



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

Consolidated annual financial statements  
together with Independent Auditor's Report  
for the year 2016

## Contents

---

	<i>Page</i>
Responsibility for the consolidated financial statements	1
Independent Auditor's Report	2-7
Consolidated Income statement	8
Consolidated Statement of other comprehensive income	9
Consolidated Statement of financial position / Consolidated Balance sheet	10-11
Consolidated Statement of changes in equity	12
Consolidated Statement of cash flows	13-14
Notes to the consolidated financial statements	15-90

---

## Responsibility for the consolidated Financial Statements

---

The Management Board of the company Hrvatska Elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37, (hereinafter: "the Company") is responsible for ensuring that the consolidated annual financial statements for the year 2016, are prepared in accordance with the Accounting Act (Official Gazette No 78/15, 120/16) and International Financial Reporting Standards, to give a true and fair view of the consolidated financial position, the consolidated results of operations, consolidated changes in equity and consolidated cash flows of the Company for that period.

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

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

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

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

Signed for and on behalf of the Management Board:

Tomislav Rosandić  
Member

Zvonko Ercegovic  
Member

Saša Dujmić  
Member

Perica Jukić  
President

Hrvatska elektroprivreda d.d.  
Ulica grada Vukovara 37  
10000 Zagreb  
Republic of Croatia  
28 April 2017

## **INDEPENDENT AUDITOR'S REPORT**

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

### **Report on the audit of the consolidated annual financial statements**

#### **Opinion**

We have audited the consolidated annual financial statements of the company Hrvatska elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37 (the "Company" or the „Group“) for the year ended 31 December 2016, which comprise the consolidated Statement of financial position (consolidated Balance Sheet) as at 31 December 2016, consolidated Income Statement, consolidated Statement of other comprehensive income, consolidated Statement of changes in equity and consolidated Statement of cash flows of the Company for the year then ended, and Notes to the consolidated financial statements, including a summary of significant accounting policies and other explanations.

In our opinion, the accompanying consolidated annual financial statements give a true and fair view of the financial position of the Company as at 31 December 2016, and of its consolidated financial performance and consolidated cash flows of the Company for the year then ended in accordance with the Accounting Act and the International Financial Reporting Standards (the "IFRS").

#### **Basis for Opinion**

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

#### **Emphasis of matter**

As described in the Note 29 to the consolidated financial statements, at 31 December 2016, the Company stated clearing debt liability in the amount of HRK 863,450 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 it has not been clearly defined whether it relates to a loan or a some other legal transaction. Our opinion has not been modified in this respect.

**Emphasis of matter (continued)**

As described in the Note 28 to the consolidated financial statements, provisions of the Water Management Act that came into force on 1 January 2010, raised a question on the ownership and legal status of the Company's property - reservoirs and ancillary facilities, used for generation of electricity from hydropower plants. Pursuant to the Water Act those property is defined as "Public water resources in general use as the property in ownership of the Republic of Croatia". The Republic of Croatia initiated several proceedings for registration of title to those properties, part of which were ruled in favour of the Republic of Croatia, part of them were rejected by the relevant courts, and part of them are in still in progress. The Company has filed a motion to the Constitutional Court for review of the constitutionality of Article 23 Paragraph 4 of the Water Act and for the cancelation of the same. During 2015, the Ministry of Agriculture has initiated the procedure for amendment and change of the Water Act, and the Ministry of Economy has also submitted its consent to the initiative of the Company for change and amendment of the Water Act. During 2016 and 2017, the Company continued activities with relevant Ministries and Institutions on the above-mentioned issue. Our opinion has not been modified in this respect.

**Key Audit Matters**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated annual financial statements for the current period. These matters were addressed in the context of our audit of the consolidated annual financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matters described below to be the key audit matters to be communicated in our Independent Auditor's report:

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

Revenues from the sale of electricity are recognized on the basis of the best estimate of the delivered energy quantity. As the actual calculation of the delivered volume of energy to customers of the household category are performed twice a year, the Group's electricity sales revenue is based on the total generated and purchased quantities of energy on the distribution network. By doing so, the total generated and purchased amount of energy is corrected for losses on the distribution network based on logarithmic regression. After analyzing several different approximation methods (five-year average, linear approximation and similar), the Management Board of the Company selected logarithmic regression as the most suitable one.

