ANNUAL **REPORT** 2018

HEP

HEP GROUP 2018
KEY DATA

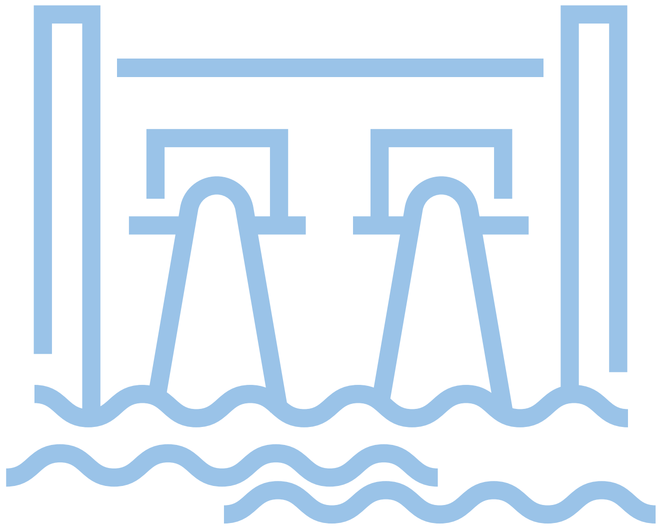
Generation facilities, transmission and distribution network

HPP and RES

installed capacity

2,163 MW[1]

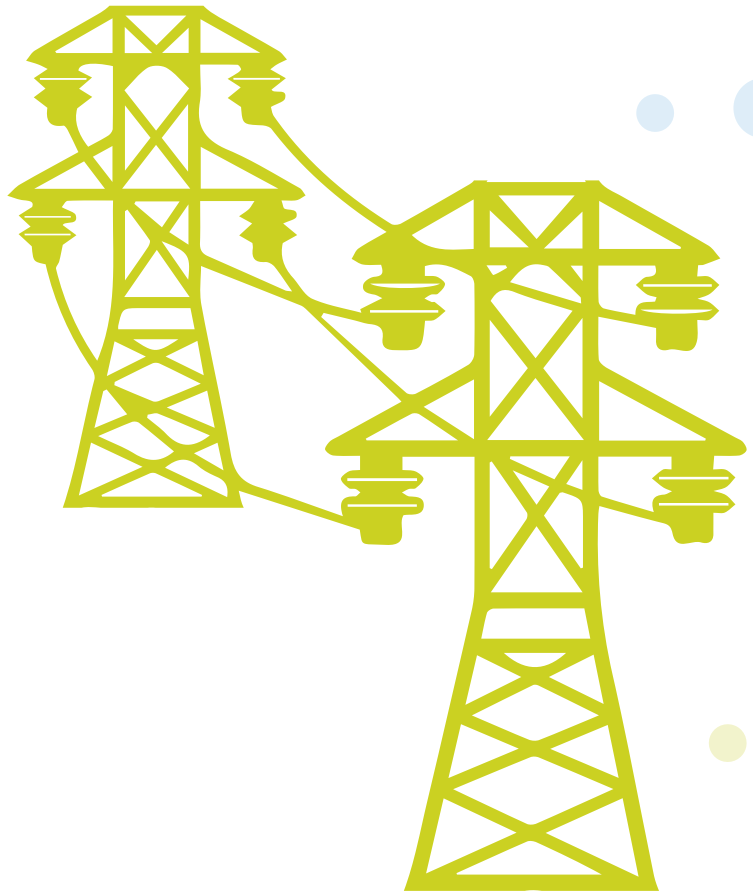
[1] excluding HPP Dubrovnik Unit B which generates electricity for Bosnia and Herzegovina



TPP and 50% NPP Krško

installed capacity

2,410 MW



179

HV substations

(400-200-110 kV)

26,421

MV and LV substations

(35-20-10 kV)

7,727 km

of HV lines (overhead and cables)[2]

[2] including 110 kV overhead lines currently operating as MV (104 km in total)

138,789 km

of MV and LV lines (overhead and cables)

HEP GROUP 2018
KEY DATA
Basic indicators

17.5 TWh
Sale of electricity[1]
+0.6%

[1] HEP sale in Croatia and abroad

2016 = 16.8 TWh
2017 = 17.4 TWh

12.9 TWh
Electricity production
+7.1%

2016 = 12.5 TWh
2017 = 12.0 TWh

1.8 TWh
Heat sales
-4.7%

2016 = 1.9 TWh
2017 = 1.9 TWh

1.4 TWh
Gas retail
-1.1%

2016 = 1.3 TWh
2017 = 1.4 TWh

5.9 TWh
Gas wholesale
-4.5%

2016 = 6.3 TWh
2017 = 6.2 TWh

15,198.3 HRK m
Operating income
+1.5%

2016 = 14,400.4 HRK m
2017 = 14,969.3 HRK m

3,876.5 HRK m
EBITDA
+3.4%

2016 = 4,617.5 HRK m
2017 = 3,749.5 HRK m

1,364.8 HRK m
HEP Group's net profit
+5.0%

2016 = 2,045.0 HRK m
2017 = 1,300.3 HRK m

40,349.6 HRK m
Total assets
+3.9%

2016 = 39,232.9 HRK m
2017 = 38,851.6 HRK m

2,376.1 HRK m
Investments
-2.3%

2016 = 2,589.1 HRK m
2017 = 2,431.9 HRK m

11,011
No. of employees
-883

2016 = 11,832
2017 = 11,894

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CHAIRMAN'S **REPORT**

Pursuant to the Decision adopted by the General Shareholders Assembly on 13 June 2018, the 11th Supervisory Board assembly was appointed. Since its constitution on 14 June 2018, the Supervisory Board has been performing its duties. During business year 2018, the Supervisory Board held eight meetings (four electronic) between two Annual General Meetings of Shareholders.

The Supervisory Board supervised the conduct of Company affairs and carried out other work-related activities pursuant to the Companies Act, the Articles of Association of the Company and the Rules of Procedure of the Supervisory Board. It discussed and accepted information provided by the Management Board concerning the overall state-of-affairs in the Company, its business policy and relations with the related companies, decisions significantly affecting the position of the Company, as well as general matters of the Company's future management. It also gave all necessary consents to decisions adopted by the Management Board pursuant to the Articles of Association of Hrvatska elektroprivreda d.d.

The Supervisory Board analysed the achievement of planned results and the implementation of core objectives set under the Company's business policy for 2018. It also took active participation in the supervision of the delivery of strategically important issues for HEP Group.

At the proposal of the Company's Management Board, the Supervisory Board gave its consent to the 2019 Consolidated Economic Plan and the 2019 Investment Plan of HEP Group. The Supervisory Board gave necessary prior consents to proposals made by the Company's Management Board regarding the sale of securities in the HEP portfolio acquired during bankruptcy and pre-bankruptcy procedures and the increase of capital reserves of HEP-Toplinarstvo d.o.o., the intention to increase the equity of HEP-ESCO d.o.o., the intention to sell its business share in Novenerg d.o.o. (limited liability company) to RWE Hrvatska d.o.o., the launch of the procedure for obtaining the consent from the Croatian Government for the prolongation of the time period for using and the increase of the framework amount for the issuance of HEP d.d. guarantees, the revision of planned finances by increasing the total amount of approved funds under the 2019 Investment Plan of HEP d.d. for the recapitalization of LNG Hrvatska d.o.o., and the revision of planned finances by increasing/decreasing a total sum of approved funds under the 2019 Investment Plan of HEP-Plin d.o.o. and HEP d.d. The Supervisory Board gave prior consents to the decisions of the Management Board of HEP d.d. regarding the write-off of bad debt owed to HEP d.d. as of 31 May 2018 as well as of bad debt and liabilities as of 30 September 2018, the acquisition of Vis solar power plant and the binding offer for the purchase of the wind park project.

By receiving regular reports and information from the President of the Management Board of HEP d.d., the Supervisory Board gave its opinions and recommendations to the Management Board aiming at the improvement of the future operational efficiency and of the strategic goal of HEP Group and, in light of new circumstances, of its positioning on the electricity market as an equal participant in market competition. The Supervisory Board has been continuously taking part in the HEP Group investment project-related activities via regular reports and information received from the Management Board of HEP d.d., as well as in the annual investment plans and documents setting the strategic investment framework.

Apart from the regular reports submitted by the Management Board of HEP d.d. on operating performance and the business environment, the Supervisory Board also carried out in-depth discussions regarding other topics of current interest for HEP Group, including the cession of due receivables for sold heat energy produced by HEP-Proizvodnja d.o.o. to HEP-Toplinarstvo d.o.o., the Consoliadated Financial Plan of HEP Group for the period 2018-2022, extraordinary expense of fixed tangible asset as of 30 April 2018 (EL-TO Zagreb CCPP), changes in financial statements for the period ended on 30 June 2018 in relation to IFRS 15, long-term loan granted to HEP d.d. by the European Bank for Reconstruction and Development and the European Investment Bank for funding the construction of EL-TO Zagreb CCPP, the intention to execute status changes of merging Program Sava d.o.o. with HEP d.d., HEP Opskrba plinom d.o.o. with HEP Trgovina d.o.o., and Plomin Holding with HEP Proizvodnja d.o.o., regulation of relations between HEP d.d. and HEP Operator distribucijskog sustava d.o.o. (HEP ODS – HEP DSO) and starting the process of rebranding HEP ODS's separate identity, measures conducted in relation to the accident in HPP Dubrovnik, transfer of assets into capital reserves of HEP-ODS d.o.o., asset ownership transfer to HOPS d.o.o., value adjustment of receivables from Petrokemija d.d., recapitalization of LNG Hrvatska d.o.o., and the approval of the short-term loan to LNG Hrvatska d.o.o.

The review of business and financial reports found that Hrvatska elektroprivreda as a joint stock company and the Group of its subsidiaries had been conducting its affairs pursuant to the provisions of the Companies Act, Articles of Association, decisions of the Shareholders Assembly and the internal rules and regulations of the Company. The annual financial reports were drafted in line with the balance existing in the Company books, showing accurate property-related and operating state of affairs of the Company. The Supervisory Board expressed no objections to the auditor's report on reviewing Company's annual financial statements and HEP Group's consolidated financial statements for 2018.

Supervisory Board Chairman
Goran Granić, PhD

PRESIDENT'S **REPORT**

In 2018, HEP Group fully accomplished its mission of sustainable, reliable and competitive production, distribution and supply of energy in line with customers' needs and at a high degree of social responsibility achieving good business results of HRK 1.36 billion in profits.

Our own generation facilities produced 12.9 TWh of electricity. A very good availability of power plants, transmission and distribution network was achieved with no significant disturbances in the supply of electricity, heat energy and gas.

With the aim of retaining a dominant share on the Croatian electricity market, HEP continued to develop and offer innovative products in 2018 tailored to customer requirements, and to carry out a number of other activities in line with sustainable development and corporate responsibility norms. Not only do we ensure the security of supply to our customers but HEP as a dominant supplier takes most credit for one of the lowest prices of electricity in the EU paid by the Croatian citizens.

The share acquired on the Croatian market increased from 85 to 89 percent. At the same time, business expansion activities continued throughout the region, primarily in Slovenia, Serbia and Bosnia and Herzegovina. In view of a significant rise of electricity prices on power exchanges, the year 2018 was expecially challenging for the supply of business customers. Coping with said circumstances, HEP Opskrba offered to its customers products and solutions which facilitated their autonomous cost management as well as various forms of education on electricity market characteristics and trends. We are planning to continue our active approach to customers and to develop our offer in line with market trends and developments.

The development of the electricity market as well as legal and regulatory changes which have a significant effect on HEP Group business operations require a continuous harmonization of our business system. In light of the above, the unbundling of the companies performing electricity distribution and universal supply was carried out in late 2017 and early 2018, first in terms of IT and then followed by a complete functional unbundling process. At the same time, the last phase of the restructuring process of HEP Operator distribucijskog sustava (distribution system operator) was completed.

HEP Group conducted a number of activities which resulted in stable financial indicators. Active liquidity management, confirmed by rating agencies in 2018, continued in 2019. Successful business operations of HEP was recognized by Standard & Poor's, the rating agency which assessed HEP Group's credit rating in late March 2019 following the upgrade of Croatia's sovereign rating, and upgraded the Group's rating to BB+ with a stable outlook. In late April 2019, Moody's affirmed its rating assessment of HEP Group and upgraded the outlook from stable to positive.

The aforementioned is important for the implementation of HEP's development strategy for the period until 2030, which takes corporate as well as national interests into account in view of all-level investment launch being one of key assumptions for the progress of national economy. HEP Group's investment policy is additionally harmonized with the requirements of the Croatian energy sector and market changes including the increasing presence of other market participants, in particular in electricity trade and supply as well as the production of electricity from renewable energy sources.

As part of the HEP's RES portfolio development, the major step forward was made in 2018 in terms of investment decisions necessary for the future of HEP as well as for the overall development of the Republic of Croatia harmonized with EU policies. In late 2018, the tender for the construction of Cres Solar Power Plant was announced, the first large non-integrated solar power plant within HEP's portfolio. Partnership contracts for the development of two other solar power plant projects were also signed, one near Vrlika and the other on the island of Vis, as well as for one wind farm which will mark HEP's first step in wind energy.

In 2018 as part of the renewable development scenario development, the HRK 3.6 billion worth revitalization of the existing hydro power plants continued as well as the construction preparation of new hydro power plants, in particular of the HRK 3.7 billion worth HES Kosinj/HPP Senj 2 project, which makes it the biggest energy project in independent Croatia to date.

The renewable scenario is also based on the construction of high efficiency cogeneration facilities, which, in light of their high fuel efficiency coefficient in the parallel production of electricity and heat energy, are preferable generation facilities from the environmental point of view. The example of such project is the new HRK 900 m worth unit in EL-TO Zagreb CCPP, which funding and maintenance was ensured in July 2018 by signing a loan and construction as well as service agreements, respectively.

Delivery of the aforementioned projects is the path to achieving a sustainable and flexible energy portfolio, which should include the ownership of diverse electricity sources which may become operational depending on the market circumstances and the price of fuels, while raising the RES share by 50 percent. Other core strategic objectives for the period until 2030 include optimization and improvement of business processes, market flexibility and strengthening of stakeholder cooperation.

In terms of distribution business activity, we are preparing for the challenges resulting from the implementation of the EU 'clean energy package'. These primarily include the strengthening of system flexibility, development of active distribution network, focus on the end customer i.e. network user, further integration of RES, and increase of energy efficiency. With this in mind, the implementation of the HRK 230 million worth introduction of smart networks pilot project will be important, which implementation by HEP ODS was awarded the HRK 150 million grant by the European Regional Development Fund.

It is our vision to become a regional energy leader, who will in cooperation with domestic and international institutions and companies develop technological opportunities, competitive edge and innovative business models focused on future user needs. HEP aims at becoming a center of excellence and a regional leader in development and implementation of advanced technological solutions for energy production, distribution and management. As one of the leading investors, we will retain our driving role in the synergy of the Croatian economy. At the same time, our role of leading Croatia's energy transition will contribute to the fulfillment of global objectives of sustainable development and Croatia's obligations as an EU member state.

President of the Management Board
Frane Barbarić

As part of HEP's RES portfolio development, the major step forward was made in 2018 in terms of investment decisions necessary for the future of HEP as well as for the overall development of the Republic of Croatia harmonized with EU policies.

COMPANY PROFILE

MISSION

Sustainable, reliable and competitive production, distribution and supply of energy in line with the customers' needs and with a high degree of social responsibility.

VISION

HEP - a regional energy leader who will in cooperation with domestic and international institutions and companies develop technological opportunities, competitive edge and innovative business models focused on future customer needs.

CORE VALUES

COMPETENCE AND CREATIVITY

Our employees are the most valuable resource and support in achieving the company's mission and vision and in creating values for the company. With openness to new ideas and creativity, we develop skills and competencies.

QUALITY AND BUSINESS EXCELLENCE

Listening to the requirements and expectations of all stakeholders, we improve the quality of our products and services. Our goal is our company's business excellence.

INTEGRITY

We act professionally and conscientiously in our relations towards customers, business partners, employees and assets. We affirm zero-tolerance for corruption. Our Code of Ethics defines the principles of business behavior.

ENVIRONMENTAL RESPONSIBILITY

We produce, transmit and distribute energy in an environmentally friendly manner. We promote the efficient use of energy among our customers as well as the development and use of renewable energy sources.

STRATEGIC GOALS

SUSTAINABLE AND FLEXIBLE ENERGY PORTFOLIO

- ownership of diverse electricity sources which can become operational depending on market availability and the prices of energy fuels thus providing sustainability and flexibility
- increasing the RES share in HEP Group portfolio by 50 percent, by modernizing and improving the existing portfolio (HPP revitalization), investing in HPP construction and in the construction and acquisition of power plants fired by other renewable energy sources with a special emphasis on wind and solar farms
- construction of high efficiency cogeneration power plants fired by biomass and natural gas

OPTIMIZATION AND IMPROVEMENT OF BUSINESS PROCESSES

- reaching performance efficiency of EU energy companies by upgrading and optimizing business processes incuding, among others, corporate and business development, IT development and integration, HR management, asset management and the upgrade of customer service quality
- encouraging a continuous improvement of employee competencies and innovativeness, as well as efficient management of knowledge at the corporate level
- building (setting up, strengthening) of efficient and user-focused business operations

MARKET FLEXIBILITY

- definition and creation of new products and services across wholesale and retail market segments focusing on the retention of the current share of the Croatian market and the increase of the regional market share
- implementation of smart networks focusing on the conventional network development, automation, smart network control and operation
- examining the possibilities of other business expansion models by means of customer and/or generation capacity acquisition or a partnership in delivery of energy projects

COOPERATION WITH STAKEHOLDERS

- timely and active participation in various development and adoption phases of EU and national legal instruments and in the process of creating the new energy market
- well designed and continuous use of all available communication channels with stakeholders for achieving Group's business objectives
- an active search for investment and/or operating support in the form of premiums, subsidies, tax reliefs and other

HEP GROUP COMPANIES (AS AT 4 JUNE 2019)

The Group consists of Hrvatska elektroprivreda d.d.[1] (HEP d.d.) as the parent company and its dependent companies.

Dependent companies	Country	Ownership share (%)	Core activity
HEP-Proizvodnja d.o.o.	Croatia	100	Production of electricity and heat
Hrvatski operator prijenosnog sustava d.o.o.[2]	Croatia	100	Electricity transmission
HEP - Operator distribucijskog sustava d.o.o.	Croatia	100	Electricity distribution
HEP ELEKTRA d.o.o.	Croatia	100	Electricity supply of customers as a public service
HEP-Opskrba d.o.o.	Croatia	100	Electricity supply
HEP-TOPLINARSTVO d.o.o.	Croatia	100	Heat production and distribution
HEP PLIN d.o.o.	Croatia	100	Gas distribution and supply
HEP-Trgovina d.o.o.[3]	Croatia	100	Electricity trade and optimization of power plants' operations
HEP ESCO d.o.o.	Croatia	100	Implementation and funding of energy efficiency projects
Plomin Holding d.o.o.	Croatia	100	Development of local infrastructure in the vicinity of Plomin TPP
CS Buško blato d.o.o.	Bosnia and Herzegovina	100	Hydro equipment maintenance
HEP Upravljanje imovinom d.o.o.	Croatia	100	Management of non-operating assets and tourism
HEP NOC	Croatia	100	Training, professional improvement and accommodation
HEP Energija d.o.o.	Serbia	100	Electricity trading
HEP Energija d.o.o.	Slovenia	100	Electricity trading
HEP Energija d.o.o.	Bosnia and Herzegovina	100	Electricity trading
HEP Energjia d.o.o.	Kosovo	100	Electricity trading
HEP Telekomunikacije d.o.o.	Croatia	100	Telecommunication services
HEP-VHS Zaprešić d.o.o.[4]	Croatia	100	Design and construction of multi-purpose hydro-technical system
Energetski park Korlat d.o.o.[5]	Croatia	100	Electricity production
Plin Vtc d.o.o.[6]	Croatia	100	Gas distribution and supply
NE Krško d.o.o.[7]	Slovenia	50	Electricity production
LNG Hrvatska d.o.o.	Croatia	50	Gas pipeline construction and operation

[1] In November 2018, HEP d.d. exited Noveneg d.o.o.; as of 31 December 2018, Program Sava d.o.o. merged with HEP d.d.; in March 2019 the Croatian Cleaner Production Center was liquidated

[2] As of 2013, HOPS operates under the Independent Transmission Operator model (ITO)

[3] HEP-Opskrba plinom d.o.o. merged with HEP-Trgovina on 31 December 2018

[4] HEP-VHS Zaprešić d.o.o. was founded in 2018 and sold to HEP-Proizvodnja d.o.o. on 31 December 2018

[5] Energetski park Korlat d.o.o. was founded in 2018; as of May 2019 HEP d.d. is its sole member

[6] Having acquired business shares, HEP Plin became the sole member of Plin Vtc d.o.o. in May 2019

[7] In consolidated financial statements, the share in NE Krško d.o.o. is shown by a the method of joint asset and liabilities management, HEP Group's share is shown for each asset and liability across income and expenditure.

HEP d.d.

Subsidiary companies wholly owned by HEP d.d.

HEP-Proizvodnja d.o.o. → CS Buško blato d.o.o. BiH, HEP-VHS Zaprešić d.o.o.

HEP-Operator distribucijskog sustava d.o.o. → HEP NOC

HEP-ELEKTRA d.o.o.

HEP-Opskrba d.o.o.

HEP-Trgovina d.o.o. → HEP-Energija d.o.o., Beograd; HEP-Energija d.o.o., Ljubljana; HEP-Energija d.o.o., Mostar; HEP-Energjia sh.p.k., Priština

HEP-Toplinarstvo d.o.o.

HEP-Plin d.o.o. → Plin Vtc d.o.o.

HEP ESCO d.o.o.

HEP-Upravljanje imovinom d.o.o.

HEP-Telekomunikacije d.o.o.

Plomin Holding d.o.o.

Energetski park Korlat d.o.o.

Companies in mixed ownership

LNG Hrvatska d.o.o.

co-owned by HEP d.d. and Plinacro d.o.o.

NE Krško d.o.o.

co-owned by HEP d.d. and GEN Energija

Independent Transmission Operator

Hrvatski operator prijenosnog sustava d.o.o. (HOPS)

SHORT HISTORICAL OVERVIEW

1895.	**First alternating current electricity system in Croatia, Krka HPP - Šibenik**
1912.	Kraljevac HPP, among the largest hydro power plants at the time, built
1925.	"Ante Šupuk i sin" (Ante Šupuk & Son), Šibenik, among UNIPEDE founders
1937.	Vice Roy's Electrica Company founded (BEP)
1941.	State electrical company founded (DEP)
1945.	Electrical company of Croatia founded (ELPOH)
1954.	Union of electricity companies of Croatia founded (ZEPH)
	Beginning of district heating: hot water pipeline for Končar factory from EL-TO Zagreb plant
1961.	Business association of electricity distribution companies of Croatia founded (ELDIH)
1965.	United electricity industry of Croatia founded
1974.	Union of electricity organizations of Croatia founded (ZEOH)
	Gas distribution and supply commenced within Elektroslavonija Osijek
1981.	Krško nuclear power plant put into operation
1990.	**Public enterprise Hrvatska elektroprivreda (HEP) founded**
1991.	Heavy war destruction to power plants and facilities
1993.	About 120 MW emergency diesel and gas power plants installed in Dalmatia
1995.	Reconstruction and refurbishment of the Peruća dam completed (blasted in 1993)
1997.	Eastern Slavonia reintegrated into the Croatian electricity system
1998.	Gas -fired power plant (2x26 MW) put into operation at the EL-TO Zagreb site
2000.	Plomin 2 TPP (210 MW) began commercial operation
2002.	**Hrvatska elektroprivreda d.d. restructured into HEP Group**
2003.	Combined cycle cogeneration unit K (200 MWe/150 MWt) at TE-TO Zagreb put into operation
2009.	Combined cycle cogeneration unit L (100 MWe, 80 MWt) at TE-TO Zagreb put into operation
2010.	HE Lešće put into operation (42 MW)
2012.	HEP d.d. issued bonds in the amount of USD 500 m
2013.	Croatian Transmission System Operator unbundled from HEP Group according to ITO model
2014	HEP d.d. became a wholesale gas market supplier
2015.	HEP d.d. issued bonds in the amount of USD 550 m
	Trial run of combined-cycle Unit C of TE-TO Sisak (230 MWe, 50 MWt)
2017.	Trial run of Osijek and Sisak CHP biomass plants
2018.	HEP launched the solar and wind farm investment cycle

We are preparing for the challenges resulting from the implementation of the EU 'clean energy package': strengthening of system flexibility, development of active distribution network, focus on the end customer i.e. network user, further integration of RES, and increase of energy efficiency.

CORPORATE GOVERNANCE

CORPORATE GOVERNANCE

In accordance with the HEP Group corporate governance model, HEP d.d. manages and carries out some corporate tasks as well as directs, coordinates and monitors activities in dependent companies. Each member of the Management Board is an executive in charge of a corporate function. The main internal organization of HEP d.d. is based on a corporate governance approach and on the authority the Company has over individual business activities.

IMPLEMENTATION OF CORPORATE GOVERNANCE CODE

In 2018, the Company implemented the Corporate Governance Code for the companies in which the Republic of Croatia has shares (OG 132/2017). The Company adheres to the provision of the Code except for those which implementation at a given moment is not possible, applicable and practical.

GOVERNING BODIES OF HEP d.d.

Management Board

The President and the members of the Management Board are appointed and revoked by the Supervisory Board of the Company. The term of office of the president and the members of the Management Board is 4 years. The Management Board of the Company consists of 6 members, one of whom is appointed the President. The current structure of the Management Board consists of six functions: president of the Management Board, Board member in charge of financial affairs support functions, financial operations, procurement and EU regulation, Board member in charge of regulatory functions, regulatory and market activities, Board member in charge of market activities, Board member in charge of production activities, and Board member in charge of investments, strategic and corporate development, project development and IT.

