HRVATSKA ELEKTROPRIVREDA

# HRVATSKA ELEKTROPRIVREDA GROUP

Consolidated financial statements

As of 31 December 2012

Together with Independent Auditor's Report

# Contents

# Responsibility for the Consolidated Financial Statements

Management Board of the Company Hrvatska elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37 (hereinafter "the Company") is responsible for ensuring that the consolidated financial statements for the year 2012 are prepared in accordance with the Accounting Law (National gazette No 109/07) and the International Financial Reporting Standards (National gazette No 136/09, 8/10, 18/10, 27/10, 65/10, 120/10, 58/11, 140/11, 15/12, 118/12) issued by the Committee for Financial Reporting Standards, nominated by the Government of the Republic of Croatia, to give a true and fair view of the financial position, the results of operations, the changes in equity and the cash flows of the Group for that period.

After making enquiries, the Board has a reasonable expectation that the Group 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 financial statements of the Group.

In preparing those consolidated financial statements, the responsibilities of the Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- applicable financial reporting standards are followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- the consolidated financial statements are prepared on the going concern basis unless such assumption is not appropriate.

The Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position and the results of operations of the Group and their compliance with the Accounting Law (National gazette No 109/07) and the International Financial Reporting Standards (National gazette No 136/09, 8/10, 18/10, 27/10, 65/10, 120/10, 58/11, 140/11, 15/12, 118/12) issued by the Committee for Financial Reporting Standards. The Board is also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Management Board:

Zlatko Koračević
President of the Board

HEP d.d.
Ulica grada Vukovara 37
10000 Zagreb
Republic of Croatia

18 April 2013

## Independent Auditor's Report

### To the Owners of Hrvatska elektroprivreda d.d.:

1. We have audited the accompanying annual consolidated financial statements of the company HEP Group (hereinafter "the Group") for the year ended 31 December 2012, which comprise of the consolidated Balance sheet/consolidated Statement of Financial Position as of that date; the consolidated Statement of Income/consolidated Statement of Comprehensive Income; the consolidated Statement of Changes in Equity; the consolidated Cash Flows Statement for the year then ended; and the accompanying Notes to the consolidated Financial Statements which concisely set out the principal accounting policies and other disclosures.

The audit of the consolidated financial statements of the Group for the yer ended 31 December 2011 was performed by another auditor, who in its report dated 16 April 2012, expressed modified opinion. Matters affecting the opinion related to the advance payment to Hrvatske autoceste d.o.o. as described in the point 4 of this report.

### Responsibility of the Company's management

2. The preparation and a fair presentation of the enclosed consolidated Financial Statements according to the International Financial Reporting Standards effective in the Republic of Croatia and also those internal controls which are determined by the Company's management as necessary to enable preparation of the financial statements free from material misstatements whether due to fraud or error are the responsibility of the Company's management.

### Responsibility of Auditor

3. Our responsibility is to express an opinion on the enclosed consolidated Financial Statements based on the audit performed. Except as stated in the paragraph Matters affecting the opinion, the audit was performed in accordance with the International Auditing Standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the consolidated financial statements are free from material misstatements.

An audit includes performing of procedures to obtain audit evidence supporting the amounts and disclosures in the consolidated Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements in the consolidated Financial Statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the Company's preparation and fair presentation of the Financial Statements 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 entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Company's management, as well as evaluating the overall presentation of the Financial Statements.

We believe that auditing proof and evidence collected by us are sufficient and suitable as the basis for our opinion.

**Matters affecting the opinion**

4. As described in the note 13, the Group advanced HRK 300 million to Hrvatske autoceste d.o.o. in December 2006 for the purchase of electricity facilities on the Croatian motorways within two years from the date of the advance payment. As of the date of these consolidated financial statements, the legal title to these facilities has not yet been transferred to the Group. The Group is the economic beneficiary of the electricity facilities, which it uses for their intended economic purposes in the supply of electricity to customers. As of the date of preparation of the consolidated financial statements for 2012, the Group has not classified the advance payment by type of assets used in the Group's business, and we have received no calculation of the economic impact of the reclassification of those assets from prepayments to assets in use and the related depreciation from the Management Board. As a result, we are unable to assess the impact of this matter on the Group's financial statements for 2012.

**Modified opinion**

5. In our opinion, except for the potential effects of the matters disclosed in paragraph 4 above, the consolidated financial statements present fairly, in all material respects, the financial position of the HEP Group at 31 December 2012, the results of its operations and its cash flows for 2012 in accordance with the Accounting Act and International Financial Reporting Standards applicable in the Republic of Croatia.

**Emphasis of matter**

6. As described in the note 28, at 31 December 2012 the Group reported a liability in the amount of HRK 689,792 thousand in respect of a clearing debt regarding a payment under a letter of credit on the basis of the consent of the Ministry of Finance with the use of the funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the HEP Group and the Ministry of Finance regarding the clearing debt, up to the issuance of our report it has not been clearly defined as either a loan or a government grant.

7. Without qualification of our opinion we draw attention to the note 26, due to financially significant value of court dispute initiated against the Group, related to compensation in respect of rehabilitation of HE Peruća.

**Other legal and regulatory requirements**

8. The preparation of the annual consolidated Financial Statements of the HEP Group for the year ended 31 December 2012 in prescribed form on the basis of Regulation on the structure and content of the annual Financial Statements (National gazette No 38/08, 12/09, 130/10) (''Standard annual financial statements'') is responsibility of the Company's management. Financial information set out in standard annual consolidated Financial Statements of the Group are identical to information stated in the annual consolidated Financial Statements of the Group shown on pages 5 to 92 which are the subject of our opinion as set out in section Opinion with reserve, above.

In Zagreb, 18 April 2013

| | |
|---|---|
| BDO Croatia d.o.o.<br>Trg J. F. Kennedy 6b<br>10000 Zagreb | Audit d.o.o.<br>Baštijanova 52a<br>10000 Zagreb |
| Jeni Krstičević, auth. auditor<br>President of the Management | Zoran Vuk, auth. auditor,<br>Member of the Management |

## Consolidated Income Statement - HEP Group

For the year ended 31 December 2012

| | Notes | 2012 HRK'000 | 2011 HRK'000 Restated |
|---|---|---|---|
| Revenue from electricity sales | 4 | 11,630,275 | 10,769,900 |
| Revenue from thermal power sales | 4 | 585,485 | 582,352 |
| Revenue from gas sales | 4 | 395,956 | 381,177 |
| Other operating income | 4,5 | 1,407,862 | 1,354,570 |
| **Total operating income** | | **14,019,578** | **13,087,999** |
| Electricity purchase cost | | (3,793,038) | (3,259,984) |
| Fuel costs | | (3,319,512) | (2,917,739) |
| Staff cost | 6 | (1,863,235) | (1,890,228) |
| Depreciation and amortization expense | 10, 11 | (1,734,157) | (1,749,518) |
| Other operating expenses | 7 | (2,916,120) | (2,803,164) |
| **Total operating expenses** | | **(13,626,062)** | **(12,620,633)** |
| **Profit from operations** | | **393,516** | **467,366** |
| Financial revenue | 8 | 67,929 | 57,718 |
| Financial costs | 8 | (352,908) | (428,989) |
| **Net financial expense** | | **(284,979)** | **(371,271)** |
| **Profit before tax** | | **108,537** | **96,095** |
| Income tax expense | 9 | (37,335) | (88,281) |
| **Profit of the current year** | | **71,202** | **7,814** |
| **Attributable to:** | | | |
| Equity holder | | 62,495 | (3,700) |
| Non-controlling interest | | 8,707 | 11,514 |
| | | **71,202** | **7,814** |

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

Signed on behalf of the Company on 18 April 2013 by:

Zlatko Koračević — President of the Board

Ivan Matasić — Member of the Board

| | Notes | 2012 HRK'000 | 2011 HRK'000 Restated |
|---|---|---|---|
| **Profit for the current year** | | **71,202** | **7,814** |
| Foreign translation differences | | 164 | 1,071 |
| Fair valuation adjustment of Janaf shares | | 6,046 | (8,921) |
| **Other comprehensive income / (loss)** | | **6,210** | **(7,850)** |
| **Total comprehensive income / (loss) for the current year** | | **77,412** | **(36)** |
| **Total comprehensive income / (loss) attributable to:** | | | |
| Equity holder | | 68,540 | (12,621) |
| Non-controlling interest | | 8,872 | 12,585 |
| | | **77,412** | **(36)** |

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

Signed on behalf of the Company on 18 April 2013 by:

Zlatko Koračević — President of the Board

Ivan Matasić — Member of the Board

| ASSETS | Note | 31 December 2012 HRK'000 | 31 December 2011 HRK'000 Restated | 1. January 2011 HRK'000 Restated |
|---|---|---|---|---|
| **Non-current assets** | | | | |
| Property, plant and equipment | 10 | 24,409,429 | 24,390,612 | 24,090,370 |
| Capital work in progress | 10 | 3,915,002 | 3,092,220 | 3,046,316 |
| Intangible assets | 11 | 73,968 | 57,647 | 65,010 |
| Investment property | 12 | 233,917 | 234,760 | 223,094 |
| Prepayments for property, plant and equipment | 13 | 372,318 | 427,039 | 386,055 |
| Investment in NPP Krško | 14 | 1,754,419 | 1,754,419 | 1,754,419 |
| Long-term loan receivables and deposits | 16 | 514 | 719 | 1,183 |
| Assets held for sale and other investments | 17 | 129,452 | 120,915 | 162,380 |
| Other non-current assets | 18 | 67,219 | 107,152 | 110,973 |
| Deferred tax assets | 9 | 238,469 | 178,903 | 159,350 |
| | | **31,194,707** | **30,364,386** | **29,999,150** |
| **Current assets** | | | | |
| Inventories | 19 | 981,641 | 1,063,520 | 1,116,671 |
| Trade receivables | 20 | 1,873,245 | 1,496,236 | 1,730,328 |
| Other short-term receivables | 21 | 243,614 | 415,105 | 144,064 |
| Cash and cash equivalents | 22 | 605,024 | 407,123 | 762,157 |
| | | **3,703,524** | **3,381,984** | **3,753,220** |
| **TOTAL ASSETS** | | **34,898,231** | **33,746,370** | **33,752,370** |

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

Signed on behalf of the Company on 18 April 2013 by:

Zlatko Koračević — President of the Board

Ivan Matasić — Member of the Board

| CAPITAL AND LIABILITIES | Note | 31 December 2012 HRK'000 | 31 December 2011 HRK'000 Restated | 1. January 2011 HRK'000 Restated |
|---|---|---|---|---|
| Share capital | 23 | 19,792,159 | 19,792,159 | 19,792,159 |
| Capital reserves | 23 | 6,046 | (438,957) | (874,074) |
| (Accumulated loss)/ retained earnings | 23 | (356,648) | 5,851 | 947,198 |
| **Equity attributable to equity holder** | | **19,441,557** | **19,359,053** | **19,865,283** |
| Non-controlling interest | 15 | 47,283 | 62,847 | 76,993 |
| **Total equity** | | **19,488,840** | **19,421,900** | **19,942,276** |
| Long-term borrowings | 24 | 1,839,630 | 2,534,489 | 2,883,554 |
| Long-term liabilities to the state | 25 | 27,544 | 30,466 | 33,734 |
| Long-term provisions | 26 | 661,411 | 778,629 | 799,945 |
| Bonds issued | 27 | 3,335,608 | 965,202 | 1,058,042 |
| Other long-term liabilities | 28 | 4,911,633 | 5,143,989 | 5,008,204 |
| Deferred tax liability | | 1,511 | - | 1,874 |
| **Total non-current liabilities** | | **10,777,337** | **9,452,775** | **9,785,353** |
| Trade payables | | 2,492,498 | 2,427,184 | 1,553,211 |
| Current portion of long-term bonds issued | 27 | 593,380 | 93,380 | 93,380 |
| Current portion of long-term borrowings | 24 | 132,084 | 1,174,713 | 1,184,921 |
| Short-term borrowings | 29 | 410,843 | 603,163 | 292,493 |
| Taxes payable | 30 | 74,116 | 40,755 | 444,985 |
| Interest payable | | 45,574 | 23,191 | 30,489 |
| Liabilities to employees | 31 | 140,568 | 127,934 | 134,226 |
| Other short-term payables | 32 | 742,991 | 381,375 | 291,036 |
| **Total current liabilities** | | **4,632,054** | **4,871,695** | **4,024,741** |
| **TOTAL CAPITAL AND LIABILITIES** | | **34,898,231** | **33,746,370** | **33,752,370** |

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

Signed on behalf of the Company on 18 April 2013 by:

| | |
|---|---|
| Zlatko Koračević | Ivan Matasić |
| President of the Board | Member of the Board |

## Consolidated Statement of Changes in Equity - HEP Group

For the year ended 31 December 2012

| | Share capital | Capital reserves | Retained earnings/ (Accumulated losses) | Equity attributable to the equity holder of the parent | Non-controlling interest | Total equity |
|---|---|---|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| **Balance at 1 January 2011, before restatement** | **19,792,159** | **(874,074)** | **816,246** | **19,734,331** | **76,993** | **19,811,324** |
| Effect of 2009 and 2010 restatements (Note 3) | - | - | 130,952 | 130,952 | - | 130,952 |
| **Balance at 1 January 2011, restated** | **19,792,159** | **(874,074)** | **947,198** | **19,865,283** | **76,993** | **19,942,276** |
| Allocation of retained earnings | - | 444,038 | (444,038) | - | - | - |
| Dividends paid to owner | - | - | (493,376) | (493,376) | - | (493,376) |
| Losses carried forward – Trgovina M | - | - | (233) | (233) | - | (233) |
| Loss/profit for the current year | - | - | (3,700) | (3,700) | 11,514 | 7,814 |
| Translation differences | - | - | - | - | 1,071 | 1,071 |
| Janaf shares fair value | - | (8,921) | - | (8,921) | - | (8,921) |
| **Total comprehensive income of the current year** | **-** | **(8,921)** | **(3,700)** | **(12,621)** | **12,585** | **(36)** |
| Non-controlling interest | - | - | - | - | (14,063) | (14,063) |
| Distribution of dividend RWE | - | - | - | - | (12,668) | (12,668) |
| **Balance 31 December 2011** | **19,792,159** | **(438,957)** | **5,851** | **19,359,053** | **62,847** | **19,421,900** |
| Allocation of retained earnings | - | 438,957 | (438,957) | - | - | **-** |
| Surpluses and deficits of land | - | - | 7,559 | 7,559 | - | 7,559 |
| IFRIC 18 effect | - | - | 6,405 | 6,405 | - | 6,405 |
| Profit for the current year | - | - | 62,495 | 62,495 | 8,707 | 71,202 |
| Translation differences | - | - | (1) | (1) | 165 | 164 |
| Janaf shares fair value | - | 6,046 | - | 6,046 | - | 6,046 |
| **Total comprehensive income of the current year** | **-** | 6,046 | (1) | **6,045** | **165** | **6,210** |
| Non-controlling interest | - | - | - | - | (11,514) | (11,514) |
| Distribution of dividend RWE | - | - | - | - | (12,922) | (12,922) |
| **Balance 31 December 2012** | **19,792,159** | **6,046** | **(356,648)** | **19,441,557** | **47,283** | **19,488,840** |

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

Signed on behalf of the Company on 18 April 2013 by:

