



HRVATSKA ELEKTROPRIVREDA d.d.

Condensed interim financial
information for the period ended

30 June 2016

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Independent Auditor's Report on Review of condensed Interim Financial Information

To the Owner of Hrvatska Elektroprivreda d.d.:

Introduction

We have reviewed the accompanying condensed interim statement of financial position of Hrvatska Elektroprivreda d.d. ("the Company") as of 30 June 2016 and the related condensed interim statement of comprehensive income, condensed interim statement of changes in equity and condensed interim statement of cash flows for the six months period then ended, and notes to the interim financial statements ("the condensed interim financial information").

Management is responsible for the preparation and fair presentation of these condensed interim financial information in accordance with IAS 34 Interim Financial Reporting.

Our responsibility is to express a conclusion on this condensed interim financial information based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying condensed interim financial information of the Company as at 30 June 2016 is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting*.

Emphasis of matter

As described in Note 1 to the condensed interim financial statements, the Company leased to its subsidiaries property, plant and equipment based on the finance lease agreements. These leases bear interests to the extent that the Company has acquired funds by external financing for construction of the corresponding asset. These receivables are carried at nominal value due to the specific organization of the HEP Group.

As described in Note 15 to the condensed interim financial statements, as at 30 June 2016, the Company stated clearing debt liability in the amount of HRK 818,034 thousand (31 December 2015: HRK 842,162 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of Finance for the use of funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the Company and the Ministry of Finance regarding the clearing debt, until the issuance of our Independent Auditor's Report on Review of condensed interim financial information, it has not been clearly defined whether it relates to a loan or a government grant.

As described in Note 19 to the condensed interim financial statements, provisions of the Water Management Act that came into force on 1 January 2010, raised a question on the ownership and legal status of the Company's property - reservoirs and ancillary facilities (canals, dams, etc.) used for generation of electricity from hydropower plants. Pursuant to the Water Act those property is defined as "Public water resources in general use as the property in ownership of the Republic of Croatia". The Republic of Croatia initiated several proceedings for registration of title to those properties, part of which were ruled in favour of the Republic of Croatia, part of them were rejected by the relevant courts, and part of them are in still in progress. The Company has filed a motion to the Constitutional Court to institute proceedings to review the constitutionality of Article 23 Paragraph 4 of the Water Management Act with the Constitution and upon conclusion of the procedure to annul the said provision.

During 2015, the Ministry of Agriculture has launched amendment procedure to the Water Act and the Ministry of Economy issued an opinion with approval of the Company's initiative to amend the Water Act.

In Zagreb, 29 August 2016

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

Irena Jadrešić, certified auditor

Zdenko Balen, Member of the
Management Board

Condensed interim statement of comprehensive income of HEP d.d.

For the six months period ended 30 June 2016

	Note	For the six months period ended	
		30 June 2016	30 June 2015
		HRK '000	HRK '000
		Unaudited	Unaudited
			Restated
Revenue from electricity sales	4	511,438	228,860
Revenue from electricity sales – related companies	16	2,326,909	2,466,180
Revenue from sale of gas on wholesale market	6	647,559	789,772
Revenue from sale of gas to related company HEP-Plin	16	76,887	106,024
Operating income – related companies	16	507,915	536,369
Sales revenue		4,070,708	4,127,205
Other operating income		28,373	51,279
Total operating income		4,099,081	4,178,484
Electricity purchase cost	7	(835,206)	(844,582)
Electricity purchase cost – related companies	16	(321,333)	(230,852)
Gas purchase cost - for sale on wholesale market		(705,672)	(811,260)
Staff cost		(41,445)	(43,660)
Depreciation and amortization costs		(35,278)	(49,438)
Remuneration cost for production and distribution of electricity - related companies	16	(1,139,423)	(1,367,083)
Other operating expenses		(269,314)	(273,520)
Total operating expenses		(3,347,671)	(3,620,395)
Operating profit		751,410	558,089
Financial income	5	834,163	774,660
Financial expenses	5	(216,292)	(220,039)
Net profit from financial activities	5	617,871	554,621
Profit before taxation		1,369,281	1,112,710
Corporate income tax expense		(151,013)	(170,058)
Profit for the period		1,218,268	942,652

Condensed interim statement of comprehensive income of HEP d.d. (continued)

For the six months period ended 30 June 2016

	For the six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited Restated
Profit for the period	1.218.268	942.652
Other comprehensive income		
Net gain on AFS financial assets	6,090	42,771
Foreign exchange differences	_____	(17,113)
<i>Net other comprehensive income to be reclassified to profit/(loss) in subsequent periods</i>	<i>6,090</i>	<i>25,658</i>
Other comprehensive income, net	6,090	25,658
Total comprehensive income for the period, net of tax	1,224,358	968,310

The accompanying notes form an integral part of this condensed interim statement of comprehensive income.

Signed on behalf of the Management Board on 29 August 2016:

Perica Jukić

Tomislav Rosandić

President of the Management Board

Member of the Management Board

Condensed interim statement of financial position of HEP d.d.

As at 30 June 2016

ASSETS	Note	30 June 2016	31 December 2015
		HRK '000 Unaudited	HRK '000 Audited
Non-current assets			
Property, plant and equipment	10	528,545	1,410,174
Assets under construction	10	618,270	447,646
Intangible assets		19,712	22,244
Investment property		14,487	14,487
Prepayments for property, plant and equipment		11,208	21,454
Investments in NE Krško		1,754,419	1,754,419
Investments and receivables from TE Plomin		252,101	252,101
Investments in subsidiaries	17	7,091,552	6,032,680
Available-for-sale and other investments		251,319	245,838
Long-term loans and deposits		46,793	28,476
Lease receivables from related companies	16	12,744,342	13,239,929
Long-term loans to related companies	16	71,229	79,129
Sub-loan receivables from related parties	16	818,964	897,024
Other receivables		720	776
Deferred tax assets		31,431	31,431
Derivative financial instruments		64,825	70,900
Total non-current assets		24,319,917	24,548,708
Current assets			
Inventories		630,500	753,624
Trade receivables	9	114,585	309,963
Current portion of long-term lease receivables from related companies	16	1,057,217	1,057,217
Current portion of long-term loans and deposits		330	330
Current portion of long-term loan receivables from related companies	16	146,033	147,893
Other short-term receivables		58,927	131,966
Receivables from related companies	16	6,497,619	6,180,063
Cash and cash equivalents		2,509,070	1,951,873
Total current assets		11,014,281	10,532,929
TOTAL ASSETS		35,334,198	35,081,637