The correction of household income as at 31 December 2016 was obtained by calculating the logarithmic curve using losses in the network of 7.87%, while for the year ended on 31 December 2015, the percentage of losses used in the calculation was 8.39% . The result is an increase in revenues for 2016 in the amount of HRK 11,462 thousand compared to the previous year, and stated liability for accrued income in the amount of HRK 22,077 thousand.

We focused on this area because it involves significant estimates of the recognition of electricity sales revenue at the reporting date.

**Related disclosures in the consolidated annual financial statements**

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

## Key Audit Matters (continued)

### Audit procedures

We have:

- Obtain an understanding of key management controls related to estimating electricity sales revenue
- Assessed the reasonableness of the key assumptions used in the estimation model including the quantities of electricity sold and the price
- Test the mathematical accuracy of the model of estimation of electricity sales revenue
- engage an IT expert to assess system reliability and internally make an independent estimate of unrecorded revenue using data on quantities and prices received by the Group, and we have compared such results with the Group's revenue estimate.

We also evaluated the adequacy of the Company's disclosure regarding the recognition of revenues from the sale of electricity to customers of universal service (household customers). The results of our tests were satisfactory.

### Contingent liabilities and court disputes

Since the Group is exposed to significant legal claims, we have focused our attention on this area. According to that, the Management Board estimates future outcomes and amounts of contingent liabilities that may arise as a result of these claims.

### Related disclosures in the consolidated annual financial statements

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

### Audit procedures

We have:

- obtain the understanding of the status of any significant claim and the historical outcomes of previous similar cases
- obtain the statements of all external legal representatives for all material proceedings
- analyse the assessment of the nature of disputes and claims by discussing the most significant cases with the Company's management and the internal legal department

Based on the collected evidence, taking into account inherent uncertainty in legal issues, we agree with the Company's management's assessment of the likelihood of future significant outflows related to these issues. We have found that issues that are likely to become future outflows are stated as provisions.

Furthermore, we assessed the adequacy of the Company's disclosure regarding Contingent liabilities and court disputes. The results of our tests were satisfactory.

## **Other Information in the Annual Report**

The Management is responsible for other information. Other information includes information included in the Annual report, but do not include the consolidated annual financial statements and our Independent auditor's report on them.

Our opinion on the consolidated annual financial statements does not include other information, except to the extent explicitly stated in the part of our Independent auditor's report, entitled Report on compliance with other legal or regulatory requirements, and we do not express any form of assurance conclusion thereon.

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

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

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

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

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

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

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

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

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

- Identify and assess the risks of material misstatement of the consolidated annual financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.
- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated annual financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated annual financial statements, including the disclosures, and whether the consolidated annual financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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



## Report on Compliance with Other Legal or Regulatory Requirements

The Management is responsible for the preparation of the Management report as part of the Annual report of the Company. We are obliged to express an opinion on the compliance of the Management report as part of the Annual report of the Company with the consolidated annual financial statements of the Company. In our opinion, based on our audit of the consolidated annual financial statements of the Company, information in the Management report as part of the Annual report of the Company for the year ended 31 December 2016, are in accordance with the financial information stated in the consolidated annual financial statements of the Company set out on pages 8 to 90 on which we expressed our opinion as stated in the section Opinion above.

In our opinion, based on the work that we performed during the audit, the Company's Management report for 2016, which is an integral part of the Annual report for 2016 is prepared in accordance with the Accounting act.

Based on the knowledge and understanding of the Company and its environment obtained while performing the audit, we have not found that there are material misstatements in the Company's Management report for 2016, which is an integral part of the Company's Annual report for 2016.

In our opinion, based on the work that we performed during the audit, the Statement that code of corporate governance is applied, included in the Annual report for 2016, is in accordance with the requirements of article 22, paragraph 1, points 3 and 4 of the Accounting Act.

The Statement that code of corporate governance is applied, included in the Annual report for 2016, includes information from article 22, paragraph 1, points 2, 5 and 6 of the Accounting Act.