Zlatko Koračević — President of the Board

Ivan Matasić — Member of the Board

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 **Restated** |
| **Cash flows from operating activities** | | |
| Profit for the year | 71,202 | 7,814 |
| Income tax expense recognised in profit | 37,335 | 88,281 |
| Net financial expense | 284,979 | 371,271 |
| Gain from real estate fair valuation | 331 | (7,676) |
| Loss on fair value adjustment of derivatives | - | 1,080 |
| Depreciation and amortization | 1,734,157 | 1,749,518 |
| Increase in provisions for doubtful receivables | 250,972 | 364,544 |
| Increase in provision for inventories | 539 | 11,330 |
| (Decrease) in provisions | (117,218) | (21,316) |
| *Operating cash flows before movements in working capital* | *2,262,297* | *2,564,846* |
| Increase in trade receivables | (627,981) | (130,452) |
| Decrease in inventories | 81,340 | 41,821 |
| Decrease/(increase) in other current assets | 171,491 | (285,084) |
| Increase in trade payables | 65,314 | 877,038 |
| Increase in other liabilities | 322,931 | 142,918 |
| (Decrease)/Increase in long-term liabilities | (213,755) | 92,160 |
| **Cash generated from operations** | **2,061,637** | **3,303,247** |
| Income tax return / Income taxes paid | 33,983 | (600,873) |
| Interest paid | (306,517) | (236,874) |
| **NET CASH FROM OPERATING ACTIVITIES** | **1,789,103** | **2,465,500** |
| **INVESTING ACTIVITIES** | | |
| Interest received | 3,766 | 12,979 |
| Acquisition of property, plant and equipment | (2,598,254) | (2,132,612) |
| Write off property, plant and equipment | 16,138 | 44,311 |
| Surpluses of real estate | (8,889) | - |
| Decrease/(increase) of other assets | 87,166 | (49,467) |
| Change in the non-controlling interest and dividend payment to RWE | (24,436) | (26,732) |
| **NET CASH USED IN INVESTING ACTIVITIES** | **(2,524,509)** | **(2,151,521)** |

| | 2012 HRK'000 | 2011 HRK'000 |
|---|---|---|
| | | **Restated** |
| **FINANCING ACTIVITIES** | | |
| Bonds received | 2,955,595 | - |
| Repayments of bonds issued | (93,380) | (92,840) |
| Long-term loans raised | 505,905 | 793,839 |
| Repayment of long-term loans | (2,242,525) | (1,193,750) |
| Short-term loans raised | 1,081,682 | 997,924 |
| Repayment of short-term loans | (1,273,970) | (680,810) |
| Dividends paid to owner | - | (493,376) |
| **NET CASH USED IN FINANCING ACTIVITIES** | **933,307** | **(669,013)** |
| **NET INCREASE / (DECREASE) IN CASH AND CASH EQUIVALENTS** | **197,901** | **(355,034)** |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR** | **407,123** | **762,157** |
| **CASH AND CASH EQUIVALENTS AT THE END OF YEAR** | **605,024** | **407,123** |

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

Signed on behalf of the Company on 18 April 2013 by:

Zlatko Koračević

President of the Board

Ivan Matasić

Member of the Board

## 1. GENERAL

Hrvatska elektroprivreda Group (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 Note 35.

HEP d.d. is registered in Zagreb, Ulica grada Vukovara 37. The principal activities of the HEP Group are the generation, transmission and distribution of electricity, and the control of the electric power systems. In addition to these main activities, the HEP Group deals with the generation and distribution of thermal power through the district heating systems in Zagreb and Osijek, 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.

At 31 December 2012, the number of staff employed by the Group was 13,562 (31 December 2011: 13,762).

These financial statements are presented in Croatian Kuna (HRK) since that is the currency in which the majority of the Group's transactions are denominated.

**Energy laws**

On 3 December 2004, the Croatian Parliament ratified the amendments to the following laws: The Energy Law, the Law on Electricity Market and the Law on the Regulation of Energy Activities.
HEP d.d. and its subsidiaries continue to provide their services as regulated public services as follows:
electricity generation for tariff-based customers, electricity transmission, electricity distribution and electricity supply for tariff-based customers.

Generation and supply of electricity for eligible customers, (eligibility as described by the group of tariff laws) and trading on the energy market are performed as market activities.

The supply of electricity to eligible customers is performed according to rules governing market relations, which allow negotiating electricity quantities and prices on a free-market basis. Electricity for households and those preferential customers that have not exercised their right to select the electricity supplier or are left without a supplier is supplied as part of the system of obligatory public services.

**1. GENERAL (continued)**

**Energy Laws (continued)**

In June 2008, the Government of the Republic of Croatia promulgated a Decision on The Electricity Generation Tariff Model, with the exemption of eligible customers, with no tariff item amounts; The Electricity Transmission Tariff Model, with no tariff item amounts; The Electricity Distribution Tariff Model, with no tariff amounts; and the Electricity Supply Tariff Model, with the exemption of eligible customers, with no tariff amounts. The Group has been applying the tariff models since 1 July 2008 to 30 April 2012 when the Government of the Republic of Croatia brought the Decision by which are changed the stated tariff items and they are applied since 1 May 2012.

In December 2008, the Law on the Amendments to the Electricity Market Law became effective, under which small customers were obliged to choose their supplier and sign a contract with that chosen supplier by 30 June 2009, which is the date until which they are entitled to receive energy supplied by suppliers of tariff customers.

Small customers failing to select their electricity supplier until the given date will be charged for the supply of electricity based on the balancing electricity price charged to customers who have not selected their supplier either.

According to the new laws, HEP d.d. restructured its operations, by forming separate companies for electricity generation, transmission of electricity, distribution of electricity, electricity supply and electricity trading. HEP d.d. has restructured the Group in accordance with the amended laws.

In February 2013 was brought a new Law on electricity energy market by which is defined further restructurization of the HEP Group and the adjustment of operations with the procedures and directives of EU.

## 1. GENERAL (continued)

### Governance and management

***General assembly***

The General assembly consists of the members representing the interests of the HEP d.d.:

| | | |
|---|---|---|
| Ivan Vrdoljak | President | Member since 21 November 2012 |
| Radimir Čačić | President | Member since 26 January 2012 until 21 November 2012 |
| Đuro Popijač | President | Member since 21 November 2009 until 25 January 2012 |

*Supervisory Board*

*Members of Supervisory Board in 2012*

| | | |
|---|---|---|
| Nikola Bruketa | President | Member since 23 February 2012 |
| Alen Leverić | Member | Member since 23 February 2012 until 9 April 2013 |
| Ante Ramljak | Member | Member since 23 February 2012 |
| Hubert Bašić | Member | Member since 23 February 2012 until 7 May 2012 |
| Igor Džajić | Member | Member since 12 July 2012 |
| Žarko Primorac | Member | Member since 23 February 2012 |
| Ivo Uglešić | Member | Member since 23 February 2012 |
| Jadranko Berlengi | Member | Member since 3 June 2008 |

*Members of Supervisory Board in 2011*

| | | |
|---|---|---|
| Darko Horvat | President | Member since 30 June 2010 and President since 20 July 2010 until 22 February 2012 |
| Dražen Bošnjaković | Member | Member since 19 October 2009 until 22 February 2012 |
| Krešimir Dragić | Member | Member since 19 October 2009 until 22 February 2012 |
| Slavko Konfic | Member | Member since 28 April 2008 until 22 February 2012 |
| Gordana Obran | Member | Member since 19 October 2009 until 22 February 2012 |
| Zvonimir Sabati | Member | Member since 19 October 2009 until 22 February 2012 |
| Jadranko Berlengi | Member | Member since 3 June 2008 |

## 1. GENERAL (continued)

*Management Board in 2012*

| | | |
|---|---|---|
| Zlatko Koračević | President | Member since 23 February 2012 |
| Zvonko Ercegovac | Member | Member since 23 February 2012 |
| Krunoslava Grgić-Bolješić | Member | Member since 23 February 2012 |
| Rodoljub Lalić | Member | Member since 23 February 2012 |
| Ivan Matasić | Member | Member since 23 February 2012 |
| Tomislav Šerić | Member | Member since 23 February 2012 |

*Management Board in 2011*

| | | |
|---|---|---|
| Leo Begović | President | Member since 25 September until 22 February 2012 |
| Dubravko Lukačević | Member | Member since 2 November 2009 until 22 February 2012 |
| Snježana Pauk | Member | Member since 2 November 2009 until 22 February 2012 |
| Miljenko Pavlaković | Member | Member since 2 November 2009 until 22 February 2012 |
| Damir Pečvarac | Member | Member since 2 November 2009 until 22 February 2012 |
| Velimir Rajković | Member | Member since 2 November 2009 until 22 February 2012 |

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the Group's principal accounting policies which have been applied consistently in the current year and with the prior year, is set out below.

### *Presentation of the financial statements*

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as published by the International Accounting Standards Board.

The financial statements have been prepared on the historical cost basis, except for certain financial instruments that are presented at fair value. The financial statements are presented in thousands of Croatian Kuna (HRK'000), since that is the currency in which the majority of the Group's transactions are denominated.

### *Basis of accounting*

The Group maintains its accounting records in the Croatian language, in Croatian kuna and in accordance with Croatian law and the accounting principles and practices observed by enterprises in Croatia. The accounting records of the Group's subsidiaries in Croatia and abroad are maintained in accordance with the requirements of the respective local jurisdictions.

The Group's financial statements are prepared in thousands of Croatian kuna (HRK'000).

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

***Adoption of new and revised International Financial Reporting Standards***

*Standards and Interpretations effective in the current period*

The following amendments to the existing standards issued by the International Accounting Standards Board and interpretations issued by the International Financial Reporting Interpretations Committee are effective for the current period:

- **Changes and amendments to IFRS 1 "First - time adoption to IFRS"** – severe hyperinflation and removal of fixed dates for the first time adopters of IFRS (effective for annual periods beginning on or after 1 July 2011),

- **Changes and amendments to IFRS 7 „Financial instruments: disclosures"** – transfer of financial assets (effective for annual periods beginning on or after 1 July 2011)

- **Changes and amendments to IAS 12 „Income tax**" – deferred taxes:return of assets with deferred taxes (effective for annual periods beginning on or after 1 January 2012),

Approval of the stated changes and supplements of the existing standards, re-make and explanations has did not brought to changes in accounting policies of the Group.

*Standards and Interpretations in issue not yet adopted*

At the date of approval of these financial statements the following standards, revisions and interpretations were in issue but not yet effective:

- **IFRS 9 „Financial instruments"** (applies to annual periods beginning on or after 1 January 2015)

- **IFRS 10 „Consolidated financial statements"** published on May 2011 and amended in 2012, supersedes the previous version of IAS 27 (2008) "Consolidated and Separate Financial Statements", (effective for annual periods beginning on or after 1 January 2013)

- **IFRS 11 „Joint Arrangements"**, published on May 2011 and amended in 2012, superseded IAS 31 "Interests in Joint Ventures" (effective for annual periods beginning on or after 1 January 2013)

- **IFRS 12 „Disclosure of Interests in Other Entities "**, published on May 2011 and amended in 2012 (effective for annual periods beginning on or after 1 January 2013),

- **IFRS 13 „Fair Value Measurement"**, published on May 2011 (effective for annual periods beginning on or after 1 January 2013)

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

*Standards and Interpretations in issue not yet adopted (continued)*

- **IAS 27 "Separate Financial Statements"** (as amended in 2011), consolidation requirements previously forming part of IAS 27 (2008) have been revised and are now contained in IFRS 10 "Consolidated Financial Statements", (effective date of IAS 27 (as amended in 2011) for annual periods beginning on or after 1 January 2013),

- **IAS 28 "Investments in Associates and Joint Ventures" (as amended in 2011)** issued. This version supersedes IAS 28 (2003*)* "Investments in Associates" (effective date of IAS 28 (as amended in 2011) for annual periods beginning on or after 1 January 2013).

- **Amendments to IFRS 1 " First –time Adoption of IFRS"** – proclaimed in March 2012, which deal with the state loans count at interest rates lower than market during the traversing to IFRS (effective for annual periods beginning on or after 1 July 2013),

- **Amendments to IFRS 7 "Financial Instruments - Disclosures"** – proclaimed in December 2011, by which is prescribed the disclosure of extended information on the set-off of financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2013),

- **Amendments to IFRS 9 „Financial instruments – classification and measurement"** – proclaimed in December 2011, by which is prescribed the disclosure of data on the first application of IFRS 9 (effective for annual periods beginning on or after 1 January 2013),

- **Amendments to IAS 1 "Presentation of Financial Statements"** - Revising the way of presenting the other comprehensive income (effective for annual periods beginning on or after 1 July 2012).

- **Amendments to IAS 19 "Employee Benefits"** – finishing of the procedure for the count of employees' benefits after the cessation of job (applies to annual periods beginning on or after 1 January 2013)

- **Alterations and amendments of IAS 32 "Financial instruments - disclosures"** – published in December 2011, by which is prescribed the disclosure of expanded information on the set-off of financial property and financial liabilities (applies to annual periods beginning on or after 1 January 2014),

- **IFRIC 20 ''Stripping costs in the production phase of a surface mine"**(applies to annual periods beginning on or after 1 January 2013),

- **Alterations and amendments to various standards and interpretations under the name "Annual improvements in the period 2009 – 2011"** which were published in May 2012 and which relate to the disclosed alterations and amendments since 2009 till 2011 and primarily have influence to five standards (IFRS 1, IAS 1, IAS 16, IAS 32, IAS 34), with the consequent alterations and amendments and the supplements of various of other standards (applied to annual periods beginning on or after 1 January 2013),

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

*Standards and Interpretations in issue not yet adopted (continued)*

HEP Group has elected not to adopt these standards, revisions and interpretations in advance of their effective dates.

*In addition is stated the review of the main requests for issued but not yet adopted standards and interpretations.*

Requires of IFRS 9 recognised financial assets that are within the scope of IAS 39 ''Financial Instruments: Recognition and Measurement'' to be subsequently measured at amortised cost or fair value

IFRS 10 replaces the parts of IAS 27 ''Consolidated and Separate Financial Statements'' that deal with consolidated financial statements. Under IFRS 10, there is only one basis for consolidation that is control. New definition of control that contains three elements: a) power over an investee, b) exposure, or rights, to variable returns from its involvement with the investee, and c) the ability to use its power over the investee to affect the amount of the investor's returns.

IFRS 11 replaces IAS 31 ''Interests in Joint Ventures''. Under IFRS 11, joint arrangements are classified as joint operations or joint ventures, depending on the rights and obligations of the parties to the arrangements. In addition, joint ventures under IFRS 11 are required to be accounted for using the equity method of accounting, whereas jointly controlled entities under IAS 31 can be accounted for using the equity method of accounting or proportionate accounting.

IFRS 12 is a disclosure standard and is applicable to entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. In general, the disclosure requirements in IFRS 12 are more extensive than those in the current standards.

IFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. The Standard defines fair value, establishes a framework for measuring fair value, and requires disclosures about fair value measurements. The scope of IFRS 13 is broad; it applies to both financial instrument items and non-financial instrument items for which other IFRSs require or permit fair value measurements and disclosures about fair value measurements, except in specified circumstances.

The amendments to IAS 1 require additional disclosures to be made in the other comprehensive income section such that items of other comprehensive income are grouped into two categories: a) items that will not be reclassified subsequently to profit or loss; and b) items that will be reclassified subsequently to profit or loss when specific conditions are met.

The amendments to IAS 19 change the accounting for defined benefit plans and termination benefits. The most significant change relates to the accounting for changes in defined benefit obligations and plan assets.

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

*Standards and Interpretations in issue not yet adopted (continued)*

By modifications and amendments of IAS 32 are added the directions how to be solved the inconsistencies determined by the application of certain criterions for the set-off. This relates to interpretation of the meaning "momentarily has a legal executable right for the set-off" and that some systems of the gross set-off may be considered as an equivalent of the net set-off.