Pursuant to the Articles of Association of the Company and for the purpose of the execution of managerial tasks and authorities, the Management Board carries out the following activities:

- manages the business affairs of the Company;
- establishes and implements the business policy, medium- and long-term plans;
- carries out decisions passed by the Supervisory Board and the Shareholders Assembly, and takes measures and issues instructions for their implementation;
- passes Company internal rules as well as organizational rules;
- represents and acts for the Company, and signs contracts within the framework of the law and these Articles of Association;
- proposes decisions on matters from the scope of work of the Supervisory Board and Shareholders Assembly of the Company;
- submits reports to the Supervisory Board on business policy and other principle issues regarding future operations as well as on deviations from earlier predictions providing the reason;
- submits annual financial reports to the Company's Supervisory Board;
- submits the report on the Company's state-of-affairs to the General Assembly once a year;
- submits the written consolidated annual company report to the General Assembly;
- appoints members of the Assembly and Supervisory Boards of the companies in which HEP d.d. has controlling interest or significant influence;
- appoints and revokes Company's employees with special authorities and responsibilities;
- passes staff and employment plans;
- proposes and takes necessary measures and issues direct orders to ensure operations of the Company, especially the safety and the operation of the power system;
- performs other work-related tasks in line with the law and Company rules.

Supervisory Board

The Supervisory Board consists of a maximum of 7 (seven) members. Six members are appointed by the Shareholders Assembly of the Company and one is elected by the Works Council pursuant to the provisions of the Labour Act. The Decision adopted by the General Assembly on appointing and revoking Supervisory Board members enters into force on the day of its adoption.

The Supervisory Board supervises the management of the Company's business affairs. Pursuant to the Company's Articles of Association and within the scope of its responsibilities, it:

- appoints and revokes the Management Board of the Company;
- examines and reviews business records, documentation, cash records, securities and other documents related to the operations of the Company;
- gives consent to annual financial reports made by the Management Board of the Company;
- gives prior consent to the decisions of the Management Board where this is set under the Articles of Association;
- submits reports to the Shareholders Assembly of the Company on the supervision carried out, especially with regard to financial operations and its consistency with business records;
- performs other activities set by the law and Company rules.

Some large transactions, long term debt and the establishment of a company in Croatia and abroad requires the consent of the Supervisory Board.

The Supervisory Board appoints the Audit Committee responsible for the objectivity and credibility of information and reports submitted to the Supervisory Board. It also supervises the implementation of internal and external audits in the Company and prepares and supervises the implementation of the SB decisions regarding report submission and audits within HEP Group.

General Shareholders Assembly

The Shareholders Assembly is composed of shareholders and/or their proxies. The Shareholders Assembly decides on issues set under the law and the Articles of Association, in particular:

- passes the Articles of Association and its amendments;
- appoints and revokes the members of the Supervisory Board;
- makes decisions on the use of profit;
- revokes members of the Management and Supervisory Boards of the Company;
- appoints the auditor of the Company;
- decides on increase or decrease in the capital stock of the Company;
- decides on status changes and a dissolution of the Company;
- carries out other work in accordance with the law and the Articles of Association of the Company.

MANAGEMENT
STRUCTURE OF HEP d.d.

Data as of 4 June 2019 is shown. The management structure and the changes which occurred during 2018 are given in the Notes to Consolidated Financial Statements (Note 1 – General).

General Shareholders Assembly

Tomislav Ćorić, Ph.D.
member (Minister of Environment and Energy)

Supervisory Board

Goran Granić, Ph.D.
Chairman

Jelena Zrinski Berger,
member

Lukša Lulić, Ph.D.,
assistant professor, member

Ivo Ivančić,
member

Meri Uvodić,
member, workers' representative

Management Board

Frane Barbarić,
President of the Board

Marko Ćosić, M.Sc.,
Board member in charge of financial operations, financial affairs-related supporting functions, procurement and EU regulation

Saša Dujmić,
Board member in charge of regulatory functions, regulatory and market activities

Nikola Rukavina,
Board member in charge of production activities

Petar Sprčić, M.Sc.,
Board member in charge of market activities

Tomislav Šambić,
Board member in charge of investments, strategic and corporate development, project development and IT

INTERNAL AUDITOR

The Internal Audit Department is responsible for the corporate function of internal audit and as such represents a part of the internal supervision of HEP Group.

Business operations of Internal Audit are defined under the Act on the Internal Control System in the Public Sector (OG 78/15) and the Internal Audit Rules, which have been harmonized with the IPPF (International Professional Practices Framework). The Rules are based on the fundamental internal audit principles (integrity, objectivity, confidentiality, expertise) and guarantee a quality normative framework necessary for the professional conduct of the internal audit department tasks. The International Professional Practices Framework is a layout of professional rules and guidelines defining the work of the internal audit, which have been structured and integrated in a document published by the IIA Global.

The Internal Audit Department carries out internal audits in line with the Strategic Plan and the Department Annual Plan adopted by the Management Board of HEP d.d. with the consent of the Audit Committee. The purpose of internal audits is to provide the Supervisory Board, the Audit Committee and the Management Board of HEP d.d. a reasonable guarantee of security, efficiency and effectiveness of the business system and processes, reliability and accuracy of information, compliance of business operations with laws, regulations and official documents of HEP d.d. as well as HEP Group's plans and business policies.

The Department also provides recommendations for enhancing business processes, assists the Management Board of HEP d.d. and the responsible management of HEP Group in improving internal controls and mitigating operating risks. Pursuant to the Audit Act and the Act on the Internal Control System in the Public Sector, the Internal Audit Department falls under the jurisdiction of the Audit Committee of the Supervisory Board of Hrvatska elektroprivreda d.d. The Audit Committee consists of the following members: Goran Granić, PhD, president, Professor Boris Tušek, PhD, independent external member and Professor Boris Cota, PhD, independent external member. In the period between two Assembly meetings, the Audit Committee held three sessions which agenda included the 2018 semiannual and annual financial reports, the Internal Audit Department operating report, the internal audit strategic plan 2019-2021, and the annaul internal audit plan for 2019.

GENERAL SHAREHOLDERS ASSEMBLY

General Shareholders Assembly 2018

The annual meeting of the General Shareholders Assembly was held on 4 June 2018. The Assembly reviewed consolidated and unconsolidated annual financial statements of HEP d.d. and of HEP Group for 2017 including the Independent Auditor's Report, the Annual Report on the state of affairs and operations of HEP d.d. and of HEP Group in 2017, and the Report of the Supervisory Board on the supervision conducted in 2017. The Decision on the use of earned profit from 2017 operations was adopted and acts of the members of the Management and the Supervisory Boards, respectively, were ratified for 2017. The General Assembly appointed BDO Croatia d.o.o. for the provision of auditing, consulting and accounting services Zagreb the auditor of HEP d.d. and its dependent companies' 2018 financial statements.

General Shareholders Assembly 2019

The annual meeting of the General Shareholders Assembly was held on 4 June 2019. The Assembly reviewed consolidated and unconsolidated annual financial statements of HEP d.d. and of HEP Group for 2018 including the Independent Auditor's Report, the Annual Report on the state of affairs and operations of HEP d.d. and of HEP Group in 2018, and the Report of the Supervisory Board on the supervision conducted in 2018. The acts of the members of the Management and the Supervisory Boards, respectively, were ratified for 2018.

HEP's development strategy for the period until 2030 takes corporate as well as national interests into account in view of all-level investment launch being one of key assumptions for the progress of national economy.

BUSINESS OPERATIONS IN 2018

BUSINESS OPERATIONS IN 2018

BUSINESS ENVIRONMENT

As the Croatian economy strengthened in 2018, the first estimated figures published by the Croatian Bureau of Statistics showed a 2.6% increase of the gross domestic product compared to 2017. This was the fourth consecutive year of the GDP growth following a long recession, albeit at a somewhat lower growth rate compared to the previous periods. The stable growth of economic activities during the year was slowed down in late 2018 as a consequence of a 6.6% drop of industrial production in December 2018. Favourable trends during the year were facilitated by the successful tourist season, a continuous growth of nominal and real salaries, which encouraged the recovery of personal consumption and the continuation of lower interest rate periods. As per 2018 data published by the Croatian Bureau of Statistics, the average registered unemployment rate decreased from the average 12.1 percent in 2017 to 9.9 percent in 2018. Favourable economic trends and weather conditions resulted in higher electricity consumption in Croatia.

Other external factors affecting HEP's business operations include the prices of electricity, energy fuel prices and CO2 emission units. The price of oil varied throughout the year from 79 USD per barrel in May to more than 85 USD per barrel in early October. Said oil price increase was the result of the announcement made by the US President on the withdrawal of the USA from the nuclear agreement with Iran, which also implied the re-introduction of economic sanctions. In light of fear from potential crude oil supply interruptions, OPEC opted for a stronger production which triggered the price decreasing trend in late 2018. The average electricity futures price in 2018 increased significantly by 18.8 percent compared to 2017. The wholesale price reached 69.4 EUR/MWh in Q4 2018. Coal prices continued to decrease, a trend which started in late 2017 only to reach its lowest level in April 2018, and then continued to rise until end 2018. According to coal price trend data[1], the price of coal dropped by 20.9 percent, from 95.2 USD/t in late 2017 to 75.2 USD/t in late 2018. The coal price reached its lowest level in late April 2018 (56.1 USD/t). High coal prices continued to facilitate a relative gas competitiveness compared to coal. In late 2018, the day ahead market price of gas at CEGH (European Gas Hub) reached 24 EUR/MWh, which was by 23.1 percent more compared to end 2017 when the price of gas was 19.5 EUR/MWh. The price of CO2 emission units in late 2017 on the EEX spot market was 8.1 EUR/t. Until end 2018, it increased by 189 percent to 23.4 EUR/t.

HEP Group fulfilled its mission of a sustainable, reliable and competitive production, distribution and supply of energy in line with the customers' needs and retaining a high level of social responsibility in 2018. Good business results were achieved strengthening the Group's financial position.

Income from the sale of electricity in Croatia increased by 1.4 percent as a result of a 1.2% increase in total consumption, the increase of HEP's share in the sale to business customers, and the increase of the average selling price to HEP Opskrba (Supply) business customers. Income from the sale of electricity abroad decreased as a result of a lower export of electricity surpluses generated by HEP Group power plants and resale, a decreased volume of supply to Slovenian customers, and a lower price of exported electricity.

[1] Source: https://markets.businessinsider.com/commodities

HEP sold 14.6 TWh of electricity to domestic customers (881 GWh more than in 2017), and 2.9 TWh of electricity to neighbouring markets (769 GWh less than in 2017). The implementation of a number of activites focused on improving the customer relation, continuous adjustment to market requirements and marketing campaigns aimed at the strengthening of HEP brand resulted in the increase of the market share in electricity supply of domestic customers at 89.1 percent. HEP Group additionally strengthened its market leader position in electricity supply by entering regional markets (Slovenia, Bosnia and Herzegovina, Serbia).

In 2018, HEP ensured 19.8 TWh of electricity i.e. 0.4 percent less than in 2017, for customer supply, sale abroad, losses in the transmission and distribution network and captive use, 12.9 TWh of which (65%) was produced by power plants owned or partially owned by HEP Group, while the remaining volume was procured on the market and purchased from the Croatian Electricity Market Operator (renewable energy sources and high-efficiency cogenerations in the system of incentives).

Income from the sale of gas to end customers increased from 22 February until 31 October 2018 as a result of supplying gas to domestic customers. In gas wholesale and heat sale, income decreased as a result of lower demand affected by weather during the heating season.

The year 2018 was characterized by favourable hydrology resulting in hydro generation of 6.9 GWh, which was by 1,9 GWh (38.7%) more than in 2017, while the production by HEP thermal power plants decreased by 838 GWh (20.7%). Electricity procurement on the market, including the repurchase from renewable sources and high efficiency cogeneration, was lower by a total of 863 GWh (11%). Such hydrology had a positive effect on variable costs resulting in a 10.9 percent decrease of energy fuel costs.

The purchase cost of sold gas increased by HRK 693.5 million in light of gas supply to domestic customers, the operation which was not conducted in 2017. Among other operating cost, the highest increase was seen in value adjustment for trade receivables by HRK 301.4 million, and CO2 emission procurement of HRK 143 million.

The Group recorded net profit of HRK 1.36 billion, which was by HRK 64.5 million (5%) more than in 2017 i.e. HRK 1.30 bn. Said profit was earned from electricity, while all other activities reported loss.

Financial activities reported profit of HRK 24.7 m, compared to the loss in 2017 of HRK 704.1 million primarily the result of the unrealized loss in the change of fair value of the cross-currency swap for the bonds issued in 2012 and 2015 of HRK 569.2 million.

All liabilities were settled within due period throughout 2018. The Group ended the business year with 2.96 billion kuna in cash on bank accounts, an increase by 938.2 million kuna (46.5%) compared to end 2017. Dividend of HRK 218.4 million was paid into the State Budget.

With HRK 2.38 bn invested, HEP Group continued to be one of the biggest investors in Croatia in 2018. Said investments were funded by the Group in light of good liquidity as a result of a good business year. The funding of the construction of the high efficiency Unit L at EL-TO Zagreb CCPP was agreed in July 2018 by means of a facility granted by EBRD and EIB development banks. The long term service agreement was also signed with FATA S.P.A. The commercial operation of wood biomass fired cogeneration plants BE-TO Osijek and BE-TO Sisak started in 2018. Equipment was being replaced on an ongoing bases as well as the reconstructions and refurbishments of the existing generation facilities and of the transmission and distribution network, which was carried out primarily by engaging domestic producers and contractors.

HEP Group had 11,011 employees at the end of 2018, which was by 883 fewer than in late 2017. Said number was the result of downsizing, which was carried out as part of the reorganization of HEP ODS (DSO) in November 2017. The new Collective Agreement for all dependent companies signed on 7 December 2017 is valid for the period 1 January 2018 until 31 December 2019.

FINANCIAL PERFORMANCE

According to financial indicators, HEP Group is one of the biggest business groups in the Republic of Croatia.

The Group generated operating profit of HRK 1,658.5 m in 2018, a decrease by HRK 634.4 m (27.7%) compared to 2017 due to a higher increase of operating expenses than operating income. As the financial activities recorded profit of HRK 24.7 m compared to a loss of HRK 704.1 m in 2017, this increase also affected the rise of net profit of HEP Group amounting to HRK 1,364.8 m, which was by HRK 64.5 m more than the 2017 net profit.

Operating income of HRK 15,198.3 m increased by HRK 229 m compared to 2017, primarily as a result of increased income from sale by HRK 780.1 m (5.8%), while other operating income decreased by HRK 551.1 m (36.5%).

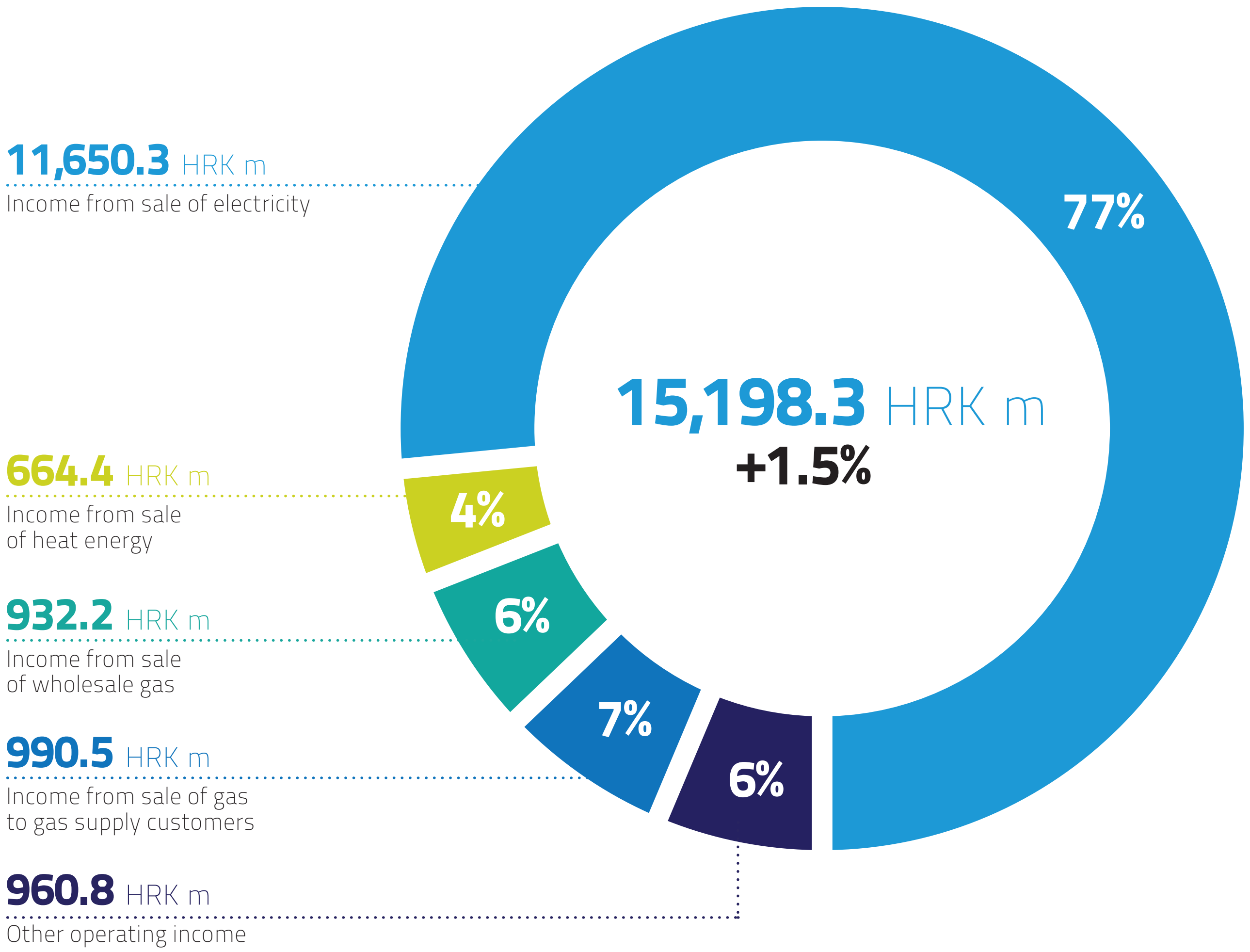
Operating expenses of HRK 13,539.8 m increased by HRK 865.4 m compared to 2017. This increase was the effect of increased purchase cost of sold gas (61.4%) primarily as the result of gas sale to a domestic customer, which did not occur in 2017, increased purchase price of gas, increased CO_2 costs (119%) due to higher prices than in 2017, and cost of electricity procurement (1.6%) as the result of higher cost of RES and cogeneration repurchase due to a higher volume of electricity purchased from HROTE (energy market operator).

CONSOLIDATED PROFIT AND LOSS ACCOUNT (abridged)	2017 HRK m	2018 HRK m	Δ 2017 HRK m	% 2017
Operating income	14,969.3	15,198.3	+229.0	+1.5%
Operating expenses	12,674.5	13,539.8	+865.4	+6.8%
Profit from operations	2,294.8	1,658.5	-636.4	-27.7%
Net profit of the Group	1,300.3	1,364.8	+64.5	+5.0%

OPERATING INCOME

In 2018, the Group generated operating income in the amount of HRK 15,198.3 m, an increase by HRK 229 m (1.5%) compared to 2017, primarily due to increased income from the sale of gas to end customes and income from the sale of electricity.

The Group earned 77% of its operating income (HRK 11.7 bn) from the sale of electricity. A 1.4% increase (HRK 156.7 m) compared to the year before was the result of increased electricity sales to customers in Croatia, HEP's increased share in the sale to business customers, and the rise of the average selling price for business customers of HEP Opskrba.



Operating income (HRK m) and its share in overall operating income (%)

Income from the sale of electricity to Croatian customers increased by 4.2%. Said income increase was the result of increased income from the use of the transmission and distribution network due to higher demand, while the income from electricity supply grew as the result of increased sale to business customers. The average price for business customers of HEP Opskrba increased by 8.1 percent compared to the 8% decrease of the average price for business customers of HEP Elektra within guaranteed supply. In light of the implementation of the Regulation passed by the Ministry of Economy on the Criteria for Obtaining the Status of a Vulnerable Customer of Energy from Networked Systems (OG 95/2015) and the Decision adopted by the General Shareholders Assembly of HEP d.d., under which the electricity price for household customers does not change, the amount of a solidarity charge reduced income from the sale of electricity to customers by HRK 169.1 million.

As of 1 April 2014, HEP d.d. has been the wholesale gas supplier including the sale of gas to suppliers that supply gas to households as part of the public service. The above was regulated under the Decision of the Croatian Government for the period until 31 March 2018, and then under the Amendments to the Gas Market Act from February 2018 under which HEP d.d. was appointed the wholesale gas supplier until 31 July 2018, when the Croatian Energy Regulatory Agency (HERA) should have announced the public tender and set the wholesale gas supplier for the period from 1 August 2018 until 31 March 2021. As no bids for the setting of the supplier on the wholesale gas market were submitted to HERA, even during the repeated tender, the Regulator appointed HEP d.d. the supplier in the period from 1 August 2018 until 31 March 2019. As per the above, the Group earned income of HRK 932.2 m accounting for 6 percent of its operating income. This was a decrease by HRK 31.6 m compared to 2017 as a result of a 4.5% lower gas sales volume.

Income from the sale of gas to end customers amounted to HRK 990.5 m accounting for 7% of its operating income, an increase by HRK 673.9 m compared to 2017 as the result of gas sale to a domestic customer and a higher average retail gas price by 6.6 percent.

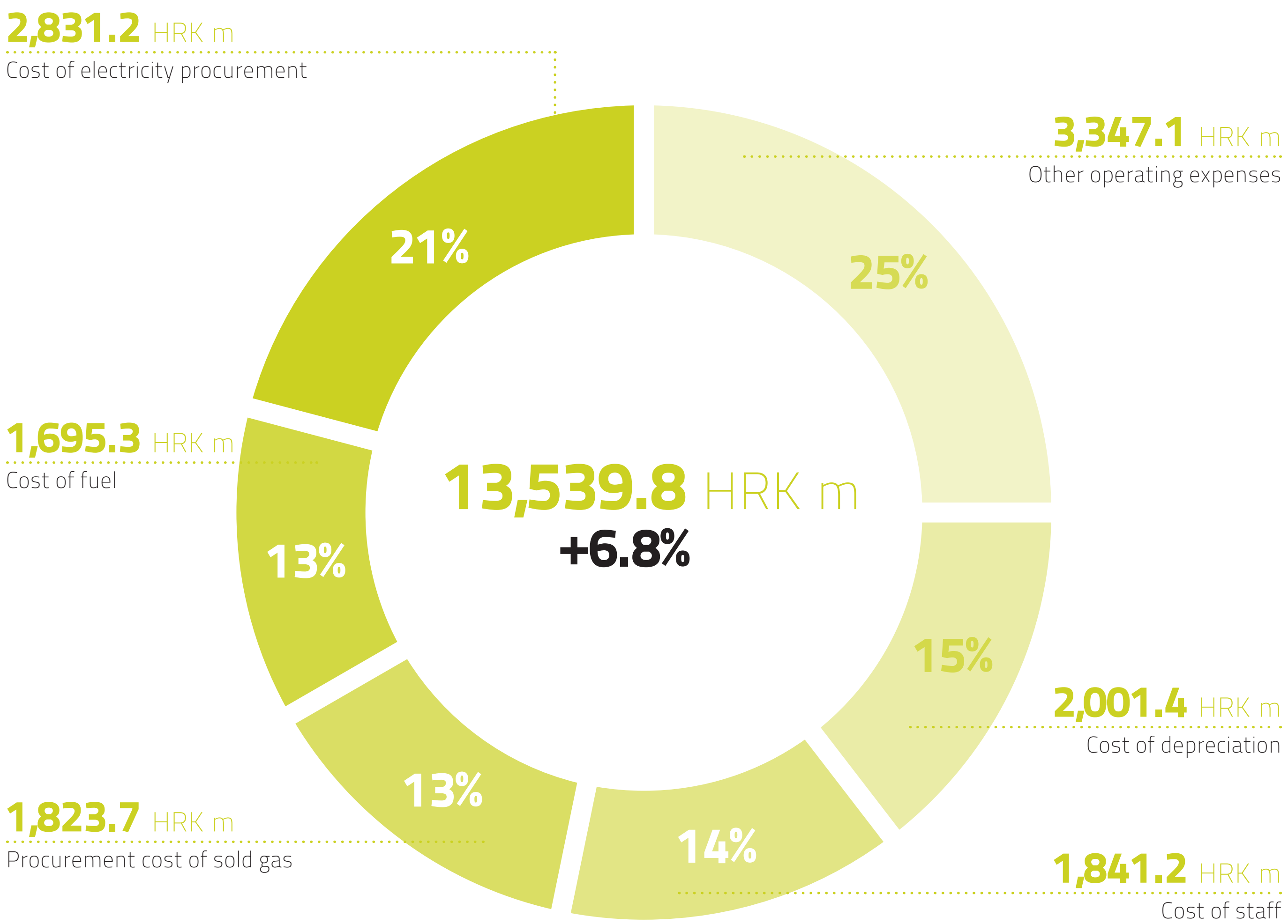
Income from the sale of heat energy amounted to HRK 664.4 m, which accounted for 4 percent of its operating income. This HRK 18.8 million decrease was the result of 4.7% lower demand at a 2.1% higher average selling price.

Other operating income in the amount of HRK 960.8 m decreased overall by HRK 551.1 m (36.5%) compared to the year before as the result of the changes in the accounting policy of recognizing income from connection fees leading to decreased income from network connection services by HRK 369 million, while income from assets financed from the connection fee increased by HRK 95.3 million. In 2017, income from cancelling fixed asset impairment of HRK 199.2 million was also generated.

OPERATING EXPENSES

The Group's operating expenses in 2018 increased by HRK 865.4 m to HRK 13,539.8 m.