The Management is responsible for the preparation of consolidated annual financial statements for the year ended 31 December 2016 in prescribed form based on the Statute of structure and content of annual financial statements (Official Gazette 95/16) and in accordance with other regulations governing the operations of the Company ("Standard consolidated annual financial statements"). Financial information presented in Company's standard consolidated annual financial statements are in accordance with the information presented in the Company's consolidated annual financial statements given on pages 8 to 90 on which we expressed our opinion as stated in the section Opinion above.

The engagement partner on the audit of consolidated annual financial statements of the Company for 2016, resulting in this Independent auditor's report is Irena Jadrešić, certified auditor.

In Zagreb, 28 April 2017

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

---

Zdenko Balen, Management  
Board member

---

Irena Jadrešić, Certified auditor

Consolidated Income statement  
For the year ended 31 December 2016

	Notes	2016 In HRK'000	2015 In HRK'000
Revenue from electricity sales	4	10,831,456	10,537,427
Revenue from thermal power sales	4	699,596	682,388
Revenue from sale of gas on wholesale market	4	1,102,728	1,298,352
Revenue from sale of gas to customers	4	341,812	386,388
<b>Sales revenue</b>		<b>12,975,592</b>	<b>12,904,555</b>
Other operating income	5	1,424,766	1,664,910
<b>Total operating income</b>		<b>14,400,358</b>	<b>14,569,465</b>
Electricity purchase cost	6	(2,148,249)	(1,943,077)
Fuel cost	6	(1,548,033)	(1,798,986)
Costs of gas sold	6	(1,246,442)	(1,352,038)
Staff cost	7	(1,904,443)	(1,923,831)
Depreciation and amortization costs	11,12	(1,780,269)	(1,825,097)
Other operating expenses	8	(3,049,765)	(2,730,671)
<b>Total operating expenses</b>		<b>(11,677,201)</b>	<b>(11,573,700)</b>
<b>Operating profit</b>		<b>2,723,157</b>	<b>2,995,765</b>
Financial income	9	232,873	70,479
Financial expenses	9	(365,669)	(670,520)
<b>Net loss from financial activities</b>		<b>(132,796)</b>	<b>(600,041)</b>
<b>Profit before taxation</b>		<b>2,590,361</b>	<b>2,395,724</b>
Corporate income tax expense	10	(545,359)	(455,667)
<b>Profit for the year</b>		<b>2,045,002</b>	<b>1,940,057</b>
<b>Attributable to:</b>			
Owners of the Parent		2,045,002	1,939,095
Non-controlling interest		-	962
		<b>2,045,002</b>	<b>1,940,057</b>

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

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovic  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board

Consolidated Statement of other comprehensive income  
For the year ended 31 December 2016

	2016 In HRK'000	2015 In HRK'000
<b>Profit for the year</b>	<b><u>2,045,002</u></b>	<b><u>1,940,057</u></b>
<b>Other comprehensive income</b>		
Exchange (losses) arising on translation of foreign operations	(18,984)	(4,453)
Net gain on AFS financial assets	<u>39,457</u>	<u>45,889</u>
Net other comprehensive income to be reclassified to income/ (loss) in subsequent periods	<u>20,473</u>	<u>41,436</u>
<b>Other comprehensive income, net</b>	<b><u>20,473</u></b>	<b><u>41,436</u></b>
<b>Total comprehensive income for the year, net</b>	<b><u>2,065,475</u></b>	<b><u>1,981,493</u></b>
<b>Total comprehensive income attributable to:</b>		
Owners of the Parent	2,065,475	1,980,788
Non-controlling interest	-	705
	<b><u>2,065,475</u></b>	<b><u>1,981,493</u></b>

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

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovic  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board

Consolidated Statement of financial position / Cosolidated Balance sheet  
As at 31 December 2016