By modifications and amendments of IFRS 7 are added the requests for the proclaiming which will enable to the users of financial reports of the company to estimate the effect or the potential effect of the set-off of financial assets and the financial liabilities including the right for the set-off.

HEP Group has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The management anticipates that the adoption of IFRS 13 “Fair Value Measurement” will result in more extensive disclosures in the financial statements.

The management of the Group anticipates that the adoption of other standards (IFRS 10 “Consolidated Financial Statements”, IFRS 11 “Joint Arrangements” and IFRS 12 “Disclosure of Interests in Other Entities”), revisions and interpretations will have no material impact on the financial statements of Group in the period of initial application.

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

***The basis of the preparation of the Group's financial statement***

The financial statements of the Group represent aggregate amounts of the assets, liabilities, capital and reserves, and the results of its operations for the year then ended. All intragroup balances and transactions have been eliminated.

***Principles and methods of consolidation***

The consolidated financial statements incorporate the financial statements of HEP d.d. and entities controlled by HEP d.d. (it's subsidiaries). A listing of the Group's subsidiaries is provided in Note 35. Control is achieved where HEP d.d. has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

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

All intragroup transactions, balances, income and expenses are eliminated on consolidation.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling's share of changes in equity since the date of the combination. Losses applicable to the non-controlling in excess of the non-controlling interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the holders of the non-controlling interests have a binding obligation and are able to make an additional investment to cover the losses.

***Reporting currency***

Financial statements of Group are prepared in Croatian kuna (HRK '000).

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

***Investments in associates***

An associate is an entity over which the Group is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the investee.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting except when classified as held for sale in accordance with IFRS 5 ''Non-current Assets Held For Sale and Discontinued Operations''.

Investments in associates are carried in the consolidated statement of financial position at cost as adjusted by post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate) are not recognised, unless the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

Any excess of the cost of acquisition over the Group's share of the fair values of the identifiable net assets of the associate at the date of acquisition is recognised as goodwill. Goodwill is included in net book value of investments and is tested for impairment as part of investment. Any deficiency of the cost of acquisition below the Group's share of the fair values of the identifiable net assets of the associate at the date of acquisition is credited to profit and loss in the period of acquisition.

Where the Group transacts with its associate, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

***Investments in jointly controlled entities***

Jointly controlled entities are entities where Group and other parties are engaged in business activities under the joint control; i.e. when strategic financial and business decisions demands unanimous approval of all parties that participate in control.

Where a Group entity undertakes its activities under joint venture arrangements directly, the Group's share of jointly controlled assets and any liabilities incurred jointly with other ventures are recognised in the financial statements of the relevant entity and classified according to their nature. Liabilities and expenses incurred directly in respect of interests in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Company's share of the output of jointly controlled assets, and its share of joint venture expenses, are recognised when it is probable that the economic benefits associated with the transactions will flow to / from the Company and their amount can be measured reliably.

Joint venture arrangements that involve the establishment of a separate entity in which each venture has an interest are referred to as jointly controlled entities. The Group reports its interests in jointly controlled entities using full consolidation.

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

***Retirement and other employee benefit costs***

The Group has no defined post-retirement benefit plans for its employees or management in Croatia or abroad. Accordingly, no provision for these costs has been included.

Legal pension and health insurance contributions are paid on behalf of the Group's employees in the Republic of Croatia. This obligation applies to all staff hired on the basis of employment contract. The contributions are paid at a certain percentage determined on the basis of gross salary.

| | **2012** | **2011** |
|---|---|---|
| Pension insurance contributions | 20% | 20% |
| Health insurance contributions * | 13% | 15% |
| Employment Fund contribution | 1.7% | 1.7% |
| Occupational injury | 0.5% | 0.5% |

* the rate is applied since 1 May 2012

The Group companies have the obligation to withhold the pension insurance contributions from the employees' gross salaries.

Contributions on behalf of the employer and the employees are recognised as cost in the period in which they are incurred (see Note 6).

***Retirement benefits and jubilee awards***

The Group provides benefits to its employees, which include long-service benefits (jubilee awards) and one-off retirement payment. The obligation and the cost of these benefits are determined using the Projected Unit Credit Method. The Projected Unit Credit Method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The obligation is measured at the present value of estimated future cash flows using a discount rate that is similar to the interest rate on government bonds where the currency and terms of the Government bonds are consistent with the currency and estimated terms of the benefit obligation. Calculations of the obligation and cost of these benefits are performed by a certified actuary.

*Jubilee bonuses*

The Company provides long-service benefits (jubilee awards) and retirement benefits to its employees. The long-service benefits range from HRK 1,500.00 to HRK 5,500.00, net, and are provided for a discontinued tenure from 10 to 45 years of continuous employment with the employer.

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

***Retirement benefits and jubilee awards (continued)***

*Severance payments*

A new Collective Agreement was adopted as of 1 January 2011 (which covers all the HEP Group members), under which the employees are entitled to a retirement benefit to the extent of 1/8 of the average gross monthly salary earned in the period of three months prior to the retirement for each completed year of continuous employment at the employer. The effective date of the Collective is until 31 December 2012.

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

***Property, plant and equipment***

Property, plant and equipment are carried 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 recognised within income statement.

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

| **Buildings** | **2012 and 2011** |
|---|---|
| Hydroelectric power plants (Dams, embankments, buildings and other structures and facilities) | 20 – 50 years |
| Thermal power plants (Buildings and other structures) | 33 – 50 years |
| Electricity transmission and distribution plants and facilities (Transmission lines and buildings of transformer stations, switch-yard, dispatch centres and others) | 20 – 40 years |
| Water and steam pipelines and other thermal power generation and transmission plants and facilities | 33 years |
| Gas pipelines | 20 - 25 years |
| Administrative buildings | 50 years |
| **Plant and equipment** | |
| Hydroelectric power plants | 10 – 33 years |
| Thermal power plants | 6 – 25 years |
| Electricity transmission plants and facilities (electric parts of transformer stations and transformer; and electric parts of transmission lines) | 15 – 40 years |
| Electricity distribution plants and facilities (electric parts of transformer stations and transformers, electric parts of distribution lines, measuring instruments, meters and other equipment) | 8 – 40 years |
| Thermal power stations, hot-water pipelines and other equipment | 15 – 30 years |
| Gas meters and other gas network equipment | 5 – 20 years |
| **Other equipment and vehicles** | |
| IT equipment | 5 – 20 years |
| Software licenses | 5 years |
| Telecommunications equipment | 5 – 20 years |
| Motor vehicles | 5 – 8 years |
| Office furniture | 10 years |

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

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

The initial cost of property, plant and equipment contain the purchase price, including all customs duties and non-refundable taxes and all costs directly attributable to bringing an asset to the condition and location for its intended use. Expenditures incurred after the property, plant and equipment have been put into use are charged to expense the period in which they are incurred.

In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment beyond its originally assessed standard performance, the expenditures are capitalised 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 withdrawal of property, plant and equipment is determined as the difference between the proceeds gains on sale and the carrying amount of the asset and are credited or charged, respectively, to the income statement.

*Impairment of tangible and intangible assets*

Items of tangible and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is charged to the income statement.

At each reporting date, the Group reviews the carrying amounts of its tangible 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 the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

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

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

The net selling price is the amount obtainable from the sale of an asset in an arm's length transaction less the cost of disposal, while value in use is the present value using a pre-tax discount rate that reflects current market assessments of the time value of money, the risks specific to the asset of the estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. Recoverable amounts are estimated for individual assets or, if it is not possible, for the relevant cash-generating unit.

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 recognised immediately in profit or loss, unless the relevant asset is land or a building other than an investment property 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, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

***Intangible assets***

Intangible fixed assets include patents, trademarks and licenses and are carried at cost less accumulated amortisation. Amortisation is provided on a straight-line basis over a period from 5 to 20 years.

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

***Investment property***

Investment properties are properties held to earn rentals and/or for capital appreciation (including property under construction for such purposes). Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, 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 in the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use as well as when no future economic benefits are expected from the disposal. Any gain or loss arising on de-recognition of the property (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period in which the property is derecognised.

***Finance and operating leases***

*The Group as lessee*

The Group has no significant finance lease arrangements and no significant operating lease arrangements were entered during 2012 and 2011. Amounts payable under operating leases are recognised as expense on a straight-line basis over the term of the relevant lease, unless there is another systematic basis that would be more representative of the time pattern of the user's benefit.

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

***Trade debtors and prepayments***

Trade receivables are carried at invoiced amount less any impairment for doubtful accounts.

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

As the collectability of certain receivables over a longer period is not certain, the Group makes an assessment of allowance for unrecoverable amounts, based on a reasonable estimate and past experience, in order to write down or write off those amounts as follows:

| | **2012 and 2011** |
|---|---:|
| Ageing of past due | Allowance percentage |
| 31-60 days | 1.5% |
| 61-90 days | 3% |
| 91-180 days | 9% |
| 181-365 days | 30% |
| Over one year | 90% |

Outstanding receivables claimed through the courts and those included in bankruptcy estate (the debt principal and interest) are fully provided, regardless of the number of past due days, and the provision is charged to expenses.

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

**Inventories**

Inventories comprise mainly of materials and small items and are carried at the lower of cost, determined using the weighted average price less allowance for obsolete and excessive inventories, and net realisable value. The management provides for inventories based on a review of the overall ageing structure of inventories and non-recurring transfers over the years, as well as of individual significant amounts of inventories.

Cost comprises the invoiced amount as well as all other costs directly attributable to brining inventories to their location and the condition of being readily available for use.

***Cash and cash equivalents***

Cash and cash equivalents comprise cash on hand and demand deposits with banks and other short-term highly 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 recognised in the statement of income in the period in which they are incurred. Short-term borrowings and supplier loans are recorded at original amount granted less repayment. Interest expense is charged to income statement on an accrual basis.

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

***Foreign currencies***

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group entity are expressed in Croatian kunas (HRK), which are the functional currency of the Group and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual Group entities, transactions in currencies other than the entity's functional currency (foreign currencies) are translated to the functional currency of the entity at the rates of exchange prevailing on the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated to the functional currency of the entity at the year-end rates. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in profit or loss for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period as finance cost except for differences arising on the retranslation of non-monetary assets available for sale, in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are expressed in Croatian kuna using exchange rates prevailing at the date of the statement of financial position. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising on the year-end translation, if any, are classified as equity and recognised in the Group's foreign currency translation reserve. Such exchange differences are recognised in profit or loss in the period in which the foreign operation is disposed of.

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

***Taxation***

The tax expense represents the sum of the tax currently payable and deferred tax.

*Current tax*

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes 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 liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of reporting period.

*Deferred tax*

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised on the basis of taxable temporary differences on investments in subsidiaries and associates and joint ventures, unless the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the 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 is settled or the asset realised, based on tax rates (and 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 amount in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

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

### *Taxation (continued)*

*Current and deferred tax for the period*

Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items credited or debited directly to equity, in which case the tax is also recognised directly in equity, or where they arise from the initial accounting for a business combination.

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

### *Financial assets*

Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into as "assets available for sale" and "loans and receivables". The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

*Effective interest method*

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

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

*Financial assets available for sale*

Unlisted shares held by the Group that are traded in an active market are classified as being AFS and are stated at fair value. Gains and losses arising from changes in fair value are recognised directly in equity in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is included in profit or loss for the period.

Dividends on AFS equity instruments are recognised in profit or loss when the Group's right to receive the dividends has been established.

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

***Financial assets (continued)***

The fair value of AFS financial assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of reporting period. The change in fair value attributable to translation differences that result from a change in amortised cost of the asset is recognised in profit or loss, and other changes are recognised in equity.

*Loans and receivables*

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

*Impairment of financial assets*

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

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

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised directly in equity.

*Investments*

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

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

***Financial liabilities***

Other financial liabilities (including borrowings) are subsequently measured at amortised cost using the effective interest method.

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

*Derecognition of financial liabilities*

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

***Derivative financial instruments***

The Group entered into an interest rate swap to manage its exposure to interest rate. Further details of derivative financial instruments are disclosed in Note 27.

Derivatives are initially recognised at fair value at the date the derivative contracts are entered into and are subsequently remeasured to their fair value at the end of each reporting period. The resulting gain or loss is recognised in profit or loss.

***Provisions***

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

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

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

The preparation of financial statements in conformity with International Reporting Financial Standards, as published by the International Accounting Standards Board requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies. The significant areas of estimation used in the preparation of the accompanying financial statements relate to employee benefits, useful lives of property, plant and equipment, impairment of assets and determination of fair values of assets and liabilities, and estimated decommissioning costs. Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effect of any changes in estimates will be recorded in the financial statements, when determinable.

***Revenue recognition***

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

Revenue from the sale of electricity is recognised according to the best management estimate of the actual energy consumed based on the energy data and tariff items under the cost-recovery models called Electricity Transmission Tariff Model With No Tariff Amounts, The Electricity Distribution Tariff Model, with no tariff amounts; and the Electricity Supply Tariff Model, with the exemption of eligible customers, with no tariff amounts. Revenue recognition is based on the Decision of the Croatian Government on the level of tariff items from June 2008 and April 2012 (see Note 1).

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

### Revenue from connection fees

As of 1 July 2009 Group has adopted IFRIC 18 ''Transfers of Assets from Customers''.

IFRIC 18 clarifies the requirements of IFRSs for agreements in which an entity receives from a customer asset (item or property, plant and equipment or cash) that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services. When the item of property, plant and equipment transferred from a customer meets the definition of an asset the Company must recognize the asset in its financial statements.

Since 1 July 2009 the connection fees received from customers have been recognized in the income when the fee is received in a moment when customer is connected to grid or in a moment when it has continuous asses to services.

### Segmental disclosures

The Group has fully adopted IFRS 8 ''Operating Segments'' and presented operating segment disclosures required by the Standard, since it has debt instruments, which are traded in public market.

## 3. CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES

***Critical judgments in applying accounting policies***

In the application of the accounting policies, which are described in Note 2, the management made certain judgments that had a significant impact on the amounts reported in the financial statements (irrespective of the underlying estimates referred to below).

These judgments are provided in detail in the accompanying notes. However, the critical judgments relate to the following areas:

*Useful lives of property, plant and equipment*

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

*Fair value of financial assets and interest-rate swap*

As described in Note 20, the management uses judgment to estimate whether trade and other receivables have suffered an impairment loss. The management believes that the carrying amount of the interest-rate swap approximates its fair value as disclosed in Note 27.

*Provisions for environmental protection*

The exact scope of activities or technologies to be applied has not been specified by the applicable laws or regulations. In determining the level of provisions for environmental protection and decommissioning, the management relies on the prior experience and its own interpretation of the current laws and regulations. Pursuant to Article 4.1 of the Law on Acknowledging the Contract between the Government of the Republic of Croatia and the Government of the Republic of Slovenia on Regulating the Status and other Legal Relations in Respect of Investments in, Exploitation and Decommissioning of, the Nuclear Power Plant Krško (Official Gazette No. 9/2002), the Croatian Government issued on 28 April 2006 a decree on the payment of the funds for the decommissioning and disposal of radioactive waste and consumed nuclear fuel of the NPPK.

The decommissioning costs of thermal power plants represent the discounted value of the estimated decommissioning costs of the Group's thermal power plants.

*Over / under billed revenue adjustment*

After analyzing a number of different methods of approximation (five-year average, a linear approximation, etc.), the Management has decided that the most appropriate is a method of logarithmic regression is the most appropriate. The amount of losses on the network distribution is calculated using the percentage of the function of the logarithmic regression on the total amount of purchased power from the transmission network - the result of the losses of electricity distribution network in the current year in MWh.