Condensed interim statement of financial position of HEP d.d. (continued)

As at 30 June 2016

EQUITY AND LIABILITIES	Note	30 June 2016	31 December 2015
		HRK '000 Unaudited	HRK '000 Audited
Share capital	12	19,792,159	19,792,159
Revaluation reserves		106,926	100,836
Retained earnings	12	6,150,759	4,932,491
Total equity		26,049,844	24,825,486
Non-current liabilities			
Liabilities under issued bonds	14	4,115,262	4,223,883
Long-term loan liabilities	13	810,367	923,161
Other long-term liabilities	15	942,203	939,287
Long-term provisions		211,164	211,589
Deferred tax liabilities		21,278	21,816
Total non-current liabilities		6,100,274	6,319,736
Current liabilities			
Trade payables	11	351,524	681,827
Current portion of long-term bonds	14	93,380	93,380
Current portion of long-term loans	13	377,381	383,525
Taxes and contributions		122,736	114,512
Interest payable		42,893	45,692
Short-term liabilities to related companies	16	2,180,922	2,578,573
Liabilities to employees		6,325	21,061
Other short-term liabilities		8,919	17,845
Total current liabilities		3,184,080	3,936,415
TOTAL EQUITY AND LIABILITIES		35,334,198	35,081,637

The accompanying notes form an integral part of this condensed interim statement of financial position.

Signed on behalf of the Management Board on 29 August 2016:

Perica Jukić

Tomislav Rosandić

President of the Management Board

Member of the Management Board

Condensed interim statement of changes in equity of HEP d.d.

For the six months period ended 30 June 2016

	Share capital	Revaluation reserves	Retained earnings	Total equity
	HRK '000	HRK '000	HRK '000	HRK '000
			Restated	Restated
Balance at 1 January 2015	19,792,159	54,947	3,328,974	23,176,080
Profit for the period	-	-	942,652	942,652
Other comprehensive income	-	25,658	-	25,658
Total comprehensive income	-	25,658	942,652	968,310
Loss carried forward - APO d.o.o.	-	-	(21,424)	(21,424)
Balance as at 30 June 2015, unaudited	19,792,159	80,605	4,250,202	24,122,966
Balance at 1 January 2016	19,792,159	100,836	4,932,491	24,825,486
Profit for the period	-	-	1,218,268	1,218,268
Other comprehensive income	-	6,090	-	6,090
Total comprehensive income	-	6,090	1,218,268	1,224,358
Balance as at 30 June 2016, unaudited	19,792,159	106,926	6,150,759	26,049,844

The accompanying notes form an integral part of this condensed interim statement of changes in equity.

Signed on behalf of the Management Board on 29 August 2016:

Perica Jukić

Tomislav Rosandić

President of the Management Board

Member of the Management Board

Condensed interim statement of cash flows of HEP d.d.

For the six months period ended 30 June 2016

	For the six months period ended	
	30 June 2016	30 June 2015
	HRK '000 Unaudited	HRK '000 Unaudited
Cash flows from operating activities		
Profit for the period	1,218,268	941,360
Corporate income tax expense recognized in profit	151,013	170,058
Net profit from financial activities	(617,871)	(554,913)
Depreciation and amortization	35,278	156,540
Increase / (decrease) in provisions	(425)	274
Increase in impairment of doubtful and disputable receivables	6,227	23,545
<i>Operating cash flows before movements in working capital</i>	<u>792,490</u>	<u>736,864</u>
Decrease in trade receivables	189,151	309,231
(Increase) in receivables from related companies	(317,556)	(607,136)
Decrease in inventories	123,124	43,383
Decrease/(Increase) in other short-term assets	73,039	(103,232)
(Increase) in other long-term assets	(272,992)	(60,902)
(Decrease) in trade payables	(330,303)	(171,154)
(Decrease) in other liabilities	(155,496)	(250,139)
(Decrease) in liabilities to subsidiaries	(397,651)	(134,660)
Cash generated from operations	<u>(296,194)</u>	<u>(237,745)</u>
Corporate income tax (paid)	(27,704)	(118,909)
Interests paid	(140,040)	(144,562)
NET CASH FROM OPERATING ACTIVITIES	<u>(463,938)</u>	<u>(501,216)</u>
INVESTING ACTIVITIES		
Interests receipts	86,619	101,461
Transfer of assets in subsidiaries and write-offs	247,668	3,770
(Increase) in property, plant and equipment	(174,689)	(101,269)
Collection of receivables from related companies	583,407	648,310
NET CASH USED IN INVESTING ACTIVITIES	<u>743,005</u>	<u>652,272</u>

Condensed interim statement of cash flows of HEP d.d. (continued)

For the six months period ended 30 June 2016

	For the six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
FINANCING ACTIVITIES		
Dividends receipts from related companies	424,534	5,735
Bond repayments	(46,691)	(46,690)
Long-term loans received	90,398	26,611
Repayments of long-term loans	(190,111)	(219,130)
NET CASH USED IN FINANCING ACTIVITIES	278,130	(233,474)
NET INCREASE / (DECREASE) IN CASH AND CASH EQUIVALENTS	557,197	(82,418)
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE PERIOD	1,951,873	730,693
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD	2,509,070	648,275

The accompanying notes form an integral part of this condensed interim statement of changes in equity.

Signed on behalf of the Management Board on 29 August 2016:

Perica Jukić

Tomislav Rosandić

President of the Management Board

Member of the Management Board

1. BASIS OF PREPARATION

These condensed interim financial information are prepared in accordance with International Accounting Standard 34 *Interim Financial Reporting*. The preparation of the unaudited condensed interim financial information for the six months period ended 30 June 2016 requires from management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed interim financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on the information available as at the date of the condensed interim financial information, and actual results could differ from those estimates. The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of revision and future periods if the revision affects both current and future periods.

The annual financial statements of Hrvatska Elektroprivreda d.d. are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by EU. The condensed interim financial information have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' ('IAS 34'). The condensed interim financial information for the six month period ended 30 June 2016 have been prepared under the same accounting policies as the financial statements for the year ended 31 December 2015.

Certain information and disclosures normally included in the annual financial statements prepared in accordance with IFRS adopted by EU have been condensed or omitted as permitted by IAS 34. The condensed interim statement of financial position as at 30 June 2016 was derived from audited annual financial statements as at 31 December 2015, but does not include all disclosures required by IFRS adopted by EU. However, the Company's management believes that disclosures in these condensed interim financial information are adequate to make the information presented not misleading.