ASSETS	Notes	31 Dec 2016	31 Dec 2015
		In HRK'000	In HRK'000
<b>Non-current assets</b>			
Property, plant and equipment	11	28,093,856	25,722,455
Assets under construction	11	2,677,233	4,386,574
Intangible assets	12	157,586	121,437
Investment property	13	231,491	236,778
Prepayments for property, plant and equipment	14	36,707	37,880
Long-term loans and deposits	17	28,973	28,605
Available-for-sale and other investments	18	295,938	245,910
Other non-current assets	19	46,941	115,795
Deferred tax assets	10	555,461	650,681
<b>Total non-current assets</b>		<b>32,124,186</b>	<b>31,546,115</b>
<b>Current assets</b>			
Inventories	20	1,405,368	1,489,289
Trade receivables	21	1,953,592	1,847,063
Other short-term receivables	22	730,917	835,753
Cash and cash equivalents	23	3,018,846	2,493,166
<b>Total current assets</b>		<b>7,108,723</b>	<b>6,665,271</b>
<b>TOTAL ASSETS</b>		<b>39,232,909</b>	<b>38,211,386</b>

Consolidated Statement of financial position / Consolidated Balance sheet -continued  
As at 31 December 2016

<b>EQUITY AND LIABILITIES</b>	<b>Notes</b>	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
Share capital	24	19,792,159	19,792,159
Revaluation reserves	24	140,293	100,836
Retained earnings	24	5,551,226	4,132,208
<b>Equity Attributable to Owners of the Parent</b>		<b>25,483,678</b>	<b>24,025,203</b>
Non-controlling interest		-	-
<b>Total equity</b>		<b>25,483,678</b>	<b>24,025,203</b>
Liabilities under issued bonds	25	3,606,173	4,223,883
Long-term loan liabilities	26	664,764	936,243
Long-term liabilities to the State	27	15,901	18,774
Long-term provisions	28	930,700	969,501
Other long-term liabilities	29	4,190,347	4,444,970
Deferred tax liabilities		26,007	21,816
<b>Total non-current liabilities</b>		<b>9,433,892</b>	<b>10,615,187</b>
Trade payables	30	1,787,338	1,740,910
Current portion of long-term bonds issued	25	586,601	93,380
Current portion of long-term loans	26	411,832	386,509
Taxes and contributions	31	157,750	199,288
Interests payable		42,569	45,693
Liabilities to employees	32	155,269	226,510
Other non-current liabilities	33	1,173,980	878,706
<b>Total non-current liabilities</b>		<b>4,315,339</b>	<b>3,570,996</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>39,232,909</b>	<b>38,211,386</b>

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

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovic  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board

Consolidated Statement of changes in equity  
For the year ended 31 December 2016

	Share capital	Revalua- tion reserves	Retained earnings / Loss carried forward	Equity attributable to Owners of the Parent	Non- controlling interests	Total equity
	In HRK'000	In HRK'000	In HRK'000	In HRK'000	In HRK'000	In HRK'000
<b>Balance at 1 January 2015</b>	<b>19,792,159</b>	<b>54,947</b>	<b>2,201,265</b>	<b>22,048,371</b>	<b>29,202</b>	<b>22,077,573</b>
Profit for the year	-	-	1,939,095	1,939,095	962	1,940,057
Other comprehensive income	-	45,889	(4,196)	41,693	(257)	41,436
<i>Total comprehensive income</i>	-	<i>45,889</i>	<i>1,934,899</i>	<i>1,980,788</i>	<i>705</i>	<i>1,981,493</i>
Land surpluses	-	-	1,401	1,401	-	1,401
Other changes	-	-	(5,357)	(5,357)	-	(5,357)
Distribution of dividends to RWE	-	-	-	-	(29,907)	(29,907)
<b>Balance at 31 December 2015</b>	<b>19,792,159</b>	<b>100,836</b>	<b>4,132,208</b>	<b>24,025,203</b>	<b>-</b>	<b>24,025,203</b>
Profit for the year	-	-	2,045,002	2,045,002	-	2,045,002
Other comprehensive income	-	39,457	(18,984)	20,473	-	20,473
<i>Total comprehensive income</i>	-	<i>39,457</i>	<i>2,026,018</i>	<i>2,065,475</i>	<i>-</i>	<i>2,065,475</i>
Distribution of dividend to the Owner	-	-	(607,000)	(607,000)	-	(607,000)
<b>Balance at 31 December 2016</b>	<b>19,792,159</b>	<b>140,293</b>	<b>5,551,226</b>	<b>25,483,678</b>	<b>-</b>	<b>25,483,678</b>