The difference between the thus obtained size of losses and over/under billed revenue balance for the current year is calculated.

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

***Critical judgments in applying accounting policies (continued)***

*Over / under billed revenue adjustment (continued)*

Such difference represents basis for calculation of over / under billed revenue and is multiplied by the average selling prices for households earned in the current year from those without a fixed monthly fee and the result is the difference that increases or decreases the revenues from selling electricity to households.

*Impairment of non-current assets*

The impairment calculation requires the estimate of the value in use of the cash generating units. Value in use is measured using the discounted cash flow projections. The most significant variables in determining cash flows are discount rates, time values, the period of cash flow projections, as well as assumptions and judgments used in determining cash receipts and expenditure. There were no impairments of assets of the Group that would result from the projections described above.

*Availability of taxable profits against which the deferred tax assets could be recognised*

A deferred tax asset is recognized only to the extent that it is probable that the related tax benefit will be realized. In determining the amount of deferred taxes that can be recognised are required, which are based on the probable quantification of time and level of future taxable profits, together with the future tax planning strategy. The carrying amounts of deferred tax assets at 31 December 2012 amounted to HRK 238,469 thousand and 31 December 2011 amounted to HRK 178,902 thousand (see Note 9).

*Actuarial estimates used in determining the retirement bonuses*

The cost of defined benefits is determined using actuarial estimates. Actuarial estimates involve assumptions about discount rates, future salary increases and the mortality or fluctuation rates. Because of the long-term nature of those plans, there is uncertainty surrounding those estimates. Provisions for jubilee awards and retirement bonuses amounted to HRK 331,147 thousand at 31 December 2012 and HRK 357,632 thousand at 31 December 2011 (see Note 26).

*Consequences of certain legal actions*

There are a number of legal actions involving the Group, which have arisen from the regular course of their operations. If there is a present obligation as a result of a past event (taking into account all available evidence, including the opinion of law experts) for which is probable that outflow of resources will be required to settle the obligation and if a reliable estimate can be made of the amount of the obligation, provisions are recorded (see Note 26).

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

***Critical judgments in applying accounting policies (continued)***

*Re-measurement of the Janaf shares and investment property at fair value*

During 2012 and 2011, the Group remeasured the Jadranski naftovod shares and the investment properties at fair value.

In 2012 and 2011 fair value was determined based on a notification of Central clearing deposit company regarding open balances as of 31 December 2012 and 2011. The market value of the Jadranski naftovod share as at 31 December 2012 was HRK 2,370 (2011: HRK 2,230).

The loss resulting from the fair valuation of the investment property in 2012 amounts to HRK 331 thousand, while a gain of HRK 7,676 thousand was recognised on the fair valuation in 2011 (see Note 5).

*Valuation of inventories*

During 2012, based on an estimation, the Group made value adjustments for obsolete inventories and materials (material with no turnover in the previous 2 years) according to the ageing structure in the total amount of HRK 539 thousand (2011: HRK 11,330 thousand) (Note 19).

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

**IFRIC 18 *Value restatement***

The international financial reporting interpretation committee (IFRIC) has brought in January 2009 the Interpretation 18 – Transfer of property from the buyers (IFRIC 18), with the obligatory implementation since 1 July 2009.

In the Republic of Croatia the stated interpretation has come into force at 1 January 2010 on the basis of the Decision of the Committee for financial reporting standards dated 11 January 2010 (National Gazette 18/2010).

Following to the stated, the Management Board of HEP d.d. brought a Decision on change of the accounting policy by which the Interpretation of the Committee for international financial reporting interpretation No 18 "Transfer of property from the buyers" is applied since 1 January 2010. In 2012 the Management Board has brought a decision on application of IFRIC 18 since 1 July 2009 and for distinguishing in the relation for the later application of IFRIC 18 the data are restated in the financial statements and for the amount of HRK 176,687 thousand are decreased other long term liabilities at 31 December 2011 and 1 January 2011.

The effect of adjustments for the period since 1 July 2009 till 31 December 2009 is the increase of other revenues, respectively the profit and retained profit and the decrease of other long term liabilities as is stated:

The effects of the restatement are as follows:

| **Effect on balance** | **31 December 2011** | **1 January 2011** |
|---|---|---|
| | HRK'000 | HRK'000 |
| Other long term liabilities before restatement | 5,320,676 | 5,170,943 |
| Restatement effect | (176,687) | (162,739) |
| Other long term liabilities, restated | **5,143,989** | **5,008,204** |
| | | |
| Other short term liabilities before restatement | 346,801 | 259,328 |
| Restatement effect | 34,615 | 31,708 |
| Other | (41) | - |
| Other short term liabilities, restated | **381,375** | **291,036** |
| | | |
| Retained profit before restatement | (136,262) | 816,246 |
| Restatement effect | 142,072 | 130,952 |
| Other | 41 | - |
| Retained profit, restated | **5,851** | **947,198** |

| **Effect on other comprehensive income** | **31 December 2011** |
|---|---|
| | HRK'000 |
| Other income from operations before restatement | 1,340,622 |
| Increase of other business income | 13,948 |
| Other business income, restated | **1,354,570** |
| | |
| Income tax before restatement | (85,453) |
| Restatement effect | (2,828) |
| Income tax, restated | **(88,281)** |
| | |
| Loss of the current year before restatement | (3,306) |
| Restatement effect | 11,120 |
| Profit, restated | **7,814** |

## 4. SEGMENT INFORMATION

The Group generates income from its operations in a single geographical area – the Republic of Croatia.

The Group's reportable segments are separated as follows: electricity (generation, transmission, distribution and sale of electricity), heating (distribution and sale of heating power), and gas (distribution and sale of gas). Each segment's operating profit or loss includes all revenue and expenses directly attributable to the reporting business segments. Information about segment financial income, expense and income tax is not provided on a segment level, as the segments are disclosed based on operating profit.

| | **Electricity** | | **Heating** | | **Gas** | | **Group** | |
|---|---|---|---|---|---|---|---|---|
| | **2012** | **2011** | **2012** | **2011** | **2012** | **2011** | **2012** | **2011.** |
| | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| Revenue | 11,630,275 | 10,769,900 | 585,485 | 582,352 | 395,956 | 381,177 | 12,611,716 | 11,733,429 |
| Other income allocated to segments | 1,321,220 | 1,255,792 | 60,607 | 68,667 | 26,035 | 30,111 | 1,407,862 | 1,354,570 |
| **Income from operations** | **824,062** | **757,148** | **(434,042)** | **(293,291)** | **3,496** | **3,509** | **393,516** | **467,366** |
| Net financial expense | | | | | | | (284,979) | (371,271) |
| Income tax | | | | | | | (37,335) | (88,281) |
| **Net profit** | | | | | | | **71,202** | **7,814** |

Segment assets consist primarily of property, plant and equipment, receivables, cash and inventories. Segment liabilities consist of trade and other payables. Non-segment assets and liabilities consist of assets and liabilities that cannot be reasonably attributed to the reporting business segments.

Total unallocated assets include investments in NPPK, a part of property, plant and equipment, and unallocated financial assets. Total unallocated liabilities include long-term loans, short-term loans and various other liabilities.

| | **Total segment assets** | | **Total segment liabilities** | |
|---|---|---|---|---|
| | **2012.** | **2011.** | **2012.** | **2011.** |
| | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | | **Restated** |
| Electricity | 29,769,194 | 28,910,912 | 7,154,363 | 7,098,415 |
| Heating | 1,215,719 | 1,138,791 | 222,638 | 241,566 |
| Gas | 350,638 | 322,338 | 176,210 | 169,170 |
| Unallocated | 3,562,680 | 3,374,329 | 7,856,180 | 6,815,319 |
| Total Group | **34,898,231** | **33,746,370** | **15,409,391** | **14,324,470** |

## 4. SEGMENT INFORMATION (continued)

### Information on the largest customers

In 2012 electricity sales amount to HRK 11,630,275 thousand (HRK 10,769,900 thousand in 2011).
Heating energy sales for the year 2012 amount to HRK 585,485 thousand (HRK 582,352 thousand in 2011).

In 2012 gas sales amount to HRK 395,956 thousand (HRK 381,177 thousand in 2011).

### Territorial business analysis

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

Presented below is the territorial analysis of the revenue that the Group generated from continuing operations with external buyers of electric energy:

| | **2012** | **2011** |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Croatia | 11,197,595 | 10,582,154 |
| European Union member states | 92,566 | 27,463 |
| Other countries –non-European Union member states | 340,114 | 160,283 |
| | **11,630,275** | **10,769,900** |

**5. OTHER OPERATING INCOME**

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Service for connection to network | 365,869 | 263,891 |
| Income from assets received free of charge | 233,362 | 231,908 |
| Subsequent collection of receivables previously provided against (Note 20) | 119,555 | 139,266 |
| Services rendered | 155,657 | 118,859 |
| Capitalised assets | 99,693 | 109,502 |
| Late-payment interest | 77,418 | 93,220 |
| Reversal of long-term provisions – vacation | 432 | 64,477 |
| Income from sale of materials | 61,968 | 52,070 |
| Income from sale of cross – border transmission capacity | 43,047 | 49,997 |
| Income from electricity in transit – foreign | 3,497 | 33,877 |
| Reversal of long-term provisions for retirement benefits and jubilee awards | 28,935 | 26,514 |
| Reversal of long-term provisions – court costs | 87,407 | 23,088 |
| Income from reversal of other provisions | 49,634 | - |
| Income in respect of the electricity bill reminders | 13,392 | 21,702 |
| Income from balancing energy | 8,537 | 14,479 |
| Income in respect of court costs on claims | 6,996 | 8,831 |
| Income upon count of fee for $SO_2$ from previous year | 4,427 | 8,008 |
| Income upon count of fee for $CO_2$ from previous year | 3,477 | 12,162 |
| Fair valuation of investment into property | (331) | 7,676 |
| Inventory surplus – fixed assets | 77 | 5,648 |
| Income from sale of tangible assets | 2,362 | 4,835 |
| Recovery of receivables previously written off | 2,155 | 4,286 |
| Other | 40,296 | 60,274 |
| | **1,407,862** | **1,354,570** |

In 2012 the Group generated income from grid connection services in the amount of HRK 365,869 thousand (2011: HRK 263,891 thousand) based on IFRIC 18 (Transfer of Assets From Customers).

## 6. STAFF COSTS

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Net salaries | 1,122,716 | 1,135,278 |
| Taxes and contributions | 740,519 | 754,950 |
| | **1,863,235** | **1,890,228** |

**Total staff costs:**

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Gross salaries | 1,863,235 | 1,890,228 |
| Reimbursement of costs to employees (Note 7) | 146.309 | 143,885 |
| Employee benefits (Note 7) | 83,691 | 108,285 |
| | **2,093,235** | **2,142,398** |

**Directors' and executives remuneration:**

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Gross salaries | 21,531 | 19,104 |
| Pension contributions | 4,821 | 4,305 |
| Other receipts | 3,022 | 2,185 |
| | **29,374** | **25,594** |

Reimbursement of costs to employees includes transportation allowances in the amount of HRK 87,751 thousand (2011: HRK 83,925 thousand), daily allowances and travelling expenses in the amount of HRK 16,620 thousand (2011: HRK 17,636 thousand), additional health insurance amounting to HRK 15,498 thousand (2011: HRK 15,530 thousand), and other similar expenses in the amount of HRK 26,440 thousand (2011: HRK 26,794 thousand).

Employee benefit costs include benefits under the Collective Agreement and consist primarily of Christmas and Easter allowances, solidarity support, jubilee awards, family separation allowances and fieldwork bonuses, holiday bonuses, child benefits and other.

## 7. OTHER OPERATING EXPENSES

| | 2012<br>HRK'000 | 2011<br>HRK'000<br>Restated |
|---|---|---|
| Maintenance costs (service and material) | 580,204 | 669,345 |
| Provisions for doubtful receivables (Note 20) | 250,972 | 364,544 |
| Gas costs | 361,070 | 352,066 |
| General and administrative expenses | 331,541 | 251,549 |
| Collective services and material | 165,386 | 118,896 |
| Refund of costs to employees (Note 6) | 146,309 | 143,885 |
| Cost of material | 87,508 | 93,871 |
| Other material employee's rights (Note 6) | 83,691 | 108,285 |
| NPPK – decommissioning expense | 106,835 | 106,005 |
| Contributions to the State | 87,396 | 96,524 |
| Litigation provisions | 40,079 | 78,265 |
| Distributions and concession for water | 64,961 | 68,789 |
| Accrual for unused vacation days | 1,359 | 63,900 |
| Fee for the usage of power plant facilities | 37,401 | 48,539 |
| Write-off of tangible assets | 14,328 | 47,854 |
| Purchase value of sold materials | 50,045 | 45,464 |
| Calculation and collection costs | 39,743 | 39,859 |
| Provisions for retirement bonuses and jubilee awards | 2,450 | 35,721 |
| Provisions for severance pays on the basis of working contract cancellation | 249,174 | - |
| Provisions for other costs to workers | 28,087 | - |
| Refund for the less taken over quantities than stipulated | 20,296 | - |
| Insurance premiums | 24,418 | 24,607 |
| Fee for environmental protection | 18,210 | 21,217 |
| Damages and indemnities | 49,632 | 16,027 |
| Provision for investment in HE Lešće | - | (39,286) |
| Provision for NPPK additional decommissioning costs | - | (53,838) |
| Other | 75,025 | 101,076 |
| | **2,916,120** | **2,803,164** |

## 8. FINANCIAL REVENUE AND COSTS

| | 2012 | 2011 |
|---|---|---|
| **Financial income** | HRK'000 | HRK'000 |
| | | **Restated** |
| Foreign exchange gains | 64,147 | 41,515 |
| Interest expense | 3,766 | 12,979 |
| Income from dividends | 16 | 3,224 |
| Total financial income | **67,929** | **57,718** |
| **Finance costs** | | |
| Interest expense | (319,868) | (242,560) |
| Foreign exchange losses | (46,303) | (160,266) |
| Amortization of deferred interest | (3,770) | (3,740) |
| Fair value of interest rate swap | - | (1,080) |
| Fair valuation adjustment of shares | (88) | (30,769) |
| Financial expenses | **(370,029)** | **(438,415)** |
| Capitalised borrowing cost allocated to PPE | 17,121 | 9,426 |
| Total financial expenses | **(352,908)** | **(428,989)** |
| **Net finance expense** | **(284,979)** | **(371,271)** |

## 9. INCOME TAX

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Current taxes | 96,901 | 107,754 |
| Deferred tax income relating to the origination and reversal of temporary differences | (59,566) | (19,473) |
| **Income tax** | **37,335** | **88,281** |

Adjustments to deferred tax assets were as follows:

| | 2012. | 2011. |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | **Restated** |
| Balance at 1 January | 178,902 | 159,430 |
| Reversal of deferred tax assets | (26,971) | (29,869) |
| Deferred tax assets recognised | 86,538 | 49,342 |
| Balance at 31 December | **238,469** | **178,903** |

**9. INCOME TAX (continued)**

Deferred tax assets have arisen on the tax not recognized, provisions for jubilee awards and regular severance pays, value provisions which are not taxable recognized and other provisions.