Leases

Property, plant and equipment and intangible assets are leased to subsidiaries of the Company at book value. Leases of property, plant and equipment and intangible assets are classified as finance leases since all the risks and awards of the ownership are transferred to the lessee. Maturity date of lease is equal to remaining useful depreciation life of leased assets.

Lease liabilities are stated with the related companies within long-term liabilities. Leases bears interests to the extent that the Company has acquired funds by external financing for construction of the corresponding asset. The fair value of leases has not been estimated due to the specific organization of the HEP Group and with the aim of disclosing underlying assets at their original book value at which they were acquired by the Group.

Consequently, for a better understanding of the Company, the accompanying condensed interim financial information should be read in conjunction with the condensed consolidated interim financial statements of the HEP Group.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

Adoption of new and revised International Financial Reporting Standards

The accounting policies adopted in the preparation of the accompanying unaudited condensed interim financial information are consistent with those followed in the preparation of the Company's annual financial statements for the year ended 31 December 2015, except for the adoption of new standards and interpretations effective as of 1 January 2016. The Company has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

Although these new standards and amendments apply for the first time in 2016, they do not have a material impact on the accompanying condensed interim financial information for the period ended 30 June 2016. The nature and the impact of each new standard or amendment are described below:

Standards and Interpretations effective for the current period

- Annual Improvements to IFRSs 2012–2014 Cycle
 - IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
 - IFRS 7 Financial Instruments: Disclosures (with consequential amendments to IFRS 1)
 - IAS 19 Employee Benefits
 - IAS 34 Interim Financial Reporting
- Amendments to IFRS 11 Accounting for Acquisitions of Interests in Joint Operations (issued in May 2014)
- Amendments to IAS 1 Disclosure Initiative (issued in December 2014)
- Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation (issued in May 2014)
- Amendments to IAS 16 and IAS 41 Agriculture: Bearer Plants (issued in June 2014)
- Amendments to IAS 27 Equity Method in Separate Financial Statements (issued in August 2014)
- Amendments to IAS 19 Defined Benefit Plans: Employee Contributions – IAS 19 requires subjects to consider employee or third party contributions in accounting defined earning. This amendment is effective in EU for accounting periods beginning on or after 1 February 2015, with earlier application permitted.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Standards and Interpretations effective for the current period (continued)

- Annual Improvements 2010-2012 Cycle, these amendments are effective in EU for accounting periods beginning on or after 1 February 2015, with earlier application permitted. They include:
 - IFRS 2 Share-based Payment,
 - IFRS 3 Business Combinations,
 - IFRS 8 Operating Segments,
 - IFRS 13 Fair Value Measurement,
 - IAS 16 Property, Plant and Equipment and IAS 38 Intangible assets,
 - IAS 24 Related Party Disclosures;

Application of the above mentioned Standards did not have effect on the on the accompanying condensed interim financial information for the period ended 30 June 2016.

New and revised IFRSs issued by the IASB but not yet adopted by the EU

The following standards and amendments to the existing standards have not been adopted by the EU yet:

- IFRS 9 Financial Instruments – in July 2014, IASB issued a final version of IFRS 9 Financial Instruments which reflects all phases of the financial instruments replacing IAS 39 Financial Instruments: Recognition and measurement and all other preceding versions IFRS 9. It is still not defined for which period IFRS 9 will be effective. The application of this standard will affect the classification and measurement of financial instruments.
- IFRS 14 Regulatory Deferral Accounts – this standard relates to subjects that operate on regulated markets and are applying IFRS for the first time. IFRS 14 is effective for the annual period beginning on or after 1 January 2016. EU will not adopt this standard.
- IFRS 15 Revenue from Contracts with Customers - IFRS 15 was issued in May 2014 and represents a new model in five steps that relate to revenue that results from contracts with customers. IFRS 15 is effective for the annual period beginning on or after 1 January 2018, earlier applications are permitted.
- IFRS 16 Leases – IFRS 16 was issued in January 2016 and represents and specifies recognition, measurement and disclosure of leases. IFRS 16 is effective for the annual period beginning on or after 1 January 2019, earlier applications are permitted.
- Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (issued in September 2014). The application of this standard has been postponed until further notice.
- Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception (issued in December 2014).
- Amendments to IFRS 11 Accounting for Acquisitions of Interests in Joint Operations (issued in May 2014).
- Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses (issued in January 2016).
- Amendments to IAS 7 – part of its disclosure initiative (issued in January 2016)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

New and revised IFRSs issued by the IASB but not yet adopted by the EU (continued)

- Clarifications to IFRS 15 Revenue from Contracts with Customers (issued in April 2016).
- Amendments to IFRS 2 – classification and measurement of share based payment transactions (issued in June 2016).

The Company's Management anticipates that the application of said standards, amendments and interpretations will not have a materially significant impact on the financial statements in the period of their initial application, except for IFRS 15 and IFRS 9 for which the Company's Management is conducting detail analysis (still in progress) regarding possible effects from the application of this Standard on the financial statements.

Use of estimates in preparation of the condensed interim financial information

Preparation of the condensed interim financial information in conformity with International Accounting Standard 34 Interim Financial Reporting, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingent liabilities. Estimates used in preparation of these condensed interim financial information relate to employee benefits, impairment of assets, determination of fair values of assets and liabilities and estimated decommissioning costs. Future events may occur which could cause changes in the assumptions used for making these estimates. The effect of any changes in estimates will be recorded in the financial statements, when determinable.

There were no changes in the use of estimates or critical judgments applied in preparation of the annual financial statements for the year ended 31 December 2015 with respect of those applied in preparation of these condensed interim financial information.

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS***Restatements*****Investment in Nuclear Power Plant Krško d.o.o.**

Based on the adoption of International Financial Reporting Standards (IFRS) 11 Joint Arrangements, which replaced the International Accounting Standard (IAS) 31 Interests in joint ventures, investment in NEK is classified in accordance with IFRS 11 as a joint operation. In 2015 the Company changed the policy of monitoring joint operation in NEK from the method of recognition of the Company's share in assets, liabilities, revenues and expenses in NEK in its financial statements, to the equity method. In order to eliminate possible concerns of individual government agencies (FINA, the Ministry of Finance, Central Bureau of Statistics, etc.) on the information in the separate financial statements of the Company, and in accordance with the provisions of IAS 1, point 19 and point 20, the Management Board adopted a decision to change that policy.

In its consolidated financial statements, the Company still recognizes its investment in NEK in accordance with IFRS 11.

