as the distribution and supply of gas in the regions of Osijek-Baranja, Požega-Slavonia and Virovitica-Podravina counties.

HEP d.d. sells electricity to customers who have chosen HEP Opskrba d.o.o. as their supplier and HEP Opskrba d.o.o. is responsible for service supply and collection from customers.

A new Law on the Electricity Market adopted in February 2013 determined further restructuring and adjustments of operations of HEP Group with European Union directives and guidelines.

Pursuant to the provisions of the Electricity Act (Official Gazette 22/2013) the Company, as the ruling company within a vertically integrated organisation and the owner of the transmission system, separated the transmission operator system in accordance with the provisions of the Act.

At the beginning of July 2013, amendments were conducted to the HEP Operator prijenosnog sustava (now: Hrvatski operator prijenosnog sustava d.o.o., abbreviated: HOPS d.o.o.) for the purpose of dividing it in accordance with the ITO model and pursuant to the Electricity Act and a decision by the HEP d.d. Assembly to select a model of an "independent transmission operator."

All these activities were conducted by the Company in accordance with valid laws, regulations and decisions by the Government of the Republic of Croatia.

As at 31 December 2017 HEP d.d. employed 451 employees (2016: 428).

The qualification structure of the employees on 31 December 2017 was as follows: PhD: 7; Master's degree: 37, Bachelor's degree: 258; Higher education: 42 and high school education: 107.

Business subjects that are part of the HEP Group and transactions with related parties are listed in the Note 28 to the non-consolidated financial statements.

### **Leases**

During restructuring process, property, plant and equipment and intangible assets are leased to subsidiaries of the Company at carrying value. Leases of property, plant and equipment and intangible assets are classified as finance leases since all the risks and awards of the ownership are transferred to the lessee. Maturity date of lease is equal to remaining useful depreciation life of leased assets. Lease liabilities are stated with the related companies within long-term liabilities. Leases bears interests to the extent that the Company has acquired funds by external financing for construction of the corresponding asset.

The fair value of leases has not been estimated due to the specific organization of the HEP Group and with the aim of disclosing underlying assets at their original carrying value at which they were acquired by the Group. Consequently, for a better understanding of the Company, the accompanying financial statements should be read in conjunction with the consolidated financial statements of the HEP Group.

## **1. GENERAL (continued)**

### **Revenue recognition**

All revenues related to the sale and supply of electricity to customers chosen by HEP Opskrba d.o.o. are transferred from HEP Opskrba d.o.o.

The company HEP Operator distribucijskog sustava d.o.o., since 2 November 2016 HEP Elektra d.o.o., recognizes revenues for delivered electricity to household customers on the basis of energy data generated by sales to customers and the amounts of tariff items according to the decision of the Croatian Energy Regulatory Agency ('HERA'), on the amount of tariff items for the supply of electricity within universal service. From the entry into force of the Act on Amendments to the Electricity Market Act, tariffs for electricity supply within the universal service are made by the supplier who is obliged to provide the public service.

The company HEP Operator distribucijskog sustava d.o.o., since 2 November 2016 HEP Elektra d.o.o., recognizes the revenues for delivered electricity to enterprise customers under the guaranteed supply based on the energy data generated by sales to customers and the amounts of tariff items in accordance with the Methodology for determining the amount of tariff items for the guaranteed electricity supply and HERA decisions on the amount of tariff items for guaranteed electricity supply.

Subsidiaries Hrvatski operator prijenosnog sustava d.o.o. and HEP Operator distribucijskog sustava d.o.o. recognize revenue in the amount of delivered and transferred electricity based on energy data of realized sales to customers and the amounts of tariff items based on the method of cost recovery according to the Tariff System for power transmission, and the amounts of tariff items and Tariff System for Electricity Distribution,. Revenue recognition is based on the Decision on the amount of tariff items for electricity distribution and the Decision on the amount of tariff items for electricity transmission made by HERA in December 2015, effective from 1 January 2016.

The company HEP Proizvodnja d.o.o. recognizes revenue for the amount of electricity produced based on the fees according to energy data on delivered electricity and realized costs for the production of electricity increased by profit made on sale of electricity to end customers, network operators for the loss of electricity and on the wholesale market.

## 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 Company's significant accounting policies which have been applied consistently in the current and previous years is set out below.

### ***Presentation of financial statements***

#### *a) Non-consolidated financial statements*

The non-consolidated financial statements for 2017 have been prepared in accordance with the Accounting Act (Official Gazette 75/15, 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).

Exceptionally, in order to have a more appropriate presentation of the financial statements and to eliminate possible obscurity and misinterpretations, the Company deviated from the specific requirements of IFRS 11 "Joint Operations" (Note 15).

Management believes that the financial statements present fairly the financial position, financial performance and cash flows.

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

The financial statements have been prepared with the application of the basic accounting assumption of the occurrence of a business event and the assumption of the going concern concept.

#### *b) Consolidated financial statements*

The Company has prepared these financial statements in accordance with Croatian legislative regulations.

The Company has also prepared consolidated financial statements for the Company and its subsidiaries, which together with the Company comprise the Group, as at 31 December 2017 and for the year then ended. The consolidated financial statements have been prepared in accordance with IFRS and were approved by the Management Board on 27 April 2018. In the consolidated financial statements, subsidiaries (listed in the Note 28) – in which the Company has more than half of voting rights or in some other way controls their business, have been entirely consolidated. These financial statements should be read in conjunction with the consolidated financial statements of the HEP Group as at and for the year ended 31 December 2017, in order to obtain complete information about the Group's financial position, the results of its operations and changes to the Group's financial position overall.

### ***Basis of accounting***

The Company 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.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### ***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.

- **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.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### ***Adoption of new and revised International Financial Reporting Standards (continued)***

*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.

- ***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.



## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### ***Adoption of new and revised International Financial Reporting Standards (continued)***

*Standards and Interpretations issued by the Standards Board that have not yet been effective and which the Company has not previously adopted (continued)*

- **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.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### ***Investments in subsidiaries***

A subsidiary company is a company in which the Company (Parent company) has control over, meaning that it manages the financial and business policies by participating in the decision making regarding financial and business policies of the subsidiary. Investments in subsidiaries are stated at the end of the reporting period impaired for individual investment.

### ***Investments in associates***

Associates are companies in which the Company is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the investee.

Investments in Associates are stated at cost with impairment value.

### ***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 Company 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 are measured using equity method.

In the consolidated financial statements the Company recognizes its investment in NE Krško d.o.o. as joint operation through its share of assets, liabilities, income and expenses in accordance with its contractual rights and obligations.

As described in the Note 14, in the non-consolidated financial statements the Company deviated from the specific requirements of IFRS 11 "Joint Operations" and recognizes its investment in NE Krško d.o.o. using equity method.

### ***Reporting currency***

The Company's financial statements are stated in Croatian Kuna (HRK '000).

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### ***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.

	<b>2017 and 2016</b>
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 pension insurance 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).

### ***Retirement allowances and jubilee awards***

The Company 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 on Croatian 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 Company 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.

#### ***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 Agreement is until 31 December 2017.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### *Property, plant and equipment*

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.

Property, plant and equipment in use are depreciated using the straight-line method on the following bases:

	<b>2017 and 2016</b>
Buildings	20-50 years
Office and IT equipment	5-20 years
Vehicles	5 years
Office furniture	10 years

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. Expenditures incurred after property, plant and equipment 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 property, plant and equipment 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 property, plant and equipment is 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 income statement.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### ***Property, plant and equipment (continued)***

#### *Impairment of property, plant and equipment and intangible assets*

At each reporting date, the Company reviews the carrying amounts of its property, plant and equipment 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 Company 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.

Recoverable amount is higher of net sales price 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 for which the estimates of future cash flows have not been adjusted.

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 land or building not used as investment property; i.e. investment in property 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.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### ***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 Company as lessee***

The Company 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 the statement of comprehensive income on a straight-line basis over the lease term.

#### ***The Company as lessor***

Property, plant and equipment and intangible assets are leased out by Company to related companies based on the carrying amount (except for HOPS as of 1 July 2013, and HEP Telekomunikacija). Leases of property, plant and equipment and intangible assets are classified as finance leases since all the risks and awards of the ownership are transferred to the lessee. Maturity date of lease is equal to remaining useful depreciation life of leased assets.

The leases bear interest to the extent that the Company has acquired external financing to construct the underlying assets. These properties are stated at cost in order to present the underlying assets at their carrying value at which the Company initially recognized them.

## 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 ageing 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 longer period, the Company 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 interest) 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.

From 2013, inventories include CO<sub>2</sub> emission rights. After Croatia joined the European system for greenhouse gas emissions trading (EU ETS), Hrvatska elektroprivreda (the Company) as an electricity and thermal energy generator, is obligated to purchase greenhouse gas emission units in the amount corresponding to verified emissions of CO<sub>2</sub> generated from the fossil fuel combustion in thermal power plants, as a result of which CO<sub>2</sub> is emitted.

Companies are obligated to have defined quantities of CO<sub>2</sub> emission rights at 30 April (yearly cycle). Due to the withdrawal of IFRIC 3 and insufficient provisions of IFRS, the Company has analysed different accounting models for CO<sub>2</sub> emission rights, and among other EFRAG discussion papers. Occasionally, the Group trades with CO<sub>2</sub> emission rights. Due to that the Company recognize these emission rights as inventory.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **Inventories (continued)**

From April 2014, the inventories also contain gas for wholesale trading and are stated at a lower value than the acquisition cost determined on the basis of the average weighted price and net expected sales value (Note 18).

For gas quantities that are directly delivered to customers to calculate inventory costs, a specific identification method of their individual costs is used.

The cost of the purchase includes the invoiced amount and other costs incurred directly in relation to bringing the inventory to a particular location and in usable 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 in the period on an accrual basis.

### ***Foreign currencies***

Separate financial statements of the Company are presented in the currency of the primary economic environment in which the entity operates (its functional currency).

In the financial statements of the Company, 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 as profit or loss in the period in which they incurred. Exchange differences arising on retranslation of non-monetary assets carried at fair value are stated as profit or loss, 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)**

### ***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 income statement 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 Company's current tax liability is calculated using tax rates that have been enacted or substantively enacted at the end of the reporting period.