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

| | 2012 | 2011 |
|---|---|---|
| | HRK'000 | HRK'000 |
| | | Restated |
| Profit before taxation | 108,537 | 96,095 |
| **Income tax at the applicable rate of 20%** | **21,707** | **19,219** |
| Non-taxable income and realisation of deferred tax asset previously | (37,878) | (4,060) |
| Tax effect of permanent differences | (59,566) | (19,473) |
| Tax effect of losses brought forward | - | (4,392) |
| Unrecognised deferred tax asset on losses carry forward | 113,072 | 96,987 |
| **Tax expense for the current year** | **37,335** | **88,281** |

The Group and its subsidiaries are subject to income tax separately, according to the tax laws and regulations of the Republic of Croatia. Other subsidiaries in the Group including HEP d.d. reported total tax losses of HRK 1,463,330 thousand (2011: HRK 1,000,859 thousand), while the Group recorded a total income tax expense of HRK 96,901 thousand (2011: HRK 107,754 thousand) and reported deferred tax assets in the amount of HRK 59,566 thousand (2011: HRK 19,473 thousand).

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

Tax losses reported by the Group and their expiry by year are presented below:

| Year of loss origination | Total tax loss reported by the Group | Year of expiry |
|---|---|---|
| 2008 | 194,136 | 2013 |
| 2009 | 116,099 | 2014 |
| 2010 | 152,800 | 2015 |
| 2011 | 434,935 | 2016 |
| 2012 | 565,360 | 2017 |
| | **1,463,330** | |

As of 31 December 2012 and 2011 the Group did not recognise deferred tax assets arising from tax losses carried forward at certain subsidiaries because the availability of future taxable profit against which the unused tax losses can be utilized is not certain.

**9. INCOME TAX (continued)**

The Croatian Tax Authorities have not performed a review of the income tax returns of the Group and its subsidiaries. In accordance with local regulations, the Tax Authority may at any time inspect the books and records of any Group company within 3 years following the year in which the tax liability is reported and may impose additional tax assessments and penalties. The Group management is not aware of any circumstances that may give rise to a potential material liability in this respect.

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

| HRK'000 | **Value adjustment of inventory** | **Provisions for jubilee and retirement benefits** | **Litigation provision** | **Depreciation at rates above statutory rates** | **Other** | **Total** |
|---|---|---|---|---|---|---|
| **At 1 January 2011** | **25,999** | **77,544** | **4,550** | **4,854** | **46,483** | **159,430** |
| Credited to profit and loss for the year | 3,385 | 1,638 | (4,550) | 2,081 | 16,919 | 19,473 |
| **At 31 December 2011** | **29,384** | **79,182** | **-** | **6,935** | **63,402** | **178,903** |
| Credited to profit and loss for the year | 1,711 | (5,487) | - | 3,026 | 60,317 | 59,566 |
| **At 31 December 2012** | **31,095** | **73,695** | **-** | **9,961** | **123,718** | **238,469** |

**10. PROPERTY, PLANT AND EQUIPMENT**

| HRK'000 | Land and buildings | Fixtures and equipment | Assets under construction | Total |
|---|---|---|---|---|
| **COST** | | | | |
| **At 1 January 2011, restated** | **34,172,805** | **33,132,075** | **3,046,316** | **70,351,196** |
| Restatement 1 January 2011 | - | 3,305 | (49) | 3,256 |
| Additions | 9,380 | 67,386 | 2,029,690 | 2,106,456 |
| Transfers from assets under construction | 759,134 | 1,196,938 | (1,956,072) | - |
| Capitalized borrowing costs | - | - | 10,427 | 10,427 |
| Inventory surpluses | 5,343 | 4,146 | 1,982 | 11,471 |
| Disposals | (51,995) | (134,329) | (40,074) | (226,398) |
| **At 31 December 2011** | **34,894,667** | **34,269,521** | **3,092,220** | **72,256,408** |
| Transfers | (14,864) | 14,085 | 954 | 175 |
| Additions | 14,065 | 165,472 | 2,401,000 | 2,580,537 |
| Capitalized borrowing costs | - | - | 17,717 | 17,717 |
| Transfers from assets under construction | 435,837 | 1,121,448 | (1,595,798) | (38,513) |
| Inventory surpluses | 10,422 | 5,092 | - | 15,514 |
| Disposals | (48,827) | (269,809) | (1,091) | (319,727) |
| **At 31 December 2012** | **35,291,300** | **35,305,809** | **3,915,002** | **74,512,111** |
| **ACCUMULATED DEPRECIATION** | | | | |
| **At 1 January 2011, restated** | **21,780,144** | **21,434,366** | **-** | **43,214,510** |
| Restatement at 1 January 2011 | - | 1,517 | - | 1,517 |
| Transfers | (2,509) | 9,043 | - | 6,534 |
| Charge for the year | 697,423 | 1,028,908 | - | 1,726,331 |
| Disposals | (50,173) | (126,279) | - | (176,452) |
| Inventory surplus | 242 | 894 | - | 1,136 |
| **At 31 December 2011, restated** | **22,425,127** | **22,348,449** | **-** | **44,773,576** |
| Transfers | (14,101) | 13,221 | - | (880) |
| Charge for the year | 696,478 | 1,014,970 | - | 1,711,448 |
| Disposals | (44,990) | (258,099) | - | (303,089) |
| Inventory surpluses | 1,611 | 5,014 | - | 6,625 |
| **At 31 December 2012** | **23,064,125** | **23,123,555** | **-** | **46,187,680** |
| **CARRYING AMOUNT** | | | | |
| **At 31 December 2012** | **12,227,175** | **12,182,254** | **3,915,002** | **28,324,431** |
| **At 31 December 2011, restated** | **12,469,540** | **11,921,072** | **3,092,220** | **27,482,832** |
| **At 1 January 2011, restated** | **12,392,661** | **11,697,709** | **3,046,316** | **27,136,686** |

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

Due to political developments in Croatia since 1990, certain local municipal land registers have not been fully established. The Group is in the process of registering, through the local courts in Croatia, its title to land and buildings. To date, no claims have been made against concerning its title to these assets over the Group.

The Group has no more pledged the property, plant and equipment because it has repaid the loan (2011: HRK 427,392 thousand) to secure the banking facilities provided to TE Plomin d.o.o.

**11. INTANGIBLE ASSETS**

| | HRK'000 |
|---|---|
| **COST** | **Intangible assets** |
| **At 1 January 2011, restated** | **568,731** |
| Transfers | (5,972) |
| Additions | 15,729 |
| Disposals | (2,304) |
| **At 31 December 2011, restated** | **576,184** |
| Activation of investments | 38,513 |
| Disposals | (344) |
| **At 31 December 2012** | **614,353** |
| **ACCUMULATED AMORTISATION** | |
| **At 1 January 2011, restated** | **503,721** |
| Transfers | (5,972) |
| Charge for the year | 23,078 |
| Disposals | (2,290) |
| **At 31 December 2011, restated** | **518,537** |
| Charge for the year | 22,343 |
| Disposals | (495) |
| **At 31 December 2012** | **540,385** |
| **CARRYING AMOUNT** | |
| **At 31 December 2012** | **73,968** |
| **At 31 December 2011, restated** | **57,647** |
| **At 1 January 2011, restated** | **65,010** |

**12. INVESTMENTS IN PROPERTIES**

As of 31 December 2012 investments in properties comprise properties held for the purpose of generating earnings from rental and/or capital appreciation, and are carried at fair value based on market price of the Management Board. Fair value comprises the estimated market value at the end of reporting period. All the investment properties are owned by the HEP d.d.

| **At fair value** | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Fair value | **234,760** | **223,094** | **202,467** |
| Depreciation charge for the year | (366) | (109) | (187) |
| Net gain/(loss) on fair value adjustment | (331) | 7,676 | 19,865 |
| Other changes | (146) | 4,099 | 949 |
| Closing balance at fair value | **233,917** | **234,760** | **223,094** |

## 13. PREPAYMENTS FOR PROPERTY, PLANT AND EQUIPMENT

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Power facilities – Hrvatske autoceste | 300,000 | 300,000 | 300,000 |
| JSC Tehnopromexport –TE Sisak | 49,659 | 94,299 | 56,530 |
| Končar GIM | 15,528 | 17,067 | 17,905 |
| Litostroj Slovenia | 2,444 | 2,891 | 4,457 |
| VOITH Siemens, Austria | 2,288 | 3,054 | 3,978 |
| Končar Inženjering d.d. TE Sisak | 622 | 2,896 | - |
| Končar Inženjering d.d. – HE Lešće | - | - | 1,249 |
| Others | 1,777 | 6,832 | 1,936 |
| | **372,318** | **427,039** | **386,055** |

In December 2006, the Group advanced a payment to Hrvatske autoceste d.o.o. for the purpose of acquisition of electricity facilities on the Croatian highways within 2 years from the advance payment.

As of the date of these financial statements, the facilities were not transferred to the Group, and an agreement was concluded with Hrvatske autoceste d.o.o. In December 2009, under which the deadline for the takeover of the electricity facilities by the Group has been prolonged for another 2 years.

The Group is the beneficial owner of these facilities, as it uses those assets for their intended economic purpose, which is to supply electricity to customers.

As of the date of issue of these financial statements, the Group has not classified these assets by type, and the economic effect of transfer of these assets from prepayments to tangible assets has not been calculated as well as the related depreciation.

## 14. INVESTMENT IN THE NUCLEAR POWER PLANT KRŠKO

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | Restated | Restated |
| Opening balance | 1,754,419 | 1,754,419 | 1,754,419 |
| | **1,754,419** | **1,754,419** | **1,754,419** |

**Investment background**

The legal status of the Nuclear Power Plant Krško ("NPPK") was regulated by inter-republic agreement dating back to 1970 and various agreements between the founders from 1974 and 1982. Pursuant to the stated agreements, the Company had a 50% interest in the NPPK in Slovenia, the other 50% was held by ELES GEN d.o.o., Ljubljana, the legal successor of the Slovenian power utility.

In 1998, the Slovene government passed a decree transforming the NPPK into a public company, Nuclear Power Plant Krško d.o.o. ("NPPK"), and nationalizing the nuclear power plant. Additionally, due to operational disputes, which include disagreements on energy prices to be charged and approval of annual budgets, the supply of power to HEP d.d. from NPPK was cut on 30 July 1998 and was not restored until 19 April 2003.

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

The agreement acknowledges the ownership rights of HEP d.d. in the newly formed company, Nuklearna elektrana Krško d.o.o. ('NPPK') in respect to its 50% holding in NPPK, which were previously denied. Both parties have agreed to extend the useful life of the power plant at least to the year 2023. The agreement also regulates that the produced electricity is supplied 50:50 to both contracting parties, and that the price of the electricity supplied is determined based on total production cost.

HEP d.d. started to receive electricity from NPPK on 19 April 2003, and expects to receive 2,550 GWh annually up to 2023, representing 16% of electricity consumption in Croatia.

By the end of 2003, the provisions of the agreement have been implemented according to which HEP d.d. and NPPK waive mutual receivables for damages and withdraw all claims arising there from up to 30 June 2002, including the disputed liabilities for electricity purchase and amounts due with respect to the previously calculated contribution for financing the decommissioning of the power plant and funds to cover the losses from previous years. After implementing the changes, the capital of NPPK as at 31 December 2003 amounted to SIT 84.7 billion (approximately: HRK 2.8 billion). Still there are some outstanding off-balance receivables from HEP d.d. to NPPK and Slovenia from the past, which do not have any influence on the current business relations.

## 14. INVESTMENT IN THE NUCLEAR POWER PLANT KRŠKO (continued)

**Current status**

According to the above stated agreement, the decommissioning of NPPK will be a joint obligation of both parties. Each party will provide half of the funds necessary to prepare the decommissioning plan and to cover the cost of implementation of the plan. In addition, each party will form a separate fund to allocate the funds for this purpose in the amounts estimated by the decommissioning plans. According to the current programme for the decommissioning of the Nuclear Power Plant Krško and disposal of nuclear waste, HEP d.d. is obliged to pay in the fund EUR 14,250 thousand per year. From 2004 to 2012, the Company disclosed radioactive waste disposal and decommissioning provisions in the amount of HRK 942,996 thousand, which is also the amount it paid onto the Fund's account in the period from 2006 to 2012.

The payment to the Fund are performed on the basis of *Regulation of the amount, time-limit and the mode of payment of assets for the financing of overhauling and the providing for of nuclear waste and the utilized unclear firing of the Nuclear plant Krško* brought by the part of the Government of the Republic of Croatia at 24 December 2008.

**Extracted financial information**

The following table presents the financial information extracted from the financial statements of NPPK as at 31 December 2012 and 2011:

| | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| Property, plant and equipment | 3,008,158 | 3,023,770 | 3,089,065 |
| Capital and reserves | 3,316,417 | 3,309,732 | 3,245,896 |
| Gross sales | 1,419,092 | 1,492,491 | 1,214,576 |
| Cash flows from operating activities | 674,550 | 495,358 | 313,211 |

Liabilities for received electrical energy from NPP Krško as at 31 December 2012 amount to HRK 61,119 thousand (2011: HRK 64,667 thousand). The Company operates at the point of coverage and the result for the financial year is equal to nil.

**15. INVESTMENT IN TPP PLOMIN**

In November 1996, HEP d.d. entered into a Joint Venture Agreement with RWE Energie Aktiengesellschaft, Germany ('RWE') regarding the completion and operation of TPP Plomin II. Consequently, a joint venture, TE Plomin d.o.o. ('Plomin') was formed in December 1996, with each partner holding 50 % of the equity of the new entity. A number of agreements were entered into, which regulate the relationship between the joint venture partners and their respective relationships with the new groups.

In accordance with the 1996 Asset Contribution Agreement, HEP d.d. contributed property, plant and equipment previously acquired for the project valued (by Croatian valuation experts) at DEM 50,000 thousand (HRK 179,138 thousand) as a contribution in kind to Plomin. Of this amount, HRK 50 thousand was allocated as share capital, while HRK 179,088 thousand was allocated to reserves.

In accordance with the Joint Venture Agreement, RWE contributed an equal amount of cash over the period of construction. The initial cash contribution of HRK 50 thousand was allocated as share capital and the remainder to reserves. The RWE capital contributed is distributed back to RWE over the term of the joint venture of 15 years, starting from the date of operation of the power plant at 30 April 2000.

In 2012 the distribution of RWE invested equity amounted to HRK 12,922 thousand (2011: HRK 12,668 thousand). The remaining undistributed RWE invested capital amounted to HRK 38 million at 31 December 2012 (2011: HRK 51 million).

Under the Statute of Plomin, RWE is entitled to an annual return during the term of the joint venture of 14% to 17% on invested capital (based on the actual number of hours of peak exploitation during the year). The invested capital includes RWE undistributed equity contribution as the unpaid portion of the accrued cumulative interest earned on investment during construction.

During the period of construction, the accrued cumulative interest on the RWE capital amounted to HRK 54,717 thousand (EUR 7,536 thousand) and is payable on a straight-line basis during the period of exploitation. At 31 December 2012, accrued undistributed interest amounted to HRK 8,846 thousand (2011: HRK 12,611 thousand).

The RWE annual return on invested capital, effectively a preferred dividend, is paid out from net profit of Plomin. The rate for 2012 is 17% as well as for 2011. The amount paid out in 2012 in respect of 2011 profits was HRK 11,514 thousand and in 2011 HRK 14,063 thousand in respect of 2010 profits.

These distributions have priority to HEP d.d. interest in the results of the joint venture and any other payments to HEP d.d.. Since HEP d.d. share has been used to pay RWE interest on capital since 2000, HEP d.d. has not realized any portion of profits earned by Plomin.

The joint venture partners entered into a number of agreements necessary for power plant operations, including: operation and maintenance agreements, a joint use and supply agreement and a power purchase agreement ('PPA'). The PPA agreement regulates the sale of electric energy to the Group by Plomin d.o.o. HEP d.d. is obliged to purchase all energy produced by TE Plomin d.o.o. at prices calculated in accordance with specified formulas in the PPA, which are designed to cover all costs of operations of Plomin, and ensure the guaranteed return on capital to RWE.