Restatements in the financial statements as at 30 June 2015***Statement of comprehensive income for the year ended 30 June 2015***

	30 June 2015 before restatement	NEK d.o.o.	30 June 2015 after restatement
	HRK '000	HRK '000	HRK '000
Other operating income	54,093	(2,814)	51,279
Total operating income	4,181,298	(2,814)	4,178,484
Electricity purchase cost	510,493	334,089	844,582
Fuel cost NEK d.o.o.	48,476	(48,476)	0
Staff cost	111,282	(67,622)	43,660
Depreciation and amortization costs	156,540	(107,102)	49,438
Other operating expenses	2,798,002	(115,287)	2,682,715
Total operating expenses	3,624,793	(4,398)	3,620,395
Operating profit	556,505	1,584	558,089
Financial income	783,285	(2,124)	781,161
Financial expenses	228,372	(1,832)	226,540
Net loss from financial activities	554,913	(292)	554,621
Profit before taxation	1,111,418	1,292	1,112,710
Corporate income tax expense	170,058	0	170,058
Profit for the period	941,360	1,292	942,652

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

3. REVENUE FROM ELECTRICITY SALES

	For the six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
		Restated
Revenue from electricity export	482,798	226,845
Revenue from electricity sales in country	28,640	2,015
	<u>511,438</u>	<u>228,860</u>

4. FINANCIAL INCOME AND EXPENSES

	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
		Restated
Financial income		
Interest	86,619	102,932
Foreign currency exchange gains	105,112	52,820
Dividend from subsidiary and associated companies	614,214	270,735
Income from dividend	26	17
Fair value swap	-	347,616
Other financial income	28,192	540
Total financial income	<u>834,163</u>	<u>774,660</u>
Financial expenses		
Interest	(122,355)	(138,061)
Foreign exchange losses	(53,772)	(80,599)
Fair value swap	(33,633)	-
Fair value of shares	(71)	(1,127)
Other financial expenses	(6,461)	(252)
Total financial expenses	<u>(216,292)</u>	<u>(220,039)</u>
Net profit from financial activities	<u>617,871</u>	<u>554,621</u>

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

5. GAS SALES

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

In the period from 1 April 2014 to 31 March 2015 the Company agreed rent of capacities of 3.600 million kWh, in the period of 1 April 2015 to 31 March 2016, the Company agreed rent of capacities of rent of 3.550 million kWh, and in the period from 1 April 2016 to 31 March 2017 the Company agreed rent of capacities of 3.500 million kWh.

The Company as a supplier on the wholesale market sells gas as public service and under regulated conditions to local suppliers for household customers, and is obligated to provide secure and reliable gas supply.

6. ELECTRICITY PURCHASE COST

The cost of electricity purchases for the six months ended 30 June 2016 (including related companies) amounted to HRK 1,156,539 thousand (for the same period last year: HRK 1,075,434 thousand). The costs are increased compared to the same period last year due to unfavourable hydrological conditions and consequently growth of import.

8. CORPORATE INCOME TAX EXPENSE

Corporate income tax expense and current taxes during the six months period ended 30 June 2016 and 30 June 2015 are accounted on the basis of actual results and the profit tax rate of 20%.

9. TRADE RECEIVABLES

Trade receivables stated in the condensed interim statement of financial position as at 30 June 2016 in the amount of HRK 114,585 mostly relate to receivables for the sale of gas to customers in the wholesale market. Trade receivables stated as at 31 December 2015 were significantly higher compared to those stated as at 30 June 2016 due to the heating season.

10. NON-CURRENT ASSETS

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at 30 June 2016 amounts to HRK 528,545 thousand (31 December 2015: HRK 1,410,174 thousand). Decrease mainly refers to the transfer of power facilities in the amount of HRK undertaken by HAC d.o.o. to the subsidiary HEP Operator distribucijskog sustava d.o.o. in the amount of HRK 654,123 thousand and to the subsidiary Hrvatski operator prijenosnog sustava d.o.o. in the amount of HRK 158,197 thousand.

10. NON-CURRENT ASSETS (CONTINUED)

ASSETS UNDER CONSTRUCTION

Assets under construction stated as at 30 June 2016 amounted to HRK 618,270 thousand, and the most important relates to the preparatory work for construction of a replacement block TE Plomin in the amount of HRK 211,750 thousand, investment in the project EDM/ECM in the amount of HRK 112,481 thousand and investment in the preparatory work for construction of HE Ombla in the amount of HRK 45,807 thousand and to investment in cogeneration plants on forest biomass BE-TO Sisak in the amount of HRK 97,156 thousand and BE-TO Osijek in the amount of HRK 89,641 thousand.

11. TRADE PAYABLES

Trade payables as at 30 June 2016 amount to HRK 351,524 thousand (31 December 2015: HRK 681,827 thousand). The difference is largely conditioned by the increased supply of gas in the heating season.

12. EQUITY AND RESERVES

During first registration on 12 December 1994, the Company's equity was registered in the amount of (Deutsche Mark) DEM 5,784,832 thousand. By subsequent change in registration of the Company dated 19 July 1995, Company's equity was stated in Croatian Kuna in the amount of HRK 19,792,159 thousand. The share capital consists of 10,995,644 ordinary shares with individual nominal value of HRK 1,800.00.

Retained earnings in the amount of HRK 6,150,759 thousand consists of the profit for the period in the amount of HRK 1,218,268 thousand, retained earnings in the amount of HRK 4,546,881 thousand and reserves in the amount of HRK 385,610 thousand.

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

13. LONG-TERM LOAN LIABILITIES

	Interest rate	30 June 2016	31 December 2015
		HRK '000	HRK '000
		Unaudited	Audited
Domestic bank loans	EURIBOR+ (1.00%-2.90 %)	1,011,485	1,219,772
Foreign bank loans	Fixed 0.07%	179,030	90,296
Total		1,190,515	1,310,068
Deferred loan originated fees		(2,767)	(3,382)
Total long-term loans		1,187,748	1,306,686
Current portion for long-term loans		(377,381)	(383,525)
Long-term portion		810,367	923,161

Loans from domestic banks are secured by bills of exchange and promissory notes, except for one club loan for which the Company is obliged to meet the required level of financial indicators (covenants) on annual and semi-annual basis: tangible net worth, EBITDA to net finance charges, total net borrowings to tangible net worth.

The Company's primary goal related to risks resulting from covenants is to protect the Company from possible defaults, respectively early maturity of loan liabilities. The agreed covenants are monitored and calculated based on the projected Balance sheet and the Statement of comprehensive income.