#### *Deferred tax*

Deferred tax is recognized 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 merger) 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 Company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

#### *Current and deferred tax for the period*

Deferred tax is recognized as an expense or income in the statement of comprehensive income, except when relate 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.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### ***Taxation (continued)***

#### ***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", "financial assets 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 recognized on an effective interest basis for debt instruments.

#### ***Available-for-sale financial assets***

Shares held by the Company 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 recognized 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 recognized directly in profit or loss for the period. Where the investment is disposed or impaired, the cumulative gain or loss previously recognized 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 Company's right to receive the dividends has 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 is 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 and determinable payments and that are not quoted on an active trading market, are classified as "loans and receivables" and 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 would 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 Available-for-sale financial assets 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 statement of comprehensive income to the extent that the carrying amount of the investment, at the date when the impairment is reversed, which does not exceed what the amortized cost would have been if the impairment has not been recognized.

In respect of Available-for-sale financial assets 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.

## **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 Company derecognizes financial liabilities only when the Company'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.

The Company brought Decision on measurement of the fair value of the cross-currency swap according to 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.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### ***Provisions***

Provisions are recognized when the Company 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.

### ***Use of estimates in preparation of the financial statements***

Preparation of the financial statements in conformity with International Financial Reporting Standards as published by the International Accounting Standards Board, 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 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 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 who chose HEP Opskrba d.o.o. as supplier, the sale of electricity to related company and in the market, and compensation for administrative services for Group companies.

## **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 financial statements (independently of those shown below).

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 Company 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 Notes 19 and 20, Management uses judgment to estimate whether trade and other receivables have suffered an impairment loss.

### 3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

#### *Provisions for power plant decommissioning*

The Management estimates the cost of provisions for the decommissioning of the Krško Nuclear Power Plant (NEK) and the thermoelectric power plants of the Group on the basis of applicable laws and regulations and its own experience.

Provisions also include activities related to environmental protection to be carried out during the decommissioning of production facilities.

Funds for decommissioning of NEK are provisioned in accordance with the Regulation on amount, deadline and method of payment of funds for financing the decommissioning and disposal of radioactive waste and used nuclear fuel of Krško Nuclear Power Plant (OG 155/08) (note 14).

The amount of provisions for the decommissioning of thermal power plants represents the discounted value of the estimated cost of decommissioning of the thermal power plants of the Group.

#### *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. The Company did not have any impairments arisen from above mentioned projections.

#### *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 realized 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. Carrying amount of deferred tax assets as at 31 December 2017 amounted to HRK 105,279 thousand, as at 31 December 2016 to HRK 19,727 thousand (see 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. Provisions for jubilee awards and severance payments amounted to HRK 15,992 thousand as at 31 December 2017, and to HRK 12,379 thousand as at 31 December 2016 (see Note 26).

#### *Consequences of certain court disputes*

The Company 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 legal 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. Provisions for court disputes as at 31 December 2017 amounts to HRK 179,391 thousand, and as at 31 December 2016: HRK 178,595 thousand (see Note 26).

### **3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)**

#### *Accounting of NEK joint operation*

As described in the Note 14, joint operation in NEK is recognized in the financial statements by using the equity method (in 2014 the Company recognized its share in assets, liabilities, revenues and expenses of NEK in its financial statements). The application of the requirements of IFRS 11 has resulted in a number of issues and concerns, as well as misinterpretation by some of users of the financial statements.

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

#### 4. SALES REVENUE

##### /i/ REVENUE FROM ELECTRICITY SALES

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Income from the sale of electricity to customers of HEP Opskrba d.o.o.	2,332,348	2,408,514
Income from the sale of electricity abroad	907,718	790,799
Income from the sale of electricity in the country	<u>77,281</u>	<u>43,224</u>
	<b><u>3,317,347</u></b>	<b><u>3,242,537</u></b>

##### /ii/ INCOME FROM GAS SUPPLY ON THE WHOLESALE MARKET

By a Decision of the Government of the Republic of Croatia in April 2014, HEP d.d. was defined as a gas supplier on the wholesale market in a period until April 2017. Pursuant to the above Decision from the Croatian Government, the Company has rented 70% of warehouse capacities in underground gas storage facilities.

The Act on Amendments to the Gas Market Act (OG, 16/17) Hrvatska elektroprivreda d.d. was appointed as gas wholesale suppliers from 1 April 2017 to the tender for the selection of suppliers on the wholesale gas market, Wholesale service provider sells gas to public service providers for the needs of household customers at regulated sales price and is obliged to provide reliable and secure gas supply.

As of 1 April 2017, the natural gas producer no longer has the obligation to deliver gas at the regulated price to which it was obliged to sell the gas to the gas supplier on the wholesale gas market for the needs of customers using the public service of supply. Pursuant to the Act on Amendments to the Market Act gas The Company has leased 60% of storage capacity in the underground gas storage facility.

Income from gas supply – unrelated companies in 2017 amounts to HRK 967,937 thousand (2016: HRK 1,106,876 thousand). Income from gas supply – related companies in 2017 amounts to HRK 132,384 thousand (2016: HRK 128,938 thousand).



## 5. OTHER OPERATING INCOME

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Receivables collected and impaired in previous years	20,917	21,562
Interest on arrears from customers	13,843	12,849
Income from leasing capacity to sell electric energy abroad	18,206	8,430
Income from the sale of tangible assets	16,040	29,021
Income from reversal of long-term provisions	-	1,820
Increase in shares of HEP Toplinarstvo d.o.o.	-	45,397
Income from connection fees	-	35,710
Other operating income	17,616	17,916
	<u><b>86,622</b></u>	<u><b>172,705</b></u>

## 6. COST OF ELECTRICITY

Costs of electricity reported in the Income statement for the year 2017 amount to HRK 2,578,790 thousand (2016: HRK 1,957,758 thousand) and relate to acquisitions outside the wholesale sales and sales system to final customers.

Costs of electricity are higher than in the previous year due to the increase in imported electricity and higher purchasing prices, as a consequence of rising prices on the wholesale market.

Electricity and gas trade is conducted bilaterally and on stock exchanges.

For the purchase of electricity and gas, futures contracts are contracted for which daily market price deviations are calculated, the price correction amounts are included in the purchase value of delivery.

## 7. STAFF COSTS

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Net salaries	52,742	48,654
Taxes and contributions from salaries	25,499	25,069
Contributions on salaries	12,936	12,387
	<b>91,177</b>	<b>86,110</b>

### Total staff costs :

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Gross salaries	91,177	86,110
Reimbursement of costs to employees (Note 8)	6,404	5,545
Material rights of employees (Note 8)	1,806	2,026
	<b>99,387</b>	<b>93,681</b>

Reimbursement of costs to employees includes commuting costs in the amount of HRK 2,062 thousand (2016: HRK 1,977 thousand), daily allowances and travelling expenses in the amount of HRK 2,080 thousand (2016: HRK 2,032 thousand) and other similar expenses.

Employee material rights include retirement bonuses for early retirement, jubilee awards and appropriate assistance.

**7. STAFF COSTS (continued)**

**Remuneration for members of the Management Board and executive directors of the Company:**

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Gross salaries	6,693	7,210
Benefits in kind	1,399	922
Contributions for pension insurance	1,578	1,626
	<b>9,670</b>	<b>9,758</b>

**Remuneration for members of the Supervisory Board of the Company:**

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Fees	189	192
Taxes and contributions	120	194
Other costs	4	18
	<b>313</b>	<b>404</b>

**8. OTHER OPERATING EXPENSES**

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
Impairment for bad and doubtful accounts	33,098	13,546
Impairment of investments	279,233	1,385
Costs for HEP d.d. from decommissioning NEK	106,386	107,196
Costs pursuant to services within subsidiary companies	35,694	32,199
Costs of services	105,756	98,922
Purchase of CO2 emission units	130,001	125,078
Taxes, contributions and allowances	10,859	8,750
Bank fees, payment operations fees and charges for loans	7,049	7,780
Benefits in kind (Note 7)	2,262	1,536
Travel allowance and transport costs (Note 7)	4,142	4,009
Insurance premiums	6,648	7,171
Write-off of uncollected receivables	1,196	1,216
Other material rights of employees (Note 7)	1,806	2,026
Costs of material	4,897	17,218
Provisions for severance packages and other staff costs	3,613	2,836
Provisions for unused vacations	3,938	845
Provisions for legal disputes	795	-
Compensation for damages	13,085	1,092
Other operating costs	18,093	35,724
	<b><u>768,551</u></b>	<b><u>468,529</u></b>

## 9. FINANCIAL INCOME AND EXPENSES

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
<b>Financial income</b>		
Interest	139,162	161,631
Foreign currency exchange gains	199,246	98,929
Dividend from subsidiary and associated companies	740,057	614,215
Income from dividend	8,935	7,176
Fair value of cross-currency swap (Note 23)	-	74,921
Income from stock market trading	-	14,894
Other financial income	2,866	2,488
<b>Total financial income</b>	<b><u>1,090,266</u></b>	<b><u>974,254</u></b>
<b>Financial expenses</b>		
Interest	(220,880)	(243,232)
Foreign exchange losses	(82,538)	(82,414)
Fair value of cross-currency swap	(569,173)	-
Revaluation of shares	(52,025)	-
Fair value of shares	(548)	-
Expenses from stock market trading	(2,243)	-
Other financial expenses	(7,620)	(8,422)
<b>Total financial expenses</b>	<b><u>(935,027)</u></b>	<b><u>(334,068)</u></b>
Capitalised borrowing costs	1,017	-
<b>Financial expenses recognized in the income statement</b>	<b><u>(934,010)</u></b>	<b><u>(334,068)</u></b>
<b>Net profit from financial activities</b>	<b><u>156,256</u></b>	<b><u>640,186</u></b>

# 10. CORPORATE INCOME TAX EXPENSE

Pursuant to tax legislation and regulations in the Republic of Croatia the Company is subject to taxes. The tax base is determined as the differences between amounts of income and expenses in the period and increased for expenses that are non-deductible. The income tax rate is 18% (2016: 20%)

	2017 in HRK'000	2016 in HRK'000
Current tax	13,891	169,960
Deferred tax expense relating to the origination and reversal of temporary differences	(85,552)	11,704
<b>Corporate income tax</b>	<b>(71,661)</b>	<b>181,664</b>

Adjustments of deferred tax assets are shown as follows:

	2017 in HRK'000	2016 in HRK'000
Balance at 1 January	19,727	31,431
Increase in deferred tax assets	85,552	(11,704)
Balance at 31 December	<b>105,279</b>	<b>19,727</b>

Deferred tax assets have arisen from tax unrecognized provisions for derivative financial instruments (SWAP), jubilee awards, severance payments and other staff costs, value adjustments of investment material inventory and doubtful receivables.