In these financial statements, the Group has presented its interest in TE Plomin using the method of full consolidation.

**15. INVESTMENT IN TPP PLOMIN (continued)**

| | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| Opening balance of non-controlling share | 62,847 | 76,993 | 91,409 |
| Capital payment | (12,922) | (12,668) | (12,382) |
| Dividend payment | (11,514) | (14,063) | (16,583) |
| Increase for the current year profit | 8,707 | 11,514 | 14,063 |
| Exchange differences | 165 | 1,071 | 486 |
| **Closing balance** | **47,283** | **62,847** | **76,993** |

## 16. LONG-TERM LOAN RECEIVABLES AND DEPOSITS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Loans given | 808 | 1,022 | 1,318 |
| Value adjustment | (158) | (167) | (135) |
| Current portion of loans given | (136) | (136) | - |
| **Long-term portion** | **514** | **719** | **1,183** |

Loans given to third parties are as follows:

| | Year loan approved | Repayment period | Loan amount | 31 December 2012 HRK'000 | 31 December 2011 HRK'000 | 1 January 2011 HRK'000 |
|---|---|---|---|---|---|---|
| | | | | | **Restated** | **Restated** |
| Town of Pregrada | 2006 | 10 years | 1,358 | 679 | 815 | 950 |
| Did d.o.o. | 2007 | 4 years | 1,010 | 129 | 207 | 368 |
| **Total** | | | | **808** | **1,022** | **1,318** |
| Value adjustment | | | | (158) | (167) | (135) |
| Current portion | | | | (136) | (136) | - |
| **Non-current portion** | | | | **514** | **719** | **1,183** |

## 17. INVESTMENTS AVAILABLE FOR SALE AND OTHER INVESTMENTS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Investments available for sale | 128,387 | 120,605 | 162,170 |
| Other investments | 1,065 | 310 | 210 |
| | **129,452** | **120,915** | **162,380** |

**17. INVESTMENTS AVAILABLE FOR SALE AND OTHER INVESTMENTS (continued)**

Changes in investments available for sale are presented below:

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | Restated | Restated |
| Beginning balance | 120,605 | 162,170 | 152,797 |
| Fair value adjustment of investments in Jadranski Naftovod d.d. | 7,558 | - | 9,373 |
| Fair valuation adjustment of investments in Jadranski naftovod d.d. presented in income | (88) | (41,565) | - |
| Fair valuation adjustment of investments in Pevec d.d. | 312 | - | - |
| | **128,387** | **120,605** | **162,170** |

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | Restated | Restated |
| **Investment in securities:** | | | |
| Jadranski Naftovod d.d. | 127,935 | 120,378 | 161,943 |
| Pevec d.d. | 312 | - | - |
| Viktor Lenac d.d. | 133 | 220 | 220 |
| Đuro Đaković d.d. | 5 | 5 | 5 |
| Kraš d.d. | 2 | 2 | 2 |
| | **128,387** | **120,605** | **162,170** |
| **Other investments** | | | |
| Geopodravina d.o.o. | 200 | 200 | 200 |
| LNG Hrvatska d.o.o. | 865 | 110 | 10 |
| | **129,452** | **120,915** | **162,380** |

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

**17. INVESTMENTS AVAILABLE FOR SALE AND OTHER INVESTMENTS (continued)**

In 2012 and 2011 fair value was determined by notification of the Central clearing deposit company as of 31 December. The market value of Jadranski naftovod shares as of 31 December 2012 is HRK 2,370 and 2011 HRK 2,230. The fair valuation of the investment in Jadranski naftovod as of 31 December 2012 has increased the investment value by HRK 7,558 thousand (2011: reduced by 41,465 thousand). The fair valuation in 2012 was performed through reserves and in 2011 through the profit and loss account.

On 1 June 2010 HEP d.d. and Plinacro d.o.o. concluded the Articles of Incorporation of LNG Hrvatska d.o.o., a liquefied natural gas company. In 2011 a decision was made to increase the share capital of LNG Hrvatska d.o.o. from HRK 20 thousand to HRK 220 thousand, and 2012 to HRK 1,730 thousand. HEP d.d. and Plinacro d.o.o. each hold 50 percent of the equity share.

**18. OTHER NON-CURRENT ASSETS**

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 **Restated** | HRK'000 **Restated** |
| Housing loan receivables | 33,649 | 38,095 | 42,890 |
| Energy efficiency receivables – long-term portion | 24,616 | 56,415 | 51,930 |
| Accrued cumulative interest – RWE | 8,846 | 12,611 | 16,078 |
| Other long-term assets | 108 | 31 | 75 |
| | **67,219** | **107,152** | **110,973** |

Prior to 1996, the Group had sold apartments it owned to its employees, the sale of which were governed by the laws of the Republic of Croatia. This property was generally sold on credit, and the related housing receivables, which are secured and bear interest at rates below market, are repayable on a monthly basis over periods of 20-35 years. Receivables for sold flats were transferred to new subsidiaries as of 1 July 2002. The housing receivables are shown in the financial statements at their discounted net present values, determined using an interest rate of 7.0 %. The amounts owed to the state, which represent 65 % of the value of the sold apartments, are included in non-current liabilities to the state (Note 25). The receivables are secured by mortgages over the sold apartments.

According to the provisions on joining, intercalary interest was accrued on all the funds invested by RWE in the period of construction at a rate of 17 percent. The accrued interest balance of EUR 7,536 thousand, equivalent to HRK 55,653 thousand has been recognised as deferred expense subject to straight-line amortisation over a period of 15 years.

Repayment of interest is done along with the repayment of invested funds from RWE Power and it started after the electric power plant was finished. In 2012 the total amount repaid was EUR 502 thousand equivalent to HRK 3,809 thousand (in 2011 EUR 502 thousand, equivalent to HRK 3,734 thousand).

As at 31 December 2012 deferred expense for the interest amounted to EUR 1,173 thousand equivalent to HRK 8,846 thousand (2011: EUR 1,675 thousand, equivalent to HRK 12,611 thousand). The related exchange differences are included in the financial revenue or financial cost for the year in which they arise.

## 19. INVENTORIES

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Inventories of fuel and other material | 526,542 | 644,113 | 748,065 |
| Electric materials | 217,167 | 187,740 | 162,486 |
| Spare parts | 221,934 | 212,512 | 175,536 |
| Construction material | 87,378 | 90,418 | 83,211 |
| Other inventories | 66,206 | 65,784 | 73,090 |
| Impairment of obsolete materials and spare parts | (137,586) | (137,047) | (125,717) |
| | **981,641** | **1,063,520** | **1,116,671** |

In 2012, the Group estimated the impariment for obsolete inventories of materials (material with no turnover in the last 2 years), in accordance with the ageing structure, at HRK 539 thousand (2011: HRK 11,330 thousand).

## 20. TRADE RECEIVABLES

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000<br>**Restated** | HRK'000<br>**Restated** |
| Electricity – Corporate customers | 1,606,227 | 1,422,139 | 1,355,919 |
| Electricity – Households | 478,424 | 313,463 | 336,814 |
| Foreign sales – Electric energy | 53,207 | 35,625 | 71,530 |
| Heating, gas and services | 502,643 | 443,354 | 446,462 |
| Connection to transmission network | 41,233 | - | 33,131 |
| Other | 83,190 | 63,255 | 61,882 |
| | **2,764,924** | **2,277,836** | **2,305,738** |
| **Impairment of bad and doubtful receivables** | (891,679) | (781,600) | (575,410) |
| | **1,873,245** | **1,496,236** | **1,730,328** |

**20. TRADE RECEIVABLES (continued)**

Ageing analysis of receivables not impaired is as follows:

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Not yet due | 1,015,832 | 876,451 | 1,044,409 |
| 0-30 days | 437,422 | 309,826 | 347,291 |
| 31-60 days | 161,682 | 138,013 | 145,786 |
| 61-90 days | 75,704 | 67,558 | 64,544 |
| 91-180 days | 89,315 | 61,198 | 68,461 |
| 181-365 days | 71,078 | 37,075 | 50,294 |
| Over 365 days | 22,212 | 6,115 | 9,543 |
| | **1,873,245** | **1,496,236** | **1,730,328** |

Movements in impairment allowance were as follows:

| | 31 December 2011 | 31 December 2010 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| **At 1 January** | **781,600** | **575,410** | **402,876** |
| Impairment for potential losses on receivables and interest on receivables (Note 7) | 250,972 | 364,544 | 332,139 |
| Reversal of prior-year provisions | (21,338) | (19,088) | (25,074) |
| Amounts collected (Note 5) | (119,555) | (139,266) | (134,531) |
| **At 31 December** | **891,679** | **781,600** | **575,410** |

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

## 21. OTHER SHORT-TERM RECEIVABLES

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| VAT receivable | 142,908 | 179,965 | 27,560 |
| Prepayments of income tax | - | 138,719 | - |
| Advances for working capital | 706 | 13,616 | 26,196 |
| Receivables from the State in respect of employees | 15,366 | 10,284 | 6,403 |
| Interest receivable | 2,995 | 2,553 | 3,564 |
| Demand and time deposits | 21,220 | 4,328 | 1,735 |
| Other short-term receivables | 60,419 | 65,640 | 78,606 |
| | **243,614** | **415,105** | **144,064** |

## 22. CASH AND CASH EQUIVALENTS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Current accounts - HRK | 156,084 | 123,916 | 71,510 |
| Current accounts - Foreign | 118,482 | 92,117 | 27,352 |
| Current accounts for special purposes | 7,403 | 6,105 | 5,710 |
| Petty cash registers - HRK | 280 | 280 | 287 |
| Deposits due till 90 days | 159,225 | 5,120 | 559,800 |
| Daily deposits | 163,550 | 179,585 | 97,498 |
| | **605,024** | **407,123** | **762,157** |

## 23. CAPITAL AND RESERVES

The share capital was first registered on 12 December 1994 in German marks (DEM) and amounted to DEM 5,784,832 thousand. On 19 July 1995, the share capital was reregistered in Croatian kuna in the amount of HRK 19,792,159 thousand. The share capital consists of 10,995,644 ordinary shares, with a nominal value of HRK 1,800.00 each.

Accumulated losses in the amount of HRK 356,648 thousand comprise legal reserves in the amount of HRK 191,094 thousand, transferred loss in the amount of HRK 610,237 thousand and profit for the year subscribed to the owner in the amount of HRK 62,495 thousand.

The non-controlling interest attributable to RWE amounts to HRK 47,283 thousand, of which HRK 8,707 thousand represents dividends attributable to the foreign equity holder.

**Capital reserves**

| | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Opening balance of reserves | (438,957) | (874,074) | (1,889,646) |
| Transfer from retained earnings | 438,957 | 444,038 | 1,008,073 |
| Other comprehensive income, net before restatement | | | 24,853 |
| Effect of restatement | | | (17,354) |
| Other comprehensive income/(loss) | 6,046 | (8,921) | 7,499 |
| Capital reserves | **6,046** | **(438,957)** | **(874,074)** |

| **Retained earnings** | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Opening balance | 5,851 | 947,198 | 403,018 |
| Increase of retained earnings | 13,963 | (-233) | 130,950 |
| Transfer to reserves | (438,957) | (444,038) | (1,008,073) |
| Dividend paid to the owner | - | (493,376) | - |
| Loss / profit for the year | 62,495 | (3,700) | 1,421,303 |
| | **(356,648)** | **5,851** | **947,198** |

Based on the Decision the Shareholders' Assembly of HEP d.d. from 24 May 2012 on the allocation of the 2011 profits and retained earnings from previous years is performed the transfer to reserves in the amount of HRK 438,957 thousand.

Based on the Decision the Shareholders' Assembly of HEP d.d. from 27 June 2011 on the allocation of the 2010 profits and retained earnings, HRK 444,038 thousand were transferred to reserves and HRK 493,376 thousand were distributed to the owner.

**24. LONG-TERM BORROWINGS**

| | Interest rates | **31 December 2012** HRK'000 | **31 December 2011** HRK'000 | **1 January 2011** HRK'000 |
|---|---|---|---|---|
| | | | **Restated** | **Restated** |
| Domestic bank borrowings | EURIBOR+ (1.00%-5.35%) | 1,961,548 | 1,681,140 | 1,040,610 |
| Foreign bank borrowings | EURIBOR+ 0.50% | 25,585 | 2,042,011 | 3,010,835 |
| Liabilities to domestic companies | EURIBOR+ 1.95% | - | - | 4,661 |
| Loan from RWE | | 5,055 | 8,828 | 12,369 |
| Total | | **1,992,188** | **3,731,979** | **4,068,475** |
| Deferred loan origination fees | | (20,474) | (22,777) | - |
| **Total long-term borrowings** | | **1,971,714** | **3,709,202** | **4,068,475** |
| Current portion | | (132,084) | (1,174,713) | (1,184,921) |
| **Long-term portion** | | **1,839,630** | **2,534,489** | **2,883,554** |

Loans of domestic banks are assured by bills of exchange and debentures. At the year end the Group from the assets assured by issuing of bonds has performed the premature returns of some long term loans, with a purpose of prolongation of maturity of the total loan portfolio. For that are repaid all the loans with unfavourable financial clauses, among which were the loans assured with the state guarantee. At 31 December 2012 the Group has no more debt covered with the Republic of Croatia guarantee.

## 24. LONG-TERM BORROWINGS (continued)

### New sources of funds

During the year the Group has not concluded new long term loans. For the financing of the investment plan and operations in 2012 the Group has utilized the assets gathered by issuing of euro bonds at the international capital market (detailed in Note 27) as well as the assets from loans in use.

### Loans in use

For the purpose of financing the investments and operations in previous years, the Group has during 2012 on its disposal the amount of EUR 84 milion from the loan of EUR 150 million concluded with a consortium of domestic banks (Privredna banka Zagreb d.d., Raiffeisenbank Austria d.d. and Zagrebačka banka d.d.).

During 2012 the utilisation of the long-term loan approved by KfW Entwicklungsbank in the amount of EUR 50 million for the financing of the projects of subsidiaries HEP ESCO d.o.o and HEP Obnovljivi izvori energije d.o.o. The key lending terms and conditions are as follows: 5-year utilisation period; quarterly repayment of principal over a period of 10 years following the expiry of the utilisation period. At 31 December 2012 the KfW loan balance was EUR 3.4 million, of which EUR 46.6 million were unutilised.

Also, during 2012 the Group had on its disposal the assets from the long term loan concluded with European bank for reconstruction and development and the union of banks in the amount of EUR 123.2 million which are intended for the financing of construction of HE Ombla near Dubrovnik. Loan trenches have the total maturity of 12 a 15 years, in which is included a period of utilization of assets of 4 years.
The beginning of the loan assets' utilization is planned in the year 2013.
The annual principal repayment schedule for the following five years is as follows:

| | |
|---|---:|
| 2013 | 132,084 |
| 2014 | 284,418 |
| 2015 | 412,694 |
| 2016 | 381,673 |
| 2017 | 380,849 |
| After 2017 | 400,470 |
| Total | **1,992,188** |

## 24. LONG-TERM BORROWINGS (continued)

The covenants, as defined in the applicable loan agreements, specifically require the Group to meet certain prescribed levels of the following ratios based on consolidated financial statements: operating ratio, debt service coverage, internal cash generation, tangible net worth capital, and net borrowing.
As at 31 December 2012 all the covenants were met.