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

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

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

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

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

13. LONG-TERM LOAN LIABILITIES (continued)

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

At 30 June 2016 covenants were not breached and the Company has met all contractual financial indicators.

The Company's total exposure to loan liabilities subject to covenant conditions as at 30 June 2016 amounts to EUR 88,235 thousand.

At 30 June 2016 the Company doesn't have any liabilities covered by sovereign loan guarantees.

Loans in use

In the first six months of 2016, the Company had available funds from long-term loan approved by KfW Entwicklungsbank in the amount of EUR 50 million for the financing of energy efficiency and renewable energy projects.

As of 30 June 2016 KfW loan balance was EUR 23,830 thousand, and the amount of EUR 26,170 thousand was unutilised.

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

	HRK '000
2016	188,690
2017	406,275
2018	426,330
2019	134,659
2020	34,561
After 2020	-
Total	<u>1,190,515</u>

Overview of long-term loans stated in foreign currency (in thousands) is shown as follows:

Currency	30 June 2016	31 December 2015
	HRK '000	HRK '000
EUR	158,466	171,586

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

13. LONG-TERM LOAN LIABILITIES (continued)

Available financing sources

For the purpose of providing solvency reserves in the following mid-term period the Company has concluded with domestic banks multi-purpose overdraft agreements in the total amount up to HRK 1 billion. Funds from agreed overdrafts the Company may use as short-term loans, as well as for issuance of guarantees, letters of credit and letters of intention in accordance with the Company's needs. In the 2nd quarter of 2016 the Company, due to good liquidity did not use funds from preapproved mid-term multipurpose overdraft agreements, so no balance of short-term loans is reported as at 30 June 2016. However, the Company is using preapproved funds for issuing guarantees for its subsidiaries on regular basis. Also, the Company has signed overdraft agreement for reverse factoring in the amount of EUR 50 million until 31 December 2016.

As of 30 June 2016 the Company has available funds from above stated overdraft agreements in total amount of up to HRK 1,334,070 thousand.

14. LIABILITIES UNDER ISSUED BONDS

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Nominal value of 2006 bonds - domestic	139,720	186,410
Discount value	(52)	(84)
Current portion of bonds	(93,380)	(93,380)
	46,288	92,946
Nominal value of 2012 bonds issued abroad	498,617	3,008,746
Repurchase of bonds (83.37%)	-	(2,806,955)
Exchange differences	(7,988)	296,826
	490,629	498,617
Nominal value of 2015 bonds issued abroad	3,706,988	3,703,533
Exchange differences	(59,384)	3,455
Discount value	(47,268)	(50,941)
	3,600,336	3,656,047
Accrued bond costs	(21,991)	(23,727)
	3,578,345	3,632,320
Total liabilities for issued bonds	4,115,262	4,223,883

14. LIABILITIES UNDER ISSUED BONDS (continued)

Bonds issued in the Republic of Croatia

Bonds in the amount of HRK 700,000 thousand, issued at the end of 2007, are repayable in 15 semi-annual instalments, commencing three years from the date of issue, and are bearing fixed interest 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. Bonds have maturity of 5 years and are bearing fixed interest of 6%. Bonds of HEP d.d. are listed at Luxembourg stock - exchange and they are actively traded.

Refinancing

In October 2015, bonds issued in 2012 were refinanced from the new bond issue and repaid 83.37% of the principal respectively USD 416,852 thousand. The amount of outstanding principal on bonds issued in 2012, on 31 December 2015 amounted to USD 83,148 thousand.

Cross currency swap

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

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

As at 30 June 2016, agreement on the cross currency swap from 2012 is in effect for undue principal in the amount of USD 83,148 thousand, until its outermost maturity date at 9 November 2017.

New bond issue

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

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

14. LIABILITIES UNDER ISSUED BONDS (continued)

Cross currency swap

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

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

Derivative financial instruments

Cross currency swap

The Company has concluded cross currency swap agreements, by which liabilities upon bonds issued abroad in 2012 and 2015 in USD is transformed in EUR for all period of bond duration, respectively until its outermost maturity dates. The purpose of this swaps was, beside reduce of the currency risk, recommendations of credit agencies related to strategic management of currency risks in order to reduce impact on the Company's business result. Annual interest rate paid by the Company semi-annually for Bonds issued in 2012 is fixed and amounts to 6.53% and for Bonds issued in 2015 weighted fixed interest rate of 4.851%.

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

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

After a final maturity of derivative financial instruments, subject receivables or liabilities will be debited to expenses or credited to revenues of the Group.

As at 30 June 2016 by this method of calculation, on bonds issued in 2012 it is stated fair value of assets in the amount of HRK 64,825 thousand (Note 18).

As at 30 June 2016 by this method of calculation, on bonds issued in 2015 it is stated fair value of liabilities in the amount of HRK 109,435 thousand (Note 18).

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

15. OTHER LONG-TERM LIABILITIES

Other long-term liabilities as at 30 June 2016 amounted to HRK 942,203 thousand, and consist of liabilities for assets funded from the clearing debt in the amount of HRK 818,034 thousand and other liabilities in the amount of HRK 124,169 thousand.

At 30 June 2016 the Company stated clearing debt liability in the amount of HRK 818,034 thousand (31 December 2015: HRK 842,162 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of Finance for the use of funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the Company and the Ministry of Finance regarding the clearing debt, it has not been clearly defined whether it relates to a loan or a government grant.

16. RELATED PARTY TRANSACTIONS

Related party transactions refer to subsidiaries in sole ownership of the Company and to related NE Krško d.o.o. 50% owned by the Company. The Company also holds 50% of ownership in the company LNG Hrvatska d.o.o..

The electricity generated by NEK is delivered to HEP d.d. at 50% of total generated quantities and at prices determined in accordance with the total generation costs.

Receivables and liabilities, and income and expenses are presented in the table below:

NE Krško d.o.o.

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Liabilities for purchased electricity	51,692	62,830

	Six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
Costs of purchased electricity	312,681	334,089

LNG Hrvatska d.o.o.

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Loan receivables	44,163	25,840

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

Related party transactions are listed below:

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

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

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

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

/v/ Long-term receivables from related companies arise from financial lease of property, plant and equipment to related companies, except HOPS. Lease is paid monthly according to depreciation of leased assets. The Company also has receivables from related companies for apartments sold to employees.