The reconciliation between the income tax and profit and loss account shown in the income statement is shown as follows:

	2017 in HRK'000	2016 in HRK'000
Profit before tax	292,362	1,505,483
<b>Tax based on tax rate in Croatia (18%/20%)</b>	<b>52,625</b>	<b>301,097</b>
Unrecognized tax (income) / expenses	(38,734)	(131,137)
<b>Tax expense for the year</b>	<b>13,891</b>	<b>169,960</b>
Effective tax rate	4.75%	11.29%

Reduction of the profit tax rate in Croatia from 20% to 18% came into effect on 1 January 2017. As a result of the change in the tax rate, the relevant positions of deferred taxes have been re-calculated for 2016.

# 10. CORPORATE INCOME TAX EXPENSE (continued)

The effects of non-deductible (income)/expenses consist of income from dividends, reversed receivables impairment, State aid for education and reduction of profit for other income.

In recent years Croatian Tax Authorities have not performed a review of the corporate income tax returns of the Company, except the short monitoring in 2013. In accordance with local regulations, the Tax Authority may at any time inspect the books and records of companies within 3 years following the year in which the tax liability is reported and may impose additional tax liabilities and penalties. The Management is not aware of any circumstances that could lead to a potential material liability in this respect.

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

	<b>31 Dec 2016</b>	Difference in corporate income tax rate	(Debited)/ credited to the income statement	<b>31 Dec 2017</b>
	in HRK'000	in HRK'000	in HRK'000	in HRK'000
Provisions for jubilee awards and retirement bonuses	<b>2,227</b>	-	651	<b>2,878</b>
Fair value adjustment - JANAF	<b>5,539</b>	-	-	<b>5,539</b>
Unrecognised tax value adjustment of receivables and interest	<b>1,198</b>	-	(1,198)	<b>0</b>
Provisions for costs of wind power plants	<b>3,894</b>	-	-	<b>3,894</b>
Provisions for Swap fair value adjustment	<b>5,805</b>	-	85,136	<b>90,941</b>
Other	<b>1,064</b>	-	963	<b>2,027</b>
	<b>19,727</b>		<b>85,552</b>	<b>105,279</b>

# 11. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Fixtures and equipment	Assets under construction	Prepayment	Total
	in HRK'000	in HRK'000	in HRK'000	in HRK'000	in HRK'000
<b>COST</b>					
<b>At 1 January 2016</b>	<b>526,331</b>	<b>1,465,703</b>	<b>447,646</b>	<b>21,454</b>	<b>2,461,134</b>
Additions	100	65,184	284,449	(14,248)	335,485
Transfer to related companies	(174,535)	(870,116)	(14,134)		(1,058,785)
Disposals	(179)	(15,017)	-		(15,196)
<b>At 31 December 2016</b>	<b>351,717</b>	<b>645,754</b>	<b>717,961</b>	<b>7,206</b>	<b>1,722,638</b>
Additions / Disposals	2,041	26,839	56,554	(1,184)	84,250
Increase by merging the company	227,640	2,032,496	192,101		2,452,237
Transfer of TE Plomin property to lease	(227,640)	(2,032,496)	(192,101)		(2,452,237)
Transfer to related companies	(1,010)	(323,581)	(55,394)		(379,985)
Activation of investment in intangible assets			(57,006)		(57,006)
Write-off		(5,944)	(274,100)		(280,044)
Transfer to investment property	(21,858)				(21,858)
<b>At 31 December 2017</b>	<b>330,890</b>	<b>343,068</b>	<b>388,015</b>	<b>6,022</b>	<b>1,067,995</b>
<b>ACCUMULATED DEPRECIATION</b>					
<b>At 1 January 2016</b>	<b>140,481</b>	<b>441,379</b>	<b>-</b>	<b>-</b>	<b>581,860</b>
Depreciation costs for the year	5,716	43,169	-	-	48,885
Disposals	0	(14,266)	-	-	(14,266)
Impairment	(51,771)	(191,112)	-	-	(242,883)
<b>At 31 December 2016</b>	<b>94,426</b>	<b>279,170</b>	<b>-</b>	<b>-</b>	<b>373,596</b>
Depreciation costs for the year	5,375	26,759	-	-	32,134
Impairment based on the merger	135,663	1,981,224	-	-	2,116,887
Impairment of assets transferred to lease	(135,663)	(1,981,224)	-	-	(2,116,887)
Impairment	-	(20,732)	-	-	(20,732)
Impairment of assets transferred to subsidiary	(213)	(79,016)	-	-	(79,229)
<b>At 31 December 2017</b>	<b>99,588</b>	<b>206,181</b>	<b>-</b>	<b>-</b>	<b>305,769</b>
<b>CARRYING AMOUNT</b>					
<b>At 31 December 2016</b>	<b>257,291</b>	<b>366,584</b>	<b>717,961</b>	<b>7,206</b>	<b>1,349,042</b>
<b>At 31 December 2017</b>	<b>231,302</b>	<b>136,887</b>	<b>388,015</b>	<b>6,022</b>	<b>762,226</b>



## 11. PROPERTY, PLANT AND EQUIPMENT (continued)

Investments in progress at 31 December 2017 in the Company amounted to HRK 388,015 thousand and the most significant relate to investment in the EDM/ECM projects amounting to HRK 56,253 thousand, investments in HE Kosiinj in the amount of HRK 27,921 thousand, cogeneration plants on forest biomass BE-TO Sisak in the amount of HRK 144,496 thousand and BE-TO Osijek in the amount of HRK 122,621 thousand. Investments in 2017 amounted to HRK 56,554 thousand, most significant being EDM/ECM project and cogeneration plants BE-TO Osijek and BE-TO Sisak.

## 12. INTANGIBLE ASSETS

**Patents and  
licences**  
in HRK'000

### COST

<b>At 1 January 2016</b>	<b>92,948</b>
Additions	10,382
Transfer between related companies	39,359
Disposals	(5,623)
<b>At 31 December 2016</b>	<b>137,066</b>
Additions	30,593
Additions based on merger	30,061
Write-offs on the basis of transfer of assets	(30,061)
Transfer from investment	57,006
Disposals	-
<b>At 31 December 2017</b>	<b>224,665</b>

### ACCUMULATED DEPRECIATION

<b>At 1 January 2016</b>	<b>70,704</b>
Depreciation costs for the year	14,240
Impairment	(5,623)
<b>At 31 December 2016</b>	<b>79,321</b>
Depreciation costs for the year	16,979
Impairment through merger of assets	30,061
Impairment through transfer of assets	(30,061)
<b>At 31 December 2017</b>	<b>96,300</b>
<b>Net carrying amount</b>	
<b>At 31 December 2016</b>	<b>57,745</b>
<b>At 31 December 2017</b>	<b>128,365</b>

### 13. INVESTMENT PROPERTY

As at 31 December 2017, investment property comprises of properties held for the purposes of earning rentals and/or capital appreciation, and are carried at fair value. The fair value comprises estimated market price at the end of the reporting period. All investment properties owned by the Company are stated at fair value.

#### Investment in property (in HRK'000)

<b>At 31 December 2016</b>	<b>15,433</b>	<b>14,487</b>
Net change in value based on adjustments	(4,065)	946
Classification of assets to investment property	21,858	-
<b>At 31 December 2017</b>	<b>33,266</b>	<b>15,433</b>

### 14. INVESTMENTS IN SHARES (EQUITY)

Investments in shares in the balance sheet as at 31 December 2017, in the amount of HRK 9,465,828 thousand (31 December 2016: HRK 9,203,125 thousand) consist of the investments shown in the table:

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
HEP - Proizvodnja d.o.o.	40	40
Hrvatski operator prijenosnog sustava d.o.o.	4,934,719	4,369,916
HEP - Operator distribucijskog sustava d.o.o.	1,764,960	1,764,960
HEP - Opskrba d.o.o.	20	20
HEP -Toplinarstvo d.o.o.	730,816	730,816
HEP - Plin d.o.o.	20	20
HEP ESCO d.o.o.	3,920	3,920
HEP – Upravljanje imovinom d.o.o.	17,995	70,020
HEP-Trgovina d.o.o.	20	20
Program Sava d.o.o.	20	20
HEP-Telekomunikacije d.o.o.	258,799	258,799
Plomin Holding d.o.o.	20	20
HEP Opskrba plinom d.o.o.	20	20
Hrvatski centar za čistiju proizvodnju	20	20
HEP Elektra d.o.o.	20	20
NE Krško (NEK) /i/	1,754,419	1,754,419
TE Plomin d.o.o. /ii/	-	250,075
	<b>9,465,828</b>	<b>9,203,125</b>

#### 14 INVESTMENTS IN SHARES (continued)

Changes in investments are shown in the table below:

	2017 in HRK'000	2016 in HRK'000
As at 1 January	9,203,125	8,036,694
Increase in share capital of HOPS d.o.o.	293,131	193,912
Increase of share capital from reinvested earnings- HOPS d.o.o.	271,672	189,680
HEP-Operator distribucijskog sustava d.o.o.,- capital reserves	-	605,280
HEP-Operator distribucijskog sustava d.o.o. – transfer of shares into HEP Elektra d.o.o.	-	(20)
HEP Elektra d.o.o., – founding capital		20
HEP Toplinarstvo d.o.o.- capital reserves	-	54,935
HEP-Telekomunikacije d.o.o.- capital reserves	-	57,604
Plomin Holding d.o.o.- reduction of share	-	(4,980)
HEP Upravljanje imovinom d.o.o. – increase / decrease of share capital	(52,025)	70,000
TE Plomin – merger to HEP-u d.d.	(250,075)	-
<b>As at 31 December</b>	<b>9,465,828</b>	<b>9,203,125</b>

#### /i/ INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK)

##### Investment background

In late 2001, the Governments of the Republic of Croatia the Republic of Slovenia signed an Agreement governing the status and other legal relations in connection with their respective investment in NEK, 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 came into force 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, Nuklearna elektrana Krško d.o.o. ('NEK') in respect to its 50% holding in NEK, 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 also clearly defined obligation towards the Croatian half of disposal of radioactive waste and used nuclear fuel from NEK. 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.