The analysis of long-term borrowings in various foreign currencies is provided below (in '000):

| **Valuta** | **31 December 2012** | **31 December 2011** | **1 January 2011** |
|---|---|---|---|
| EUR | 263,349 | 495,587 | 549,223 |

## 25. LONG-TERM LIABILITIES TO THE GOVERNMENT

The long-term debt to the Government in the amount of HRK 27,544 thousand in 2012 (2011: HRK 30,466 thousand) relates to the obligation arising on the sale of housing units to employees under the Government program, which was discontinued in 1996. According to the law regulating housing sales, 65% of the proceeds from the sale of apartments to employees were payable to the state at such time as the proceeds were collected. According to the law, HEP d.d. has no liability to remit the funds, unless and until they are collected from the employee.

## 26. LONG-TERM PROVISIONS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Litigation provision | 204,292 | 217,621 | 162,443 |
| Provision for retirement bonuses | 285,739 | 314,081 | 302,157 |
| Provision for jubilee awards | 45,408 | 43,551 | 46,268 |
| Provision for the de-commissioning of thermal power plants | 104,341 | 100,044 | 93,121 |
| Provision for NPPK decommissioning (long-term) | - | - | 53,838 |
| Provision according to damages contract | - | 80,800 | 80,800 |
| Provision for electricity purchased from wind power plants | 21,631 | 22,532 | 22,031 |
| Provision for investment in HE Lešće | - | - | 39,287 |
| | **661,411** | **778,629** | **799,945** |

The thermal power plant decommissioning provision in the amount of HRK 104,341 thousand represents a discounted value of the estimated decommissioning costs of the Group's thermal power plants.

Movements in the present value of defined benefit obligations in the current period were as follows:

| | Legal actions | Retirement bonuses | Jubilee awards | Decommissioning of TPPs | Other | Total |
|---|---|---|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| **At 1 January 2012** | **217,621** | **314,081** | **43,551** | **100,044** | **103,332** | **778,629** |
| Transfer | 34,000 | - | - | - | (34,000) | - |
| New provisions made | 40,079 | 21,955 | 4,218 | 4,297 | - | 70,549 |
| Decrease in provisions (amounts paid) | (76,091) | (22,459) | (7,136) | - | (47,701) | (153,387) |
| Decrease in provision on valuation | (11,317) | (27,838) | 4,775 | - | - | (34,380) |
| **At 31 December 2012** | **204,292** | **285,739** | **45,408** | **104,341** | **21,631** | **661,411** |

**26. LONG-TERM PROVISIONS (continued)**

*Legal cases provision*

The Group has booked the provision for legal actions refers to cases where possible outcome has been determined as uncertain or negative and was recognised in the total amount of HRK 204,292 thousand (in 2011: HRK 217,621 thousand). The most important court case provided against is the one of HEP Proizvodnja d.o.o. for a dispute with Zagrebački Holding which in 2012 has the provision in the amount of HRK 84,821 thousand and which relates to compensation for the waste water treatment plant.

The official decision is in course of the one materially significant dispute related to HEP Peruća which was started in 1995, for which was in 2012 brought the first instance decision in favour of the accuser. As according to the stand of the Group and the County State Practice of Law this decision is legally and factually untenable, the Group has lodged a complaint.

Management Board of HEP d.d. has estimated that exists the high grade probability for the Group of the positive result of the subject dispute.

*Retirement bonuses and jubilee awards*

Movements in the present value of defined benefit obligations in respect of employee benefits during the current period were as follows:

| | **Retirement benefits** HRK'000 | **Jubilee awards** HRK'000 | **Total** u tisućama kuna |
|---|---|---|---|
| **At 1 January 2011** | **314,081** | **43,551** | **357,632** |
| Cost of services | 10,333 | 2,399 | 12,732 |
| Interest expenses | 11,608 | 1,814 | 13,422 |
| Salaries paid | (22,459) | (7,136) | (29,595) |
| Benefits paid | 14 | 5 | 19 |
| Actuarial gains/(losses) | (27,838) | 4,775 | (23,063) |
| **At 31 December 2012** | **285,739** | **45,408** | **331,147** |

The following assumptions were used in preparing the calculations:

- The termination rate is from 0% to 6.23% percent and is based on the statistical fluctuation rates for the Group in the period from 2005 to 2012.
- The probability of death by age and sex is based on Croatian Mortality Tables 2000 published by the Croatian Statistical Bureau. It is assumed that the population of employees of the Company represents average with respect to mortality and health status.
- We assumed the annual salary will not increase in other years.
- The present value of the obligation was determined using a 4.4% discount rate for all the companies within the Group.

**27. ISSUED BONDS**

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | Restated | Restated |
| Nominal value of bonds | 1,200,000 | 1,200,000 | 1,200,000 |
| Cumulative repayment | (233,450) | (140,070) | (46,690) |
| Discount value | (814) | (1,348) | (1,888) |
| Current portion of bonds | (593,380) | (93,380) | (93,380) |
| | **372,356** | **965,202** | **1,058,042** |
| Nominal value of bonds - foreign | 2,955,595 | | |
| Foreign exchange differences | (92,198) | | |
| Liabilities according to SWAP | 99,855 | | |
| | **2,963,252** | | |
| | **3,335,608** | | |

**Bonds issued abroad**

Bonds in the amount of HRK 500,000 thousand, issued in 2006, are due in 2013, and bear interest at a fixed rate of 5.00 percent. Bonds in the amount of HRK 700,000, issued at the end of 2007, are repayable in 15 semi-annual installments, commencing three years from the date of issue, and bear interest at a fixed rate of 6.50 percent. The HEP d.d. bonds are listed on the Zagreb Stock Exchange.

**Bonds issued abroad**

In November 2012, the Company has issued bonds in the amount of USD 500,000 thousand at international capital market. Bonds have maturity of 5 years, in full mature in November 2017 and carry fixed interest of 6%.Bonds of HEP d.d. are inserted at the market of the Luxembourg stock-exchange and they are actively traded.

Part of assets assured by issuing of bonds is utilized for the return of short-term loans and the refinancing (premature returns) of the existing long term loans, with a purpose of prolongation of maturities of the total loan portfolio, while the remaining part of assets is utilized for the financing of investments in current year.

For the purpose of protection of currency risk, respectively the change in movements of dollar value, in the same time is concluded the contract on currency exchange (swap) by which the dollar liability is transformed into euro and that for the whole period of duration of liability upon issued bonds, up to its outermost maturity at 9 November 2017.

## 27. ISSUED BONDS (continued)

### Interest swap

The Group has concluded contract on interest swap by which is protected the Group's exposure on the basis of liabilities at changeable interest rates. According to contract, six -month interest rate which pays the Group is fixed and amounts 5.39%, while the swap interest rate is equal to six-month EURIBOR.
Payments according to the contract were performed each six months and the Contract has expired at 25 October 2012.

### Currency swap

For the purpose of currency risk protection, i.e. change in movement of the dollar value, the Group has concluded the contract on currency swap ,by which the dollar liability upon issued bonds abroad is transformed in euro and this for all period of bond duration, respectively till its outermost maturity date at 9 November 2017.
According to contract, a six month interest rate which is paid by the Group is fixed and amounts 6.53%,while the interest rate which the Group demands as creditor from contractual parties according to swap is equal to fixed rate at which bonds are issued and amounts 6.00%.

**28. OTHER NON-CURRENT LIABILITIES**

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Deferred income for property financed by third parties | 4,220,301 | 4,440,468 | 4,590,815 |
| Long term liabilities for assets financed by clearing debt | 689,792 | 701,012 | 414,938 |
| Long-term debt under interest rate swap | - | 850 | 672 |
| Other | 1,540 | 1,659 | 1,779 |
| | **4,911,633** | **5,143,989** | **5,008,204** |

Deferred revenue is related to fixed assets contributed by customers and others without charge. The revenue is recognized into income over the same periods as the related assets are amortized, which applies to contracts for connection to the network concluded by 3 June 2009. After 1 July 2009 the connection fee is recognized as income in the amount of funds received from the customer in the period when the customer is connected to the grid or when permanent access to the delivery of the service is given.

At 31 December 2012 the Group reported a liability in the amount of HRK 689,792 thousand in respect of a clearing debt (2011: HRK 701,012 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of Finance with the use of the funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the HEP Group and the Ministry of Finance regarding the clearing debt, it has not been clearly defined as either a loan or a government grant.

## 29. SHORT-TERM BORROWINGS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Borrowings from domestic banks and foreign banks, denominated in various currencies on the following terms: | 400,000 | 592,778 | 282,252 |
| Interest rate from EURIBOR/TZ Min. of fin. + margin (2.60% – 5.70%) | | - | - |
| Secured by bills of exchange | | | |
| Borrowings from domestic companies | 3,261 | 2,806 | 2,805 |
| Short term part of the RWE loan | 7,582 | 7,579 | 7,436 |
| | **410,843** | **603,163** | **292,493** |

During 2012, the Group used short-term loans from domestic banks for working capital purposes and for the settlement of trade payables. In addition to the prolongation of current loans arranged during the year, the Group also concluded new credit lines for the purpose of keeping financial stability.

By the premature return of the majority short term loans at the year end, short term indebtedness is decreased for 32% in relation to the year beginning. At 31 December 2012, the Group disposes with HRK 902 million unutilized short term loan resources.
Short term loans are assured with bills of exchange and debentures.

## 30. LIABILITIES FOR TAXES AND CONTRIBUTIONS

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Liabilities for income tax | 28,521 | - | 357,228 |
| Utility and other fees | 17,519 | 12,680 | 25,596 |
| Contributions on salaries | 20,111 | 23,205 | 23,953 |
| Liabilities for customs | 908 | 2,239 | 20,153 |
| Contributions and taxes for benefits in kind | 3,519 | 1,984 | 14,880 |
| Other | 3,538 | 647 | 3,175 |
| | **74,116** | **40,755** | **444,985** |

## 31. LIABILITIES TO EMPLOYEES

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Net salaries | 75,220 | 78,074 | 81,133 |
| Contributions | 39,179 | 40,363 | 41,953 |
| Other | 26,169 | 9,497 | 11,140 |
| | **140,568** | **127,934** | **134,226** |

## 32. OTHER PAYABLES

| | 31 December 2012 | 31 December 2011 | 1 January 2011 |
|---|---|---|---|
| | HRK'000 | HRK'000 | HRK'000 |
| | | **Restated** | **Restated** |
| Deferred income and received advances for connections | 216,610 | 193,125 | 110,538 |
| Deferred income for other advances received | 98,344 | 15,538 | 7,214 |
| Accrued expenses for unused vacation days | 64,827 | 63,900 | 64,477 |
| Deferred income from sale of el. energy to households | 19,426 | 10,905 | - |
| Liabilities for renewable sources | 11,477 | 8,017 | 16,446 |
| Decommissioning NPPK accrued expenses | - | - | 5,023 |
| Accounted costs of severance pays to employees | 249,174 | - | - |
| Other accrued expenses | 31,163 | 3,203 | 9,459 |
| Current portion of the liability under interest rate swap | - | 850 | 2,203 |
| Other payables | 51,970 | 85,837 | 75,676 |
| | **742,991** | **381,375** | **291,036** |

Value adjustment of receivables from Households as at 31 December 2012 was calculated by using logarithmic curve with losses on the supply network of 8.7%, while for the year ended 31 December 2011 the percent of loss was 8.3%. The result is the decrease of revenue in the amount of HRK 8,521 thousand in the respect to the previous year.

## 33. RELATED PARTY TRANSACTIONS

The Group has a 50% ownership in the capital of NPPK (NE Krško d.o.o.).

The produced electric energy at NPPK is delivered to HEP d.d. at 50% of total produced quantities at a price which is determined in accordance with the total production costs of NPPK.

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

| | **31 December 2012** | **31 December 2011** |
|---|---|---|
| | HRK'000 | HRK'000 |
| **NE Krško d.o.o.** | | |
| Liabilities for purchased electricity | 61,119 | 64,667 |
| Cost of purchased electricity | 707,758 | 737,565 |

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

| | Sales revenue | | Purchases | |
|---|---|---|---|---|
| HRK'000 | **2012** | **2011** | **2012** | **2011** |
| **Enterprises controlled by the Government** | | | | |
| Hrvatske Željeznice | 112,500 | 108,259 | 12,765 | 9,279 |
| INA-Industrija nafte | 155,192 | 121,110 | 132,403 | 1,419,311 |
| Prirodni plin | - | - | 2,531,088 | 1,011,225 |
| Plinacro | 2,135 | 1,975 | 34,760 | 34,296 |
| Hrvatske telekomunikacije | 85,744 | 83,937 | 24,318 | 27,400 |
| Croatia osiguranje | 5,508 | 6,481 | 16,371 | 16,924 |
| Hrvatska pošta | 23,245 | 22,062 | 60,553 | 54,523 |
| Hrvatske šume | 6,474 | 5,785 | 6,087 | 12,113 |
| Jadrolinija | 1,102 | 727 | 647 | 787 |
| Narodne novine | 2,590 | 2,855 | 5,120 | 6,236 |
| Croatian Radio & Television | 12,437 | 12,441 | 1,185 | 1,079 |
| Plovput | 579 | 551 | 692 | 230 |
| Croatia Airlines | 780 | 788 | - | 2 |
| Petrokemija Kutina | 29,028 | 9,428 | 118 | 46 |
| Ministry of Foreign Affairs | 525 | 563 | - | - |
| Ministry of Defense | 22,530 | 17,597 | - | - |
| Ministry of Interior | 25,187 | 24,862 | - | - |
| Elementary and secondary schools | 82,888 | 79,120 | - | - |
| Judicial institutions | 12,185 | 10,506 | - | - |
| Colleges and universities | 31,594 | 30,649 | 4,145 | 3,160 |
| Legislative, executive and other bodies of the Republic of Croatia | 30,482 | 29,169 | 6,572 | 5,848 |
| Health institutions and organisations | 89,538 | 81,711 | 3,233 | 3,502 |
| Other users | 12,025 | 70,472 | 16,669 | 15,883 |
| **TOTAL** | **744,268** | **721,048** | **2,856,726** | **2,621,844** |

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

| | Receivables | | Payables | |
|---|---|---|---|---|
| HRK'000 | **31 December 2012** | **31 December 2011** | **31 December 2012** | **31 December 2011** |
| **Enterprises controlled by the Government** | | | | |
| Hrvatske Željeznice | 45,902 | 22,615 | 2,460 | 866 |
| INA-Industrija nafte | 18,927 | 14,709 | 12,707 | 206,061 |
| Prirodni Plin | - | - | 297,100 | 371,656 |
| Plinacro | 355 | 351 | - | 4,380 |
| Hrvatske telekomunikacije | 9,331 | 8,092 | 7,625 | 8,179 |
| Croatia osiguranje | 610 | 582 | 4,356 | - |
| Hrvatska pošta | 3,107 | 3,380 | 3,791 | 4,568 |
| Hrvatske šume | 1,041 | 1,262 | 365 | 1,288 |
| Jadrolinija | 178 | 57 | 592 | 761 |
| Narodne novine | 263 | 284 | 1,361 | 1,790 |
| Croatian Radio & Television | 2,385 | 2,006 | 152 | 231 |
| Plovput | 65 | 64 | 102 | 49 |
| Croatia Airlines | 148 | 149 | 276 | - |
| Petrokemija Kutina | 5,026 | 266 | - | - |
| Ministry of Defense | 3,260 | 4,209 | - | - |
| Ministry of Interior | 3,402 | 7,286 | - | - |
| Elementary and secondary schools | 15,191 | 15,096 | - | - |
| Judicial institutions | 3,841 | 2,599 | - | - |
| Colleges and universities | 4,847 | 4,136 | - | - |
| Legislative, executive and other bodies of the Republic of Croatia | 5,825 | 5,183 | - | - |
| Health institutions and organizations | 18,789 | 35,810 | - | - |
| Other users | 3,569 | 5,842 | 6,351 | 11,008 |
| **TOTAL** | **146,062** | **133,978** | **337,238** | **610,837** |

Under the Croatian energy laws, the Group is an eligible gas buyer.