Energy fuel for electricity and heat production and electricity procurement accounted for 33 percent of overall costs amounting to HRK 4,526.5 million. The cost of energy fuel decreased by HRK 207.8 m in 2018 due to lower thermal power plant production as the result of favourable hydrology and shutting down the production in TPP Plomin 1, while electricity procurement increased by HRK 44.7 million as the result of a higher purchase volume from renewable sources and cogeneration.



Operating expenses (HRK m) and its share in overall operating expenses (%)

278 GWh more electricity was purchased from eligible producers in the system of incentives at 0.42 HRK/kWh, retaining the 2017 level. The costs also rose in light of a discount for excessively billed electricity from RES and cogeneration which resulted in a decreased cost of purchase in 2017 by HRK 113.9 million. Electricity import lowered by 1.1 TWh at 7.7 percent higher purchase price than in 2017. The electricity purchase from off-system producers and traders in Croatia increased by 94 GWh at a 38.4 percent higher price.

The cost of energy fuel decreased by HRK 207.8 million (10.9%) compared to 2017. Due to a lower electricity production in gas-fired thermal power plants (by 904 TWh), the consumption of natural gas decreased by 22.6 percent at a 19.4% higher price of natural gas. In light of shutting down the production in TPP Plomin 1 in May 2017, only TPP Plomin 2 was operational consuming 6.1% less coal at a 4% higher price than in 2017. Fuel oil costs were also eliminated as said fuel is no longer used for electricity and heat energy production. However, newly emerged is the cost of wood biomass in light of the launch of commercial production of BE-TO Osijek and BE-TO Sisak, biomass fired plants non-existent in 2017.

The procurement value of sold gas was HRK 1,823.7 million, an increase by HRK 693.5 million (61.4%) compared to 2017 primarily due to gas procurement for sale to a domestic customer, which was non-existent the year before. As the obligation imposed to INA d.d., the producer of natural gas, of gas supply to HEP d.d. for the supply of the gas wholesale market at the price set by the Croatian Government was cancelled as of 1 April 2017, the average procurement price of sold gas, which was now procured under market conditions, increased by 16.9 percent compared to the 2017 price.

The cost of staff was HRK 1,841.2 m, a decrease by HRK 105.7 million (5.4%) as a result of downsizing during the reorganization of HEP Distribution System Operator. In addition, the cost of gross salaries in 2017 included the taxable bonus payment at Christmas, which was replaced in 2018 by the Performance Award, a non-taxable payment pursuant to the new Income Tax Rulebook in effect as of 1 December 2018.

Compared to 2017, the 12.6% increase of other operating expenses was primarily the result of the increase of value adjustment of trade receivables by HRK 301.4 million and of the cost of CO2 emission units by HRK 143 million as the result of a 182 percent higher price. In addition, maintenance costs, service costs, severance provisions under employment contract terminations, fees paid for the use of power plant facilities, costs of gas procurement for the supply of customers due to higher purchase prices, and thermal power plant decommissioning provisions also increased. The costs of fixed asset write-off (in 2017, the cost of fixed asset write-off and of the value adjustment of fixed intangible asset occurred as a result of the uncertainty of TPP Plomin C and HPP Ombla projects delivery), the cost of chargeable services and materials, the value adjustment of trade receivables and long-term provisions for severances and jubilee awards under the Collective Agreement decreased.

RESULTS BY ACTIVITIES

The major share of the Group's operating income (82.4%) and of the Group's overall operating profit was earned from electricity. Compared to 2017, said operating profit decreased as a result of lower other operating income in light of the income earned in 2017 from cancelling the impairment of fixed asset value of Unit L in TE-TO Zagreb CHP, while in 2018 income from connection services was reduced as the result of accounting policy changes. District heating accounted for 4.8% of operating income and recorded operating loss of HRK 240 million. Compared to the year before, the loss was higher due to a higher cost of energy fuel resulting from the higher price of natural gas and the increase of the value adjustment of launched cogeneration investments. The share of gas wholesale and retail in operating income accounted for 12.8 percent recording HRK 367.7 million of operating loss compared to HRK 22.4 m of operating loss in 2017. Poorer performance was the result of increased losses from gas wholesale and the adjustment of value of reprogrammed trade receivables domestically.

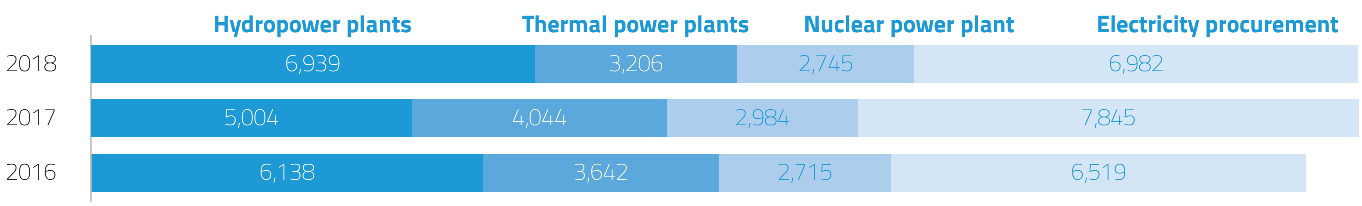
OPERATING RESULT IN HRK M	electricity			heat			gas		
	2017	**2018**	**% 2017**	**2017**	**2018**	**% 2017**	**2017**	**2018**	**% 2017**
Operating income	12,903.6	12,529.0	-2.9%	753.3	722.0	-4.1%	1,312.4	1,947.2	+48.4%
Operating expenses	10,520.5	10,262.9	-2.4%	819.2	962.0	+17.4%	1,334.8	2,314.9	+73.4%
Profit (loss) from operations	2,383.1	2,266.1	-4.9%	-65.9	-240.0	264.1%	-22.4	-367.7	

ELECTRICITY

Electricity generation, transmission, distribution and supply are carried out by HEP Group across the entire territory of Croatia. The Group is the biggest supplier of electricity in the Republic of Croatia with 14.6 TWh of sold electricity. 2,859 GWh more was supplied to customers in Slovenia, Serbia, Bosnia and Herzegovina and as export of surplus electricity and resale. In 2018, the operating profit of HRK 2,266.1 m was generated, which was by HRK 117 million less than in 2017.

Income from the sale of electricity totalled at HRK 11,650.3 m, 91.7% (HRK 10,687.4 m) of which from the supply of domestic customers, and 8.3 % (HRK 963 m) from the sale abroad.

Electricity production and procurement (GWh)

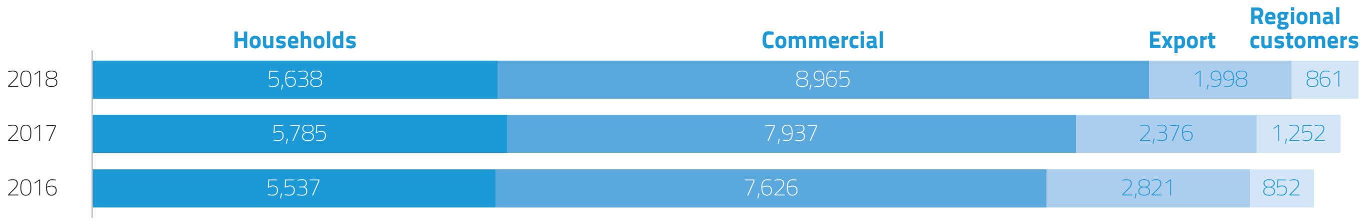


Note: hydro, thermal and biomass plant generation in the system of incentives was 460 GWh in 2018 (in 2017: 564 GWh; in 2016: 244 GWh)

Power plants wholly or partially owned by the Group generated 12.9 TWh of electricity, which was by 865 GWh more than in 2017 accounting for 65% of the overall electricity turnover recorded by the Group in 2018. Due to favourable hydrology in 2018, hydro power plants generated 6,939 GWh of electricity, which was by 1,935 GWh more compared to 2017 generation, accounting for 35 percent of total electricity demand. Electricity generation in thermal power plants and cogeneration facilities decreased by 838 GWh to 3,206 GWh, accounting for 16 percent of total energy demand in 2018. Krško nuclear power plant supplied 2,745 GWh, which was by 239 GWh less than in 2017 due to the regular power plant overhaul conducted in April 2018.

As a result of improved hydrology and increased customer supply in Croatia and the region, 6,982 GWh of energy was procured off-system (35 percent of demand), which was by 863 GWh less compared to 2017. From the overall procured amount, electricity import for satisfying customer supply accounted for 4,592 GWh. Furthermore, 2,209 GWh was purchased by HEP Group from HROTE for the production from the existing renewable energy sources and cogeneration in the system of incentives, while 31 GWh was purchased from the off-system producers and traders in Croatia. 151 GWh was procured for covering off-system network losses.

Sale of electricity (GWh)



14.6 TWh of electricity was sold to domestic customers: 5.6 TWh (38.6%) to households and 9.0 TWh (61.4%) to commercial customers. HEP sales accounted for 89.1% share in the overall electricity sale to end customers in Croatia in 2018. The sale abroad of 2.9 TWh showed a mild drop due to a lower export of electricity surpluses generated by HEP Group power plants and a lower resale by 378 GWh. The supply of regional customers decreased as well by 391 GWh (termination of sale to the Slovenian distribution system operator).

Compared to 2017, income from the sale of electricity increased by HRK 156.7 million (1.4%) to HRK 11,650.3 billion. Increased income from domestic sale by HRK 384.7 m (3.7%) was the result of increased demand, the increased share of HEP in the sale to business customers, and the rise of average selling price for business customers of HEP Opskrba. Income from the export of electricity amounted to HRK 963.0 m, a decrease by HRK 228.0 million (19.1%).

DISTRICT HEATING

Heat energy production, distribution and supply are conducted on the territory of Zagreb, Osijek, Velika Gorica, Zaprešić, Samobor and Sisak.

A total of 2,255 GWh of heat energy was produced in 2018, which was by 47 GWh or 2.1 percent less than in 2017.

The sale of heat energy in 2018 amounted to 1,823 GWh, a 4.7% or 91 GWh decrease compared to 2017, of which households and business customers accounted for 57.4% (1,046 GWh) and 42.6% (777 GWh), respectively. The sale to households and business customers in 2018 decreased overall by 5.7 and 3.4 percent, respectively compared to 2017. Said decrease is the result of warmer weather during the major part of the heating season.

District Heating recorded operating loss of HRK 240 million in 2018. Compared to 2017, the loss increased by HRK 174 million, primarily due to increased costs of heat production resulting from higher gas and CO2 emission rates as well as increased costs of the value adjustment of fixed assets and a reduced income from lower heat sales volume.

GAS

HEP Group conducts the activity of retail distribution and customer supply. As of 1 April 2014, it has also become the wholesale market supplier. These business activities recorded loss from operations of HRK 367.7 million compared to HRK 22.4 million of loss incurred in 2017.

Retail gas distribution and supply is conducted in the following counties: Osječko-baranjska, Virovitičko-podravska and Požeško-slavonska. Following the liberalization of the gas market, HEP Plin started supplying customers across other distribution areas (Zagreb, Varaždin, Sveta Nedjelja, Pula, Bjelovar, Zadar, Križevci, Kutina, Ivanić Grad, Sisak, Slavonski Brod, Samobor, Koprivnica, Pitomača, Virovitica, Rijeka, Vinkovci, Đurđevac, Čakovec, Zabok, Karlovac, Jastrebarsko, Vrbovec, Dugo Selo, Pakrac, Orahovica, Umag, Pitomača, Nova Gradiška, Vukovar, Daruvar, Krapina, etc.)

Income from retail gas distribution and supply decreased in 2018 by 1.1 percent. The sale of gas to household customers decreased by 4.3 percent, while it recorded a 1.9% increase to business customers. The sale to customers on HEP Plin own distribution area decreased by 4.3% compared to a 19.6% increase of gas sale to customers on other distribution areas in Croatia. Despite decreased sale, income from gas distribution and supply earned by HEP Plin increased in light of a 6.6% higher average selling price.

Also, in 2018 HEP sold gas to a domestic customer, which income coupled with the income earned by HEP Plin amounted to HRK 990.5 million, which was an increase by HRK 673.9 million.

Gas wholesale earned income of HRK 932.2 million accounting for 6.1 percent of HEP Group's total operating income. Said income was by HRK 31.6 million lower compared to 2017 due to a 4.5% lower gas sale.

The price at which HEP sells gas to suppliers under public service obligation was set by the Croatian Government for the period until 31 March 2018. Pursuant to the Gas Market Act, the Methodology for setting the amount of tariff items for the public service of gas supply and guaranteed supply was adopted in April 2018 under which the price of gas for the wholesale market supplier and the suppliers under the obligation of public supply supplying household customers was set.

The purchase price of sold gas was HRK 1,823.7 million, an increase by HRK 693.5 million compared to 2017 primarily due to the procurement cost of gas for the sale to a domestic customer, which was non-existent the year before, and the increase of the average purchase price for gas wholesale as the result of cancelling the obligation of supplying gas wholesale market imposed to INA d.d. as a natural gas producer as of 1 April 2017.

FINANCIAL POSITION

CONSOLIDATED BALANCE (abridged)	31 Dec 2017		31 Dec 2018		%2018/2017
	HRK m	share	HRK m	share	
Long-term asset	32,538.4	84%	33,041.6	82%	+1.5%
Short-term asset	6,313.2	16%	7,308.1	18%	+15.8%
Total asset	**38,851.6**	**100%**	**40,349.6**	**100%**	**+3.9%**
Capital and reserves	25,996.0	67%	24,369.4	60%	-6.3%
Long-term provisions	1,018.5	3%	1,067.5	3%	+4.8%
Long-term liabilities	8,255.7	21%	11,112.0	28%	+34.6%
Short-term liabilities	3,581.4	9%	3,800.8	9%	+6.1%
Total liabilities and equity	**38,851.6**	**100%**	**40,349.6**	**100%**	**+3.9%**

ASSET

The value of HEP Group's total assets at the end of 2018 was HRK 40.3 bn, an increase by HRK 1.5 bn. Long-term assets accounted for 82% of the Group's asset value, which marked an increase of HRK 503.2 m resulting from the increased value of property, plants and equipment by HRK 649 m as well as of deferred taxable asset by HRK 352.1 m. The ongoing investments were reduced by HRK 459.9 million. Advance payments made towards property, plants and equipment also increased.

The value of short-term assets of HRK 7.3 bn represents an increase by HRK 994.9 million due to increased cash and cash equivalents by HRK 938.2 m and reserves by HRK 289.9 m in light of increased CO2 emission unit, fuel and wholesale gas, electric material and other reserves. Trade receivables increased by HRK 119.6 m due to increased trade receivables for sold electricity, while other short-term receivables decreased by HRK 352.9 million as the result of reduced deposits and term deposits for the period exceeding 3 months, reduced receivables from HROTE for overpaid electricity procured under mandatory purchase and receivables for supplied electricity as well as reduced receivables towards corporate tax.

CAPITAL AND LIABILITIES

Capital and reserves at the end of 2018 amounted to HRK 24.4 bn, a decrease of HRK 1.6 billion in comparison with 2017. Retained profit decreased as the result of profit adjustment for the previous period caused by the changes in the accounting policy of recognizing income from connection fees (implementation of IFRS 15 Revenue from Contracts with Customers). The dividend in favour of the State Budget of HRK 214.8 million was paid in 2018, accounting for 60 percent of profit after tax of HEP d.d., the parent company, for 2017. These changes caused the share of capital and reserves to reduce from 67 percent to 60 percent.

Long-term liabilities increased by HRK 49 million due to increased provision amounts for severances and thermal power plant decommissioning.

Long-term liabilities amounted to HRK 11.1 bn accounting for 28% of the Group's total liabilities and equity. They increased by HRK 2.9 bn primarily due to increased deferred income including income for received assets or assets funded from connection fees as the result of the implementation of IFRS 15.

Short-term liabilities amounted to HRK 3,8 bn. They increased by HRK 219.4 m compared to early 2018. Trade liabilities increased by HRK 408.6 million, while the current maturity of long-term loans decreased by HRK 293 million. Staff liabilities decreased by HRK 132.6 million as the result of reduced severance provisions.

CREDIT RATING

HEP is rated by both Standard&Poor's and Moody's. In 2018, Standard & Poor's (S&P) affirmed the stand-alone assessment of Hrvatska elektroprivreda (bb), as well as the overall assessment of HEP's credit rating (BB). It upgraded the rating outlook from stable to positive following the sovereign rating upgrade. In March 2018, Moody's affirmed the long-standing credit rating on HEP (Ba2) as well as the stable credit rating outlook.

In late March 2019, Standard & Poor's upgraded HEP's credit rating to BB+ with a stable outlook. Due to the methodology and criteria used by the Agency in the assessment of HEP, this upgrade came after the upgrade of Croatia's sovereign rating. In late April 2019, Moody's upgraded the outlook from stable to positive following the upgrade of Croatia's sovereign rating.

CREDIT AGENCY	Baseline credit assessment	Standalone credit quality
Standard & Poor's	BB+ (stable)	bb
Moody's	Ba2 (positive)	ba2

INVESTMENTS

In 2018, the Group made investment in the amount of HRK 2.376.1 m. Main investments focused on the reconstruction and the modernization of generation facilities and electric power system plants, the construction of new generation facilities and the reconstruction of the existing and the construction of new transmission and distribution network infrastructure.

The preconditions for the erection of the first HEP's wind farm and non-integrated solar power plants were met in 2019. The independent development of several RES projects focusing on the creation of conditions for the construction thereof in the following two years continued.

Apart from the above, investments were made in district heating and gas distribution systems as well as in the upgrade of IT and telecommunication infrastructure and the expansion and development of the EV charging station network in the cities and along the motorways in Croatia.

INVESTMENTS in HRK m	2016	2017	2018	% 2018
Investments in property, plants and equipment	2,589.1	2,431.9	2,376.1	-2.3%

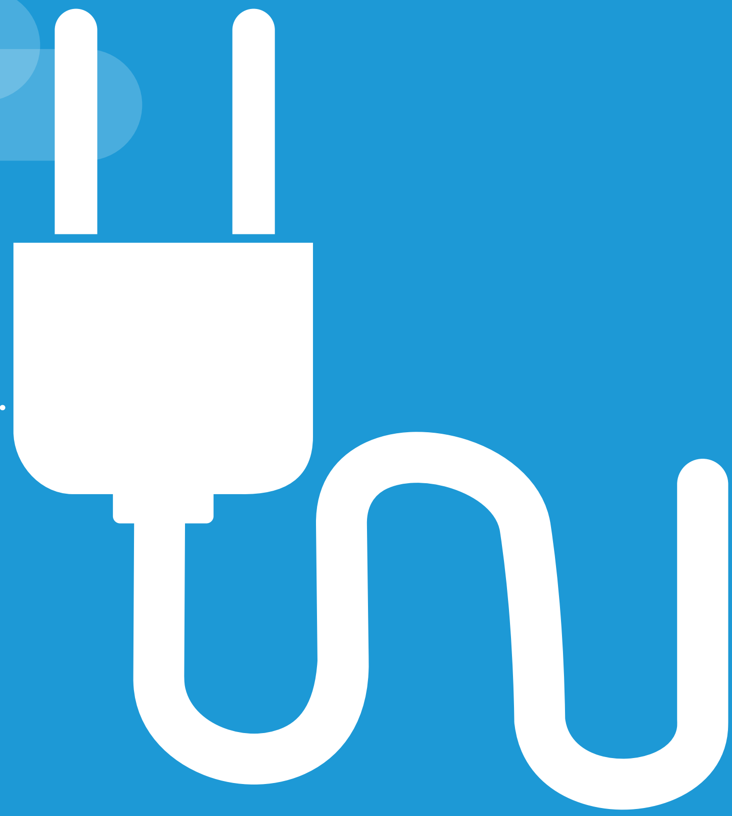
Through continuous investments in the maintenance and modernization of the existing facilities and the construction of new generation capacities and network systems, HEP meets the following objectives: security of energy supply, competitiveness of HEP's power system, the development of HEP Group's business system, contribution to sustainability and the continuity of the Croatian energy sector by taking into consideration the increasing presence of other participants on the open market, especially in electricity supply and electricity generation from renewable energy sources.

Through investments, HEP Group meets preconditions for Croatia's future reach of an adequate level of energy independence in electricity sector, by taking current electricity consumption and the projection of its growth into consideration as well as necessary decommissioning of thermal facilities, unable to meet the prescribed conditions of environment protection due to their technological old age.

MAJOR INVESTMENTS

- BE-TO Osijek and BE-TO Sisak CHP biomass fired cogeneration plants were issued operating permits. Both plants have concluded a contract with HROTE for the off-take of incentivized electricity.
- The technical inspection of the fourth replaced unit was carried out in HPP Zakučac. The operating permit was issued. The completion of the remaining reconstruction works is planned for the period 2019-2021.
- Positive environmental impact assessment decisions were issued for HES Kosinj and HPP Senj 2 projects in 2018.
- In July 2018, the EPC Contract for the construction of the replacement Unit L in EL-TO Zagreb CCPP was signed. Preparatory works were conducted during the year to ensure the site readiness for the launch of said construction in 2019.
- Contracts for taking over project companies for the erection of Korlat Wind Farm and Vis Solar Power plants were signed as well as the Contract for the receipt of project documentation for the erection of Cres Solar Power Plant and the Contract for the Vrlika South Wind Farm project takeover.
- In terms of distribution, the construction, reconstruction, transformation upgrade or the construction of additional MV plants in several 110/10(20)kv, 35/10(20)kv electric power facilities and the MV network was completed. The recovery of voltage conditions and the increase of the security of supply in distribution network continued as well as investments into the replacement and the regulation of metering points and connections.
- In terms of district heating, the activities on connecting Zagreb districts of Dubrava onto the central heating system, the revitalisation of the hot water and steam pipeline network of the city of Zagreb, the revitalisation of the warm-water network in Velika Gorica, the revitalisation of the hot water and steam pipeline network of the city of Osijek, the preparation of the remote operation and reading of heating stations, as well as the revitalisation of the hot water network and the remote control systems in Sisak continued.
- In terms of gas distribution, the construction of the gas network in Osijek-Baranja County (Klisa, Velika, Gajić, Draž, Vučjak Feričanački and Beketinci) continued.
- Continuous investments are made in the development of the telecommunication infrastructure and the construction of the telecommunication network which ensures the connection of important facilities and business infrastructure to HEP's telecommunication system as well as setting the conditions for the implementation of the smart grid concept.
- The upgrade of the SAD EDM/ECM solution continued in 2018. It included a period of intensive support to the operation of the ECM system, which was put in operation in December 2017, while the EDM part of the project included the harmonization of the project expansion scope and the redefinition of solution architecture, all aimed at EDM, as part of SAP, becoming production ready, which is expected to occur in late 2019.
- Within the project of e-mobility, a development and construction of the public EV charging infrastructure continued across Croatia ensuring the existence of a future platform for the acquisition of new customers and the facilitation of the smart grid concept as a support to the entire electric power system.

Active liquidity management,
confirmed by rating agencies in 2018,
continued in 2019.



FINANCIAL **STATEMENTS**

Consolidated annual financial statements

and Independent Auditor's Report for the year 2018

CONTENTS

Responsibility for the consolidated annual financial statements

The Management Board of the company Hrvatska Elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37, (hereinafter: "the Company") is responsible for ensuring that the consolidated annual financial statements for the year 2018, are prepared in accordance with the Accounting Act (Official Gazette No 78/15, 120/16, 116/18) and International Financial Reporting Standards as determined by the European Commission and published in the Official Journal of the EU, to give a true and fair view of the consolidated financial position, the consolidated results of operations, consolidated changes in equity and consolidated cash flows of the Company for that period.

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

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

- selection and consistent application of suitable accounting policies in accordance with the applicable financial reporting framework;
- giving reasonable and prudent judgments and estimates; and
- using the going concern basis of accounting in preparation of consolidated 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 consolidated financial position, the consolidated results of operations, consolidated changes in equity and consolidated cash flows of the Company, and also their compliance with the Accounting Act and the International Financial Reporting Standards. The Management is also responsible for safe keeping the assets of the Company and also for taking reasonable steps for prevention and detection of fraud and other irregularities.

Signed for and on behalf of the Management Board:

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

Hrvatska elektroprivreda d.d.
Ulica grada Vukovara 37
10000 Zagreb
Republic of Croatia
30 April 2019

INDEPENDENT AUDITOR'S REPORT

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

REPORT ON THE AUDIT OF THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

Opinion

We have audited the consolidated annual financial statements of the company Hrvatska elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37 (the "Company" or "the Group"), which comprise the Consolidated statement of financial position (Consolidated Balance Sheet) as at 31 December 2018, Consolidated statement of profit or loss, Consolidated statement of other comprehensive income, Consolidated statement of changes in equity and Consolidated statement of cash flows for the year then ended, and Notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated annual financial statements give a true and fair view of the consolidated financial position of the Company as at 31 December 2018, and of its consolidated financial performance and consolidated cash flows of the Company for the year then ended in accordance with the Accounting Act and the International Financial Reporting Standards (the "IFRS"), determined by the European Commission and published in the Official Journal of the EU.

Basis for Opinion

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

Emphasis of matter

As described in the Note 29 to the consolidated financial statements, at 31 December 2018, the Company stated clearing debt liability in the amount of HRK 779,214 thousand (31 December 2017: HRK 775,189 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 some other legal transaction. Our opinion has not been modified in this respect.

Emphasis of matter (continued)

As described in the Note 35 to the consolidated financial statements, provisions of the Water Management Act that came into force on 1 January 2010, raised a question of ownership and legal status of the Company's property - reservoirs and ancillary facilities used for generation of electricity from hydropower plants, as they are defined as Public water resources in general use 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. In May 2018, the Law on Amendments to the Water Act (OG 46/18) entered into force, by which the Republic of Croatia establishes the construction rights on public water resources - land on which water structures were built through Company's or its predecessors' investments; except for the land on which the accumulation was constructed and the supply and drainage channels and tunnels built. These rights are granted in favour of the Company, without compensation for a period of 99 years. As long as this right is resumed, the Company is granted the right to manage, on behalf of the Republic of Croatia, public good / land on which constructions of electricity generation with accumulation and supply and drainage channels and tunnels are built. In view of the above, it is necessary to initiate relevant procedures for entering these rights into land registers. Our opinion has not been modified in this respect.