## **14 INVESTMENTS IN SHARES (continued)**

### **/i/ INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK) (continued)**

#### **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 NEK, 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 NEK 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 NEK has obtained from the Slovenian nuclear safety administration a safety license to operate without any limitations in 2012, at the beginning of 2016 HEP d.d. 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 NEK was preceded by an investment feasibility study of long-term investments in the power plant.

##### **Accounting of NEK joint operation**

Joint operation in NEK is recognized in the financial statements by using the equity method. The application of the requirements of IFRS 11 has resulted in a number of issues and concerns, as well as misinterpretation by some of users of the financial statements.

In order to eliminate possible concerns of individual government agencies (FINA, the Ministry of Finance, Central Bureau of Statistics, etc.) about the information in the separate financial statements of the Company, and in accordance with the provisions of IAS 1, point 19 and point 20, the Management adopted a decision to change said policy.

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

**14 INVESTMENTS IN SHARES (continued)**

**/i/ INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK) (continued)**

**Financial effect from deviation**

**Income statement for the year ended 31 December 2017**

	in HRK'000 HEP d.d.	in HRK'000 NEK d.o.o.	in HRK'000 HEP d.d. + NEK d.o.o.
<b>Total operating income</b>	<b>7,733,579</b>	<b>5,409</b>	<b>7,738,988</b>
<b>Total operating expenses</b>	<b>(7,597,473)</b>	<b>(5,965)</b>	<b>(7,603,438)</b>
<b>Operating profit/loss</b>	<b>136,106</b>	<b>(556)</b>	<b>135,550</b>
<b>Net profit/loss from financial activities</b>	<b>156,256</b>	<b>556</b>	<b>156,812</b>
<b>Profit before taxation</b>	<b>292,362</b>	<b>0</b>	<b>292,362</b>
Corporate income tax expense	71,661	0	71,661
<b>Profit for the year</b>	<b>364,023</b>	<b>0</b>	<b>364,023</b>

**Income statement for the year ended 31 December 2016**

	in HRK'000 HEP d.d.	in HRK'000 NEK d.o.o.	in HRK'000 HEP d.d. + NEK d.o.o.
<b>Total operating income</b>	<b>7,867,923</b>	<b>5,813</b>	<b>7,873,736</b>
<b>Total operating expenses</b>	<b>(7,002,626)</b>	<b>(3,132)</b>	<b>(7,005,758)</b>
<b>Operating profit/loss</b>	<b>865,297</b>	<b>2,681</b>	<b>867,978</b>
<b>Net profit/loss from financial activities</b>	<b>640,186</b>	<b>(983)</b>	<b>639,203</b>
<b>Profit before taxation</b>	<b>1,505,483</b>	<b>1,698</b>	<b>1,507,181</b>
Corporate income tax expense	(181,664)	-	(181,664)
<b>Profit for the year</b>	<b>1,323,819</b>	<b>1,698</b>	<b>1,325,517</b>

**14 INVESTMENTS IN SHARES (continued)**

**// INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK) (continued)**

**Financial effect from deviation (continued)**

**Balance sheet as at 31 December 2017**

	in HRK'000 <b>HEP d.d.</b>	in HRK'000 <b>NEK d.o.o.</b>	in HRK'000 <b>HEP d.d + NEK d.o.o.</b>
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	368,189	1,261,391	1,629,580
Financial assets	1,754,419	(1,652,665)	101,754
Other non-current assets	25,726,104	-	25,726,104
<b>Total non-current assets</b>	<b>27,848,712</b>	<b>(391,274)</b>	<b>27,457,438</b>
<b>Current assets</b>	<b>6,519,095</b>	<b>557,688</b>	<b>7,076,783</b>
<b>TOTAL ASSETS</b>	<b>34,367,807</b>	<b>166,414</b>	<b>34,534,221</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Total equity</b>	<b>25,149,873</b>	<b>1,698</b>	<b>25,151,571</b>
<b>Non-current liabilities</b>	<b>5,370,072</b>	<b>53,354</b>	<b>5,423,426</b>
<b>Current liabilities</b>	<b>3,847,862</b>	<b>111,362</b>	<b>3,959,224</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>34,367,807</b>	<b>166,414</b>	<b>34,534,221</b>

**14 INVESTMENTS IN SHARES (continued)**

**/i/ INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK) (continued)**

**Financial effect from deviation (continued)**

**Balance sheet as at 31 December 2016**

	in HRK'000 HEP d.d.	in HRK'000 NEK d.o.o.	in HRK'000 HEP d.d + NEK d.o.o.
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	623,875	1,200,993	1,824,868
Financial assets	1,754,419	(1,667,912)	86,507
Other non-current assets	25,601,681	-	25,601,681
<b>Total non-current assets</b>	<b>27,979,975</b>	<b>(466,919)</b>	<b>27,513,056</b>
<b>Current assets</b>	<b>7,530,821</b>	<b>553,689</b>	<b>8,084,510</b>
<b>TOTAL ASSETS</b>	<b>35,510,796</b>	<b>86,770</b>	<b>35,597,566</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Total equity</b>	<b>25,581,761</b>	<b>1,698</b>	<b>25,583,459</b>
<b>Non-current liabilities</b>	<b>5,408,991</b>	<b>35,854</b>	<b>5,444,845</b>
<b>Current liabilities</b>	<b>4,520,044</b>	<b>49,218</b>	<b>4,569,262</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>35,510,796</b>	<b>86,770</b>	<b>35,597,566</b>

## 14 INVESTMENTS IN SHARES (continued)

### /i/ INVESTMENTS IN KRŠKO NUCLEAR POWER PLANT (NEK) (continued)

Extract from financial statements

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

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Property, plant and equipment	2,522,782	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

### /ii/ INVESTMENT IN TE PLOMIN

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.

The Agreement between HEP d.d. and RWE expired in May 2015 and in accordance with its provisions HEP decided to exercise its right related to the possibility that 15 years after the start of production, HEP can takeover RWE's shares in TE Plomin d.o.o. and become sole owner of 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. Fixed and current assets of TE Plomin acquired through merger with HEP, was transferred to lease to HEP Proizvodnja d.o.o. in 2017.

### Balance sheet at the merger date

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



# 15. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Available-for-sale investments	282,718	288,493
Other investments	1,445	1,445
	<b>284,163</b>	<b>289,938</b>

Movements on available-for-sale investments are presented below:

	2017	2016
	in HRK'000	in HRK'000
<b>Opening balance</b>	<b>288,493</b>	<b>244,773</b>
Fair value of investment available for sale (Janaf)	(5,398)	43,648
Fair value of investment available for sale – other shares	130	72
Fair value of investment through income statement	(507)	-
<b>Closing balance</b>	<b>282,718</b>	<b>288,493</b>

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
<b>Investments in securities:</b>		
Jadranski Naftovod d.d. /i/	280,701	286,099
Viktor Lenac d.d.	305	177
Đuro Đaković Aparati 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.	14	72
Pominvest d.d.	35	35
	<b>282,718</b>	<b>288,493</b>

**15. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS (continued)**

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>Other investments :</b>		
Geopodravina d.o.o.	200	200
Novenerg d.o.o.	380	380
LNG Hrvatska d.o.o. /ii/	865	865
	<u><b>1,445</b></u>	<u><b>1,445</b></u>

/i/ 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 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 2017, total amount of investment was decreased by HRK 5,398 thousand (2016: increased by HRK 43,184 thousand). The fair valuation in 2017 and 2016 was recognised through equity (revaluation reserves).

/II/ 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 company dealing with liquefied natural gas . 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. HEP d.d. has a 50% stake in the company, and Plinacro d.o.o. has other 50%. As registered at Commercial court, on 4 February 2013 LNG Hrvatska d.o.o. was recapitalized by Plinacro d.o.o. in the amount of HRK 22,600 thousand. Subscribed capital of LNG Hrvatska d.o.o. is stated in the amount of HRK 24,330 thousand. Consequently, the Company owns 3.5% stake and Plinacro owns 96.5% stake, while voting rights are 50%: 50%

## 16. LONG TERM LOANS

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Related parties- financial lease (Note 28)	17,638,839	17,363,344
Non-related parties - loan LNG Hrvatska d.o.o. /i/	61,879	54,596
Related parties - loan /ii/	63,200	79,129
Related parties - sub loan /iii/	660,760	889,414
Non-related parties - loan /iv/	-	2,634
	<b>18,424,678</b>	<b>18,389,117</b>
Current maturity	(1,355,636)	(1,342,170)
	<b>17,069,042</b>	<b>17,046,947</b>

### /i/ Loans given to non-related parties

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
LNG Hrvatska d.o.o.	61,879	54,596
Current maturity	(25,772)	(25,752)
	<b>36,107</b>	<b>28,844</b>

The contracted interest rate is discounted, variable, which was 3% in 2016 and 2017, Loan is secured by a promissory note.