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

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	Six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
Revenues from sale of electricity		
Revenues from sale of electricity to HEP-ODS	1,084,082	1,250,068
Revenues from sale of electricity to customers of HEP-Opkrba d.o.o.	1,183,648	1,190,857
Revenues from sale of electricity to HEP-Energija d.o.o. Ljubljana	33,453	11,560
Revenues from sale of electricity to HEP-Trade d.o.o. Beograd	5,578	-
Revenues from sale of electricity to HEP-Trade d.o.o. Mostar	13,658	-
Revenues from sale of electricity to other companies within HEP Group	6,490	5,334
Revenues from sale of electricity – HOPS d.o.o.	-	8,361
	2,326,909	2,466,180
Revenues from sale of gas - HEP Plin d.o.o.	76,887	106,024
Operating income		
Revenues from invoiced losses on distribution network	295,488	335,674
Revenues from administrative services	77,212	80,443
Revenues from balancing energy	1,095	1,007
Revenues from lease of business services	5,801	4,784
Revenues from sale of CO2 emissions	125,078	110,188
Other revenues	3,241	4,273
	507,915	536,369
Revenues from sale to related companies	2,911,711	3,108,573
Financial income		
Interest income on lease of assets	60,863	73,879
Interest income on loans to related companies	19,818	26,121
	80,681	100,000

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	Six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
Electricity purchase costs – related companies	Unaudited	Unaudited
TE Plomin d.o.o.	186,258	230,005
HEP Energija d.o.o. Ljubljana	1,032	3
HEP-Trade d.o.o. Beograd	562	113
HEP-Trade d.o.o. Mostar	133,481	539
HOPS d.o.o.	-	192
	<u>321,333</u>	<u>230,852</u>

	Six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
Costs	Unaudited	Unaudited
HEP Proizvodnja d.o.o. - fee for generation of electricity	961,767	1,183,385
HEP Opskrba d.o.o. - fee for supply of electricity	19,460	18,789
HEP Opskrba d.o.o. - fee for supply of electricity – HEP OIE	144,773	134,705
HEP Trgovina d.o.o.	6,434	5,491
Electricity balancing costs	1,242	22,460
Supply of gas	2,679	2,207
Costs of HEP for losses on distribution network	3,068	46
	<u>1,139,423</u>	<u>1,367,083</u>

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

Long-term receivables	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Lease receivables		
HEP Operator distribucijskog sustava d.o.o.	6,626,322	6,889,940
HEP Proizvodnja d.o.o.	6,170,297	6,371,366
HEP Toplinarstvo d.o.o.	720,719	745,212
HEP Upravljanje imovinom d.o.o.	112,147	112,457
HEP Plin d.o.o.	140,468	144,681
HEP Noc d.o.o.	12,109	12,484
HEP Opskrba d.o.o.	3,792	4,231
HEP Trgovina d.o.o.	719	755
HEP Esco d.o.o.	1,722	1,987
Program Sava d.o.o.	318	325
HEP Opskrba plinom d.o.o.	254	301
	13,788,867	14,283,739
Receivables for sold flats		
HEP Operator distribucijskog sustava d.o.o.	6,974	7,353
HEP Proizvodnja d.o.o.	4,208	4,386
HOPS d.o.o.	1,336	1,457
HEP Toplinarstvo d.o.o.	174	211
	12,692	13,407
	13,801,559	14,297,146
Current portion of lease	(1,057,217)	(1,057,217)
Long-term portion	12,744,342	13,239,929

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

Long-term loans to related companies	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
HEP-Toplinarstvo d.o.o.	86,900	94,800
HEP-Opkrba d.o.o.	129	129
	87,029	94,929
Current portion	(15,800)	(15,800)
	71,229	79,129
Receivables from related companies – for KfW loan funds	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Receivables for sub-loans HEP ESCO d.o.o.	55,350	55,350
Receivables for sub-loans HOPS	893,847	973,767
	949,197	1,029,117
Current portion	(130,233)	(132,093)
	818,964	897,024

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

Short-term receivables	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
HEP Operator distribucijskog sustava d.o.o. – sold electricity and interests	272,213	277,777
HEP Operatora distribucijskog sustava d.o.o. – losses on distribution network	46,904	85,459
HEP Opskrba d.o.o. - sold electricity and interests	479,934	456,977
HOPS d.o.o. – losses on transmission network	25,620	37,047
HEP Energija d.o.o. Ljubljana - sold electricity	15,250	9,203
HEP Trade d.o.o. Beograd - sold electricity	1,842	3,007
HEP Trade d.o.o. Mostar - sold electricity	1,026	-
Electricity balancing	427	2,837
	843,216	872,307
Costs of common functions		
HEP Proizvodnja d.o.o.	4,670	604
HEP Operator distribucijskog sustava d.o.o.	8,649	6,634
HEP Toplinarstvo d.o.o.	3,235	1,232
HEP Plin d.o.o.	15,300	12,843
HEP Upravljanje imovinom d.o.o.	321	9,720
HEP Trgovina d.o.o.	3,406	2,066
HEP Opskrba d.o.o.	839	2,679
HEP NOC	251	11
ESCO d.o.o.	585	659
Program Sava d.o.o.	318	1,180
HEP Telekomunikacije d.o.o.	225	1,342
HEP Opskrba plinom d.o.o.	125	541
	37,924	39,511

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Receivables for leased assets		
HEP Proizvodnja d.o.o.	40,094	39,026
HEP Toplinarstvo d.o.o.	42,084	8,260
HEP Operator distribucijskog sustava d.o.o.	342,516	288,464
HEP Plin d.o.o.	32,197	33,394
HEP Upravljanje imovinom d.o.o.	243	22,247
HEP NOC	9,360	9,967
HEP Trgovina d.o.o.	65	61
HEP Opskrba d.o.o.	84	205
HEP Esco d.o.o.	52	98
Program Sava d.o.o.	13	-
HEP Opskrba plinom d.o.o.	7	-
	466,715	401,722
Other short-term receivables	80,989	168,713
Receivables for paid investments and other receivables		
HEP Proizvodnja d.o.o.	2,615,078	2,389,041
HOPS d.o.o.	70,014	84,223
HEP Operator distribucijskog sustava d.o.o.	1,598,107	1,439,150
HEP Toplinarstvo d.o.o.	116,404	86,563
HEP Plin d.o.o.	29,288	39,339
HEP ESCO d.o.o.	1,085	1,028
HEP NOC	951	840
HEP Upravljanje imovinom d.o.o.	1,369	34,332
HEP Opskrba d.o.o.	718	450
Program Sava d.o.o.	8,749	8,736
HEP Trgovina d.o.o.	376	-
HEP Telekomunikacije d.o.o.	1	1
HEP Opskrba plinom d.o.o.	64	41
Plomin Holding d.o.o.	1,350	1,350
Hrvatski centar za čistiju proizvodnju	1,195	1,192
	4,444,749	4,086,286