Other matters

Attention is drawn to the Note 35 to the consolidated 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 Consolidated statement of financial position (Consolidated Balance Sheet). Our opinion has not been modified in this respect.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, are of most significance in our audit of the 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 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

Revenue recognition from electricity sales to customers of universal service (Households) and application of IFRS 15

Revenues from the sale of electricity are recognized on the basis of the best estimate of the delivered energy quantity. As the actual calculation of delivered energy quantities to customers of the household category is performed twice a year, the Group bases its electricity sales revenue on the total generated and purchased quantities of energy distributed in the distribution network.

Key audit matter (continued)

Revenue recognition from electricity sales to customers of universal service (Households) and application of IFRS 15 (continued)

By doing so, the total produced and purchased amount of energy is corrected for losses on the distribution network based on logarithmic regression. After analysing several different approximation methods (five-year average, linear approximation and similar), the Management Board selected logarithmic regression as the most suitable one. Correction of revenue from households as at 31 December 2018 was obtained by calculating a logarithmic curve using 7.75% network losses, while for the year ended 31 December 2017, the percentage of losses used in the calculation was 7.71%. The result was a decrease in revenues of HRK 37,349 thousand in 2018 compared to the previous year, and the liability for accrued income amounted to HRK 6,250 thousand.

Furthermore, the application of the new International Financial Reporting Standard 15 - Revenue from Contracts with Customers has a significant impact on the 2018 annual financial statements that will continue in the future. The Group has chosen, in accordance with the transitional provisions, not to modify comparable periods and to apply this standard retroactively with the cumulative effect of initial application on 1 January 2018. The cumulative effect of the initial application of IFRS 15 is recognized as a decrease in the initial balance of retained earnings (in the amount of HRK 2,685,047 thousand), increase in initial amount of deferred income and increase in initial amount of deferred tax assets for the remaining amount of recognised higher income from the connection fee, which required accounting treatment in accordance with previous standards and interpretations.

We focused on this area because it involves significant estimates of revenue recognition from electricity sales on the reporting date and the material impact and complexity of the application of the new standard.

Related disclosures in the accompanying annual consolidated financial statements

See Notes 2, 3, 22 and 33 in the accompanying consolidated annual financial statements.

How we addressed the key audit matter

Our audit procedures related to this area, among other things, included:

- Acquiring understanding of key management controls related to estimating revenue from electricity sales;
- Evaluation of the reasonableness of the key assumptions used in the estimation model including the quantities of electricity sold and the price;
- Mathematical accuracy test of the model of estimation of revenues from electricity sales;
- Involvement of an IT expert to evaluate the reliability of the system and we internally made an independent estimate of the unrecorded revenues using data on quantities and prices received by the Group, and we have compared the results so obtained with the Group's revenue estimates;
- Detailed analysis of accounting treatment of revenue from the connection fee in accordance with IFRS 15 - Step 5 model.

We also assessed the adequacy of the Company's disclosure regarding the revenue recognition from the sale of electricity to universal service customers (household customers) and the application of IFRS 15.

Key audit matter

Contingent liabilities and court disputes

Since the Group is exposed to significant legal claims, we have focused our attention on this area. Any contingent liability disclosed, or their 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 consolidated financial statements, if applicable, is subject to a subjective assessment. According to that, the Management Board estimates future outcomes and amounts of contingent liabilities that may arise as a result of these claims.

Related disclosures in the consolidated annual financial statements

See Notes 2, 3 and 28 in the accompanying consolidated annual financial statements.

How we addressed the key audit matter

Our auditing procedures, related to this area included, among others:

- Receiving and analysing the attorneys' responses to our written inquiries and considering certain issues with them;
- Critical review of the used assumptions and estimates pertaining to the claims. This includes assessing the likelihood of unfavourable outcome of court proceedings and the reliability of the assessment of the related amount of obligation;
- Assessment of the adequacy of disclosure in the consolidated financial statements, taking into account sensitivity and possible prejudice in the disclosure of detailed information.

Furthermore, we assessed the adequacy of the Company's disclosure regarding Contingent liabilities and court disputes.

Other Information in the Annual Report and separate nonfinancial report

The Management is responsible for other information. Other information include information contained in the Annual report, but do not include the consolidated annual financial statements and our Independent auditor's report on them which we received before the date of this Independent Auditor's Report and a separate non-financial report that we expect to be made available after that date.

Our opinion on the 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 relation with our audit of the 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 consolidated annual financial statements or with our knowledge obtained in the audit or otherwise, appears to be materially misstated; as well as whether the separate nonfinancial 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.

Other Information in the Annual Report and separate nonfinancial report (continued)

When we read a separate nonfinancial 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 consolidated annual financial statements

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the consolidated annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an 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 consolidated annual financial statements.

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

- Identify and assess the risks of material misstatement of the consolidated annual financial statements, whether due to fraud or error; design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal controls relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal controls.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.

Auditor's responsibilities for the audit of the consolidated annual financial statements (continued)

- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated annual financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated annual financial statements, including disclosures, and whether the consolidated annual financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain enough audit evidence related to financial information from individuals or business activities within the Group to express our opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We are solely responsible for expressing our auditor's opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal controls 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.

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

Report on Compliance with Other Legal or Regulatory Requirements

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

On 5 June 2018, we were appointed by the General Assembly of the Company, based on the suggestion of the Supervisory Board, to audit the consolidated annual financial statements for 2018.

At the date of this Report, we have been continuously engaged in carrying out the Company's statutory audits since audit of the Company's consolidated annual financial statements from 2012, up to the audit of the Company's annual financial statements for 2018, total of 7 years.

Report on Compliance with Other Legal or Regulatory Requirements (continued)

In addition to the matters we have mentioned in our Independent Auditor's Report as Key Audit Matters, 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 2018, 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 consolidated 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 consolidated 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 consolidated financial statements as a whole, we are required to modify our opinion in an Independent Auditor's Report.

During the audit of the consolidated annual financial statements of the Company for the year 2018, we have determined the significance for the annual financial statements, as a whole, in the amount of HRK 213,500 thousand, which represents about 1.5% of the total sales revenues of the Company for 2018, 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 2018 and the date of this report, we did not provide the Company or its subsidiaries, 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 subsidiaries.

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 2018, as part of the Annual report of the Company for the year 2018, are in accordance with the financial information stated in the consolidated annual financial statements of the Company set out on pages 10 to 100 on which we expressed our opinion as stated in the Opinion section above.

In our opinion, based on the work we performed during the audit, the Company's Management report for 2018, which is an integral part of the Company's Annual report for 2018, 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 2018 which is an integral part of the Company's Annual report for 2018.

In our opinion, based on the work that we performed during the audit, the Corporate governance statement, included in the Annual report for 2018, is prepared in accordance with the requirements of article 22, paragraph 1, points 3 and 4 of the Accounting Act.

The Corporate governance statement, included in the Annual report for 2018, includes information from the article 22, paragraph 1, and 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 2018 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 annual financial statements given on pages 10 to 100 on which we expressed our opinion as stated in the section Opinion above.

Engagement partner in the audit of the consolidated annual financial statements of the Company for 2018, which has resulted in this Independent Auditor's Report, is Zdenko Balen, certified auditor.

Zagreb, 30 April 2019

BDO Croatia d.o.o.

Trg J. F. Kennedy 6b

10000 Zagreb

Vedrana Stipić, Member of the Management Board

Zdenko Balen, Certified Auditor

Consolidated Statement of profit or loss

For the year ended 31 December 2018

	Notes	2018 in '000 HRK	2017 in '000 HRK
Revenue from electricity sales	4	11,650,333	11,493,664
Revenue from thermal power sales	4	664,442	683,264
Revenue from sale of gas on wholesale market	4	932,243	963,887
Revenue from sale of gas to customers	4	990,516	316,576
Sales revenue		***14,237,534***	***13,457,391***
Other operating income	5	960,766	1,511,894
Total operating income		**15,198,300**	**14,969,285**
Electricity purchase expenses	6	(2,831,169)	(2,786,423)
Fuel expenses	6	(1,695,300)	(1,903,145)
Costs of gas sold	6	(1,823,664)	(1,130,144)
Employee benefit expenses	7	(1,841,220)	(1,946,892)
Depreciation and amortization costs	11,12	(2,001,355)	(1,935,963)
Other operating expenses	8	(3,347,135)	(2,971,895)
Total operating expenses		**(13,539,843)**	**(12,674,462)**
Profit from operations		**1,658,457**	**2,294,823**
Finance income	9	290,077	235,826
Finance expenses	9	(265,345)	(939,913)
Net profit / (loss) from finance activities		**24,732**	**(704,087)**
Profit before tax		**1,683,189**	**1,590,736**
Tax expense	10	(318,437)	(290,437)
Profit for the year		**1,364,752**	**1,300,299**
Attributable to:			
Owners of the parent		1,364,752	1,300,299

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

Signed for and on behalf of the Management Board on 30 April 2019:

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

Consolidated Statement of other comprehensive income

For the year ended 31 December 2018

	2018 in '000 HRK	2017 in '000 HRK
Profit for the year	**1,364,752**	**1,300,299**
Other comprehensive income		
Exchange differences from foreign currency translations	(18,645)	(15,609)
Changes in fair value of available-for-sale financial assets	(74,143)	(3,565)
Changes in fair value of financial assets at fair value through other comprehensive income		
Reserves	-	25,514
Items that may be reclassified to comprehensive income	*(92,788)*	*6,340*
Other comprehensive income / (loss), net	**(92,788)**	**6,340**
Total comprehensive income, net	**1,271,964**	**1,306,639**
Attributable to:		
Owners of the parent	1,271,964	1,306,639

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

Signed for and on behalf of the Management Board on 30 April 2019:

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

Consolidated Statement of financial position / Consolidated Balance Sheet

As at 31 December 2018

ASSETS	Notes	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Non-current assets			
Property, plant and equipment	11	31,222,257	31,033,112
Advances for property, plant and equipment	14	87,170	15,252
Investment property	13	303,726	305,630
Intangible assets	12	178,578	210,502
Investments calculated using the equity method	16	23,512	865
Loans	17	35,790	36,107
Financial assets available-for-sale	18	-	283,578
Financial assets at fair value through other comprehensive income	18	197,307	-
Other financial assets	19	30,764	42,918
Deferred tax assets	10	962,466	610,389
Total non-current assets		**33,041,570**	**32,538,353**
Current assets			
Inventories	20	1,547,172	1,257,292
Trade receivables	21	2,200,632	2,081,000
Other current assets	22	604,930	957,817
Cash and cash equivalents	23	2,955,325	2,017,095
Total current assets		**7,308,059**	**6,313,204**
TOTAL ASSETS		**40,349,629**	**38,851,557**

Consolidated Statement of financial position / Consolidated Balance Sheet (continued)

As at 31 December 2018

EQUITY	Notes	31 Dec 2018. in '000 HRK	31 Dec 2017 in '000 HRK
Share capital	24	19,792,159	19,792,159
Reserves	24	65,921	162,242
Retained earnings	24	4,511,318	6,041,625
Total capital		**24,369,398**	**25,996,026**
Liabilities under issued bonds	25	3,560,375	3,595,828
Loans	26	220,450	265,895
Liabilities to the State	27	10,281	13,065
Provisions	28	1,067,491	1,018,467
Other liabilities	29	7,315,415	4,356,607
Deferred tax liabilities		5,441	24,305
Total non-current liabilities		**12,179,453**	**9,274,167**
Trade payables	30	2,051,676	1,643,033
Current maturity of loans	26	115,479	408,481
Taxes and contributions	31	223,310	80,202
Interests		39,308	35,593
Employee benefit liabilities	32	141,557	274,173
Other current liabilities	33	1,229,448	1,139,882
Total current liabilities		**3,800,778**	**3,581,364**
TOTAL EQUITY		**40,349,629**	**38,851,557**

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

Signed for and on behalf of the Management Board on 30 April 2019:

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

Consolidated Statement of changes in equity

For the year ended 31 December 2018

	Share capital in '000 HRK	Reserves in '000 HRK	Retained earnings / (carried loss) in '000 HRK	Total equity in '000 HRK
Balance at 1 Jan 2017	**19,792,159**	**140,293**	**5,551,226**	**25,483,678**
Profit for the year	-	-	1,300,299	1,300,299
Other comprehensive income	-	21,949	(15,609)	6,340
Total comprehensive income	-	*21,949*	*1,284,690*	*1,306,639*
Dividends	-	-	(794,291)	(794,291)
Balance at 31 Dec 2017	**19,792,159**	**162,242**	**6,041,625**	**25,996,026**
Prior year adjustment – IFRS 9 – *Note 2*	-	(22,178)	27,046	4,868
Prior year adjustment – IFRS 15 – *Note 2*	-	-	(2,685,047)	(2,685,047)
Total prior year adjustment	**-**	**(22,178)**	**(2,658,001)**	**(2,680,179)**
Balance at 1 Jan 2018	**19,792,159**	**140,064**	**3,383,624**	**23,315,847**
Profit for the year	-	-	1,364,752	1,364,752
Other comprehensive income	-	(74,143)	(18,645)	(92,788)
Total comprehensive income	-	*(74,143)*	*1,346,107*	*1,271,964*
Dividends	-	-	(218,413)	(218,413)
Balance at 31 Dec2018	**19,792,159**	**65,921**	**4,511,318**	**24,369,398**

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

Signed for and on behalf of the Management Board on 30 April 2019:

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

Consolidated Statement of cash flow

For the year ended 31 December 2018

	2018 in '000 HRK	2017 in '000 HRK
OPERATING ACTIVITIES		
Profit before tax	1,683,189	1,590,736
Net loss from financing activities	181,395	213,512
Fair value of investment property	1,904	(7,654)
Depreciation of property, plant and equipment; amortisation of intangible assets	2,001,355	1,935,733
Non-depreciated value of disposed assets	32,950	9,334
Impairment of fixed assets	112,626	307,830
Income from reversal of impairment	-	(199,207)
Impairment of receivables	352,750	(60,756)
Inventory impairment	18,884	7,217
Increase in provisions	49,024	87,767
Cash from operating activities before changes in working capital	*4,434,077*	*3,884,512*
(Increase) in trade receivables	(472,382)	(66,652)
(Increase) in inventories	(308,764)	140,859
(Increase)/decrease in other non-current assets	(8,042)	32,998
Decrease/(increase) in other current assets	330,240	(226,900)
Increase/(decrease) in trade payables	408,643	(144,305)
Increase in other current liabilities	156,996	141,712
(Decrease)/ increase in other non-current liabilities	(99,526)	143,013
Cash generated from operations	**4,441,242**	**3,905,237**
Income taxes paid	(441,054)	(514,421)
Interests paid	(181,253)	(230,788)
NET CASH FLOWS FROM OPERATING ACTIVITIES	**3,818,935**	**3,160,028**
INVESTING ACTIVITIES		
Interests received	41,791	44,902
Purchases of property, plant and equipment	(2,376,070)	(2,431,933)
NET CASH USED IN INVESTING ACTIVITIES	**(2,334,279)**	**(2,387,031)**

Consolidated Statement of cash flow (continued)

For the year ended 31 December 2018

	2018 in '000 HRK	2017 in '000 HRK
Financing activities		
Loans and borrowings	76,207	12,149
Repayment of loans and borrowings	(404,220)	(408,099)
Repayment of issued bonds	-	(584,507)
Dividends paid	(218,413)	(794,291)
NET CASH (USED IN)/FROM FINANCING ACTIVITIES	**(546,426)**	**(1,774,748)**
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	**938,230**	**(1,001,751)**
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**2,017,095**	**3,018,846**
CASH AND CASH EQUIVALENTS AT END OF YEAR	**2,955,325**	**2,017,095**

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

Signed for and on behalf of the Management Board on 30 April 2019:

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

1. GENERAL

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

HEP d.d. is registered in Zagreb, Ulica grada Vukovara 37. The principal activities of the Group are generation, transmission and distribution of electricity, and the control of the electric power systems. In addition to main activities, HEP Group also produces and distributes thermal power through the district heating systems in Zagreb and Osijek, sale of gas on the wholesale market, and the distribution of gas in Osijek and Đakovo.

All the Group's activities are governed by applicable laws, regulations and decisions issued by the Croatian Government. As at 31 December 2018 the Group employed 11,011 employees (2017: 11,894), excluding Krško Nuclear Power Plant which employed 633 employees (2017: 608).

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

Laws regulating the energy sector

On 19 October 2012, the Croatian Parliament adopted the Energy Act and the Law on Regulation of Energy Activities and on 8 February 2013 the Electricity Market Act. The Gas Market Act was adopted on 22 February 2013, and the Heat Market Act on 21 June 2013. On 17 October 2014, the Croatian Parliament adopted the Energy Efficiency Act, on 10 September 2015, the Law on Renewable Energy Sources and Highly Effective Cogeneration, and on 18 September 2015, the Law on Amendments to the Electricity Market Act. On 17 February 2017, the Croatian Parliament adopted the Law on Amendments to the Gas Market Law. On 16 February 2018, the Croatian Parliament adopted the Gas Market Act and its entry into force annulled the validity of the Gas Market Act (OG 28/13, 14/14 and 16/17). On 23 August 2018, the Government of the Republic of Croatia adopted the Regulation on Amendments to the Heat Energy Market Act. On 13 July, the Croatian Parliament adopted the Law on Amendments to the Law on Regulation of Energy Activities. On 7 December 2018, the Croatian Parliament adopted the Law on Amendments to the Renewable Energy Sources Act and Highly Effective Cogeneration. On 14 December 2018, the Croatian Parliament adopted the Law on Amendments to the Energy Efficiency Act.

1. GENERAL (continued)

Laws regulating the energy sector (continued)

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

Pursuant to the Electricity Market Act, every customer has the right to a free choice of suppliers, and household customers have the right to supply electricity as a universal service. Customers who have not exercised their right to choose a supplier or are left without supplier are using a guaranteed supply service.

Electricity supply is conducted at market rules and energy entities are free to contract the quantity and price of electricity delivered. Electricity supply that is performed as a guaranteed service is performed as a public service under regulated conditions customers other than households, who under certain conditions remain without the supplier.

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

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

In September 2015, the Croatian Energy Regulatory Agency (HERA) adopted the Methodology for determining the amount of tariff items for electricity distribution and Methodology for determining the amount of tariff items for electricity transmission, and in December 2015 the Decision on the amount of tariff items for electricity distribution and Decision on the amount of tariffs for electricity transfers to be applied from 1 January 2016. In December 2018 HERA adopted the Decision on the amount of tariff items for electricity distribution and Decision on the amount of tariffs for electricity transfers to be applied from 1 January 2019.

Since the Act on Amendments to the Electricity Market Act is in force, the decision on the amount of tariff items for the supply of electricity within the universal service is made by HEP Operator Distribucijskog Sustava d.o.o. or HEP Elektra d.o.o. from 2 November 2016. In accordance with the provisions of the Electricity Market Act, on 17 December 2013, HERA adopted a Methodology for determining the amount of tariff items for guaranteed electricity supply. Customers who are supplied with electricity in a guaranteed supply from 1 July 2014 pay the supply by the tariff items in accordance with the HERA decisions on the amount of tariff items for guaranteed electricity supply. In February 2019 HERA adopted a Methodology for determining the amount of tariff items for guaranteed electricity supply, which came into force on 1 March 2019.

1. GENERAL (continued)

General Assembly

The General assembly consists of the members representing the interests of the sole 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 2018

Goran Granić	President	President since 7 December 2017
Marko Primorac	Member	Member from 7 December 2017 to 25 July 2018
Jelena Zrinski Berger	Member	Member since 7 December 2017
Lukša Lulić	Member	Member since 29 October 2018
Ivo Ivančić	Member	Member since 29 October 2018
Dubravka Kolundžić	Member	Member from 1 July 2015 to 10 January 2018
Višnja Komnenić	Member	Member from 11 January 2018 to 22 October 2018
Meri Uvodić	Member	Member since 4 December 2018

Members of Supervisory Board in 2017

Nikola Bruketa	President	President from 23 February 2012 to 6 December 2017
Goran Granić	President	President since 7 December 2017
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
Marko Primorac	Member	Member from 7 December 2017
Jelena Zrinski Berger	Member	Member from 7 December 2017
Dubravka Kolundžić	Member	Member from 1 July 2015 to 10 January 2018

1. GENERAL (continued)

Management Board

Management Board in 2018

Frane Barbarić	President	President since 1 January 2018
Saša Dujmić	Member	Member since 4 December 2014
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

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
Saša Dujmić	Member	Member from 4 December 2014
Tomislav Rosandić	Member	Member from 2 January 2015 to 31 December 2017

Basis of preparation

The consolidated financial statements for 2018 have been prepared in accordance with the Accounting Act (Official Gazette 75/15, 120/16, 116/18), the International Financial Reporting Standards ("IFRS"), determined by the European Commission and published in the Official Journal of the EU; as well as in accordance with the Ordinance on the structure and content of annual financial statements (Official Gazette 95/16).

The consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments that are presented in revalued amounts. All amounts in the consolidated financial statements are presented in thousands of Croatian Kuna (HRK '000) as the Group's functional currency, unless otherwise stated. The Group keeps accounting records in Croatian language, in Croatian Kunas, and in accordance with Croatian legal requirements and accounting principles and practices applied by legal entities in Croatia.

The consolidated 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.

Principles and methods of consolidation

The Company's consolidated financial statements represent the aggregate of assets, liabilities, capital and reserves and the Group's business results for the year ended. Consolidated financial statements comprise the financial statements of the Company and the entities it controls - its subsidiaries. Subsidiaries within the Group are listed in Note 36. The Company has control over the entity if, based on its participation in it, it is exposed to variable yield, i.e. it has rights to them; and the ability to influence the yield by its predominance in that entity.

1. GENERAL (continued)

Principles and methods of consolidation (continued)

As the Company has 100% equity in all subsidiaries and is the sole member of the company, which makes it possible to appoint management and decision making, all of these companies are included in the consolidated financial statements as subsidiaries. Inclusion of subsidiaries in consolidation begins on the date on which the Company as a parent acquires control over that company and ceases when the Company as a parent loses control over it.

Adjustments were made in the financial statements of subsidiaries as necessary to align their accounting policies with those used by the Group. All significant transactions and balances between Group companies were eliminated during consolidation. Non-controlling interests in the net assets of consolidated subsidiaries are presented in these consolidated financial statements separately from the shares of the Company in them. Non-controlling shares include the amount of the share on the business combination date and the share in changes in equity from the date of the business combination that belongs to the non-controlling interest. Gains or losses and any portion of other comprehensive income are attributed to parent's shareholders and non-controlling interests, even if this results in a negative amount of non-controlling interest.

A change in the equity of a subsidiary, without loss of control, is accounted for as a principal transaction.

If the Company loses control of a subsidiary, it discontinues recognising related assets (including goodwill) and liabilities, uncontrolled interest and other equity components, and any gain or loss is recognized in profit or loss. Any remaining investment is recognized at fair value.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES

a) Changes in accounting policies

ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

New standards, interpretations and amendments effective

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

IFRS 9 Financial Instruments: Classification and Measurement

The standard is effective for annual periods beginning on or after 1 January 2018, with early application permitted. The final version of IFRS 9 Financial Instruments reflects all phases of the financial instruments project and replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, hedge accounting, and DE recognition. The Group adopted the standard on its effective date.

IFRS 9 Financial Instruments replaced IFRS 39 - Financial Instruments: Recognition and Measurement and had the following effect on the Group:

Investments that were classified as financial assets available for sale in accordance with *IAS 39 - Financial Instruments: Recognition and Measurement*, in accordance with *IFRS 9 - Financial Instruments* are classified as financial assets at fair value through other comprehensive income. All gains arising from measurement at fair value of the asset in question are recognized in other comprehensive income and are not transferred to the consolidated statement of profit or loss. Previously, in accordance with *IAS 39 - Financial Instruments: Recognition and Measurement* impairment of the asset for which there was an objective evidence of impairment, was recognized in the statement of profit or loss as well as gains and losses accumulated in revaluation reserves at the time of derecognition of that asset.

Impairment of financial assets classified as available for sale previously recognized in the consolidated statement of profit or loss in the amount of HRK 27,046 thousand in accordance with *IAS 39 - Financial Instruments: Recognition and Measurement* (and subsequently accrued in retained earnings) were transferred to the revaluation reserve in the amount of HRK 22,178 thousand and in a deferred tax liability in the amount of HRK 4,869 thousand to ensure that such reserve and deferred tax liability reflect cumulative gains and losses on that asset from initial recognition.

The Group has chosen not to adjust comparable periods and to apply this Standard retroactively with the cumulative effect of initial application on 1 January 2018, and the changes are presented in the consolidated Statement of Changes in Equity for the year ended 31 December 2018.

If the Group continued to report in accordance with IAS 39 - Financial Instruments: Recognition and Measurement for the year ended 31 December 2018, the following amounts would be reported in these financial statements:

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

a) Changes in accounting policies (continued)

ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

New standards, interpretations and amendments effective (continued)

IFRS 9 Financial Instruments replaced IFRS 39 - Financial Instruments: Recognition and Measurement and had the following effect on the Group (continued):

	Reported in accordance with IFRS 9 in '000 HRK	Effect in '000 HRK	Reported if IFRS 9 was not applied in '000 HRK
EQUITY			
Reserves	65,921	22,178	88,099
Retained earnings including current profit	4,511,318	(27,046)	4,484,272
Deferred tax liabilities	5,441	4,869	10,310

IFRS 15 Revenue from Contracts with Customers

The standard is effective for annual periods beginning on or after 1 January 2018. IFRS 15 establishes a five-step model that will apply to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry. The standard's requirements will also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., sales of property, plant and equipment or intangibles). Extensive disclosures will be required, including disaggregation of total revenue; information about performance obligations; changes in contract asset and liability account balances between periods and key judgments and estimates.