## 34. CONTINGENT LIABILITIES AND COMMITMENTS

In 2012, the Group established a provision for legal actions estimated to be ruled against HEP d.d.

The Group has long-term financial investments in the territory of Bosnia and Herzegovina, and Serbia, which in 1994 had a historical cost of HRK 1,243,970 thousand. At the time of the transformation of the Company into a joint stock company in 1994, this amount was excluded from the net asset value.

**Operating commitments**

As at 31 December 2012, as part of its investing activities, the Group has concluded contracts under which the construction of a number of significant facilities and other investments has commenced but has not been completed. In 2012 the value of unrealised contracts for the most significant projects amounts to approximately HRK thousand 1,690,780 thousand (2011: HRK 1,670,904 thousand).
Most significant investments refers to investments in HEP Proizvodnja d.o.o., HEP Operator Prijenosnog Sustava d.o.o. and HEP Operator Distribucijskog Sustava d.o.o.

**Environmental matters**

HEP Group monitors and analyses the environmental impact of its business activities on an on-going basis. The key impact indicators comprise emissions of pollutants into air and the quantity of production waste, which HEP reports to the competent institutions, local self-government units and public stakeholders on a regular and timely basis. The staffs engaged in environmental and nature protection undergo training and seminars and workshops where they receive information about the obligations and measures provided in the applicable environmental laws and regulations.

There is an environmental expenditure monitoring system (RETZOK) at the Company from 2004 which monitors all investments in environmental and nature protection.

The Company is in the process of performing analyses and achieving readiness with respect to compliance with the requirements imposed by EU legislation in terms of more stringent pollutant emission limits and reduced greenhouse gas emissions, the greenhouse gas emission trading scheme, integrated environmental permitting system, as well as the system of ecologically important areas and corridors (the National Ecological Network).

To the Ministry of environmental protection and the nature are delivered the requests for the obtaining of integrated conditions for the environmental protection and in the course is the procedure of the obtaining of permits.
By the decision of the Management of HEP is maintained the greenhouse gas emission unit trade system in which are stated the liabilities and the time-limits of implementation of sector liabilities and the companies included in the HEP trading system. To the agency for the environmental protection, national administrator of the Croatian part of the EU Greenhouse gas register, were delivered the requests for the opening of the Plant operator's account.

### 34. CONTINGENT LIABILITIES AND COMMITMENTS (continued)

To the Environmental protection fund are proved the investments into environmental protection projects and the improvement of energetic efficacy at the level of the whole HEP Group which has resulted by stimulative corrective factors by which are decreased fees for the omission of contaminating substances in the environment of 50%.
In course is the continuation of implementation of the management environmental protection system according to standard ISO 14001 into productive HEP plants.
In 2012 is continued with the maintenance of informative system of environmental protection in HEP Group with a goal of combining data related to nature protection and environment.

**Separation of the company HEP Operator prijenosnog sustava d.o.o. from the Group**

Law on electric energy market (National gazette 22/2013) became valid at 2 March 2013 (hereinafter: Law). Substatutory acts prescribed by Law should be brought in a time-limit of twelve months from the date of entering into force of the Law, and the substatutory acts should be prescribed by Law on energy (National gazette 120/2012) in a time-limit of six months from the date of entering of law into force.

According to provisions of the Law on electric energy market (National gazette 22/2013), Hrvatska elektroprivreda d.d. as a leading company inside the vertically integrated subject and the owner of the transmission system is liable to perform separation of the transmission system operators according to Law provisions,and to undertake all the activities for the fulfilment of requests for the separation of the transmission system operators with a goal of certification of transmission system operators during 2013.

Assembly of Hrvatska elektroprivreda d.d. at 9 April 2013 has brought a decision on separation of the transmission system operators according to independent transmission operator model (ITO-Independent transmission Operator).

HEP Operator prijenosnog sustava d.o.o. will bring a request for certification,which according to the Law performs Hrvatska energetska regulatorna agencija – Croatian energetic regulatory agency (hereinafter: HERA).Together with the request is to be applied the documentation which proves that the eficaciously separation is performed from the part of HEP d.d. and the other related companies,which under the definition from the Law comprise vertically integrated subject,including the independence of the total managing structure of the company HEP Operator prijenosnog sustava d.o.o.,and to possess all the human,technical, physical and financial resources for the performing of electric energy transfer activity as also the fulfilment of other prescribed liabilities.

In the procedure of certification, HERA will the explained draft of certificate deliver for the opinion to the European commission, which opinion has to be taken into regard in a degree, as greater as possible.

**35. SUBSIDIARIES**

As at 31 December 2012, the Group had the following subsidiaries:

| Subsidiary | Country | Interest in (%) | Main activity |
|---|---|---|---|
| HEP-Proizvodnja d.o.o. | Croatia | 100 | Electricity generation and heating |
| HEP-Operator prijenosnog sustava d.o.o. | Croatia | 100 | Electricity transmission |
| HEP-Operator distribucijskog sustava d.o.o. | Croatia | 100 | Electricity distribution |
| HEP Opskrba d.o.o. | Croatia | 100 | Electricity supply |
| HEP-Toplinarstvo d.o.o. | Croatia | 100 | Thermal power generation and distribution |
| HEP - Trgovina d.o.o. | Croatia | 100 | Electrical energy trading and optimization of power plants production |
| HEP-Plin d.o.o. | Croatia | 100 | Gas distribution |
| TE Plomin d.o.o. | Croatia | 50 | Electricity generation |
| APO d.o.o., usluge zaštite okoliša | Croatia | 100 | Special waste management |
| HEP ESCO d.o.o. | Croatia | 100 | Financing of energy efficiency projects |
| Plomin Holding d.o.o. | Croatia | 100 | Development of infrastructure in area around Plomin |
| CS Buško Blato d.o.o. | BiH | 100 | Maintenance of hydro power plants |
| HEP-Odmor i rekreacija d.o.o. | Croatia | 100 | Accommodation and recreation services |
| HEP-NOC Velika | Croatia | 100 | Accommodation and training |
| HEP-Obnovljivi izvori energije d.o.o. | Croatia | 100 | Electricity generation |
| HEP – Razvoj višenamjenskih nekretninskih projekatata d.o.o. | Croatia | 100 | Purchase and sale of electrical energy |
| HEP-Trgovina d.o.o. Brežice | Slovenija | 100 | Purchase and sale of electrical energy |
| HEP- Magyarorszag Energia KFT | Mađarska | 100 | Trgovanje električnom energijom |

The majority of these subsidiaries were created for the purpose of reorganization and re-structuring the core business activities driven by the new energy legislation, which came into effect as of 1 January 2002, as indicated in Note 1.

## 36. FINANCIAL INSTRUMENTS

***Capital risk management***

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

The capital structure of the Company consists of debt, which includes the borrowings and issued bonds disclosed in Note 24, 27 and 29, cash and cash equivalents and equity attributable to equity holders of the parent, comprising issued capital, legal and other reserves and retained earnings.

***Gearing ratio***

The Group's risk management committee reviews the capital structure on a semi-annual basis. As part of this review, the committee considers the cost of capital and the risks associated with each class of sources of funding. The gearing ratio at the yearend can be presented as follows:

| | **31 December 2012** HRK'000 | **31 December 2011** HRK'000 |
|---|---|---|
| Debt | 6,311,545 | 5,370,947 |
| Cash and cash equivalents | (605,024) | (407,123) |
| Net debt | 5,706,521 | 4,963,824 |
| Equity | 19,488,840 | 19,421,900 |
| Net debt to equity ratio | **29%** | **25%** |

***Significant accounting policies***

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in Note 2 to the financial statements.

***Categories of financial instruments***

| | **31 December 2012** HRK'000 | **31 December 2011** HRK'000 |
|---|---|---|
| **Financial assets** | | |
| Financial property available for sale | 129,452 | 120,915 |
| Loans and receivables (including cash and cash equivalents) | 2,563,609 | 1,989,496 |
| Other non-current assets | 67,732 | 107,872 |
| **Financial liabilities** | | |
| Non-current liabilities | 5,894,114 | 4,233,678 |
| Current liabilities | 3,814,947 | 4,449,565 |

## 36. FINANCIAL INSTRUMENTS (continued)

### *Financial risk management objectives*

The Group's Treasury function in the extent of the HEP Group provides to companies the 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*

The Group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates and interest rates (see below). Market risk exposures are supplemented by sensitivity analysis. There has been no change to the Group's exposure to market risks or the manner in which it manages and measures the risk.

### *Foreign currency risk management*

The Group undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters utilising forward foreign exchange contracts.

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

| | **Assets** | | **Liabilities** | |
|---|---|---|---|---|
| | **31 December 2012** | **31 December 2011** | **31 December 2012** | **31 December 2011** |
| | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| European Union (EUR) | 44,664 | 16,101 | 683,215 | 548,280 |
| USD | 1,492 | 109 | 8,449 | 48,716 |

**36. FINANCIAL INSTRUMENTS (continued)**

***Foreign currency sensitivity analysis***

The Group is mainly exposed to the changes of euro (EUR) and US dollar (USD). The following table details the Group's sensitivity to a 10% increase and decrease in the HRK against 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 only outstanding foreign currency denominated receivables and liabilities and adjusts 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 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.

| | **2012** | **2011** |
|---|---|---|
| | HRK'000 | HRK'000 |
| **EUR change impact** | | |
| Profit or loss | 481,826 | 400,753 |
| **USD change impact** | | |
| Profit or loss | 3,984 | 28,288 |

**36. FINANCIAL INSTRUMENTS (continued)**

***Interest rate risk management***

The Group is exposed to interest rate risk as it borrows funds at floating interest rates. The Group's exposures to interest rates on financial assets and financial liabilities are shown in section of this note, the liquidity risk management. The Group manages this risk by maintaining an appropriate mix between fixed and floating rate borrowings, by the use of interest rate swap contracts.

***Interest rate sensitivity analysis***

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

If interest rates had been 50 basis points higher/lower and all other variables were held constant, the Group's:

- Profit for the year ended 31 December 2012 would decrease/increase by HRK 11,807 thousand (2011: HRK 19,597 thousand), based on exposure to interest rate risk. This is mainly attributable to the Group's exposure to interest rates on its variable rate borrowings, which accounted for 37% (2011: 73%); and
- The Group's sensitivity to interest rates has decreased during the current period mainly due to the reduction in variable rate of debt instruments.

**Credit risk management**

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

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

Except as detailed in the following table, the carrying amount of financial assets recorded in the financial statements, which is net of impairment losses, represents the Group's maximum exposure to credit risk without taking account of the value of any collateral obtained.

**36. FINANCIAL INSTRUMENTS (continued)**

***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 Company manages liquidity risk by maintaining adequate reserves, banking facilities and other sources of financing, 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 that will be earned on those assets except where the Group anticipates that the cash flow will occur in a different period.

***Maturity of non-derivative financial assets***

| | **Weighted average effective interest rate** | **Less than 1 month** | **1 - 3 months** | **3 -12 months** | **1 - 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|---|---|---|
| | | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| 2012 | | | | | | | |
| Non-interest bearing | | 1,582,046 | 662,390 | 448,507 | 65,559 | 2,156 | 2,760,658 |
| Variable interest rate instruments | 5,00% | 23 | 46 | 66 | - | - | 135 |
| **Total** | | **1,582,069** | **662,436** | **448,573** | **65,559** | **2,156** | **2,760,793** |
| 2011 | | | | | | | |
| Non-interest bearing | | 754,298 | 897,131 | 461,614 | 99,238 | 5,788 | 2,218,069 |
| Variable interest rate instruments | 5,00% | 22 | 43 | 149 | - | - | 214 |
| **Total** | | **754,320** | **897,174** | **461,763** | **99,238** | **5,788** | **2,218,283** |

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

**36. FINANCIAL INSTRUMENTS (continued)**

***Liquidity and interest rate risk tables (continued)***

**Maturity of non-derivative financial liabilities**

| | **Weighted average effective interest rate** | **Less than 1 month** | **1 - 3 months** | **3 -12 months** | **1 - 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|---|---|---|
| | % | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 | HRK'000 |
| **2012** | | | | | | | |
| Non-interest bearing | | 1,337,387 | 881,754 | 470,775 | 707,064 | 536 | 3,397,516 |
| Variable interest rate instruments | 3.41% | 14,532 | 52,140 | 543,036 | 1,792,940 | 387,757 | 2,790,405 |
| Fixed interest rate instruments | 6.31% | - | - | 824,881 | 5,004,943 | 15,926 | 5,845,750 |
| **Total** | | **1,351,919** | **933,894** | **1,838,692** | **7,504,947** | **404,219** | **12,033,671** |
| **2011** | | | | | | | |
| Non-interest bearing | **-** | 1,430,610 | 1,151,841 | 452,560 | 274,667 | 2,618 | 3,312,296 |
| Variable interest rate instruments | 4.37% | 71,634 | 395,827 | 1,367,154 | 3,547,752 | 684,184 | 6,066,551 |
| Fixed interest rate instruments | 5.60% | 8,437 | - | 178,950 | 1,037,917 | 112,162 | 1,337,466 |
| Total | | **1,510,681** | **1,547,668** | **1,998,664** | **4,860,336** | **798,964** | **10,716,313** |

The Group has access to financing facilities, the total unused amount of which is HRK 2,183,142 thousand at the reporting date. The Group expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

**36. FINANCIAL INSTRUMENTS (continued)**

*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 (excluding derivative instruments) is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions.
- fair value of derivative instruments is calculated using the listed price. Where such prices are not available, the analysis uses discounted cash flows using the current yield curve for the period of the instruments under optional derivatives, while the optional derivative used models for pricing options. Forward currency contracts are valued using quoted forward exchange rates and yield curves derived from quoted interest rates for contracts with similar maturity. Interest rate swaps are valued at the present value of estimated future cash flows and discounted based on the current yield curve derived from quoted interest rates.

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

The table below analyzes the financial instruments remeasured subsequently at fair value, classified into three groups depending on the availability of indicators of fair value:

1. Level 1 observable indicators - indicators of fair value derived from (unadjusted) prices quoted in active markets for identical assets and liabilities are identical

2. Level 2 observable indicators - indicators of fair value derived from data other than quoted prices from Level 1 for observable assets or liabilities (i.e. their prices) or indirectly (derived from the price), and

3. Level 3 indicators - indicators derived from valuation techniques using as input data on the assets or liabilities that are not based on available market data (unobservable input).

The indicators of fair value recognized in the statement of financial position

| | **1st level**<br>HRK'000 | **2nd level**<br>HRK'000 | **3rd level**<br>HRK'000 | **Total**<br>HRK'000 |
|---|---|---|---|---|
| **2012** | | | | |
| Assets available for sale | 129,452 | - | - | **129,452** |
| **2011** | | | | |
| Assets available for sale | 120,915 | - | - | **120,915** |
| Interest swap liability (current and noncurrent portion) | - | 850 | - | **850** |

## 37. APPROVAL OF THE FINANCIAL STATEMENTS

These financial statements were approved by the Board and authorised for issue on 18 April 2013.

Signed on behalf of the Group on 18 April 2013:

| | |
|---|---|
| Zlatko Koračević | Ivan Matasić |
| President of the Board | Member of the Board |