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Receivables for sold investment and other material		
HEP Operator distribucijskog sustava d.o.o.	313,473	313,473
HEP Proizvodnja d.o.o.	257,847	257,847
HEP Plin d.o.o.	2,680	2,680
HEP Toplinarstvo d.o.o.	99	99
	574,099	574,099
Other receivables		
HEP Plin d.o.o.	18,240	18,195
HEP Noc d.o.o.	14,675	13,564
	32,915	31,759
Receivables from TE Plomin d.o.o.		
current portion of long-term receivables	2,127	2,127
other receivables	-	532
	2,127	2,659
Loan receivables from HEP Trade d.o.o. Beograd	2,282	2,313
Loan receivables from HEP KS	761	694
Loan receivables from HEP Trade d.o.o. Mostar	6,842	-
Receivables from Trgovina d.o.o.	5,000	-
	14,885	3,007
	6,497,619	6,180,063

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Short-term liabilities		
HEP Opskrba – for electricity supply fee	8,453	11,339
HEP Proizvodnja d.o.o. – for electricity generation fee	537,033	603,632
HEP Opskrba d.o.o. – supply fee from renewable energy resources	22,890	24,553
HEP Trgovina d.o.o. – fee for services of optimizing the structure of the electricity power source	1,427	134
HOPS d.o.o. – for losses on transmission network	3,842	-
Liabilities for energy balancing	693	-
HEP Proizvodnja – liabilities of HEP-a d.d. based on the cession agreement	966,235	966,235
HEP Opskrba plinom – liabilities for gas supply	664	987
Other	3,771	21,436
	<u>1,545,008</u>	<u>1,628,316</u>

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	30 June 2016	31 December 2015
	Unaudited	Audited
Other liabilities		
Liabilities to HEP ODS d.o.o. - connectors	189,816	193,307
Liabilities to HEP ODS d.o.o. – funds allocated based on the Agreement on mutual relations dated 1 July 2014	303,373	648,032
Liabilities toward HEP ODS d.o.o. – paid investments	24,405	21,505
Liabilities to other companies	29,792	13,865
	547,386	876,709
TE Plomin d.o.o. for delivered electricity	52,185	73,418
HEP MagyarorszagEnergiakft for delivered electricity	-	130
Liabilities to HEP Trade Mostar – non-invoiced electricity	36,343	-
	88,528	73,548
Total short-term liabilities	2,180,922	2,578,573

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	Sales revenue		Purchase costs	
	Six months period ended		Six months period ended	
HRK '000	30 June 2016	30 June 2015	30 June 2016	30 June 2015
	Unaudited	Unaudited	Unaudited	Unaudited
Companies controlled by the State	HRK '000	HRK '000	HRK '000	HRK '000
Hrvatske Željeznice	35,492	35,342	-	-
INA d.d.	38,777	41,224	669,689	805,079
Prirodni Plin	-	-	-	-
Plinacro	-	-	51,194	34,227
Croatia osiguranje	-	-	65	143
Hrvatska pošta	3	1	6,994	7,396
Hrvatske šume	-	-	1,173	1,304
Jadrolinija	-	-	-	-
Narodne novine	529	584	58	76
Hrvatska radiotelevizija	2,588	2,832	36	26
Plovput	-	-	-	-
Croatia Airlines	235	215	-	-
Petrokemija Kutina	6,982	8,160	-	-
Ministry of Foreign Affairs	-	-	-	-
Ministry of Defence	-	-	-	-
Ministry of the Interior	4,691	-	-	-
Elementary and high schools	5,155	5,466	-	-
Judicial institutions	1,327	42	-	-
Colleges and universities	3,136	1,886	12	70
Legislative, executive and other bodies of Republic of Croatia	2,306	2,165	-	-
Health institutions and organizations	17,696	17,222	-	-
Other users	-	1,175	2,997	439
TOTAL	118,917	116,314	732,218	848,760

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

16. RELATED PARTY TRANSACTIONS (continued)

	Receivables		Liabilities	
	30 June 2016	31 December 2015	30 June 2016	31 December 2015
	Unaudited	Audited	Unaudited	Audited
Companies controlled by the State	HRK '000	HRK '000	HRK '000	HRK '000
Ministry of Finance	-	-	-	-
INA-Industrija nafte	-	-	94,842	128,506
Croatia osiguranje	-	-	5	47
Hrvatska pošta	-	-	17	1,419
Narodne novine	-	-	9	7
Other	66	92	17,464	26,020
	66	92	112,337	155,999

Remunerations for members of the Board and executive directors of the Company:

	Six months period ended	
	30 June 2016	30 June 2015
	HRK '000	HRK '000
	Unaudited	Unaudited
Gross salaries	3,607	3,492
Contributions for pension insurance	813	808
Benefits in kind	458	547
	4,878	4,847

There were no other payments to the Management Board members in addition to regular wages and benefits in kind.

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

17. SUBSIDIARIES

As of 30 June 2016 the Company owned the following subsidiaries:

Subsidiary	Country	Ownership interest in %	Principal activity
HEP-Proizvodnja d.o.o.	Croatia	100	Electricity generation and heating
Hrvatski operator prijenosnog sustava d.o.o.	Croatia	100	Electricity transmission
HEP-Operator distribucijskog sustava d.o.o.	Croatia	100	Electricity distribution
HEP Opskrba d.o.o.	Croatia	100	Electricity supply
HEP-Toplinarstvo d.o.o.	Croatia	100	Thermal power generation and distribution
HEP-Plin d.o.o.	Croatia	100	Gas distribution
TE Plomin d.o.o.	Croatia	100	Electricity generation
HEP ESCO d.o.o.	Croatia	100	Financing of energy efficiency projects Development of infrastructure in area around Plomin
Plomin Holding d.o.o.	Croatia	100	Maintenance of hydro power plants equipment
CS Buško Blato d.o.o.	BH	100	
HEP Upravljanje imovinom d.o.o.	Croatia	100	Accommodation and recreation services
HEP Trgovina d.o.o.	Croatia	100	Electrical energy trading and optimization of power plants production
HEP-Energija d.o.o. Ljubljana	Slovenia	100	Electricity trading
HEP- MagyarorszagEnergia KFT	Hungary	100	Electricity trading
HEP – Trade d.o.o. Mostar	BH	100	Electricity trading
HEP KS sh.p.k	Kosovo	100	Electricity trading
HEP Trade d.o.o. Belgrade	Serbia	100	Electricity trading
Program Sava d.o.o.	Croatia	100	Spatial planning, design, construction and supervision
HEP-Telekomunikacije d.o.o.	Croatia	79,94	Telecommunication services
HEP-Opskrba plinom d.o.o.	Croatia	100	Gas distribution
Hrvatski centar za čistiju proizvodnju	Croatia	100	Training and consulting in the field of cleaner production and environmental management systems