IFRS 15: Revenue from Contracts with Customers (Clarifications)

The Clarifications apply for annual periods beginning on or after 1 January 2018 with earlier application permitted. The objective of the Clarifications is to clarify the IASB's intentions when developing the requirements in IFRS 15 Revenue from Contracts with Customers, particularly the accounting of identifying performance obligations amending the wording of the "separately identifiable" principle, of principal versus agent considerations including the assessment of whether an entity is a principal or an agent as well as applications of control principle and of licensing providing additional guidance for accounting of intellectual property and royalties.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

a) Changes in accounting policies (continued)

ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

New standards, interpretations and amendments effective (continued)

IFRS 9 Financial Instruments replaced IFRS 39 - Financial Instruments: Recognition and Measurement and had the following effect on the Group (continued):

IFRS 15: Revenue from Contracts with Customers (Clarifications) - (continud)

The Clarifications also provide additional practical expedients for entities that either applies IFRS 15 fully retrospectively or that elect to apply the modified retrospective approach.

IFRS 15 - Revenue from Contracts with Customers have been replaced by IAS 18 - Revenues and IAS 11 - Construction Contracts and Related Interpretations, including IFRIC 18 - Transfer of Assets from Customers. Replacement of IFRIC 18 - Transfer of Assets from Customers to IFRSs 15 - Revenue from Contracts with Customers on the Group affected the following:

Connection fees received from customers for contracts concluded until 30 June 2009 have been recognized as deferred income and recognized as income for the period, together with the amortization of the related assets (connections). After the entry into force of IFRIC 18, connection fees received from customers as from 1 July 2009 were recorded as revenue in the amount of money received from the buyer at the time the customer joined the network or was provided permanent access to service delivery. The Group applied IFRIC 18 prospectively, that is, to contracts that were concluded after July 1, 2009, while retaining prior accounting for contracts concluded prior to that date. In accordance with the provisions of IFRS 15, the scope of which are the network connection agreements, the network connection fee is associated with distribution, transmission and electricity supply services and cannot be considered as a separate execution obligation.

In accordance with IFRS 15, the network connection is considered to be a reimbursement for future network services and electricity, heat and gas supplies and will therefore be recognized as revenue after providing these future services. Furthermore, by providing network and electricity supply, heat and gas services, the customer simultaneously receives and uses the benefits arising from the Group's performance, which means that the IFRS 15 criterion for recognition of revenue during the execution of the service has been met. An acceptable approach to determining the service provision period is the lifetime of a terminal asset as the connections become part of the distribution network and relate to the Group's obligation to provide the customer with access to the network over the entire useful life of the connections. Therefore, revenue should be systematically allocated over the period of useful life of the constructed asset or transferred asset used for the provision of fixed services, and the fees received from the customers to be recorded as deferred income and recognized as the income of the period simultaneously with the amortization of the assets (connections).

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

a) Changes in accounting policies (continued)

ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

New standards, interpretations and amendments effective (continued)

IFRS 15 - Revenue from Contracts with Customers have been replaced by IAS 18 - Revenues and IAS 11 - Construction Contracts and Related Interpretations, including IFRIC 18 - Transfer of Assets from Customers. Replacement of IFRIC 18 - Transfer of Assets from Customers to IFRSs 15 - Revenue from Contracts with Customers on the Group affected the following (continued):

The Group has elected not to restate comparative periods and apply this standard retroactively with the cumulative effect of the initial application on 1 January 2018. The cumulative effect of initial application of IFRS 15 is recognized as a reduction in the initial balance of retained earnings, an increase in the initial amount of deferred income and an increase in the initial amount of deferred tax asset for the remaining amount of recognized higher income than the related fee that required accounting treatment in accordance with IFRIC 18. The above impact on the Group's balance sheet position as at 1 January 2018 is as follows:

- Reduction of retained earnings in the amount of 2,685,047 ('000 HRK)
- Increase in deferred income in the amount of 3,009,663 ('000 HRK)
- Increase in deferred tax assets in the amount of 324,616 ('000 HRK)

If the Group continued to report in accordance with I IFRIC 18 - Transfer of Assets from Customers for the year ended 31 December 2018; the following amounts would be reported in these financial:

	Reported in accordance with IFRS 15 in '000 HRK	Effect in '000 HRK	Reported if IFRS 15 was not applied in '000 HRK
Statement of profit or loss			
Revenue from sales of services and other operating revenues	960,766	273,491	1,234,257
Profit before tax	**1,683,189**	**273,491**	**1,956,680**
Income tax	(318,437)	(48,461)	(366,898)
Profit for the year	**1,364,752**	**225,030**	**1,589,782**
ASSETS			
Deferred tax assets	962,466	(310,149)	652,317
Tax receivables	9,593	(48,461)	(38,868)
EQUITY			
Retained earnings including current tax	4,511,318	2,965,555	7,476,873
Deferred income for assets financed from connection fees	6,209,712	(3,324,645)	2,885,067

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

a) Changes in accounting policies (continued)

ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS (CONTINUED)

New standards, interpretations and amendments not yet effective

IFRS 16: Leases

The standard is effective for annual periods beginning on or after 1 January 2019. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The new standard requires lessees to recognize most leases on their financial statements. Lessees will have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. The Group decided not to apply the new lease standard retroactively, but the exemption for the lessee will be used. When converting to the new standard, liabilities based on existing operating leases will be discounted using the appropriate incremental borrowing rate and will be recognized as a lease liability. Assets with the right to use property will be recognised in the amount of lease liability adjusted to the amount of prepaid or calculated lease payments.

The Company estimates that the application of the new standard will have approximately the following effects:

- Increase of assets with right to use for approximately HRK 65,966 thousand
- Increase in liabilities by approximately HRK 65,966 thousand

Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)

The Amendments are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. It clarifies that an entity applies IFRS 9 Financial Instruments to long-term interests in an associate or joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied. These Amendments have not yet been endorsed by the European Union.

The Group will adopt amendments with their effective date and does not expect them to have a significant influence on the Group's financial statements.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies

Investments in joint ventures

Joint ventures are classified in accordance with IFRS 11 in:

Joint management - a common affair in which parties that have joint control have rights to assets and liabilities based on the financial obligations of the venture in question

A joint venture - a joint venture in which parties who have joint control have the right to net assets from the venture in question.

When classifying investments in joint ventures the Group considers:

- The structure of a joint venture
- The legal form of joint venture structured through separate legal entities
- Contractual terms of joint venture
- All other facts and circumstances (including any other contractual arrangements).

Shares in joint ventures are reported using the equity method.

The Group calculates its investment in joint management by recognizing its share of assets, liabilities, revenues and expenses in accordance with its contractual rights and obligations.

As a joint management, the group identified an investment in the Krško Nuclear Power Plant (Note 15).

As a joint venture, the Group identified an investment in LNG Hrvatska d.o.o. (Note 16).

Defined benefit schemes and other employee benefits

The Group does not manage the defined benefit plans after retirement for its employees and executives. Accordingly, there is no provision for these costs. The Group has the obligation to pay contributions to pension and health insurance funds in Croatia in accordance with legal regulations. This obligation applies to all persons who are in employment under the employment contract. The aforementioned contributions are paid at a certain percentage determined on the basis of gross salary.

	2018 and 2017
Pension contributions	20%
Health contributions	15%
Employment contributions	1.7%
Professional injury contribution	0.5%

The Group member companies are required to suspend contributions from employees' gross salaries. Contributions on behalf of the worker and on behalf of the employer are calculated as the expense of the period in which they were incurred (see note 7).

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Pension benefits and jubilee awards

The Group pays jubilee awards and one-off retirement severance payments to its employees. The liability and the cost of these benefits are determined by applying the projected unit credit method. With the projected unit credit method, each period of working life is viewed as the basis for the additional unit of earnings rights and each unit is measured separately until the final commitment is made. The liability is determined on the basis of the present value of estimated future cash outflows using a discount rate similar to the interest rate on government bonds in the Republic of Croatia with currencies and maturities in accordance with the currencies and estimated liability duration. Liabilities and expenses of these fees are calculated by an authorized actuary.

Jubilee awards

The Group pays to its employees some benefits for long-term work (jubilee awards) and pension benefits when retiring. The reward for long-term work ranges from HRK 1,500 to HRK 5,500 net for working continuously in the Group for 10 to 45 years.

Severance payments

From 1 January 2018, the Collective Agreement (which applies to all members of the HEP Group) is effective, on the basis of which every employee, when retiring, is entitled to severance pay in the amount of 1/8 gross average monthly salary paid to the employee for the previous three months before the termination of the employment contract and for each year of continuous employment. This Collective Agreement is valid until 31 December 2019.

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 methods are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Property, plant and equipment (continued)

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

	2018 and 2017
Buildings	
Hydroelectric power plants (dams, embankments, buildings and other structures and facilities)	20 – 50 years
Thermal power plants (buildings and other building facilities)	33 – 50 years
Facilities and plants for the transmission and distribution of electricity (substations, overhead and cable lines, dispatch centres etc.)	20 – 40 years
Power plants, pipelines and other structures for the production and transmission of heat energy	33 years
Gas pipelines by 2014	20 – 25 years
Gas pipelines from 2014	40 years
Administrative buildings	50 years
Plant and equipment	
Hydropower plants	10 – 33 years
Thermal power plants	6 – 25 years
Electricity transmission plants (Electrical part of the substation transformers, power lines fraction)	15 – 40 years
Electricity distribution plants (Electrical part of substations and transformers, electrical part of the power lines, measuring instruments, meters and other equipment)	8 – 40 years
Thermal power stations, hot-water pipelines and other equipment	15 -30 years
Gas meters and other gas network equipment	5 – 20 years
Other equipment and vehicles	
Information technology	5 – 20 years
Licenses for computer software	5 years
Telecommunication equipment	5 – 20 years
Motor vehicles	5 – 8 years
Office furniture	10 years

The cost of property, plant and equipment 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.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Property, plant and equipment (continued)

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 property, plant and equipment. 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 is recognized as an expense or income in the statement of profit or loss.

Impairment of property, plant and equipment and intangible assets

At each reporting date, the Group 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 Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

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

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.

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 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 immediately 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. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal 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 from 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 2018 and 2017. Operating lease payments are recognized as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

Inventories

Inventories comprise material and small inventory and are carried at lower of cost and expected net sales 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_2 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_2 generated from the fossil fuel combustion in thermal power plants, as a result of which CO_2 is emitted.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Inventories (continued)

Companies are obligated to have defined quantities of CO_2 emission rights at 30 April (yearly cycle). Due to withdrawal of IFRIC 3 and insufficient provisions of IFRS, the Group has analysed different accounting models for CO_2 emission rights, and among other EFRAG discussion papers. Occasionally, the Group trades with CO_2 emission rights. Due to that the Group recognizes these emission rights as inventory.

From April 2014 inventories also contain gas for wholesale trading and are stated at a lower of value acquisition cost determined on the basis of the average weighted price and net expected sales value (Note 20).

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

The cost of the purchase includes the invoiced amount and other costs incurred directly in relation to bringing the stock to a particular location and in usable condition.

Cash and cash equivalents

Cash and cash equivalents comprise 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 to which it relates to.

Foreign currencies

The individual financial statements of each entity are presented in the currency of the primary economic environment in which the entity operates their functional currency. The results and financial position of each Group entity are presented in the consolidated financial statements in Croatian Kuna (HRK), which is the functional currency of the Group and the presentation currency for the consolidated financial statements. In the individual financial statements of each entity, transactions in foreign currencies are translated to the functional currency of the entity at the applicable exchange rate prevailing on the date of transaction.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Foreign currencies (continued)

At each reporting date, monetary balances denominated in foreign currencies are retranslated to the functional currency of the entity at the applicable exchange rate 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 rate 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 from the settlement of monetary items, and their retranslation, are stated as profit or loss of the period. Exchange differences arising from retranslation of non-monetary assets carried at fair value are stated as financial expense in the consolidated statement of profit or loss, except for exchange differences arising from 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.

When presenting the consolidated financial statements, the Group's assets and liabilities are translated into HRK at the exchange rate prevailing on the consolidated balance sheet date. These parts of the business are linked to EUR. Since the core objective of the monetary policy of the CNB is the stability of the exchange rate, the same is done by maintaining a strong HRK-EUR ratio. Income and expenditure items (together with comparative data) are translated at the average exchange rate period. However, if the exchange rate oscillation exceeds 10%, the Group applies the exchange rate on the transaction date. Foreign exchange differences arising from the translation at the end of the year are recognized within the Group's reserves and recognized as a profit or loss for the period of the sale of foreign operations.

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 consolidated statement of profit or loss because of items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's current tax liability is calculated using tax rates that have been enacted or substantively enacted at the end of the reporting period.

Deferred tax

Deferred tax is the amount expected to be payable or recovered on the basis of the difference between the carrying amount of assets and liabilities in the consolidated financial statements and the related tax base used to calculate the taxable profit and is calculated using the balance sheet liability method.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Taxation (continued)

Deferred tax (continued)

Deferred tax liabilities are generally recognized for all taxable temporary differences, and deferred tax assets are recognized to the extent that it is probable that there will be available taxable profits 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 Group 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 consolidated statement of profit or loss, except when it relates 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 in business combinations. In case of a business combination, tax effect is taken into account for the measurement of goodwill or in determining the excess of the acquirer's interest in the net fair value of identifiable assets, liabilities and contingent liabilities over cost.

Financial assets

The Group recognizes financial assets in its financial statements when it becomes party to the contractual provisions of the instrument. Depending on the business model for asset management and contractual features cash flows for the said asset, the Group measures financial assets at amortized cost, fair value through other comprehensive income or fair value through statement of profit or loss.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Financial assets (continued)

Asset items are classified and measured as follows:

DESCRIPTION	Classification / measurement
Fixed assets	
Long-term loans	Held for collection / amortised cost
Financial assets at fair value through other comprehensive income	Equity instruments / held for collection and sale / fair value through other comprehensive income
Other financial assets (non-current receivables)	Held for collection /amortised cost
Current assets	
Trade receivables	Held for collection / amortised cost
Other receivables	Held for collection / amortised cost
Cash and cash equivalents	Held for collection / amortised cost

The Group's business models reflect the way in which the Group manages assets in order to realize cash flows regardless of whether the Company's objective is solely to collect contractual cash flows from assets (held for collection) or to collect contractual cash flows and cash flows arising from the sale of assets (held for collection and sale), and if none of the above applies, financial assets are classified as part of another business model and are measured at fair value through profit or loss.

i) Financial assets at fair value through other comprehensive income

This group of assets consists of equity instruments held by the Group and traded in an active market. Expected credit losses are not accounted for or recognized, and fair value changes are recognized in other comprehensive income (FVOCI) without reclassification to the statement of profit and loss. In case the equity instrument is sold, the accumulated revaluation reserve is reclassified to retained earnings. Dividends from these financial assets are recognized in the statement of profit or loss provided that they do not result in impairment losses at the same time.

ii) Loans granted

Group loans are held within a business model whose purpose is to hold a financial asset in order to charge contractual cash flows. Contractual terms at a particular date are cash flows that represent only payments of principal and interest. At that, the principal is the fair value of the asset at initial recognition.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Financial assets (continued)

ii) Loans granted (continued)

Based on the above, the given loans were measured at amortized cost.

Measurement at amortized cost implies the following;

- Interest income is calculated using the effective interest rate method and applied to the gross book value of the asset at the calculation. The effective interest method is the method of calculating the cost of depreciation of financial assets and the allocation of interest income over the relevant period. Effective interest rate is the rate that discounts future cash receipts through the expected period of financial assets or a shorter period, if appropriate.

iii) Trade and other receivables

Trade and other receivables are held with the strategy of collecting contracted cash flows. Trade receivables that do not have a significant financial component at initial recognition have been measured in accordance with IFRS 15 at their transaction price.

iv) Impairment

Based on expected credit losses the Group recognizes impairment of financial assets. At each reporting date, the Company measures expected credit losses and recognizes the same in the financial statements. Expected credit losses from financial instruments are measured in a manner that reflects:

- Impartial and weighted sum of probability which is determined by assessing the range of possible outcomes,
- Time value of money,
- Reasonable and acceptable data on past events, current conditions and predictions of future economic conditions.

For the purposes of calculating the expected loan loss, the financial asset portfolio is divided into three levels: level 1, level 2 and level 3. At the date of first recognition, financial assets are included in level 1, and the subsequent reclassification to levels 2 and 3 depends on the increase of the credit risk of financial instrument after the initial recognition, i.e. the credit quality of the financial instrument.

The Group applies a simplified approach to IFRS 9 to measure expected credit losses using expected credit loss provisions for credit losses in trade receivables. To measure expected credit losses on an aggregate basis, trade receivables are grouped based on similar credit risk and age structure.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Financial assets (continued)

iv) Impairment (continued)

The rates of expected credit losses are based on historical credit losses that occurred over a period of three years before the end of the period. Historical loss rates are then adjusted for current and future information on macroeconomic factors affecting the Company's customers. The Company has identified domestic product (GDP), unemployment rate and inflation rate as key factors for the country in which the Company operates. The Group applied a new standard as follows:

- Receivables from domestic and foreign customers are considered in full

Through the analysis of age structure, it has been determined that the Group has no significant due receivables, the most significant part of the receivables has is not yet due and the Group estimates that it will be fully paid. No significant credit losses were identified.

Notwithstanding the foregoing, the Group separately considers the customers in difficulties and, in accordance with the estimate, generates expected credit losses that are most often in full value of the receivables.

v) Derecognition of financial assets

The Group ceases to recognize financial assets when contractual rights to cash flows from financial assets expire or financial assets are transferred and the transfer fulfils conditions for termination of recognition.

The Group transfers financial assets if, and only, either transfers contractual rights to receive cash flows from financial assets, or retains contractual rights to receive cash flows from a financial asset but assumes a contractual obligation to pay cash flows to one or more recipients in the arrangement.

When the Group transfers financial assets, it is required to estimate the extent to which it retains the risks and rewards of ownership of the financial asset. In this case, when all risks and rewards of ownership are transferred, the Group ceases to recognize financial assets and recognizes separately, as assets or liabilities, all rights and obligations that have arisen or are retained in the transfer. If almost all the risks and rewards of ownership of financial assets are retained, the Group continues to recognize financial assets. If the Group neither transfers nor retains almost all the risks and rewards of ownership of financial assets, the Group determines whether it has retained control of the financial asset. If no control over financial assets is retained, the Group derecognises financial assets and recognizes separately. as assets or liabilities. all rights and obligations that have arisen or are retained in the transfer. If control is retained, the Group continues to recognize financial assets to the extent that it continues to participate in that financial asset.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Derivative financial instruments

The Group uses derivative financial instruments to reduce foreign exchange exposure. Additionally, the Group has concluded a Cross Currency Swap Agreement by which the Dollar obligation on bonds has been converted into the Euro obligation for the entire duration of the bonds, i.e. up to their maturity on 23 October 2022. More detailed information on derivative financial instruments is disclosed in Note 37.

Derivative financial instruments are initially recognized at fair value at the date of the conclusion of the contract and subsequently redeemed at fair value at the end of each reporting period. The Cross Currency Swap Agreement is classified as hedge of fair value with respect to the nature of the hedged item. Profit or loss from re-measurement of the hedging instrument at fair value is immediately recognized in the statement of profit or loss. Any gain or loss on a hedged item attributable to a hedged risk is adjusted to the carrying amount of the hedged item and is recognized in the statement of profit or loss.

The Group made the decision to measure the fair value of the currency swap with the "Markt To Market" "(MTM)" value, according to the calculation of commercial banks. The positive value of "MTM" is recorded as a receivable, i.e. it generates financial income for the period, and the negative value of "MTM" is recorded as a liability and forms the financial expense of the reporting period. Upon the final maturity of the derivative financial instrument, the relevant receivables or liabilities will be discontinued at expense or in favour of the Group's income.

Commodity contracts

In accordance with IFRS 9, certain commodity contracts are treated as financial instruments and fall within the scope of the standard. Purchase and sale contracts concluded by the Group provide for the physical delivery of quantities that are intended for consumption or sale as part of the normal business of the Group; such contracts are therefore excluded from the area of application of the standard.

It is especially considered that term purchases and sales for physical deliveries of energy that are concluded as part of the Group's regular business are excluded from the scope of IFRS 9. This is demonstrated by the fulfilment of the following conditions:

/i/ Physical delivery of contracted quantities;

/ii/ The quantities purchased or sold correspond to the Group's business requirements;

/iii/ The contract cannot be considered as a written option defined by IFRS 9.

The Group therefore considers the transactions agreed with the aim of balancing the volume between buying and selling energy as part of its regular business as an integrated energy company, therefore not falling within the scope of IFRS 9.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Financial liabilities

Initial Recognition and Measurement

Financial liabilities are classified as financial liabilities that are measured at amortized cost. All financial liabilities are initially recognized at fair value plus associated transaction costs. Financial liabilities include trade payables and other payables, overdrafts and loans and borrowings.

Subsequent measurement

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest rate method.

Derecognition

The Group ceases to recognize the liability in the financial statements when, and only then, the obligation has been settled. When the existing financial liability is replaced by another by the same creditor under substantially different terms or the terms of existing liabilities have changed significantly, such change or modification is treated as termination of the original liability and recognition of the new liability, and the difference in the corresponding carrying amounts is recognized in the statement of profit or loss.

Provisions

Provision is recognized only if the Group has a present obligation (statutory or derivative) as a result of the past event, and if it is probable that settlement of the obligation will require the outflow of resources with economic benefits, and if a reliable estimate can determine the amount of the liability. Provisions are reviewed at each reporting date and adjusted according to the latest best estimates. If the effect of the time value of the money is significant, the amount of the provision is the present value of the costs that are expected to be needed to settle the obligation. In the case of discounting, the increase in the provisions reflecting the time elapses is recognized as an interest expense (Note 28).

Revenue recognition

Business revenues are primarily generated through the sale of electricity, heat energy and gas to households, industrial and other customers in the Republic of Croatia.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Revenue recognition (continued)

In accordance with the new IFRS 15, the Company applies a five-step model for recognizing a contract with customer:

1. Identification of the contract with the customer(s)
2. Identification of the separate performance obligations in the contract
3. Determination of the transaction price
4. Allocation of the transaction price to the separate performance obligations
5. Recognition of revenue as each performance obligation is satisfied

Revenue is recognized for each separate contractual obligation in the transaction price amount. The transaction price is the amount of contractual remuneration that the Group expects to be entitled to in return for the delivery of the promised goods or services.

Revenues from the sale of electricity are recognized on the basis of the best estimate of the delivered energy quantity. As the actual calculation of the delivered volume of energy to customers of the household category is performed twice a year, the Group's electricity sales revenue is based on the total generated and purchased quantities of electricity distributed distribution network corrected for losses on the distribution network based on logarithmic regression. From the entry into force of the Act on Amendments to the Electricity Market Act (OG 102/2015), price regulation for the public service of electricity supply of households within the universal service and the amounts of tariff items for electricity supply by the supplier who is obliged to provide the public service is terminated. The Group does not have a separate accounting model for recognizing any deferral that would result from regulated tariffs. Accordingly, the Group recognizes revenue based on the prices approved by the regulatory agency, or the company's obligation to provide the public service. Alternatively, the Group provides its customers with the option to choose a market model, and in this case, revenues are recognized in accordance with free market prices (HEPI tariff model).

Revenues from the sale of heat energy to households as well as to industrial and other customers in the Republic of Croatia are recognized at a time when the customer acquires control over the product, i.e. when the heat is delivered to the buyer and if the Group is likely to receive a fee.

Gas sales revenue is recognized at the time the buyer acquires control over the product, i.e. when the gas is shipped to buyers and if it is likely that the Company will receive a fee. Gas price is regulated by the Croatian Energy Regulatory Agency (HERA). The Group does not have a separate accounting model for recognizing any deferral that would result from regulated tariffs.

2. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES AND THE SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

b) Summary of principal accounting policies (continued)

Revenue recognition (continued)

Income from connection fees

In accordance with IFRS 15 Revenue from contracts with customers, which is effective from 1 January 2018, revenue from connection to the network is recognised systematically over the period of useful life of the asset (the connection), and fees received from customers for connection to the network are recognized as a deferred income and is recognized as the revenue of the period at the same time as the related amortization.

Segmental analysis

The Group has fully adopted IFRS 8 "Operating Segments" and discloses segment business data, as the Group trades in debt instruments on publicly traded markets (Note 4).

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The compilation of consolidated financial statements in accordance with International Financial Reporting Standards requires the Board to provide estimates, assumptions and judgments that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent liabilities. Future events are possible that will cause changes in assumptions based on which estimates are given, and thus changes in the estimates themselves. The effect of any change in the estimate will be reflected in the consolidated financial statements when it is possible to determine it. The estimates are presented in detail in the accompanying notes and the most significant of them relate to the following:

Life span of property, plant and equipment

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

Provision for decommissioning of power plants

The Management Board estimates the cost of provisions for the decommissioning of the Krško Nuclear Power Plant and Group's thermal power plants on the basis of the applicable laws and regulations and its own experience. The provision also includes activities related to environmental protection to be carried out during the decommissioning of production facilities.

Decommissioning funds for Krško Nuclear Power Plant are reserved in accordance with the Regulation on Amount, Deadline and Method of Payment of Funds for Financing Decommission and Disposal of Radioactive Waste and Used Nuclear Fuel of Krško Nuclear Power Plant (OG 155/08) (Note 15).

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

Recognition of revenues from electricity sales to customers of universal service (household customers)

As the billing is based on prepayments with an actual calculation twice a year, the Group estimates revenue from electricity sales. The estimate is based on the total amount of electricity produced in a way that is produced or purchased, reducing the amount for estimated losses on the distribution network. After analysing several different approximation methods (five-year average, linear approximation and similar), the Management has chosen logarithmic regression as the most suitable one.

The difference between previously estimated income and actual payments is recognized in the consolidated balance sheet as other short-term liabilities or other short-term receivables.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Impairment of fixed assets

The impairment calculation requires the estimate of the use value of the cash generating units. This value is measured based on the projection of the discounted cash flow. The most significant variables for determining the cash flow are the discounted rate, the term value, the time for which the cash flow projections are made, as well as the assumptions and judgments used to determine cash receipts and expenditures.