### /ii/ Loans given to related parties

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
HEP-Toplinarstvo d.o.o.	63,200	79,000
HEP- Opskrba d.o.o	-	129
	<b>63,200</b>	<b>79,129</b>
Current maturity	(15,800)	(15,800)
	<b>47,400</b>	<b>63,329</b>

# 16. LONG TERM LOANS (continued)

Loans were granted under following terms:

<b>Beneficiary:</b>	<b>Year of approval</b>	<b>Interest rate</b>	<b>Repayment</b>	<b>Amount granted in HRK'000</b>	<b>31 Dec 2017 in HRK'000</b>	<b>31 Dec 2016 in HRK'000</b>
HEP- Toplinarstvo d.o.o.	2007	4%	15 years 5 years grace period	158,000	63,200	79,000
HEP-Opkrba d.o.o.	2007	1mj, ZIBOR+3,5%	4 year	1,010	-	129
<b>Total</b>				<b>159,010</b>	<b>63,200</b>	<b>79,129</b>

## /iii/ Claims for sub loans to affiliates within the Group

	<b>31 Dec 2017 in HRK'000</b>	<b>31 Dec 2016 in HRK'000</b>
Claim for sub loan HEP ESCO d.o.o. – long-term portion	46,127	55,337
Claim for sub loan HOPS d.o.o.	614,633	834,077
	<b>660,760</b>	<b>889,414</b>
Current maturity	(116,723)	(216,681)
	<b>544,037</b>	<b>672,733</b>

## Sub loans

Claims for sub loan to HEP-ESCO d.o.o. are based on contracts concluded between the Company and financial institutions intended to finance energy efficiency projects. The Company has allocated funds to the sub loan to HEP-ESCO d.o.o. under the same conditions. Considering that from bonds, among other loans, are prematurely repaid loans for the financing of the above mentioned projects, debt claims are now characterized by the same commercial conditions as for issued bonds.

On 31 December 2012, the Company ended the agreement with the Croatian Hrvatski operator prijenosnog sustava d.o.o. on the lease of property, plant and equipment in the amount of assets that is in accordance with the provisions of the Electricity Market Act required for carrying out the transfer activity and the property is transferred to the ownership of the Hrvatski operator prijenosnog sustava d.o.o. For the unpaid part of the loan used to finance assets of the Hrvatski operator prijenosnog sustava d.o.o. the obligations of the Hrvatski operator prijenosnog sustava d.o.o. based on a lease agreement were transferred to long-term lending obligations under the same conditions that the Company has contracted with banks.

## 16. LONG TERM LOANS (continued)

### /iv/ Loans to non-related parties

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
City of Pregrada	-	122
City of Dubrovnik	-	2,512
	<u>-</u>	<u>2,634</u>

## 17. OTHER RECEIVABLES

### Housing loans

As at 31 December 2017 receivables from housing loans amounted to HRK 543 thousand (2016: HRK 666 thousand). Prior to 1996, the Company 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. The housing loan receivables are stated in the financial statements at their discounted net present values. The liability to the State, which represents 65% of the value of sold apartments, is included in other non-current liabilities (Note 25). The receivables are secured by mortgages over the sold apartments.

## 18. INVENTORIES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Inventories of gas for wholesale	353,600	379,488
CO2 emission units	106,248	222,957
Inventories of investment materials	6,784	2,026
Inventories of other materials	1,270	941
	<u>467,902</u>	<u>605,412</u>

## 19. TRADE RECEIVABLES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Trade receivables in the country	212,862	260,087
Trade receivables of gas on the wholesale market	147,582	140,207
Receivables for electricity from abroad	99,280	55,296
	<u>459,724</u>	<u>455,590</u>
Impairment of receivables	(134,718)	(135,529)
	<u><b>325,006</b></u>	<u><b>320,061</b></u>

Aging structure of unimpaired trade receivables in 2017 and 2016:

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Undue	292,189	285,830
Up to 30 days	22,865	26,906
31-60 days	1,364	1,893
61-90 days	852	737
91-180 days	2,323	2,097
181-365 days	5,413	2,586
More than 365 days	-	12
	<u><b>325,006</b></u>	<u><b>320,061</b></u>

Movements in impairments were as follows:

	2017	2016
	in HRK'000	in HRK'000
Balance at 1 January	135,529	130,246
Impairment of trade receivables	1,484	5,283
Reversal of impairments	(2,295)	-
Balance at 31 December	<u><b>134,718</b></u>	<u><b>135,529</b></u>

## 20. OTHER SHORT-TERM RECEIVABLES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Derivative financial assets (Note 23)	-	96,196
Receivables for prepayment of VAT	135,383	29,034
Advance prepayments to suppliers	54,439	5,272
Receivables for interest from companies with participating interests	3,254	1,434
Receivables for deposits	78,898	50,574
Prepaid costs	17,128	14,435
Other receivables	3,240	4,789
	<b>292,342</b>	<b>201,734</b>

## 21. CASH AND CASH EQUIVALENTS

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Current accounts - HRK	88,176	380,491
Short-term deposits (daily deposits)	261,151	441,547
Foreign accounts	350,766	162,970
Deposits with a maturity up to 90 days	148,904	1,304,847
Investment funds	75,252	75,322
Cash for special purposes	921	921
Petty cash – HRK	4	2
	<b>925,174</b>	<b>2,366,100</b>

## 22. 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.

### Reserves

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Opening balance	140,292	100,836
Other comprehensive income/(loss), JANAF	(3,565)	39,456
	<b>136,727</b>	<b>140,292</b>

### Retained earnings

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Opening balance	5,649,310	4,932,491
Merger effects	1,945	-
Dividends paid	(794,291)	(607,000)
Profit for the year	364,023	1,323,819
	<b>5,220,987</b>	<b>5,649,310</b>



## 23. 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
Current portion of bonds	(93,030) 0	(93,030)
	<b>0</b>	<b>0</b>
Value of bonds issued abroad in 2012	493,571	498,617
Current portion of bonds	(491,477)	-
Exchange differences	(2,094)	(5,046)
Current maturity on bonds	-	(493,571)
<b>Bonds issued in 2012</b>	<b>0</b>	<b>0</b>
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
	<b>3,612,610</b>	<b>3,626,428</b>
Accrued bond expenses	(16,782)	(20,255)
<b>Bonds issued in 2015</b>	<b>3,595,828</b>	<b>3,606,173</b>
<b>Total liabilities for issued bonds</b>	<b>3,595,828</b>	<b>3,606,173</b>

### Bonds issued in the Republic of Croatia

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 final instalment was paid, i.e. bonds were paid in full.

### **23. LIABILITIES FOR ISSUED BONDS (continued)**

#### **Bonds issued abroad**

In November 2012, the Company had 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 the Luxembourg stock - exchange and they are actively traded. In November 2017 bonds were paid in full.

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

Bonds issued in 2015, for the most part, were used to repurchase 83.37% of the amount of bonds issued in 2012 (i.e. a repo of USD 416,852 thousand). The remaining issue amount was intended to finance the business activities of the Company,

The bond has been listed on the Luxembourg Stock Exchange and is actively traded with,

The stated discounted value of the bond issued in 2015 is the yearly amount of the discount,

#### *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 annual interest rate of 5.875%.

Bonds issued in 2015, were 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 was 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 the entire period of bond duration, respectively until its outermost maturity date at 23 October 2022.

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 including swap cost).

### **23. LIABILITIES FOR ISSUED BONDS (continued)**

#### ***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 concluded cross currency swap agreements, by which liabilities upon issued bonds abroad in 2012 and 2015 in USD are converted in EUR for the entire period of bond duration, respectively until their 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 it 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' calculations for the reporting period.

A positive "MTM" value is recorded as a receivable and respectively as financial income for the period, and negative "MTM" value is recorded as a liability and as financial expense of the reporting period.

After a final maturity of derivative financial instruments, subject receivables or liabilities will be debited to the expense or credited to the income of the Company.

In November 2017, with the final maturity of bond repayments of bonds issued in 2012, the contractual currency swap (MTM value) was written off in the amount of HRK 96,196 thousand as expense.

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 505,228 thousand (31 December 2016: HRK 32,251 thousand). (Note 28).

## 24. LONG-TERM LOAN LIABILITIES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Domestic bank loans	445,468	827,728
Foreign bank loans	219,793	237,817
<b>Total long-term loan liabilities</b>	<b>665,261</b>	<b>1,065,545</b>
Deferred loan originated fees	(923)	(2,152)
<b>Total long-term loan liabilities</b>	<b>664,338</b>	<b>1,063,393</b>
Current portion	(405,219)	(408,711)
<b>Long-term portion – HEP</b>	<b>259,119</b>	<b>654,682</b>
<b>Total liabilities for long-term loans</b>	<b>259,119</b>	<b>654,682</b>

In 2017, the Company contracted loans with domestic and foreign banks with floating and fixed interest rates ranging from 0.44% to 2.57%

Loans from domestic banks are secured by bills of exchange and promissory notes. At 31 December 2017, the Company doesn't have any liabilities covered by *sovereign loan guarantees*.

### New financing sources

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

### Loans in use

During 2017, the Company still had available funds from long-term loan approved by KfW Entwicklungsbank in the amount of EUR 50 million for the financing of energy efficiency and renewable energy projects. As of 30 December 2017, the KfW loan balance was EUR 33,1 million, and the unutilised amount of EUR 16,9 million was cancelled and the payment of the loan began. As at 31 December 2017 the Company has no other loans in use.

#### 24. LONG-TERM LOAN LIABILITIES (continued)

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

	<b>Amount</b>
	in HRK'000
2018	405,219
2019	113,513
2020	36,632
2021	36,632
2022	36,632
after 2022	36,632
	<hr/> <b>665,260</b> <hr/>

Loans from domestic banks are secured by bills of exchange and promissory notes, except for one club loan for which the Company 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 Company from possible defaults, i.e. early maturity of loan liabilities.

The agreed covenants are monitored and calculated based on the projected Balance sheet and the Income statement.

The Company prepares preliminary calculations of the covenants in the upcoming mid-term period, and follows 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 Company.

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 represents 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 Company's exposure to credit risk, liquidity risk and market risk, which would result from a possible non-compliance with covenants is minimal.

## 24. LONG-TERM LOAN LIABILITIES (continued)

For the purpose of providing solvency reserves for the following mid-term period, the Company has concluded 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 intent in accordance with the HEP Group needs.

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

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

## 25. OTHER NON-CURRENT LIABILITIES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Long-term liabilities for assets financed from clearing debt	755,189	863,450
Cross currency swap (Note 23)	505,228	32,251
Long-term liabilities to the State	828	878
Other	12,562	12,945
<b>Other non-current liabilities</b>	<b>1,273,807</b>	<b>909,524</b>

### Clearing debt

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 some other legal relationship.