The majority of these subsidiaries were founded for the purpose of reorganization and restructuring of the core business activities driven by the new energy legislation, which came into force as of 1 January 2002. The company HEP-Telekomunikacije d.o.o. was founded in 2013 and HEP-Opskrba plinom d.o.o. in 2014. In 2014 the company HEP-RVNP changed its name to Program Sava d.o.o. In May 2015, the company APO d.o.o., for environmental protection, was merged with the Company, and in July 2015 HEP Obnovljivi izbori energije d.o.o. was merged with the company HEP Proizvodnja d.o.o.

On 24 April 2016, the company HEP Odmor i rekreacija d.o.o. changed its name to HEP Upravljanje imovinom d.o.o.

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

17. SUBSIDIARIES (continued)

The Agreement signed between HEP and RWE expired on 28 May 2015 and upon expiration HEP d.d. become the sole owner of TE Plomin d.o.o.

Movements on investments are shown as follows:

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
Balance at 1 January	6,032,580	5,325,094
Investment in NOVENERG d.o.o.	-	380
Investment in capital reserves HEP Operator distribucijskog sustava d.o.o.	605,280	444,304
Reinvested profit HOPS d.o.o.	189,680	265,000
Investment in registered capital HOPS d.o.o.	193,912	-
Recapitalization of the company Upravljanje imovinom d.o.o.	70,000	-
Merger of APO	-	(2,198)
TE Plomin d.o.o.	100	100
	<u>7,091,552</u>	<u>6,032,680</u>

	30 June 2016	31 December 2015
	HRK '000	HRK '000
	Unaudited	Audited
HEP – Proizvodnja d.o.o.	40	40
Hrvatski operator prijenosnog sustava d.o.o.	4,369,916	3,986,324
HEP – Operator distribucijskog sustava d.o.o.	1,764,980	1,159,700
HEP – Opskrba d.o.o.	20	20
HEP –Toplinarstvo d.o.o.	675,881	675,881
HEP – Plin d.o.o.	20	20
HEP ESCO d.o.o.	3,920	3,920
HEP –Upravljanje imovinom d.o.o.	70,020	20
HEP - Trgovina d.o.o.	20	20
Program Sava d.o.o.	20	20
HEP-Telekomunikacije d.o.o.	201,195	201,195
HEP-Opskrba plinom d.o.o.	20	20
Plomin Holding d.o.o.	5,000	5,000
NOVENERG d.o.o.	380	380
Hrvatski centar za čistiju proizvodnju	20	20
TE Plomin d.o.o.	100	100
	<u>7,091,552</u>	<u>6,032,680</u>

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

18. 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 by applying the current yield curve for the period of non-derivative instruments.

Fair value measurements recognized in the statement of financial position

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

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

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

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

	1st level	2nd level	3rd level	Total
	HRK '000	HRK '000	HRK '000	HRK '000
30 June 2016, unaudited				
Available-for-sale assets	250,254	-	-	250,254
Derivative financial assets	-	-	64,825	64,825
Derivative financial liabilities	-	-	109,435	109,435
Investment property	-	14,487	-	14,487
31 December 2015, audited				
Available-for-sale assets	245,838	-	-	245,838
Derivative financial assets	-	-	70,900	70,900
Derivative financial liabilities	-	-	81,876	81,876
Investment property	-	14,487	-	14,487

19. CONTINGENT LIABILITIES

Water Management Act

According to an interpretation by the State Attorney's Office, *Water Management Act* that came into force on 4 January 1996 and the new *Water Management Act* that came into force on 1 January 2010, bring into question the property-legal status of the asset for electricity production from the hydro-power plant because the land on which the hydro-power plants was constructed is classified as 'Public Water Resources' which by its legal nature is considered to be real estate for common use owned by the Republic of Croatia and cannot be the subject of ownership of a physical or legal entity. There are currently several out of court settlement procedures between HEP d.d. and Republic of Croatia relating the right of registering ownership of hydro power plants in favour of Republic of Croatia. There is no uniform case law regarding this issue.

The Company has disputed the interpretation of the Water Management Act as aforementioned property was included in balance sheet of the Group during ownership transformation and therefore cannot be subject to laws that came into force after transition was conducted. This interpretation by the Company is in accordance with the Decision by the Croatian Constitutional Court, Ref. No. U-III-3049/2007. Also, it is necessary to consider overall electrical energy security of the Republic of Croatia, and the fact that the Company has built and invested significant resources in these facilities, that the Company maintains these facilities, and is the owner of all equipment necessary for the operation and functionality of the above mentioned hydro-power plants.

The Company has filed a motion to the Constitutional Court to institute proceedings to review the constitutionality of Article 23 Paragraph 4 of the Water Management Act with the Constitution and upon conclusion of the procedure to annul the said provision. Furthermore, in 2015 the Ministry of Agriculture has launched amendment procedure to the Water Act. As part of this process and with consideration of all of the above mentioned, the Company has submitted a proposal for amendment of the provisions of the Water Act, with the aim of clearing the property-legal relations and ownership of the Republic of Croatia over facilities for electricity production built by legal persons in the majority ownership of the Republic of Croatia. The competent Ministry of Economy issued an opinion with approval of the Company's initiative to amend the Water Act.

Notes to the condensed interim financial statements of HEP d.d. (continued)

For the six months period ended 30 June 2016

20. EVENTS AFTER THE REPORTING PERIOD

On 28 July 2016, the General Assembly adopted a decision on dividend payment for 2014 and 2015 in favour of the State Budget of the Republic of Croatia in the amount of HRK 607,000 thousand.

21. APPROVAL OF THE CONDENSED INTERIM FINANCIAL STATEMENTS

These condensed interim financial statements for six month period ended 30 June 2016 were approved by the Management Board and authorised for issue on 29 August 2016.

Signed on behalf of the Management Board on 29 August 2016:

Perica Jukić

Tomislav Rosandić

President of the Management Board

Member of the Management Board