The availability of taxable profit for which deferred tax assets can be recognized

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that a profit will be generated that will enable the use of related tax benefits. The determination of deferred tax assets that can be recognized requires the application of significant judgment, which is based on the probable time and level of future taxable profits, together with future tax planning strategy (see Note 10).

Actuarial estimates used to calculate retirement benefits

The defined benefit cost was determined using actuarial estimates. Actuarial estimates include determining assumptions on discount rates, future increases in income and mortality or fluctuation rates. Due to the long-term nature of these plans, these estimates are a matter of insecurity (see Note 28).

Consequences of certain legal disputes

The Group is a party to numerous court disputes arising from regular business. Provisions are recorded if there is a present obligation as a result of the past event (taking into account all available evidence including the opinion of legal experts) where it is likely that settlement of the obligation will require a resource outflow and if the amount of the liability can be estimated reliably (Note 28).

Expected credit loss model

With IFRS 9, the expected loss credit model (ECL) is introduced. The measurement of the expected impairment loss is based on reasonable and supporting information available without excessive expense and effort and which includes information on past events, current and foreseeable future conditions and circumstances. The Group recognizes a 12-month or lifetime ECL, depending on whether there has been a significant increase in credit risk from initial recognition (or when a liability or guarantee is assumed). For the purpose of calculating the ECL model, the portfolio of financial assets is divided into three stages: level 1, level 2 and level 3. At the date of first recognition, financial assets are included in step 1 and the subsequent reclassification to steps 2 and 3 depends on the increase of the credit risk instrument after initial recognition, i.e. the credit quality of a financial instrument. For trade receivables, a simplified approach is applied whereby expected credit losses are recognized for the entire term of the receivable.

4. SEGMENT INFORMATION

Most of the Group's operating income is realized in the Republic of Croatia.

The reporting segments of the Group are divided into the following: electricity (production, transmission, distribution and sale of electricity), heating (production, distribution and sale of heat energy) and gas (distribution and sales of gas).

The profit or loss of each segment is the result of all revenues and expenses that directly relate to a particular segment. Information on financial income or expense and income tax is not stated at the segment level, as the basis for representation is the segment's operating profit.

	Electricity		Heating		Gas		Group	
	2018 in '000 HRK	2017 in '000 HRK	2018 in '000 HRK	2017 in '000 HRK	2018 in '000 HRK	2017 in '000 HRK	2018 in '000 HRK	2017 in '000 HRK
Revenue from main operations	11,650,333	11,493,664	664,442	683,264	1,922,759	1,280,463	14,237,534	13,457,391
Other segment revenue	878,706	1,409,955	57,591	70,016	24,469	31,923	960,766	1,511,894
Profit / loss from operations	**2,266,124**	**2,383,133**	**(239,954)**	**(65,908)**	**(367,713)**	**(22,402)**	**1,658,457**	**2,294,823**
Net financial expense							24,732	(704,087)
Corporate income tax							(318,437)	(290,437)
Net profit							**1,364,752**	**1,300,299**

Segment assets consist primarily of property, plant and equipment, receivables, cash and inventories. Segment liabilities comprise trade payables and other liabilities. Assets and liabilities not belonging to segments represent property and liabilities that cannot reasonably be allocated to business segments. Total unallocated assets include investment in NPP Krško, part of property, plant and equipment and unallocated financial assets. Total unallocated liabilities include long-term loans, short-term loans and other various liabilities.

	Total segment assets		Total segment liabilities	
	2018 in '000 HRK	2017 in '000 HRK	2018 in '000 HRK	2017 in '000 HRK
Electricity	32,238,163	31,631,552	8,305,271	6,034,166
Heating	1,155,130	1,205,007	198,267	167,969
Gas	390,921	365,519	89,909	93,308
Unallocated	6,565,415	5,649,479	7,386,784	6,560,088
Total Group	**40,349,629**	**38,851,557**	**15,980,231**	**12,855,531**

4. SEGMENT INFORMATION (continued)

Information on the largest customers

Revenues from electricity sales in 2018 amount to HRK 11,650,333 thousand (in 2017 HRK 11,493,664 thousand).

Revenues from the sale of thermal energy in 2018 amount to HRK 664,442 thousand (in 2017 HRK 683,264 thousand).

Gas sales revenue in 2018 refers to gas sales in the wholesale market in the amount of HRK 932,243 thousand and gas sales to customers of gas supply in the amount of HRK 990,516 thousand (2017 sales of gas in the wholesale market amounted to HRK 963,887 thousand and sales gas to gas supply customers 316,576 thousand).

Territorial business analysis

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

The following is a territorial analysis of revenues generated by the Group from the active parts of the business from external customers of electricity:

	2018 in '000 HRK	2017 in '000 HRK
Croatia	10,687,377	10,302,678
EU member states	742,009	1,038,870
Non EU member states	220,947	152,116
	11,650,333	**11,493,664**

5. OTHER OPERATING REVENUE

	2018 in '000 HRK	**2017** in '000 HRK
Network connection services	3,071	372,088
Revenue from assets funded from connection fees	319,745	224,404
Collected value adjusted receivable (Note 21)	54,822	79,971
Revenue from external services	77,898	94,233
Penalty charges	42,908	38,961
Revenue from sale of materials	37,652	32,728
Revenue from the sale of cross-border transmission capacity	120,067	130,169
Revenues from the HOPS inter-compensation mechanism - overseas	37,140	5,513
Revenue from reversal of provisions for impaired fixed assets	-	199,207
Income from reversal of long-term provisions for unused annual vacations	4,271	15,348
Income from reversal of provisions payments under the collective agreement	12,752	-
Income from reversal of long-term provisions for severance payments and jubilee awards	5,119	187
Revenues from termination of long-term provisions for legal disputes	34,612	66,928
Revenue from reversal of other provisions	2,825	-
Collected pre-settlement receivables	6,891	11,640
Revenue from customer notices	216	1,345
Revenue from court costs	7,011	7,385
Gains from sale of tangible assets	5,192	18,043
Claims written off	5,325	1,829
Income from subsidies, grants, reimbursements and compensation	3,170	2,803
More accrued fees in the previous year on CO_2 emissions for electricity generation	11,428	13,109
Other operating income NE Krško	9,141	5,409
Other	159,510	190,594
	960,766	**1,511,894**

6. PURCHASE EXPENSES

	2018 in '000 HRK	**2017** in '000 HRK
Electricity purchase	2,831,169	2,786,423
Fuel costs	1,695,300	1,903,145
Gas purchase for sale on the wholesale market	1,823,664	1,130,144
	6,350,133	**5,819,712**

Procurement of electricity and gas refers to purchases outside the system for the sale on the wholesale market and to final customers.

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

7. EMPLOYEE BENEFITS EXPENSES

	2018 in '000 HRK	**2017** in '000 HRK
Net salaries	1,044,604	1,112,785
Net salaries NPP Krško	94,258	93,171
Taxes and contributions	662,213	703,795
Taxes and contributions NPP Krško	40,145	37,141
	1,841,220	**1,946,892**

Total employee benefits:

	2018 in '000 HRK	**2017** in '000 HRK
Gross salaries	1,706,817	1,816,580
Gross salaries NPP Krško	134,403	130,312
Reimbursement of costs to employees (Note 8)	117,175	120,018
Material rights of employees (Note 8)	97,958	99,520
Unused vacations (Note 8)	12,884	5,077
	2,069,237	**2,171,507**

7. EMPLOYEE BENEFITS EXPENSES (continued)

Key management personnel compensation

	2018 in '000 HRK	2017 in '000 HRK
Gross salaries	30,215	28,881
Pension contributions	6,677	6,430
Other fees	3,759	3,508
	40,651	**38,819**

Supervisory Board members compensation

	2018 in '000 HRK	2017 in '000 HRK
Compensation fees	278	367
Taxes and contributions	23	30
Other expenses	6	10
	307	**407**

Employee benefits expense include commuting expenses in 2018 in the amount of HRK 70,168 thousand (2017: HRK 73,602 thousand), daily allowances and travel expenses in 2018 in the amount of HRK 24,550 thousand (2017: HRK 22,679 thousand), supplementary health insurance in the amount of HRK 7,372 thousand (2017: HRK 8,697 thousand) and other similar expenses in 2018 in the amount of HRK 15,085 thousand (2017: HRK 15,040 thousand).

Costs of material rights of employees include benefits under the Collective Agreement. The largest part relates to payments under the Collective Agreement in the amount of HRK 72,109 thousand, and to a lesser extent to solidarity assistance, disability allowance, child allowance and other.

Members of the Management Board were not paid other than regular salaries and receipts in the amount of HRK 3,759 thousand in 2018 (2017: HRK 3,508 thousand).

8. OTHER OPERATING EXPENSES

	2018 in '000 HRK	2017 in '000 HRK
Maintenance costs	665,890	566,004
Impairment of trade receivables (Note 21)	452,582	151,143
Gas acquisition costs	137,996	116,673
Cost of external services and materials	430,353	388,086
Daily Services and Material	87,839	179,522
Gas Supply Charges	-	6,690
Cost of CO_2 Emission Units	263,125	120,163
Write-off of fixed assets	26,653	223,128
Impairment of inventories	18,884	7,216
Impairment of fixed assets	96,014	39,630
Impairment of intangible assets	10,178	72,680
Employee Benefits Fee (Note 7)	117,175	120,018
Other material rights of employees (Note 7)	97,958	99,520
NE Krško - costs of decommissioning by Government decision	105,613	106,386
Contributions, taxes and fees to the state	102,129	96,027
Litigation provisions	11,188	18,471
Contributions and concessions for water	73,541	65,079
Provisions for unused annual vacations (Note 7)	12,884	5,077
Fee for the use of power plant space	99,675	75,138
Fee for purification and drainage water	14,040	12,447
Cost of materials sold	25,740	19,806
The cost of billing	27,866	24,807
Provision for severance payments and jubilee awards	65,765	101,164
Provisions for severance payments on termination of employment contract	33,403	-
Insurance premiums	10,918	11,835
Environmental protection fees	709	835
Damage charges	28,438	21,311
Written off unclaimed receivables	11,612	14,936
Provision for decommissioning of thermal power plants	22,255	8,711
Other costs	296,712	299,392
	3,347,135	**2,971,895**

9. FINANCE INCOME AND EXPENSES

	2018 in '000 HRK	2017 in '000 HRK
Finance income		
Net foreign exchange gain	80,627	215,803
Interest income	9,417	9,275
Fair value of the cross-currency swap	197,972	-
Dividend income	18	8,935
Other finance income	935	701
NE Krško - Interest	1,108	1,112
Total finance income	**290,077**	**235,826**
Finance expenses		
Interest expenses	(190,986)	(222,787)
Negative foreign exchange loss	(68,037)	(95,090)
Fair value of the cross-currency swap	-	(569,172)
Fair value of shares	-	(548)
NE Krško – interest	(934)	(556)
Impairment of financial assets	(1,409)	(6,000)
Other finance expenses	(3,979)	(46,777)
Total finance expenses	**(265,345)**	**(940,930)**
Capitalized borrowing costs	-	1,017
Finance expenses recognised in the statement of profit or loss	**(265,345)**	**(939,913)**
Net profit from finance activities	**24,732**	**(704,087)**

10. CORPORATE INCOME TAX

	2018 in '000 HRK	2017 in '000 HRK
Current tax	(345,898)	(345,365)
Deferred tax expense / (income) related to origination and reversal of temporary differences	27,461	54,928
Tax expense	**(318,437)**	**(290,437)**

Adjustments of deferred tax assets are shown as follows:

	2018 in '000 HRK	2017 in '000 HRK
Balance at 1January	610,389	555,461
Prior period adjustment – application of IFRS 15	324,616	-
Balance at 1 January	935,005	555,461
Reversal of deferred tax assets	(100,436)	(124,329)
Recognition of deferred tax assets	127,897	179,257
Balance at 31 December	**962,466**	**610,389**

Deferred tax asset has arisen from tax non-deductible provisions for jubilee awards and severance payments for regular retirement benefits, allowances which are not tax deductible and other provisions.

Reconciliation between income tax and profit reported in the statement of profit or loss is set out below:

	2018 in '000 HRK	2017 in '000 HRK
Profit before tax	1,683,189	1,590,736
Tax at the effective rate (20%/18%)	**(302,974)**	**(286,332)**
Non-deductible income	(37,104)	(57,369)
Tax effect of temporary differences	27,461	54,928
Non-deductible deferred tax assets of Companies operating with loss	(5,820)	(1,664)
Tax expense for the current year	**(318,437)**	**(290,437)**
Effective tax rate	19%	18%

Reducing income tax rates in Croatia from 20% to 18% entered into force on 1 January 2017. As the result of the change in the tax rate, the relevant positions of deferred taxes are re-calculated.

10. CORPORATE INCOME TAX (continued)

The Group and each of its subsidiaries are liable to pay income tax in accordance with the tax laws and regulations of the Republic of Croatia. Subsidiaries within the Group reported tax losses of HRK 304,834 thousand (2017: HRK 479,834 thousand), while the Group calculated profit tax in the amount of HRK 345,898 thousand (2017: HRK 345,365 thousand) and deferred tax assets in amounting to HRK 27,461 thousand (2017: HRK 54,928 thousand).

Existing tax losses can be transferred and recognized as a deductible item in the tax calculation in the next tax periods up to their statutory expiry date, which is 5 years from the end of the year in which the tax losses were incurred.

The Group's tax losses and their expiry dates are shown in the following table:

Year of tax loss	Total tax loss – Group in '000 HRK	Year of transfer cessation
2014	168,027	2019
2015	69,009	2020
2016	26,221	2021
2017	9,243	2022
2018	32,334	2023
	304,834	

Group companies that continuously operate with loss do not recognize deferred tax assets. The Company realizes profit and has no tax losses for the transfer. In accordance with Croatian regulations, tax losses cannot be utilized on a consolidated basis. Each individual company determines its tax liability.

As at 31 December 2018, deferred tax assets deriving from transferred tax losses in the amount of HRK 304,834 thousand were not recognized.

In accordance with the tax regulations, the Tax Administration may at any time review the books and records of the Company and its subsidiaries for a period of three years after the expiration of the year in which the tax liability is reported and may impose additional tax liabilities and penalties. The Management Board is not aware of any circumstances that could lead to potential significant obligations in this respect.

In 2018, the Tax Administration conducted tax supervision for 2016 in the subsidiary HEP Toplinarstvo d.o.o. and HEP Opskrba d.o.o. Tax Supervision in 2018 for 2016 is started in HEP subsidiary company Telekomunikacije d.o.o. and is still in progress.

10. CORPORATE INCOME TAX (continued)

The table below summarizes the changes in deferred tax assets over the year:

	Inventory impairment in '000 HRK	Provision for jubilee awards and severance payment in '000 HRK	Depreciation above prescribed rates in '000 HRK	Provision for MTM bonds in '000 HRK	Impairment of fixed assets in '000 HRK	Carried tax losses in '000 HRK	Other in '000 HRK	Total in '000 HRK
1 Jan 2017	**42,676**	**75,312**	**9,489**	**5,805**	**394,578**	**1,340**	**26,261**	**555,461**
Credited to statement of profit or loss for the year	1,087	17,585	1,776	85,136	(56,753)	(1,341)	7,438	54,928
31 Dec 2017	**43,763**	**92,897**	**11,265**	**90,941**	**337,825**	**(1)**	**33,699**	**610,389**
Restatement	**-**	**-**	**-**	**-**	**-**	**-**	**324,616**	**324,616**
1 Jan 2018	**43,763**	**92,897**	**11,265**	**90,941**	**337,825**	**(1)**	**358,315**	**935,005**
Credited to statement of profit or loss for the year	3,126	8,799	2,007	(35,635)	(10,703)	-	59,867	27,461
31 Dec 2018	**46,889**	**101,696**	**13,272**	**55,306**	**327,122**	**(1)**	**418,182**	**962,466**

11. PROPERTY, PLANT AND EQUIPMENT

	Buildings and land in '000 HRK	Inventory and equipment in '000 HRK	Assets under construction in '000 HRK	Total in '000 HRK
COST				
1 Jan 2017	**39,163,741**	**48,087,337**	**2,677,233**	**89,928,311**
Transfers	97,261	(45,316)	(51,397)	548
Additions	14,173	238,886	1,964,703	2,217,762
Additions NEK	-	-	195,306	195,306
Activation of assets under construction	623,767	1,254,726	(1,938,594)	(60,101)
Activation of assets under construction NEK	12,878	114,280	(127,158)	-
Disposal	(74,532)	(386,870)	(277,534)	(738,936)
Transfer to investment property	(97,431)	-	-	(97,431)
31 Dec 2017	**39,739,857**	**49,263,043**	**2,442,559**	**91,445,459**
Transfers	21,592	(21,338)	(188)	66
Additions	3,573	174,577	1,816,782	1,994,932
Additions NEK	-	-	291,798	291,798
Activation of assets under construction	494,043	1,762,607	(2,263,490)	(6,840)
Activation of assets under construction NEK	17,651	268,759	(286,410)	-
Disposal	(63,229)	(409,656)	(18,368)	(491,253)
31 Dec 2018	**40,213,487**	**51,037,992**	**1,982,683**	**93,234,162**
ACUMULATED DEPRECIATION				
1 Jan 2017	**27,034,457**	**32,122,765**	**-**	**59,157,222**
Depreciation for the year	674,478	1,087,016	-	1,761,494
Depreciation for the year NEK	26,072	100,763	-	126,835
Asset valuation IAS 36 /i/	(10,357)	(188,850)		(199,207)
Investment write-off IAS 36	14,070	25,560		39,630
Transfer	13,115	(12,662)	-	453
Disposal	(80,851)	(383,442)	-	(464,293)
Transfer to investment property	(9,787)	-	-	(9,787)
31 Dec 2017	**27,661,197**	**32,751,150**	**-**	**60,412,347**
Depreciation for the year	677,438	1,150,734	-	1,828,172
Depreciation for the year NEK	26,500	90,515	-	117,015
Investment write-off IAS 36	5,957	88,301	-	94,258
Transfer	2,105	(2,048)	-	57
Disposal	(56,284)	(383,660)	-	(439,944)
31 Dec 2018	**28,316,913**	**33,694,992**	**-**	**62,011,905**
NET BOOK VALUE				
31 Dec 2018	**11,896,574**	**17,343,000**	**1,982,683**	**31,222,257**
31 Dec 2017	**12,078,660**	**16,511,893**	**2,442,559**	**31,033,112**

11. PROPERTY, PLANT AND EQUIPMENT (continued)

The Group owns a large number of real estate, but ownership of certain real estate is not fully resolved. The Group is in the process of registering ownership of the Group's real estate. Due to the large number of real estates, there is a possibility that not all business property owned by the Group is recorded in the business books. There is also the possibility that for the property recorded in business books the Group has no registered ownership.

On 27 June 2013, the Management Board of the Company issued a Decision on measures and activities related to resolving the ownership status of the Company and its subsidiaries.

In the Decision are given tasks and the deadlines for submitting proposals to the competent land registry courts for registration of ownership. Activities on land registration conditions are continuing and in 2018.

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

In July 2016, Block L in TE TO Zagreb was granted a status of eligible producer on the basis of the Decision on Acquiring the Status of Preferred Electricity Producer issued by the Croatian Energy Regulatory Agency (HERA) according to which it entered the system of incentives and electricity sales at a preferential price a period of twenty-five years. Said circumstance, after establishing sustainability of the financing model on which it was based on in 2017, has been recognized as an indication of changes in the value of the assets. In accordance with it the revaluation, has been made by an independent consultant that has shown the need to abolish the impairment loss recognized on Block L in TE TO Zagreb in the amount of HRK 199,207 thousand, resulting in an increase of the present value of the property as well as an increase in the income from the reversal of asset impairment. Calculating the recoverable amount is based on five-year plans for electricity and heat production. The calculation of the recoverable amount implies a terminal growth rate after a five-year period of 0%. Cash flow projections are discounted using a discount rate reflecting the risk of the asset in question and tested at each balance sheet date if any impairment indicators are observed.

12. INTANGIBLE ASSETS

	in '000 HRK
COST	**Licence**
31 Dec 2016	**797,775**
Transfers	(548)
Additions	40,320
Investment activation	60,101
Disposal	(38,532)
31 Dec 2017	**859,116**
Transfers	(66)
Additions	17,422
Investment activation	6,840
Disposal	(280)
31 Dec 2018	**883,032**
ACCUMULATED AMORTISATION AND IMPAIRMENT	
31 Dec 2016	**640,189**
Transfer	(453)
Amortisation of the year	47,404
Disposal	(38,526)
31 Dec 2017	**648,614**
Transfer	(57)
Depreciation for the year	56,168
Disposals	(271)
31 Dec 2018	**704,454**
NET BOOK VALUE	
31 Dec 2018	**178,578**
31 Dec 2017	**210,502**

13. INVESTMENT PROPERTY

As at 31 December 2018 and 2017, investment property includes real estate held for the purpose of earning income from the lease and / or capital appreciation, and are stated at fair value based on the best estimate of the Management Board. Fair value includes the estimated market price at the end of the reporting period. All investment property is owned by the Company.

Estimates of the fair value of real estate were performed by the official appraisers or internal services of the Group whose estimate is based on available market price information of real estate at appropriate positions. These prices were collected from a variety of sources, including available statistics from the Central Bureau of Statistics, the Real Estate Agency, HGK, and the like. These values of average prices are adjusted for the characteristics and specifics of certain real estates.

At fair value	**31 Dec 2018** in '000 HRK	**31 Dec 2017** in '000 HRK
Fair value	**305,630**	**231,491**
Net value change through adjustment of fair value	(1,904)	7,654
Transfer from property	-	66,485
Balance at year end – at fair value	**303,726**	**305,630**

14. ADVANCES FOR PROPERTY, PLANT AND EQUIPMENT

	31 Dec 2018 in '000 HRK	**31 Dec 2017** in '000 HRK
Bio energana Bjelovar	417	-
Dalekovod d.d.	84	-
Đuro Đaković Holding d.d.	-	1,325
FATA S.P.A.	74,695	-
General Electrics Hrvatska	-	3,764
HELB d.o.o.	6,400	-
Končar inženjering Zagreb	869	3,043
Končar KET	787	2,208
Siemens d.d.	2,529	336
TPK Orometal d.d.	-	1,445
Other	1,389	3,131
	87,170	**15,252**

Advances for property, plant and equipment are related to the construction of production facilities.

15. INVESTMENT IN KRŠKO NUCLEAR POWER PLANT

Investment history

At the end of 2001, a treaty was signed between the Government of the Republic of Croatia and the Government of the Republic of Slovenia to regulate the status and other legal affairs related to the investment, exploitation and decommissioning of Krško Nuclear Power Plant (NEK) and the Contract between HEP d.d. and ELES GEN d.o.o. The Treaty was ratified by the Parliament of the Republic of Croatia in mid-2002 and entered into force on 11 March 2003, after it was ratified by the Parliament of the Republic of Slovenia on 25 February 2003.

This treaty recognizes previously revoked ownership rights of HEP d.d. in the newly-formed company NEK in the amount of 50% of the share in the power plant. Both sides agreed that the life span of the power plant is at least until 2023. The produced electricity is delivered in a ratio of 50:50 for both parties, and the price of the delivered energy is determined according to the actual production costs.

This treaty also clearly defined the obligation of the Republic of Croatia for the disposal of half of radioactive waste and used nuclear fuel from NEK. Each country has an obligation to provide half of the funding needed to finance the costs of developing decommission program and costs of program implementation. Each party shall allocate funds for these purposes into their own funds in the amounts foreseen for decommissioning programs. According to the current NEK program of decommissioning and disposal of radioactive waste and used nuclear fuel, HEP d.d. is obliged to pay funds to the Fund in the amount of EUR 14,250 thousand a year.

Current status

Payments to the Fund for financing NEK decommission

Pursuant to the Regulation on the amount, deadline and method of payment of funds for the NEK program of decommissioning and disposal of radioactive waste and used nuclear fuel issued by the Government of the Republic of Croatia on 24 December 2008; from 2006 until the end of 2018 HEP d.d. the amount of paid HRK 1,587,528 thousand in the Fund. The current annual liability in the amount of EUR 14,250 thousand is paid to the Fund quarterly.

Extension of life span

After NEK received a license without time constraints from the Board for nuclear safety of the Republic of Slovenia in 2012; at the beginning of 2016 HEP d.d. and GEN energija d.o.o. have decided to extend the power plant life until 2043. The decision was made with the consent of the Intergovernmental Commission for NEK and was preceded by an economic study of the viability of investing in a long-term power plant.

15. INVESTMENT IN KRŠKO NUCLEAR POWER PLANT (continued)

Accounting of Joint operation in NEK

Joint operation in NEK is recognized in the Company's financial statements using the equity method. Application required by IFRS 11 has resulted in numerous issues and ambiguities, as well as misunderstandings with some users of financial statements.

With the aim of eliminating possible doubts of individual state bodies (FINA, Ministry of Finance, Central Bureau of Statistics, etc.) about information in separate financial statements of the Company, the Company's Management made a decision to change this policy in accordance with IAS 1, paragraph 19 item 20.

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

The following table shows the extract from the financial statements of NE Krško d.o.o. in 100% amounts as at 31 December 2018 and 31 December 2017:

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Property, plant and equipment	2,839,470	2,522,384
Capital and reserves	3,268,569	3,308,725
Gross sales revenue	1,172,816	1,181,749
Cash flows from operating activities	333,732	317,624
Profit for the year	-	-

16. INVESTMENTS CALCULATED USING THE EQUITY METHOD

Hrvatska elektroprivreda d.d. (hereinafter: HEP d.d.) and Plinacro d.o.o. concluded on 1 June 2010 the Contract on the Establishment of LNG HRVATSKA d.o.o. for liquefied natural gas business. According to the contract, LNG HRVATSKA d.o.o. became the coordinator of the LNG terminal project on Krk. Based on the Contract HEP d.d. and Plinacro d.o.o. became members and co-owners of LNG HRVATSKA d.o.o. each with a 50% of equity, management and property rights.