Long-term liabilities to the State in the amount of HRK 828 thousand (2016: HRK 878 thousand) 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

## 26. PROVISIONS

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Provisions for severance payments and jubilee	15,992	12,379
Provisions for court disputes	179,391	178,595
Other provisions	21,631	21,631
<b>Total provisions</b>	<b>217,014</b>	<b>212,605</b>

### Provisions for court disputes

Provisions for court disputes relate to cases where possible outcome has been determined as uncertain or negative for the Company. Total amount of provisions for court disputes as at 31 December 2017 amounts to HRK 179,391 thousand (2016: HRK 178,595 thousand). Most significant provision relates 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 Kartnersparkass amounting to HRK 9,903 thousand.

### Movements in long-term provisions are stated as follows:

	Retirement bonuses	Jubilee awards	Court disputes	Other provisions	Total
	in HRK'000	in HRK'000	in HRK'000	in HRK'000	in HRK'000
<b>At 1 January 2016</b>	<b>8,427</b>	<b>1,116</b>	<b>180,415</b>	<b>21,631</b>	<b>211,589</b>
Additional provisions	2,652	184	652	-	3,488
Decrease in provisions based on payment	-	-	(920)	-	(920)
Decrease in provisions based on estimate	-	-	(1,552)	-	(1,552)
<b>At 31 December 2016</b>	<b>11,079</b>	<b>1,300</b>	<b>178,595</b>	<b>21,631</b>	<b>212,605</b>
Additional provisions	3,583	30	796	-	4,409
Decrease in provisions based on payment	-	-	-	-	-
Decrease in provisions based on estimate	-	-	-	-	-
<b>At 31 December 2017</b>	<b>14,662</b>	<b>1,330</b>	<b>179,391</b>	<b>21,631</b>	<b>217,014</b>

## 26. PROVISIONS (continued)

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

	<b>Retirement bonuses</b> in HRK'000	<b>Jubilee awards</b> in HRK'000	<b>Total</b> in HRK'000
<b>At 1 January 2016</b>	<b>8,427</b>	<b>1,116</b>	<b>9,543</b>
Cost of services	505	97	602
Interest expense	288	33	321
Benefits paid	-	(114)	(114)
Past service cost	55	17	72
Actuarial gain/(loss)	1,804	151	1,955
<b>At 31 December 2016</b>	<b>11,079</b>	<b>1,300</b>	<b>12,379</b>
Cost of services	688	98	786
Interest expense	407	36	443
Benefits paid	(6)	(132)	(138)
Past service cost	106	23	129
Actuarial gain/(loss)	2,388	5	2,393
<b>At 31 December 2017</b>	<b>14,662</b>	<b>1,330</b>	<b>15,992</b>

Provisions for retirement bonuses and jubilee awards are based on calculations by a certified actuary.

The following assumptions were used in preparing the calculations:

- The termination rate is 5.08% and is based on the statistical fluctuation rates for the Company 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 Company represents average with respect to mortality and health status.
- It is assumed that the annual salary growth will be 2%.

Present value of the obligation was determined using a 3% discount rate.



## 27. OTHER LIABILITIES

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
Trade payables /i/	494,183	630,250
Liabilities for taxes and contributions	70,047	76,595
Liabilities for interests	35,593	42,568
Liabilities to employees /ii/	6,627	6,104
Other liabilities /iii/	45,646	11,013
	<b>652,096</b>	<b>766,530</b>
/i/ Trade payables		
Domestic trade payables	351,004	471,085
Foreign trade payables	5,883	8,975
Liabilities toward suppliers for electricity within EU and abroad	122,502	138,308
Liabilities toward suppliers within the EU	14,794	11,882
	<b>494,183</b>	<b>630,250</b>
/ii/ Liabilities to employees		
Net salaries	3,982	3,841
Contributions	2,097	2,057
Other liabilities	548	206
	<b>6,627</b>	<b>6,104</b>
/iii/ Other liabilities		
Accrued expenses for unused vacations	7,805	3,868
Accrued expenses for unused CO2 emission unit quotas	25,573	-
Accrued expenses to HAC	-	2,122
Insurance premiums	2,106	492
Deferred revenue from EU grants	2,484	-
Other accrued expenses	1,184	-
Other liabilities	6,494	4,531
	<b>45,646</b>	<b>11,013</b>

## 28. RELATED PARTY TRANSACTIONS

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 –MagyarországEnergiaKft	Hungary	100	Electricity trading
HEP Energija d.o.o.	BIH	100	Electricity trading
HEP Energija KS sh.p.k.	Kosovo	100	Electricity trading
HEP Energija d.o.o.	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	79,94	Telecommunication services
Hrvatski centar za čistiju proizvodnju (u likvidaciji)	Croatia	100	Teaching and counselling in the field of cleaner production and environmental management systems

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

Company HEP-Telekomunikacije d.o.o. was founded in 2013, HEP-RVNP d.o.o. in 2014 year changed its name to Program Sava d.o.o while in 2014, a new HEP Opskrba plinom d.o.o. was founded.

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

TE Plomin was merged to the company in 2017.

## 28. RELATED PARTY TRANSACTIONS (continued)

Related party transactions relate to subsidiaries in sole ownership of the Company and to NE Krško d.o.o. (NEK) where HEP d.d. has a 50% ownership.

Related party transactions are stated as follows:

/i/ Company's revenues arise from re-invoiced income of related companies for electricity sales (except for universal service to households and guaranteed service), accounting, legal and other similar services, as well as lease of business premises. The amount of these revenues from related companies is determined on the basis of the following sizes: the value of assets of related company, the cost of employees and the total cost of the related company.

/ii/ Interest on long-term lease of property, plant and equipment and intangible assets are charged to tenants based on loans that were used for construction of those assets and are stated as interest income from related companies.

/iii/ Costs with related companies arise from rendered services of production, transmission and distribution of electricity. Costs for services of transmission and distribution and losses in distribution network are invoiced on a monthly basis in accordance with the provisions and tariffs set by the Croatian Energy Regulatory Agency ("HERA").

/iv/ Short-term receivables from related companies arise from the sale of fuel, materials and spare parts, for the electricity sold by the company HEP Operator distribucijskog sustava d.o.o., HEP Elektra d.o.o. and HEP Opskrba d.o.o., for the cost of the Company's common functions as well as for investments in progress financed by the Company. After completion of the construction, those assets are transferred to related companies as a finance lease.

/v/ Long-term receivables from related companies arise from financial lease of property, plant and equipment to related companies. Lease is paid monthly according to depreciation of leased assets, increased by interests from long-term loans by which the assets were financed. The Company also has receivables from related companies for apartments sold to employees.

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

## 28. RELATED PARTY TRANSACTIONS (continued)

	2017	2016
	in HRK'000	in HRK'000
<b>Operating income</b>		
Income from the sale of electricity to HEP Elektra d.o.o.	2,080,167	339,789
Income from the sale of electricity to HEP ODS d.o.o.	-	1,790,010
Revenue from invoiced electricity to cover losses on the distribution network	416,703	516,203
Revenue from invoiced electricity to cover losses on the transmission network	88,071	122,976
Income from the sale of electricity to Companies of HEP Group	36,840	24,073
Income from balancing energy	67,617	1,095
Income from the sale of electricity to HEP Energija d.o.o. Ljubljana	178,929	65,954
Income from the sale of electricity to HEP Energija d.o.o. Beograd	11,920	15,284
Income from the sale of electricity to HEP Energija d.o.o. Mostar	36,106	21,654
Income from the sale of electricity to HEP Energija SH,P,K, Kosovo	4,997	-
<b>Income from the sale of electricity – related parties</b>	<b>2,921,350</b>	<b>2,897,038</b>
<b>Income from the sale of gas to HEP Plin – related party</b>	<b>132,384</b>	<b>128,938</b>
Income from conducting administrative services	157,726	158,793
Income from lease of business premises	18,432	14,415
Income from the sale of CO2 emission units	130,000	125,078
Other income	1,781	21,543
<b>Operating income – related companies</b>	<b>307,939</b>	<b>319,829</b>
	<b>3,361,673</b>	<b>3,345,805</b>
<b>Financial income</b>		
Income from interest on lease of property	104,251	116,347
Income from interest on loans to related companies	33,555	38,988
	<b>137,806</b>	<b>155,335</b>
<b>Expenses for electricity supplies – related companies</b>		
TE Plomin d.o.o.	208,884	449,945
HEP Energija d.o.o. Ljubljana	766	1,614
HEP Energija d.o.o. Beograd	-	561
HEP Energija d.o.o. Mostar	130	132,800
	<b>209,780</b>	<b>584,920</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	<b>2017</b> in HRK'000	<b>2016</b> in HRK'000
<b>Expenses</b>		
Supply of electricity – HEP Proizvodnja d.o.o.	2,204,507	2,040,752
Supply of electricity from renewable resources – HEP Opskrba d.o.o.	376,404	330,319
Fee for supply of electricity - HEP Opskrba d.o.o.	48,247	41,804
HEP Trgovina d.o.o. trading fee for electricity and gas	14,554	14,075
HEP Opskrba plinom d.o.o. gas supply fee	6,175	5,902
Electricity of balancing - HEP Operator distribucijskog sustava d.o.o.	79,225	92,995
Electricity of balancing - HOPS d.o.o.	46,357	11,001
Electricity of balancing -HEP Opskrba d.o.o.	-	22,961
HEP ODS – impairment of receivables	-	38,361
	<b>2,775,469</b>	<b>2,598,170</b>

Costs from balancing energy in 2017 in the amount of HRK 125,582 thousand (2016: HRK 126,957 thousand) are realised based on sales/purchase of energy balancing pursuant to the valid Rules of balancing of the energy system.

	<b>31 Dec 2017</b> in HRK'000	<b>31 Dec 2016</b> in HRK'000
<b>Long-term receivables</b>		
<b>Receivables for assets in long-term lease</b>		
HEP Operator distribucijskog sustava d.o.o.	8,161,303	8,086,042
HEP Proizvodnja d.o.o.	8,302,002	8,219,593
HEP Toplinarstvo d.o.o.	846,931	754,294
HEP Upravljanje imovinom d.o.o.	120,935	114,027
HEP Plin d.o.o.	175,977	157,101
HEP Noc d.o.o.	12,187	12,104
HEP Opskrba d.o.o.	2,547	3,248
HEP Trgovina d.o.o.	826	1,061
HEP Esco d.o.o.	2,613	2,092
Program Sava d.o.o.	252	314
HEP Opskrba plinom d.o.o.	170	237
HEP Elektra d.o.o.	2,177	1,211
	<b>17,627,920</b>	<b>17,351,324</b>

## 28. RELATED PARTY TRANSACTIONS (continued)

	31 Dec 2017	31 Dec 2016
	in HRK'000	in HRK'000
<b>Receivables for sold flats</b>		
HEP Operator distribucijskog sustava d.o.o.	6,143	6,610
HEP Proizvodnja d.o.o.	3,687	4,048
Hrvatski operator prijenosnog sustava d.o.o.	958	1,215
HEP Toplinarstvo d.o.o.	131	147
	<b>10,919</b>	<b>12,020</b>
	<b>17,638,839</b>	<b>17,363,344</b>
Current portion of lease (Note 16)	(1,197,341)	(1,083,937)
<b>Receivables for long-term lease – related companies</b>	<b>16,441,498</b>	<b>16,279,407</b>

Receivables for long-term loans – related companies	31 Dec 2017	31 Dec 2016
(See Note 16)	in HRK'000	in HRK'000
HEP-Toplinarstvo d.o.o.	63,200	79,000
HEP-Opisrba d.o.o.	-	129
	<b>63,200</b>	<b>79,129</b>
Current portion	(15,800)	(15,800)
	<b>47,400</b>	<b>63,329</b>
<b>Total long-term receivables</b>	<b>16,488,898</b>	<b>16,342,736</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>Short-term receivables</b>		
Receivables from HEP Elektra d.o.o. for sold electricity	385,444	220,754
Receivables from HEP Operator distribucijskog sustava d.o.o. for losses on distribution grid	87,336	119,948
Receivables from HEP Opskrba d.o.o. for sold electricity	413,152	500,155
Receivables from HEP Operator distribucijskog sustava d.o.o. for losses on transmission grid	16,632	25,620
Receivables from HEP Energija d.o.o. Ljubljana	47,005	16,441
Receivables from HEP Energija d.o.o. Beograd for sold electricity	832	1,615
Receivables from HEP Energija d.o.o. Mostar for sold electricity	17,673	860
Receivables of HEP-a d.d. from HEP- Energija SH,P,K, Kosovo for sold electricity,	1,029	-
Receivables from HEP Proizvodnje d.o.o. for sold heating energy	1,276	-
Receivables for balancing energy - HOPS d.o.o.	65,990	-
Other receivables	12,880	14,742
	<b>1,049,249</b>	<b>900,135</b>
<b>Receivables for administrative costs</b>		
HEP Proizvodnja d.o.o.	1,545	1,750
HEP Operator distribucijskog sustava d.o.o.	10,799	8,131
HEP Toplinarstvo d.o.o.	521	3,542
HEP Plin d.o.o.	143	9,372
HEP Upravljanje imovinom d.o.o.	4,007	1,579
HEP Trgovina d.o.o.	196	1,212
HEP Opskrba d.o.o.	3,397	2,545
HEP NOC	8	186
HEP ESCO d.o.o.	71	664
Program Sava d.o.o.	55	901
HEP Telekomunikacije d.o.o.	1,157	163
Opskrba plinom d.o.o.	60	303
Hrvatski centar za čišćiju proizvodnju	516	276
HEP Elektra d.o.o.	2,905	495
	<b>25,380</b>	<b>31,119</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>Short-term receivables for lease of long-term assets</b>		
HEP Proizvodnja d.o.o.	64,290	41,357
HEP Toplinarstvo d.o.o.	12,139	23,565
HEP Operator distribucijskog sustava d.o.o.	141,478	62,200
HEP Plin d.o.o.	2,762	12,275
HEP Upravljanje imovinom d.o.o.	1,544	1,122
HEP NOC	9,280	9,434
HEP Trgovina d.o.o.	61	43
HEP Opskrba d.o.o.	249	258
HEP Esco d.o.o.	105	76
Program Sava d.o.o.	8	15
HEP Opskrba plinom d.o.o.	13	8
HEP Elektra d.o.o.	305	104
	<b>232,234</b>	<b>150,457</b>
<b>Other short-term receivables</b>	<b>432,185</b>	<b>231,443</b>



## 28. RELATED PARTY TRANSACTIONS (continued)

	31 Dec 2017	31 Dec 2016
Receivables for paid investments and other receivables	in HRK'000	in HRK'000
HEP Proizvodnja d.o.o.	521,765	356,635
Hrvatski operator prijenosnog sustava d.o.o.	74,589	57,375
HEP Operator distribucijskog sustava d.o.o.	293,761	458,665
HEP Toplinarstvo d.o.o.	35,084	83,217
HEP Plin d.o.o.	6,891	36,591
HEP ESCO d.o.o.	8,733	786
HEP Noc d.o.o.	837	919
HEP Upravljanje imovinom d.o.o.	656	-
HEP Opskrba d.o.o.	84,096	17,937
Program Sava d.o.o.	8,732	8,705
HEP Opskrba plinom d.o.o.	42	42
Plomin Holding d.o.o.	1,350	1,350
Hrvatski centar za čišćenje proizvodnje	1,244	1,192
	<b>1,037,798</b>	<b>1,023,414</b>
<b>Receivables for sold investment and other materials</b>		
HEP Operator distribucijskog sustava d.o.o.	313,473	313,473
HEP Plin d.o.o.	2,680	2,680
HEP Toplinarstvo d.o.o.	-	99
	<b>316,153</b>	<b>316,252</b>
<b>Other receivables</b>		
HEP Plin d.o.o.	37,800	18,240
HEP Noc d.o.o.	18,066	15,793
Hrvatski centar za čišćenje proizvodnje	472	-
	<b>56,338</b>	<b>34,033</b>
<b>Receivables from TE Plomin d.o.o.</b>		
- current portion of long-term receivables (Note 16)	-	2,127
- other receivables	-	532
	<b>0</b>	<b>2,659</b>
<b>Receivables for short-term loans</b>		
HEP Energija d.o.o. Beograd	2,282	2,296
HEP Energija sh,p,k, Kosovo	1,416	888
	<b>3,698</b>	<b>3,184</b>
	<b>3,153,035</b>	<b>2,692,696</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>Short-term liabilities</b>		
HEP Proizvodnja for electricity	166,340	640,743
HEP Opskrba for fee for supply from renewable resources	59,863	41,848
HEP Opskrba for fee for electricity supply	2,320	4,341
HEP Trgovina for fee of trading	739	1,362
HEP Opskrba plinom d.o.o.	777	1,081
HEP Operator distribucijskog sustava d.o.o. – liabilities for balancing energy	89,525	85,693
HOPS d.o.o. - liabilities for balancing energy	3,336	10,627
HEP Proizvodnja – liability based on contract of cession	966,235	966,235
Other	14,781	9,621
	<b>1,303,916</b>	<b>1,761,551</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>Other liabilities</b>		
<b>HEP Operator distribucijskog sustava d.o.o.</b>		
– for paid connection fees	178,717	183,381
- for cash paid to treasury	151,337	149,741
- for customer payments and paid investments from sub-accounts	74,732	67,488
<b>HEP Elektra d.o.o. for cash paid to treasury</b>	659,251	485,162
<b>HEP Proizvodnja d.o.o.-profit prepayment for 2017</b>	365,000	-
Liabilities to other companies for the payment of customers and investments paid from the sub-accounts	57,594	20,339
	<b>1,486,631</b>	<b>906,111</b>
TE Plomin d.o.o. for electricity supplied	-	90,334
HEP Energija d.o.o. Ljubljana for electricity supplied	-	206
	<b>0</b>	<b>90,540</b>
<b>Total short-term liabilities</b>	<b>2,790,547</b>	<b>2,758,202</b>

Transactions with NE Krško d.o.o. (NEK) are shown as follows:

	<b>31 Dec 2017</b>	<b>31 Dec 2016</b>
	in HRK'000	in HRK'000
<b>NE Krško d.o.o. (NEK)</b>		
Liabilities for purchased electricity	49,603	52,444
Costs of purchased electricity	585,443	609,026

**28. RELATED PARTY TRANSACTIONS (continued)**

	Sales revenue		Purchase costs	
	2017	2016	2017	2016
	in HRK'000	in HRK'000	in HRK'000	in HRK'000
<b>Companies in majority ownership by the State</b>				
INA-Industrija nafte d.d.	77,974	92,876	1,211,442	1,258,033
Hrvatske Željeznice	58,572	70,858	-	-
Croatia osiguranje d.d.	-	-	2,515	93
Hrvatska pošta d.d.	-	3	13,882	15,564
Croatian Ministry od Defence	-	-	-	-
Hrvatske šume d.o.o.	1,746	510	2,176	2,346
Narodne novine d.d.	2,026	894	158	122
Hrvatska radio televizija	4,342	4,934	176	73
Plinacro d.o.o.	-	-	109,111	106,519
Plovput d.d.	499	43	-	-
Croatia Airlines d.d.	706	454	-	-
Petrokemija Kutina d.d.	12,114	14,212	237	-
Ministry of the Interior	9,514	9,566	-	-
Elementary and high schools	16,176	9,389	-	-
Judicial institutions	4,027	2,601	-	-
Colleges and universities	11,614	6,182	740	641
Legislative, executive and other bodies of Republic of Croatia	7,504	4,526	-	-
Health institutions and organizations	46,203	37,356	-	-
Other users	-	103	3,364	5,347
Prirodni plin d.o.o.	-	-	-	-
HROTE d.o.o.	28,988	25,160	34,852	40,075
	<b>282,005</b>	<b>279,667</b>	<b>1,378,653</b>	<b>1,428,813</b>

**28. RELATED PARTY TRANSACTIONS (continued)**

	Amount of receivables		Amount of liabilities	
	31 Dec 2017	31 Dec 2016	31 Dec 2017	31 Dec 2016
	In HRK'000	in HRK'000	in HRK'000	in HRK'000
<b>Companies in majority ownership by the State</b>				
INA-Industrija nafte d.d.	-	-	41,373	112,899
Croatia osiguranje d.d.	-	-	1,775	28
Hrvatska pošta d.d.	-	-	1,163	1,315
Narodne novine d.d.	-	-	20	14
HROTE d.o.o.	8,243	1,924	3,422	3,120
Others	64	72	18,125	37,458
	<b>8,307</b>	<b>1,996</b>	<b>65,878</b>	<b>154,834</b>

## 29. CONTINGENT LIABILITIES AND COMMITMENTS

### Court disputes

In 2017, the Company made provisions for court cases for which it is estimated that are unlikely to be solved in favor of HEP d.d. and subsidiaries.