Pursuant to the decision of the Government of the Republic of Croatia on the designation of the LNG terminal project (construction of a liquefied natural gas terminal on the island of Krk, Omišalj municipality) as the strategic investment project of the Republic of Croatia (OG 78/15) of 16 July 2015 the LNG terminal design project was proclaimed a strategic investment project of the Republic of Croatia.

In November 2015, the European Commission adopted a list of projects of common interest (PCI) containing a list of key energy infrastructure projects, including the LNG terminal on the island of Krk. LNG Croatia has concluded contracts with INEA (Innovation and Networks Executive Agency) to co-finance projects of project licensing documentation preparation and a contract for co-financing construction.

The LNG Terminal Gas Act (OG 57/18), adopted by the Parliament on 18 June 2018, established that the construction of LNG terminal was in the interest of the Republic of Croatia and the LNG Hrvatska d.o.o. is appointed as the entity to implement the project.

Changes in investments calculated using the equity method are shown as follows:

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Investments calculated using the equity method		
Investment in LNG Hrvatska d.o.o.	23,512	865
	23,512	**865**

The following table shows the excerpt from the financial statements of LNG Hrvatska d.o.o. in 100% amounts as at 31 December 2018 and 31 December 2017.

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Property, plant and equipment	120,569	101,219
Capital and reserves	19,409	426
Sales revenue	47	101
Cash flows from operating activities	(13,227)	(17,947)
Loss for the year	(7,328)	(7,856)

17. LONG-TERM LOANS

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Receivables for loans	35,790	61,879
Current maturity of loans granted	-	(25,772)
Long-term portion	**35,790**	**36,107**

Loans to companies in business combinations:

	Year of approval	Repayment period	Approved amount in '000 EUR	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
LNG Hrvatska	2015	5 years	4,900	35,645	61,879
Current maturity				-	(25,772)
Other loans				145	-
Long-term portions				**35,790**	**36,107**

18. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Financial assets available-for-sale	-	283,578
Financial assets at fair value through other comprehensive income	197,307	-
	197,307	**283,578**

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Opening balance of financial assets at fair value through other comprehensive income	**283,578**	**288,493**
Prior period adjustment – application of IFRS 9	(22,178)	-
Balance of financial assets at fair value through other comprehensive income at 1 Jan 2018	**261,400**	**288,493**
Changes in fair value of assets	(64,684)	(5,495)
Closing balance of financial assets at fair value through other comprehensive income	**196,716**	**282,998**

Changes in financial assets at fair value through other comprehensive income presented in the table above are presented in gross amount. In the consolidated statement of comprehensive income, other comprehensive income includes changes in the fair value of assets through other comprehensive income less profit tax on net profit/loss through other comprehensive income.

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Investments through other comprehensive income (securities)		
Jadranski Naftovod d.d.	195,411	280,701
Viktor Lenac d.d.	128	305
Đuro Đaković d.d.	5	5
Kraš d.d.	3	3
Pevec d.d.	6	547
Jadran d.d.	204	364
Elektrometal d.d.	40	41
Optima Telekom d.d.,	186	298
Institut IGH d.d.,	136	191
Međimurje beton d.d.	153	153
HTP Korčula d.d.	66	61
Lanište d.o.o.	110	61
Pominvest d.d.	35	35
Konstruktor Inženjering d.d. u stečaju	233	233
Total investment through other comprehensive income	**196,716**	**282,998**

18. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME (continued)

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Other investment		
Cropex	591	-
Geopodravina d.o.o.	-	200
Novenerg d.o.o.	-	380
Total other investment	**591**	**580**
Total investment through other comprehensive income	**197,307**	**283,578**

During December 2008, by the decision of the Government of the Republic of Croatia on the transfer of shares of Jadranski naftovod d.d., HEP d.d. acquired 53,981 shares with a nominal value of HRK 2,700, i.e. the total nominal value of up to HRK 145,748,700. The Management Board it was decided that the shares of Jadranski naftovod d.d. are classified as available-for-sale assets. The registration of shares in the Central Depository Agency was completed on 19 March 2009.

In 2018 and 2017, a fair valuation was made on the basis of a notification by the Central Depository Clearing Company on the balance sheet date at 31 December. Market share price of Jadranski naftovod d.d. was HRK 3,620 as at 31 December 2018, and HRK 5,200 as at 31 December 2017. Through fair valuation of investments in Jadranski naftovod d.d; as on 31 December 2018 the value of the share was reduced by HRK 85,290 thousand (2017: decreased by HRK 5,398 thousand). The fair valuation effect in 2018 and 2017 was carried out through equity reserves.

19. OTHER FINANCIAL ASSETS

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Receivables for housing loans	9,415	13,685
Trade receivables for energy efficiency project – long-term portion	15,730	23,610
Other fixed assets	5,619	5,623
	30,764	**42,918**

Before 1996, the Company sold its own apartments to its employees in accordance with the laws of the Republic of Croatia. The sale of this property was mainly on loans and receivables, with interest rates lower than the market rates, are repayable monthly for a period of 20 to 35 years. Receivables for sold flats were transferred to new subsidiaries as of 1 July 2002. Said receivables are reported in the financial statements at discounted net present value using the interest rate of 7.0%. The liability towards the state, representing 65% of the value of sold housing, is recorded in other long-term liabilities (Note 27). Receivables are secured by mortgages on sold real-estate.

20. INVENTORIES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Fuel and chemicals	113,583	109,854
Electric material	447,957	367,226
Spare parts	205,449	201,458
Construction material	12,289	15,100
Gas for wholesale	375,950	353,600
CO_2 emission units	234,050	106,248
Other inventories	86,736	57,001
Nuclear fuel – NE Krško	223,543	172,044
Other material – NE Krško	106,791	115,053
	1,806,348	**1,497,584**
Impairment of outdated material and spare parts	(259,176)	(240,292)
	1,547,172	**1,257,292**

21. TRADE RECEIVABLES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Electricity – corporate	1,515,436	1,449,741
Electricity – households	579,469	521,542
Electricity – foreign markets	148,111	155,966
Heat, gas and services	1,066,272	717,772
Receivables from NE Krško customers	8,696	15,788
Other	71,038	55,831
	3,389,022	**2,916,640**
Impairment of trade receivables	(1,188,390)	(835,640)
	2,200,632	**2,081,000**

21. TRADE RECEIVABLES (continued)

The age structure of trade receivables not impaired in 2018 and 2017 is as follows:

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Not due	1,550,159	1,441,335
Up to 30 days	311,907	349,467
From 31 to 60 days	122,541	109,038
From 62 to 90 days	65,369	62,517
From 91 to 180 days	76,237	51,319
From 181 to 365 days	49,591	57,504
Over 365 days	24,828	9,820
	2,200,632	**2,081,000**

Changes in impairment allowance were as follows:

	2018 in '000 HRK	2017 in '000 HRK
1 Jan	**835,640**	**896,396**
Impairment of trade receivables (Note 8)	452,582	151,143
Write-offs and other	(45,010)	(131,928)
Collected impaired receivables (Note 5)	(54,822)	(79,971)
31 Dec	**1,188,390**	**835,640**

Management provides for doubtful receivables based on the overall aging of all receivables and a specific review of significant individual amounts receivable.

22. OTHER CURRENT RECEIVABLES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Receivables for income tax	72,053	98,093
Receivables for VAT	166,522	10,084
Advances for working capital	15,298	54,777
Receivables from the state for employees	4,163	3,642
Demand and time deposits for a period longer than 3 months	99,573	129,845
Demand and time deposits for a period longer than 3 months NE Krško	111,464	252,244
Short-term loans in the country - reprogram	14,896	94,486
Receivables from HEP-ESCO d.o.o. from the energy efficiency project users	9,989	8,145
Receivables for loans granted to related companies with participating interest	-	28,772
Receivables for apartments sold	5,919	6,116
Receivables for invoiced fee OIE - HROTE	31,858	48,766
Other receivables from HROTE	-	128,752
Receivables for accrued income from electricity - household	-	31,099
Other receivables NE Krško	2,466	2,431
Other short-term receivables	70,729	60,565
	604,930	**957,817**

23. CASH AND CASH EQUIVALENTS

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Current accounts in HRK	2,228,672	1,037,821
Foreign currency accounts	282,724	412,724
Restricted cash	35,445	69,104
Petty cash	198	186
Deposits with maturity up to 90 days	60,704	160,730
Daily deposits	172,361	261,150
Cash funds	175,099	75,252
Current and foreign currency accounts – NE Krško	122	128
	2,955,325	**2,017,095**

24. CAPITAL AND RESERVES

At the first registration of the Company on 12 December 1994, the Company's capital was entered in the German mark (DEM) in the amount of DEM 5,784,832 thousand. By the subsequent registration of the Company, on 19 July 1995, the capital was expressed in Croatian kuna in the amount of HRK 19,792,159 thousand. Share capital consists of 10,995,644 ordinary shares with a nominal value of HRK 1,800.

Capital reserves

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Opening balance	162,242	140,293
Prior period adjustment – application of IFRS 9	(22,178)	-
1 January 2018	140,064	140,293
Other comprehensive income, net	(74,143)	21,949
	65,921	**162,242**

Retained earnings

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Opening balance	6,041,625	5,551,226
Prior period adjustment – application of IFRS 9	27,046	-
Prior period adjustment – application of IFRS 15	(2,685,047)	-
1 January 2018	3,383,624	5,551,226
Foreign exchange differences on translation of foreign operations	(18,645)	(15,609)
Dividend paid	(218,413)	(794,291)
Profit for the year	1,364,752	1,300,299
	4,511,318	**6,041,625**

25. BOND LIABILITIES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Nominal value of domestic bonds issued in 2007	-	93,030
Discounted value	-	-
Due repayment	-	(93,030)
Current maturity of bonds	-	-
	-	**-**
Value of bonds issued abroad in 2012	-	493,571
Due repayment	-	(491,477)
Exchange rate difference	-	(2,094)
Current maturity of bonds	-	-
Bonds issued in 2015	**-**	**-**
Value of bonds issued abroad in 2012	3,612,610	3,626,428
Exchange rate differences	(46,645)	(21,431)
Discount value	7,720	7,613
	3,573,685	**3,612,610**
Accrued cost of bonds	(13,310)	(16,782)
Bonds issued in 2015	**3,560,375**	**3,595,828**
Total bonds payable	**3,560,375**	**3,595,828**

Bonds issued abroad in 2015

In October 2015, the Group issued corporate bonds in the amount of USD 550,000 thousand, at a discount, the maturity of 7 years and a fixed interest rate of 5.875% per annum. Bonds issued in 2015, for the most part, were used to repurchase 83.37% of the bonds issued in 2012 (i.e. the repurchase of USD 416,852 thousand). The remaining amount was intended to finance the Company's business activities. The bond has been listed on the Luxembourg Stock Exchange and is actively traded on it.

Derivative financial instruments

Cross currency swap

In order to reduce exposure to currency risk, i.e. the exposure to US dollar exchange rate, the Group concluded a cross currency swap agreement, by which are the dollar liabilities on bonds converted into euro, for the entire period, that is, until the final maturity on 23 October 2022.

25. BOND LIABILITIES (continued)

Derivative financial instruments (continued)

Cross currency swap (continued)

According to the cross currency swap agreement from 2015, the annual interest rate paid by the Group is fixed and amounts to 4.851% (weighted interest rate) and is payable semi-annually (the interest rate also includes swap cost).

The purpose of the cross currency swap is to reduce currency risk and recommendations of credit agencies on the importance of strategic currency risk management in order to reduce the impact on the Group's business

The Group's fair value of derivative financial instruments is linked to the Mark to market value "MTM", according to official calculations of banks, for the reporting period.

The positive value of "MTM" is recorded as a receivable, i.e. it generates financial income for the period, and the negative value of "MTM" is recorded as a liability and forms the financial expense of the reporting period. Upon the final maturity of the derivative financial instrument, the relevant receivable or liability will be discontinued and charged or credited to the Group's income.

As at 31 December 2018, using the said method, the fair value of liabilities in the amount of HRK 307,255 thousand (2017: HRK 505,228 thousand) was stated on the bonds issued in 2015 (Note 29).

26. LOAN LIABILITIES

	Interest rates	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Loans from domestic banks	Floating	75,898	445,468
Loans from foreign banks	Fixed	257,144	219,793
Finance lease	Fixed	6,413	10,038
Total loan liabilities		**339,455**	**675,299**
Deferred loan fees		(3,526)	(923)
Total loan liabilities		**335,929**	**674,376**
Current maturity		(112,061)	(405,219)
Current maturity of financial lease (Note 33)		(3,418)	(3,262)
Long-term portion		**220,450**	**265,895**

The Company has contracted loans with domestic and foreign banks with variable and fixed interest rates which ranged from 0.44% to 2.57% in 2018. The Group has contracted financial lease with a fixed interest rate of 5.6%.

Loans from domestic banks are secured by bills of exchange and promissory notes. On 31 December 2018, the Company has no debt covered by the guarantee of the Republic of Croatia.

New sources of funding

To finance the investment plan and operating activities in 2018, the Company used its own funds and funds from the loan in use.

On 24 July 2018, a loan agreement was signed with the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB) for the financing of the project of construction of KKE EL-TO Zagreb in the amount of EUR 130 million. The EBRD accounts for EUR 87 million and EIB for EUR 43. The EBRD loan consists of two tranches, namely Tranche A (EUR 43.5 million) provided by the EBRD alone and Tranche B (EUR 43.5 million) in cooperation with the commercial banks trade union.

Loans in use

In December 2018, EBRD and EIB loans were used to finance the KKE EL-TO Zagreb construction project. As at 31 December 2018 the outstanding balances of long-term loans amounted to EUR 6,9 million from the EBRD and EUR 3,4 million from the EIB. The use of the loan was contracted until 20 July 2021.

26. LOAN LIABILITIES (continued)

The principal repayment schedule for long-term loans maturing in the next five years:

	in '000 HRK
2019	115,479
2020	38,863
2021	39,555
2022	43,242
2023	43,242
After 2023	55,548
	335,929

In 2018, two loans contracted with domestic banks (HPB and Banking Club[1]) were fully repaid. On the loan from HPB, the Group had EUR 20 million and a loan of EUR 150 million from the Banking Club.

Domestic banks' loans are secured by bills of exchange and promissory notes, while loans from development banks, the EBRD and the EIB have contracted financial guarantees in the form of financial indicators according to which the Group is obliged to meet certain prescribed levels on the annual and semi-annual basis of the following indicators: net financial debt/EBITDA, EBITDA net financial expenses, net financial debt/total net value.

The Group's basic objective regarding the risks borne by the financial indicators is to protect the Group from possible breach of contractual obligations, or premature maturities of contracted credit debts.

Contracted financial indicators are monitored and calculated based on the projected balance sheet and statement of profit or loss.

The Group prepares preliminary financial statements in the upcoming mid-term period and monitors their trends.

If the projections of the balance sheet and the statement of comprehensive income at the end of the business year indicate the possibility of exceeding the individual financial ratios, the Company shall inform the bank of the existence of a breach of contract and promptly request waiver from the bank.

In the event that a bank does not approve a waiver, the potential scenario is a premature maturity of debt representing the liquidity risk for the Group. The Management believes that in case of exceeding an individual indicator, the Company may obtain a waiver from the creditor, since the payment of liabilities to financial institutions is a priority obligation of the Company and the Company has never been in default towards financial institutions.

Due to all of the above, the Board estimates that the possibility of early maturity of credit liabilities resulting from exceeding in financial indicators as well as the Group's exposure to credit risk, liquidity risk and market risk that may arise as a result of overcoming the financial indicators are minimal.

1 PBZ, ZABA, RBA

26. LOAN LIABILITIES (continued)

As at 31 December 2018, the Group met all contractual financial indicators.

The total exposure of the Group on the basis of contracted credit lines related to financial indicators as at 31 December 2018 amounts to EUR 10,290 thousand.

Below is an overview of long-term loans denominated in foreign currencies (in '000):

Currency	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
EUR	45,288	89,876

For the purpose of securing liquidity reserves in the next medium term, the Company has concluded multilateral framework contracts with domestic banks, totalling HRK 1,015 million. Funds from these limits may be used by the Company for short-term loans and issuance of guarantees, letters of credit, and letters of intent according to the needs of the Group companies. During 2018, short-term lines were used solely for the purpose of issuing guarantees and opening letters of credit, using funds of all banks equally.

From the aforementioned mid-term multi-purpose frameworks, there was no need for short-term loans due to good liquidity during 2018.

As at 31 December 2018 the total amount of available short-term funds amounts to HRK 904,384 thousand.

27. LIABILITIES TO STATE

Long-term liabilities to the state in the amount of HRK 10,281 thousand (2017: 13,065 thousand) related to the sale of housing units to employees under the Government program, which was discontinued in 1996. According to the legislation, 65% of the proceeds from the sale of apartments to employees were payable to the state upon receipt of funds. By law, the Company and its subsidiaries have no obligation to transfer the funds before they are collected from employees.

28. PROVISIONS

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Provisions for legal disputes	275,079	298,504
Provisions for severance payments	494,845	429,489
Provisions for severance payments, jubilee awards and other - NE Krško	40,159	52,611
Provisions for jubilee awards	41,373	46,083
Provisions for thermal power plant decommissioning	194,404	170,149
Provisions for delivered energy from wind farms	21,631	21,631
	1,067,491	**1,018,467**

Provision for decommissioning costs of thermal power plants in the amount of 194,404 thousand represents a discounted value of the estimated decommissioning costs of thermal power plants of the Group.

The table below summarizes the changes in provisions during the period presented:

	Provisions for legal disputes in '000 HRK	Provisions for severance payments in '000 HRK	Provisions for jubilee awards in '000 HRK	Provisions for thermal power plant decommissioning in '000 HRK	Other in '000 HRK	Total in '000 HRK
1 Jan 2017	**337,899**	**329,693**	**44,986**	**161,438**	**56,684**	**930,700**
Additional provisions	27,104	156,516	2,614	8,711	-	194,945
Decrease in provision – payment	(13,215)	(4,036)	(600)	-	-	(17,851)
Decrease in provision – estimate	(53,284)	(73)	(917)	-	(35,053)	(89,327)
31 Dec 2017	**298,504**	**482,100**	**46,083**	**170,149**	**21,631**	**1,018,467**
Transfer	-	394	16	-	-	410
Additional provisions	11,186	61,446	273	24,255	-	97,160
Decrease in provision – payment	(30,776)	(8,902)	(3,743)	-	-	(43,421)
Decrease in provision – estimate	(3,835)	(34)	(1,256)	-	-	(5,125)
31 Dec 2018	**275,079**	**535,004**	**41,373**	**194,404**	**21,631**	**1,067,491**

28. PROVISIONS (continued)

Provisions for legal disputes

The Group reserves costs for legal disputes for which it is estimated that it is unlikely to be in the favour pf the Company or its subsidiaries. The most significant provisions relate to a case related to HPP Peruča, initiated in 1995, for which a first-instance verdict was issued in 2012 in favour of the plaintiff. The value of the dispute amounted to about HRK 330,000 thousand, and reserved funds amounted to 50% of the value of the dispute; HRK 165,000 thousand.

Other major disputes relate to Kartnersparkass in the amount of HRK 9,903 thousand.

There are several legal procedures conducted against HEP Proizvodnja d.o.o. for which the Company has made a provision. The most significant of them is dispute Sanac, whose value as at 31 December 2018 amounts to HRK 9,710 thousand. Based on the legal decision HEP d.d. and HEP - Production d.o.o,. as solidary debtors, have paid the costs to the plaintiff Sanac d.o.o. in the amount of HRK 10.5 million and interests of HRK 11.4 million on 4 March 2019; each company 50% of the total amount.

Provisions for severance payments and jubilee awards

Changes in the present value of defined liabilities based on employee benefits in the current period are shown below:

	Severance payments in '000 HRK	Jubilee awards in '000 HRK	Total in '000 HRK
1 January 2017	**329,693**	**44,986**	**374,679**
Service expenses	17,239	2,486	19,725
Interest expenses	9,897	1,044	10,941
Benefits paid	(26,330)	(6,438)	(32,768)
Past service cost	25,322	915	26,237
Actuarial gains/(losses)	73,668	3,090	76,758
31 December 2017	**429,489**	**46,083**	**475,572**
NE Krško	52,611	-	52,611
Total 31 December 2017	**482,100**	**46,083**	**528,183**
Service expenses	20,362	2,421	22,783
Interest expenses	8,806	726	9,532
Benefits paid	(8,130)	(4,625)	(12,755)
Past service cost	(4,519)	(369)	(4,888)
Actuarial gains / (losses)	48,837	(2,863)	45,974
31 December 2018	**547,456**	**41,373**	**588,829**
NE Krško	(12,452)	-	(12,452)
Total 31 December 2018	**535,004**	**41,373**	**576,377**

28. PROVISIONS (continued)

The following assumptions were used in preparing the calculations:

- The termination rate is from 0% to 5.68% and is based on the statistical fluctuation rates for the Group in the period from 2006 to 2018.
- 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%.
- To calculate present value of the obligation the following discount rates were used: .
  - 2.9% (HEP ESCO d.o.o., HEP Trgovina d.o.o., Program Sava d.o.o., HEP Telekomunikacije d.o.o.)
  - 2.4% (HEP Opskrba d.o.o., HEP ELEKTRA d.o.o., HEP NOC)
  - 1.9% (HEP d.d., HEP Toplinarstvo d.o.o., HEP Plin d.o.o., HEP Upravljanje imovinom d.o.o., HEP ODS d.o.o.)
  - 1.8% (HEP Proizvodnja d.o.o.)
  - 1.1% (HEP Opskrba plinom d.o.o.)

29. OTHER NON-CURRENT LIABILITIES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Deferred income for assets financed by others	6,209,712	3,080,826
Long-term liabilities for assets financed from clearing debt	779,214	755,189
Derivative financial liabilities on swap-transactions (Note 25)	307,255	505,228
Other non-current liabilities	19,234	15,364
	7,315,415	**4,356,607**

Deferred income refers to income for the received property or property financed from the connection fee. Revenue from this property is recognized at the same time as the depreciation of the tangible asset to which it applies, as applicable for the contracts for connection to the network concluded with the customers by 30 June 2009. After 1 July 2009, the connection fee is recognized as revenue in the amount of money that is received from the customer at the time the customer connects to the network or when allowed permanent access to the delivery of services.

On 31 December 2018 the Company has an obligation to clearing debt in the amount of HRK 779,214 thousand (2017: HRK 755,189 thousand), relating to the payment of letters of credit, based on the approval of the Ministry of Finance on the use of funds based on interbank agreements. Given that there is no other document that would regulate the relationship between the Company and the Ministry of Finance in relation to the above clearing debt, is not defined whether it is a loan or other legal relationship.

30. TRADE PAYABLES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Trade payables – domestic suppliers	1,610,060	1,407,038
Trade payables – foreign suppliers	114,071	70,504
Trade payables – EU suppliers	174,911	93,241
Trade payables – NE Krško	152,634	72,250
	2,051,676	**1,643,033**

31. LIABILITIES FOR TAXES AND CONTRIBUTIONS

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Income tax liability	62,461	-
VAT liability	116,193	-
Utilities and other fees	17,241	33,636
Contributions on salaries	19,307	21,034
Taxes and contributions on employee material rights	4,668	21,772
Other	3,440	3,760
	223,310	**80,202**

32. EMPLOYEE BENEFIT LIABILITIES

	31 Dec2018 in '000 HRK	31 Dec2017 in '000 HRK
Net salaries	76,308	80,331
Contributions from salaries	33,999	36,099
Severance payment – retirement benefit	3,982	123,487
Net salaries NE Krško	9,899	15,290
Other	17,369	18,966
	141,557	**274,173**

33. OTHER CURRENT LIAB ILITIES

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Liabilities for advances received for connections	478,849	432,357
Liabilities for other advance payments received	145,422	144,013
Accrued costs of unused annual vacations	69,608	60,995
Accrued income from electricity sales to households	6,250	-
Liability for accrued solidarity fee	14,765	15,064
Liability for renewable sources fees	135,053	128,859
Accrued severance pay to workers	33,403	179,820
Accrued interest expenses	-	-
Accrued costs for CO_2 emissions	263,125	120,148
Other accrued expenses	6,271	9,008
Current portion of financial lease (Note 26)	3,418	3,262
Liabilities NE Krško	35,292	23,822
Other liabilities	37,992	22,534
	1,229,448	**1,139,882**

Accrued income from the sale of electricity to households in the amount of HRK 6,250 thousand in 2018 (Note 33) and 31,099 thousand in 2017 (Note 22) is based on the calculation of correction income of households obtained by calculating the logarithmic curve. Correction of household income as at 31 December 2018 was obtained by calculating a logarithmic curve using 7.75% loss in network; while for the year ended 31 December 2017, the percentage of losses used in the calculation was 7.71%. In 2018, the result of the reduction of revenues was HRK 37,349 thousand compared to 2017, and a liability of HRK 6,250 thousand was reported. In 2017, the result was an increase in revenues of HRK 53,177 thousand compared to 2016, and a receivable amounting to HRK 31,099 thousand was reported.

According to the Air Protection Act (OG 130/2011, 47/2014, 61/2017, 118/2018) and the related by-laws in the field of greenhouse gas emissions; the Company has been classified as EU ETS payer and nine HEP plants are in the EU-ETS system since 1 January 2013.

The Group has obtained greenhouse gas emissions permits for all nine HEP plants in the EU-ETS and monitors plant emissions in accordance with approved monitoring plans and submits data on the amount of CO_2 emissions to all 9 accounts opened in the European Union Register no later than 31 March each year for the previous calendar year.

On the basis of verification of the amount of CO_2 emissions carried out by an independent accredited body, the Group is obliged to, no later than 30 April of the current year, submit the quantity of emission allowances to the EU Register in the amount corresponding to the total greenhouse gas emissions from the installation in the previous calendar year, in accordance with the verified report.

HEP's EU-ETS plants have submitted to the EU Registry the quantities of verified emissions for 2013, 2014, 2015 and 2016, 2017 and 2018.

33. OTHER CURRENT LIAB ILITIES (continued)

In accordance with the stated, costs of purchasing greenhouse gas emissions consist of the amount of CO_2 emitted (eq) and the unit price of the emission allowances that the Group calculates on the passive accruals (expense) and the expense of the period in the year in which the emissions of greenhouse gases emerged.

34. RELATED PARTY TRANSACTIONS

The Company has a 50% stake in the capital of NE Krsko. Although the investment in NE Krško is reported in the financial statements as common assets (joint operations) due to the fact that NE Krško is a separate legal entity here we present Transactions between NE Krško and the Company.

Electricity produced in NE Krško is delivered to HEP in the amount of 50% of the total quantity produced at a price determined by total production costs.

Receivables and liabilities and income and expenses with related parties are presented in the following table:

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
NE Krško		
Liabilities for purchased electricity	49,580	49,603
Costs of purchased electricity	577,283	585,443

Management remuneration is described in Note 7.

34. RELATED PARTY TRANSACTIONS (continued)

	Sales revenue		Purchase expense	
	2018 in '000 HRK	2017 in '000 HRK	2018 in '000 HRK	2017 in '000 HRK
State majority-owned companies				
Companies of Croatian Railways Group	111,473	97,956	54	439
INA-Industrija nafte d.d.	165,828	153,580	1,411,177	1,007,305
Prirodni Plin d.o.o.	-	-	-	-
Plinacro d.o.o.	593	2,104	146,150	156,944
Croatia osiguranje d.d.	6,265	2,591	7,078	8,754
Hrvatska pošta d.d.	22,751	6,728	38,564	34,537
Hrvatske šume d.o.o.	5,481	4,475	3,108	2,852
Jadrolinija d.o.o.	1,245	585	852	554
Narodne novine d.d.	2,234	2,450	4,174	3,748
Hrvatska radio televizija	12,839	11,650	1,566	1,594
Plovput d.d.	696	564	149	155
Croatia Airlines d.d.	776	781	-	4
Petrokemija Kutina d.d.	677,669	16,616	1,206	374
Ministry of Foreign Affairs	702	5	-	-
Ministry of Defence	20,280	21,284	-	-
Ministry of Interior	26,333	23,788	-	-
Primary and secondary schools	46,346	50,702	41	14
Judicial institutions	7,578	7,155	86	163
Universities and colleges	27,133	25,091	2,215	1,611
Legislative, executive and other State bodies	22,512	20,071	4,965	68,824
Health institutions and organisations	151,654	96,089	550	639
HROTE d.o.o.	272,747	389,600	971,638	763,968
Other users	9,470	6,089	5,634	7,053
TOTAL	**1,592,605**	**939,954**	**2,599,207**	**2,059,532**

34. RELATED PARTY TRANSACTIONS (continued)

	Amount of receivables		Amount of liabilities	
	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
State majority-owned companies				
Companies of Croatian Railways Group	28,242	25,911	37	245
INA-industrija nafte d.d.	15,185	16,053	170,712	45,264
Plinacro d.o.o.	669	861	19,580	20,078
Croatia osiguranje d.d.	538	213	1,693	1,944
Hrvatska pošta d.d.	3,794	3,446	8,568	6,930
Hrvatske šume d.o.o.	1,112	1,038	263	2
Jadrolinija d.o.o.	239	76	45	22
Narodne novine d.d.	406	529	797	897
Hrvatska radio televizija	2,109	2,514	12	50
Plovput d.d.	84	67	44	48
Croatia Airlines d.d.	111	98	-	-
Petrokemija Kutina d.d.	9,460	3,095	347	419
Ministry of Defence	3,602	3,522	-	-
Ministry of Interior	6,909	6,030	-	-
Primary and secondary schools	8,155	12,037	-	-
Judicial institutions	847	1,144	-	-
Universities and colleges	3,916	4,664	-	-
Legislative, executive and other State bodies	3,907	3,712	-	-
Health institutions and organisations	32,283	20,218	-	-
HROTE d.o.o.	14,026	281,259	77,541	116,278
Other users	3,854	17,998	4,139	6,587
TOTAL	**139,448**	**404,485**	**283,778**	**198,764**

35. UNFORSEEN EVENTS AND CONTINGENT LIABILITIES

Disputes

In 2018, the Group recorded provisions for legal disputes for which it was estimated were unlikely to be solved in favour of HEP d.d. and subsidiaries.

The Group has long-term investments in the territory of Bosnia and Herzegovina and Serbia in the amount of HRK 1,243,970 thousand. During the conversion of the Company to a stock company in 1994, this amount was excluded from the net asset value.

The Group 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.

Liabilities from operations

As a part of regular investment activities, the Group, on 31 December 2018, had concluded contracts according to which investments in various facilities and equipment were started, but not yet finished. The value of contracted unfinished works for the most significant projects was HRK 1,932,701 thousand (2017: HRK 944,834 thousand).

Environmental Protection

The Group continuously monitors and analyses the impact of its business processes on the environment. The most important indicators of such impacts are emissions of air pollutants and the amount of generated waste. The Group reports on the state of these indicators, timely and objectively, to relevant institutions, units of local self-government and the interested public. The Group reports on its environmental, economic and societal impact within the framework of the non-financial report on sustainability, prepared under the GRI-Global Reporting Initiative guidelines and, since 2017, under GRI Standard Guidelines and publishes them on its website http://www.hep.hr/o-hep-group/publications/report-on-sustainability/1,401. Employees in charge of environmental protection are additionally trained at seminars and workshops, where they are informed about the obligations and activities arising from the provisions of legal regulations in the field of nature protection and the environment.

The Group has a system for monitoring environmental expenditures (RETZOK), monitoring expenditures in nature and environment since 2004.

All HEP's thermal power plants with rated thermal inputs greater than 50 MW have obtained Environmental permits from the Ministry of Environmental Protection and Energy. By the decision of the Management Board of the Group, a greenhouse gas emission trading system was established in 2012, and the Republic of Croatia and HEP joined the European GHG Emission Trading Scheme (EU-ETS) on 1 January 2013. The Croatian Environment and Nature Agency (since 1 January 2019 merged to the Ministry of Environmental Protection and Energy), at the Group's request, opened nine accounts of plant operators in the EU register. The Group successfully fulfilled its obligation to hand over emission units to the EU Greenhouse Gas Register for 2017, and for 2018 data on verified CO_2 emissions were verified by verifiers, and emission units were submitted to all nine plant operator accounts in amounts that corresponded with verified CO_2 emissions.

35. UNFORSEEN EVENTS AND CONTINGENT LIABILITIES (continued)

Environmental Protection (continued)

In 2018, a non-financial sustainability report for 2017 was completed for the HEP Group under the Global Reporting Initiative Standard (GRI Standard) guidelines. The Sustainability Report is published on the Company's website and in a printed version in Croatian and English.

Report on the Status of the Nonfinancial Sustainability Report for the Group for 2018

The preparation of a separate non-financial statement on the Group's sustainability for 2018 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 balance sheet date, i.e. until 30 June 2019. The report will be published, as well as the previous four non-financial sustainability reports, on the following link http://www.hep.hr/o-hep-grupi/publikacije/izvjesca-o-odrzivosti/1401

In the preparation of these reports HEP Group uses the guidelines of the Global Reporting Initiative Standard (GRI Standard) and indicators in the above standard - general and standard indicators and sector supplement for the energy sector.

Course content of the sustainability report for 2018:

- Introduction by the president of the Management Board
- HEP approach to sustainability, includes goals, integrity and sustainability and how they are integrated in business policies, description of sustainability risk
- Materiality (description and impact assessment), sustainability framework according to UN development goals
- Stakeholders: analysis, inclusion, limitations
- Transparency of operations, including management approach, the principles of corporate governance, business ethics, professionalism and accountability in the work, transparency of communication and information (all according to the required GRI indicators). Responsibility in the working environment, data relating to employees (and prescribed by the GRI indicators), security and safety at work. The chapter also includes representative stories and case studies describing accountability and sustainability.
- Market access. HEP Group on the market. General approach. Business and responsibility, for each HEP Group company. Describes the most important trends related to market operations, supply chain, according to the requirements of the GRI indicator. The chapter also includes representative stories and case studies describing accountability and sustainability.
- Caring about the environment. Data on environmental protection, investments, projects and initiatives. Data are given by environmental protection areas (segments of activity). Data is indicated by GRI indicators. The chapter also includes representative stories and case studies describing accountability and sustainability.
- HEP in the community. It describes the various forms of community investment, cooperation with stakeholders, dialogue, information and education campaigns, initiatives aimed at cooperation and similar. The chapter also includes representative stories and case studies describing accountability and sustainability.
- Indicators

35. UNFORSEEN EVENTS AND CONTINGENT LIABILITIES (continued)

Report on the Status of the Nonfinancial Sustainability Report for the Group for 2018 (continued)

- HEP Proizvodnja d.o.o. has introduced and certified an integrated environmental, quality and energy management system in accordance with international standards ISO 14001:2015, ISO 9001:2015 and ISO 50001:2011 and, with its 35 components, it is among the largest environmental, quality and energy management systems in the Republic of Croatia. Efficient quality, environment and energy management is part of HEP-Proizvodnja d.o.o.'s business strategy in the production of electrical and thermal energy and in providing auxiliary services to the electro-energy system. Certification according to the new standards ISO 14001:2015 and ISO 9001:2015 and certification according to ISO 50001:2011 was carried out and confirmed by the certification company TÜV Croatia d.o.o. As one of the largest manufacturing companies in Croatia, and with regard to the activities covered by the number of employees, HEP-Proizvodnja d.o.o., aware of its environmental impacts, introduced the Environmental, Quality and Energy Management Policy that it has set for achieving maximum drive readiness and reliability of production capacities by implementing environmental protection measures and increasing the share of electricity generation and thermal energy in a regional market based on the principles of environmentally sound production, energy efficiency and sustainable business.
- By establishing and certifying quality management and environmental protection according to ISO 9001:2015 and ISO 14001:2015 HEP-Toplinarstvo d.o.o. has created the precondition for successful management of its processes, thus seeking to increase its competitiveness, position and reputation in the market.
- HEP ODS has established a certified health and safety management system in 2017, in accordance with the requirements of OHSAS 18001:2007, which continually achieves the defined health and safety management policy and set goals of the Company. Indicators of supervisory-transitional external auditors in 2018 confirmed that the applied environmental management system, certified for the first time in 2013, is in compliance with the requirements of ISO 14001:2015 and is continuously implementing the defined environmental management policy and the Company's set objectives. The fundamental commitment of the Energy Management Company is to achieve a lasting improvement of energy performance on all business facilities, equipment and devices, including the reduction of losses in the distribution network through the implemented energy management system according to ISO 50001:2011, which was also certified by an independent certification company TÜV Croatia Ltd.
- Customer Service of HEP-Supply d.o.o., through exceptional commitment and high level of service provided, was, as the first in Croatia, awarded the ISO 9001:2015 certificate for quality of service. In the second part of 2017, preparations for certification of the ISO 9001:2015 Customer Service were actively started. The process was successfully completed at the end of the planned period, and the Customer Service received ISO certification for a period of three years with mandatory recertification audits each year.
- In March 2017, implementation of an integrated management system in accordance with ISO / IEC 27001:2013, ISO 9001:2015, ISO 50001:2011, ISO 14001:2015 and BS OHSAS 18001:2007 started in HEP d.d. and HEP-Upravljanje imovinom d.o.o. In June 2017, there was a first series of lectures and workshops for team members participating in the implementation of these systems, which lasted until July 2018.

35. UNFORSEEN EVENTS AND CONTINGENT LIABILITIES (continued)

Water Act

Provisions of the Water Management Act that came into force on 1 January 2010, raised a question of ownership and legal status of the Company's property - reservoirs and ancillary facilities used for generation of electricity from hydropower plants, as they are defined as Public water resources in general use in ownership of the Republic of Croatia". The Group acquired the said property from their previous owners, merging an exceptionally large number of particles, which by the construction of the dam were flooded, resulting in accumulation. 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.

In May 2018, the Law on Amendments to the Water Act (OG 46/18) entered into force, by which the Republic of Croatia establishes the construction rights on public water resources - land on which water structures were built through Company's or its predecessors' investments; except for the land on which the accumulation was constructed and the supply and drainage channels and tunnels built. These rights are granted in favour of the Company, without compensation for a period of 99 years. As long as this right is resumed, the Company is granted the right to manage, on behalf of the Republic of Croatia, public good / land on which constructions of electricity generation with accumulation and supply and drainage channels and tunnels are built.

Supply to the wholesale gas market

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

In accordance with the Act on Amendments to the Gas Market Act, at its session held on 28 February 2017, the Government of the Republic of Croatia adopted a Decision on the price of gas at which the gas wholesale supplier is obliged to sell gas to gas supply providers in the public gas supply service for household customers; which determines the price at HRK 0.1809 / kWh. On 1 March 2018 HERA issued a Decision on the amount of tariff items for the public gas supply service for the period from 1 April to 31 July 2018 (OG, 23/18), according to which the gas price did not change in relation to the price valid until 31 March 2018. In accordance with the methodology for determining tariff items for the public service of gas supply and a guaranteed supply (OG 34/18), the selling price of gas for the period from 1 August 2018 to 31 March 2019 amounted to HRK 0.1809 / kWh.

The Gas Market Act (OG 18/18) stipulates the selection of suppliers in the wholesale market for the period from 1 August 2018 to 31 March 2021, after which the role of the supplier in the wholesale market will abolished. HERA carried out tenders for the selection of suppliers on the wholesale market for the period from 1 August 2018 to 31 March 2021 (on 15 May and 13 June 2018). As no proposals were received for these calls, in accordance with the provisions of the Act, on 27 June 2018 HERA, in consultation with the Ministry of Environmental Protection and Energy, appointed HEP d.d. as a wholesale supplier for a period of time shorter than the Act envisaged, i.e. from 1 August 2018 to 31 March 2019.

35. UNFORSEEN EVENTS AND CONTINGENT LIABILITIES (continued)

Supply to the wholesale gas market (continued)

As of 1 April 2017, the natural gas producer has no longer the obligation to deliver gas and the regulated price at which it was obliged to sell gas to the supplier on the wholesale gas market for the needs of customers using the public service supply is so longer valid.

Pursuant to the Act on Amendments to the Gas Market Act HEP d.d. as a wholesale market supplier, was awarded 60%, or 61 storage capacity packages in the underground gas storage facility.

In the period from 1 April 2014 to 31 March 2015 HEP d.d. as a wholesale market supplier, has leased a capacity of 3,600 million kWh; in the period from 1 April 2015 to 31 March 2016 3,550 million kWh; from 1 April 2016 to 31 March 2017 3,500 million kWh; while in the period from 1April 2017 to 31 March 2022, contracted capacity is 3,050 million kWh.

36. SUBSIDIARIES

At 31 December 2018 the Group owned the following subsidiaries:

Subsidiary	Country	Share (%)	Main activity
HEP-Proizvodnja d.o.o.	Croatia	100	Production of electricity and heating
Hrvatski operator prijenosnog sustava d.o.o.	Croatia	100	Transfer of electricity
HEP-Operator distribucijskog sustava d.o.o.	Croatia	100	Distribution of electricity
HEP ELEKTRA d.o.o.	Croatia	100	Supply of electricity
HEP-Opskrba d.o.o.	Croatia	100	Supply of electricity
HEP-Toplinarstvo d.o.o.	Croatia	100	Production and distribution of heating
HEP-Plin d.o.o.	Croatia	100	Gas distribution
HEP ESCO d.o.o.	Croatia	100	Financing energy efficiency projects
Plomin Holding d.o.o.	Croatia	100	Development of Ploming and surrounding infrastructure
CS Buško Blato d.o.o.	BiH	100	Hydro power plant equipment maintenance
HEP-Upravljanje imovinom d.o.o.	Croatia	100	Hospitality services
HEP NOC Velika	Croatia	100	Accommodation and education services
HEP-Trgovina d.o.o.	Croatia	100	Trading in electricity and optimising plant operations
HEP Energija d.o.o. Ljubljana	Slovenia	100	Trading in electricity
HEP Energija d.o.o.	BIH	100	Trading in electricity
HEP Energjia sh.p.k.	Kosovo	100	Trading in electricity
HEP Energija d.o.o.	Serbia	100	Trading in electricity
HEP-Telekomunikacije d.o.o.	Croatia	100	Telecommunications
HEP-VHS Zaprešić d.o.o.	Croatia	100	Design and construction of multi-purpose hydro technical system
Nuklearna elektrana Krško d.o.o.	Slovenia	50	Production of electricity
LNG Hrvatska d.o.o.	Croatia	50	Liquefied gas operations

Most of these subsidiaries were established under the reorganization and restructuring of core business under the new energy laws that entered into force on 1 January 2002 (Note 1).

Company HEP-Telekomunikacije d.o.o was founded in 2013. HEP-RVNP d.o.o. in 2014 changed its name to Sava d.o.o program, and on 31 December 2018 was merged to the Company. In 2014 HEP Opskrba plinom d.o.o. was founded and on 31 December 2018 merged to HEP-Trgovina d.o.o.

Liquidation process of the company Hrvatski centar za čistiju proizvodnju (The Croatian Cleaner Production Centre) started on 9 November 2017 and it was liquidated on 7 March 2019.

HEP-Magyarorszag Energia Kft. was removed from the court registry on 22 March 2018.

In 2018 Program Sava d.o.o. founded HEP-VHS Zaprešić d.o.o., and on 31 December 2018 HEP-VHS Zaprešić d.o.o. was sold to HEP-Proizvodnja d.o.o.

37. FINANCIAL RISK MANAGEMENT

Capital risk management

The Group manages its capital to ensure that it will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance.

The capital structure of the Group consists of debt, which includes loans and issued bonds disclosed in the Notes 25 and 26, cash and cash equivalents and equity attributable to owners of the parent, comprising of share capital, legal and other reserves and retained earnings.

Gearing ratio

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

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Debt	3,896,304	4,270,205
Cash and cash equivalents	(2,955,325)	(2,017,095)
Net debt	940,979	2,253,110
Equity	24,369,398	25,996,026
Net debt to equity ratio	**4%**	**9%**

Significant accounting policies

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

37. FINANCIAL RISK MANAGEMENT (continued)

Categories of financial instruments

	31 Dec 2018 in '000 HRK	31 Dec 2017 in '000 HRK
Financial assets		
Financial assets available-for-sale	-	283,578
Financial assets at fair value through other comprehensive income	197,307	-
Loans and borrowings (including cash and cash equivalents)	5,429,653	4,525,801
Other non-current assets	60,935	73,402
Financial liabilities		
Financial liabilities at fair value through statement of profit or loss	307,255	505,228
Non-current liabilities	4,581,178	4,641,233
Other current liabilities	2,179,059	2,078,873

Financial risk management objectives

The HEP Group'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 Group through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

Market risk

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

Foreign currency risk management

The Group undertakes certain transactions denominated in foreign currencies and thus the Group is exposed to foreign currency risk. Foreign currency risk exposure is managed within approved policy parameters utilizing cross currency swap contracts. The carrying amounts of the Group's foreign currency denominated monetary assets and liabilities at the reporting date are as follows:

	Assets		Liabilities	
	31 Dec 2018 in '000	31 Dec 2017 in '000	31 Dec 2018 in '000	31 Dec 2017 in '000
European Union (EUR)	167,563	252,468	542,978	678,756
USD	1,181	9,590	122,084	122,572

37. FINANCIAL RISK MANAGEMENT (continued)

Foreign currency sensitivity analysis

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

	2018 in '000 HRK	2017 in '000 HRK
EUR change effect		
Gain or loss	278,463	320,298
USD change effect		
Gain or loss	78,214	70,836

Interest rate risk management

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

Interest rate sensitivity analysis

An analysis of the effect of interest rate changes has been made for the financial instruments for which the Group is exposed to interest rate risk on the consolidated balance sheet date. For variable interest rates, the analysis was made on the assumption that the outstanding amount of the liability at the date of the consolidated balance sheet was unavailable for the entire year. The 50-base rate change is used for internal reporting to the Management and represents the Management's estimate of reasonably possible interest rate changes.

37. FINANCIAL RISK MANAGEMENT (continued)

Interest rate sensitivity analysis (continued)

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

- The Group's profit for the year ended 31 December 2018 would decrease by HRK 441 thousand (2017: HRK 1,918 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 3.18% of all interest-bearing loans (2017: 10.30%); and
- The Group's sensitivity to interest rates decreased during the current period due to the reduced share of borrowings contracted at variable interest rates in total debt and due to low reference interest rates on the market.

Credit risk management

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

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

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

Liquidity risk management

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

Liquidity and interest rate risk tables

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

37. FINANCIAL RISK MANAGEMENT (continued)

Maturity of non-derivative financial assets

	Weighted average effective interest rate	Less than 1 month in '000 HRK	1 - 3 months in '000 HRK	3 -12 months in '000 HRK	1 - 5 years in '000 HRK	Over 5 years in '000 HRK	Total in '000 HRK
31 Dec 2018							
Interest free		4,853,005	584,078	140,371	97,547	616	5,675,617
Floating interest							
Fixed interest	0.77%	-	-	-	41,887	-	41,887
Total		**4,853,005**	**584,078**	**140,371**	**139,434**	**616**	**5,717,504**
31 Dec 2017							
Interest free		4,069,586	514,463	123,992	111,298	-	4,819,339
Floating interest	0.72%	25,772	-	-	44,685	-	70,457
Fixed interest		-	-	-	-	-	-
Total		**4,095,358**	**514,463**	**123,992**	**155,983**	**-**	**4,889,796**

37. FINANCIAL RISK MANAGEMENT (continued)

Liquidity risk management

Maturity of non-derivative financial liabilities

The following table details the remaining contractual maturity of the Group for non-derivative financial liabilities. The table is made on the basis of undiscounted cash flows on the basis of the earliest date that the Group may be required to pay.

	Weighted average effective interest rate	Less than 1 month in '000 HRK	1 - 3 months in '000 HRK	3 -12 months in '000 HRK	1 - 5 years in '000 HRK	Over 5 years in '000 HRK	Total in '000 HRK
31 Dec 2018							
Interest free		1,338,102	657,107	112,528	1,099,341	-	3,207,078
Floating interest	1.02%	51	19,127	57,462	16,931	35,414	128,985
Fixed interest	4.63%	369	614	214,754	4,240,200	24,089	4,480,026
Total		**1,338,522**	**676,848**	**384,744**	**5,356,472**	**59,503**	**7,816,089**
31 Dec 2017							
Interest free		1,077,182	531,957	109,911	1,271,673	-	2,990,723
Floating interest	1.95%	68,432	28,762	278,727	77,506	-	453,427
Fixed interest	4.60%	311	622	217,356	4,511,748	36,756	4,766,793
Total		**1,145,925**	**561,341**	**605,994**	**5,860,927**	**36,756**	**8,210,943**

The Group has access to sources of financing. The total unused amount at the end of the reporting period was HRK 1,792,344 thousand. The Group expects to meet its other obligations from operating cash flows and proceeds from matured financial assets.

Fair value of financial instruments

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

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

37. FINANCIAL RISK MANAGEMENT (continued)

Fair value of financial instruments (continued)

- 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.

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 (i.e. their prices) or indirectly (i.e. derived from prices), and
3. Level 3 inputs – Indicators derived using valuation methods in which asset data or liabilities that are not based on available market data (unavailable input data) are used as input data.

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.

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

	Level 1 in '000 HRK	Level 2 in '000 HRK	Level 3 in '000 HRK	Total in '000 HRK
31 December 2018				
Financial assets at fair value through other comprehensive income	197,307	-	-	**197,307**
Derivative financial liabilities	-	-	307,255	**307,255**
Investment property	-	303,726	-	**303,726**
31 December 2017				
Financial assets available for sale	283,678	-	-	**283,678**
Derivative financial liabilities	-	-	505,228	**505,228**
Investment property	-	305,630	-	**305,630**

38. OTHER DISCLOSURES

The auditors of the Group's financial statements provided services in the amount of HRK 644 thousand in 2018 (in 2017: HRK 730 thousand). Services in 2018 and 2017 mainly relate to audit costs, review of condensed interim financial information and audits of financial reports prepared for regulatory purposes.

Fees for tax consultancy amounted to HRK 142 thousand in 2018 (2017: HRK 134 thousand).

39. APPROVAL OF THE CONSOLIDATED ANNUAL FINANCIAL STATEMENTS

These consolidated financial statements were approved by the Management Board and authorized for publication on 30 April 2019.

Signed for and on behalf of the Management Board on 30 April 2019:

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

NOTES

Name of the Group and the Company

Unless required otherwise by the context, the term 'HEP Group', 'HEP', or 'Group' means Hrvatska elektroprivreda d.d. together with its dependent companies. The term 'Company' means Hrvatska elektroprivreda d.d.

Timeframe of the Report

This Annual Report gives an overview of the business year 2018 – from January 1 to December 31, 2018. Data on the events important for HEP Group operations occurring after 31 December 2018 is also provided, but no later than June 4, 2019.

Financial reports of HEP Group

The 2018 non-consolidated financial statements of Hrvatska elektroprivreda d.d. with the independent auditor's report are available on:

http://www.hep.hr/UserDocsImages//dokumenti/fin-izvj/ne-konsolidirana/2018//HEP_DD_Revizorsko_2018.pdf

The 2018 financial reports of HEP Group Companies with the independent auditor's reports have been published on web pages of HEP Proizvodnja, HEP Operator distribucijskog sustava, HEP Elektra, HEP Opskrba, HEP Toplinarstvo and HEP Plin.

Overview of non-financial data

This Annual Report of HEP Group makes an integral whole with the non-financial report i.e. the HEP Group's 2018 Sustainability Report available on

http://www.hep.hr/o-hep-grupi/publikacije/izvjesca-o-odrzi-vosti/1401

Made in line with the Global Reporting Initiative guidelines, said Report contains operating aspects not presented in the Annual Report focused on the environment, the supply chain, human resources, customer and community relations, etc.

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