The Company 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 Company had concluded agreements for investments in various facilities and equipment that has commenced but has not been completed. The value of the most significant contracted investments in progress amounted to HRK 35,593 thousand (2016: HRK 126,947 thousand).

The Company also has shares in HEP - Proizvodnja d.o.o, HEP- Toplinarstvo d.o.o., HEP ESCO d.o.o. and HEP Upravljanje imovinom d.o.o., which have recorded operational losses and the Company is ready to facilitate the necessary funds to enable these companies to continue operations and execute all their due liabilities.

### Environmental protection

The Company 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. The Company 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. The Company's 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<sub>2</sub> 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<sub>2</sub> emission, which were after confirmation by Croatian officials submitted onto all nine Accounts of plant operators with the relevant quantities that corresponded with the verified CO<sub>2</sub> emissions.

## **29. CONTINGENT LIABILITIES AND COMMITMENTS (continued)**

### **Environmental 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

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).

## **29. CONTINGENT LIABILITIES AND COMMITMENTS (continued)**

### **Environmental protection (continued)**

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.

### **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. The 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 1 April 2017, the natural gas producer is no longer obligated to deliver gas at 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.



## 29. CONTINGENT LIABILITIES AND COMMITMENTS (continued)

### 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 and 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.

## 30. FINANCIAL RISK MANAGEMENT

### Capital risk management

The Company 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 Company consists of debt, which includes loans and issued bonds disclosed in the Notes 26 and 27, 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 in HRK'000	31 Dec 2016 in HRK'000
Debt	4,260,166	5,256,167
Cash and cash equivalents	(925,174)	(2,366,100)
Net debt	3,334,992	2,890,067
Equity	25,149,873	25,581,761
Net debt to equity ratio	<b>13%</b>	<b>11%</b>

### 30. FINANCIAL RISK MANAGEMENT (continued)

#### 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 non-consolidated financial statements.

#### Categories of financial instruments

	31 Dec 2017 in HRK '000	31 Dec 2016 in HRK'000
<b>Financial assets</b>		
Available-for-sale	282,718	289,558
At fair value through profit or loss	-	96,196
Loans and receivables (including cash and cash equivalents)	5,836,870	6,749,536
Other non-current assets	17,069,585	17,044,965
<b>Financial liabilities</b>		
At fair value through profit or loss	505,228	32,251
Non-current liabilities	4,623,526	5,138,128
Current liabilities	3,734,143	4,433,477

Other assets mostly relate to long-term loan receivables from related companies for lease of property.

#### Financial risk management objectives

The Company's Treasury function provides services to the business, co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Company 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 management

The activities of the Company are primarily exposed to the financial risk of exchange rate and interest rates fluctuations (see below). Market risk exposure is monitored and managed through sensitivity analysis. There have been no changes in the Company's exposure to market risks or in the manner in which the Company manages and measures the risk.

### 30. FINANCIAL RISK MANAGEMENT (continued)

#### Foreign currency risk management

The Company undertakes certain transactions denominated in foreign currencies and thus the Company 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 Company's foreign currency denominated monetary assets and liabilities at the reporting date are as follows:

	Assets		Liabilities	
	31 Dec 2017 In HRK'000	31 Dec 2016 In HRK'000	31 Dec 2017 In HRK'000	31 Dec 2016 In HRK'000
EU- EUR	169,446	195,258	22,242	716,260
USD	9,590	10,034	120,450	2

#### Foreign currency sensitivity analysis

The Company is mainly exposed to the changes of EUR and USD currency. The following table details the Company'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
<b>EUR change effect</b>		
Gain or loss	(320,727)	393,762
<b>USD change effect</b>		
Gain or loss	(69,507)	(7,192)

#### Interest rate risk management

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

### **30. FINANCIAL RISK MANAGEMENT (continued)**

#### ***Interest rate sensitivity analysis***

The sensitivity analysis has been determined only for financial instruments with floating interest rate, based on the Company'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. If interest rates had been 50 basis points higher/lower and all other variables were held constant:

- The Company's profit for the year ended 31 December 2017 would decrease by HRK 931 thousand (2016: HRK 2,301 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 10.33% of all interest-bearing loans (2016: 15.55%); 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 Company. The Company 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 Company does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The Company 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 Company's ability to disconnect such customers from the power supply network.

Carrying amount of financial assets presented in the non-consolidated financial statements, less losses arising from impairment, represents the Company'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 Company's short, medium and long-term funding and liquidity management requirements. The Company 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.

### 30. FINANCIAL RISK MANAGEMENT (continued)

#### *Liquidity and interest rate risk tables*

The following table details the remaining period to contractual maturity for the Company'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 Company anticipates that the cash flow will occur in a different period.

#### 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 December 2017							
Interest free		1,669,811	1,635,271	705,208	488,667	-	4,498,957
Floating interest	1.63%	35,422	19,785	93,726	122,191	-	271,124
Fixed interest	4.74%	-	9,174	29,747	499,208	-	538,130
Fixed interest		109,234	218,469	973,889	5,206,367	11,756,385	18,264,344
<b>Total</b>		<b>1,814,467</b>	<b>1,882,699</b>	<b>1,802,570</b>	<b>6,316,433</b>	<b>11,756,385</b>	<b>23,572,555</b>
31 December 2016							
Interest free		3,591,316	1,221,921	290,226	437,174	0	5,540,637
Floating interest	1.51%	35,923	20,323	95,572	232,038	0	383,856
Fixed interest	5.02%	0	9,806	138,648	68,893	534,612	751,959
Fixed interest	6.50%	100,595	201,190	898,498	4,801,134	12,176,359	18,177,776
<b>Total</b>		<b>3,727,834</b>	<b>1,453,240</b>	<b>1,422,944</b>	<b>5,539,239</b>	<b>12,710,971</b>	<b>24,854,228</b>

The following table details the Company'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 Company can be required to pay.

### 30. FINANCIAL RISK MANAGEMENT (continued)

#### Maturity of non-derivative financial liabilities

	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
<b>31 Dec 2017</b>							
Interest free		1,822,527	1,105,514	392,282	1,271,673	-	4,591,996
Floating interest	1.95%	68,432	28,762	278,727	77,506	-	453,427
Fixed interest	4.60%	-	-	214,556	4,504,624	36,756	4,755,936
<b>Total</b>		<b>1,890,959</b>	<b>1,134,276</b>	<b>885,565</b>	<b>5,853,803</b>	<b>36,756</b>	<b>9,801,359</b>
<b>31 Dec 2016</b>							
Interest free		2,139,553	1,205,696	87,893	875,104	32,251	4,340,497
Floating interest	2.09%	70,981	29,634	297,689	693,488	-	1,091,792
Fixed interest	4.84%	-	-	834,282	952,781	3,850,940	5,638,003
<b>Total</b>		<b>2,210,534</b>	<b>1,235,330</b>	<b>1,219,864</b>	<b>2,521,373</b>	<b>3,883,191</b>	<b>11,070,292</b>

The Company has access to sources of financing. The total unused amount at the end of the reporting period was HRK 1,319,608 thousand. The Company 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.
- Fair value of derivative instruments is calculated using the listed price. Where such prices are not available, the analysis uses discounted cash flows by applying the current yield curve for the period of non-derivative instruments.

### 30. FINANCIAL RISK MANAGEMENT (continued)

#### *Fair value measurements recognized in the statement of financial position*

The table below analyses the financial instruments subsequently measured at fair value, classified within 3 groups according to IFRS 13:

1. Level 1 inputs – inputs are quoted prices in active market for identical assets or liabilities, that the entity can access at the measurement date
2. Level 2 inputs – are inputs other than quoted market prices included within Level 1, that are observable for the asset or liability either directly or indirectly, and
3. Level 3 inputs – inputs are unobservable inputs for the asset or liability (entry data unavailable)

The measurement of fair value of cross currency swap is tied to the Mark-to-market value ("MTM") according to the calculation from the banks and the change in fair value in subsequent period is recognized through profit or loss.

	1st level in HRK'000	2nd level in HRK'000	3rd level in HRK'000	Total in HRK'000
<b>2017</b>				
Available-for-sale assets	282,718			<b>282,718</b>
Derivative financial assets	-	-	-	-
Derivative financial liabilities	-	-	505,228	<b>505,228</b>
Investment property		33,266		<b>33,266</b>
<b>2016</b>				
Available-for-sale assets	289,558	-	-	<b>289,558</b>
Derivative financial assets	-	-	96,196	<b>96,196</b>
Derivative financial liabilities	-	-	32,251	<b>32,251</b>
Investment property	-	15,433	-	<b>15,433</b>

### 31. 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.

Fees for tax consultancy amounted to HRK 134 thousand in 2017 (2016: HRK 134 thousand).

### 32. EVENTS AFTER THE REPORTING DATE







On 1 January 2018, a new Management Board was appointed (note 1).

Other than that, after the balance sheet date there were no events that would significantly affect the Company's annual financial statements for 2017, which should, accordingly, be disclosed.

### 33. APPROVAL OF THE FINANCIAL STATEMENTS

These non-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 Čosić	Nikola Rukavina	Petar Sprčić	Tomislav Šambić	Saša Dujmić	Frane Barbarić
Member	Member	Member	Member	Member	President

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