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

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovac  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board

Consolidated Statement of cash flows  
For the year ended 31 December 2016

	2016 In HRK'000	2015 In HRK'000
<b>OPERATING ACTIVITIES</b>		
Profit for the year	2,045,002	1,940,057
Corporate income tax expense recognized in profit	545,359	455,667
Net loss from financial activities	132,796	600,041
Fair value of property investment	5,287	(625)
Value adjustment of non-current assets	108,256	47,507
Depreciation and amortization	1,780,269	1,825,097
Receivables value adjustment	(149,202)	71,419
Inventories value adjustment	13,353	14,257
Increase /(decrease) in provisions	(38,801)	66,722
<i>Operating cash flows before movements in working capital</i>	<i>4,442,319</i>	<i>5,020,142</i>
(Increase) in trade receivables	42,673	(53,802)
Decrease /(increase) in inventories	70,568	109,751
(Increase) in other current assets	163,636	(317,544)
Increase/(decrease) in trade payables	46,428	150,165
Increase in other current liabilities	286,318	63,034
(Decrease) in other non-current liabilities	(224,969)	(247,223)
<b>Cash generated from operations</b>	<b>4,826,973</b>	<b>4,724,523</b>
Corporate income tax paid	(553,691)	(843,656)
Interests paid	(244,612)	(389,097)
<b>NET CASH FROM OPERATING ACTIVITIES</b>	<b>4,028,670</b>	<b>3,491,770</b>
<b>INVESTING ACTIVITIES</b>		
Interest receipts	49,335	49,420
Increase in property, plant and equipment	(2,589,126)	(2,528,144)
Disposal of property, plant and equipment	2,392	25,674
Increase in other non-current assets	(30,796)	(23,966)
<b>NET CASH (USED IN) INVESTING ACTIVITIES</b>	<b>(2,568,195)</b>	<b>(2,477,016)</b>

Consolidated Statement of cash flows - continued  
For the year ended 31 December 2016

	2016	2015
	In HRK'000	In HRK'000
<b>FINANCING ACTIVITIES</b>		
Receipts from bonds issued	-	3,703,533
Long-term loans received	147,623	66,722
Repayment of long-term loans	(382,038)	(417,915)
Repayment of issued bonds	(93,380)	(2,900,335)
Repayment of short-term loans	-	(8,981)
Dividends paid to the owner	(607,000)	-
Dividends paid to RWE	-	(44,512)
<b>NET CASH (USED IN) / FROM FINANCING ACTIVITIES</b>	<b>(934,795)</b>	<b>398,512</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>525,680</b>	<b>1,413,266</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR</b>	<b>2,493,166</b>	<b>1,079,900</b>
<b>CASH AND CASH EQUIVALENTS AT END OF THE YEAR</b>	<b>3,018,846</b>	<b>2,493,166</b>

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

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovic  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board



## 1. GENERAL

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

HEP d.d. is registered in Zagreb, Ulica grada Vukovara 37. The principal activities of the Group are generation, transmission and distribution of electricity, and the control of the electric power systems. In addition to main activities, HEP Group also produces and distributes thermal power through the district heating systems in Zagreb and Osijek, and the distribution of gas in Osijek and Đakovo. All the Group's activities are governed by applicable laws, regulations and decisions issued by the Croatian Government.

As at 31 December 2016 the Group employed 11,832 employees (2015: 11,935), excluding Krško Nuclear Power Plant which employed 617 employees (2015: 648).

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

### Laws regulating the energy sector

The Croatian Parliament adopted following Acts and Regulations that are regulating the Group's activities:

- the Energy Act and the Regulation of Energy Activities Act (adopted on 19 October 2012),
- the Electricity Market Act (adopted on 8 February 2013),
- the Gas Market Act (adopted on 22 February 2013),
- the Heat Energy Market Act (adopted on 21 June 2013),
- Law on Amendments of the Electricity Market Act (adopted on 18 September 2015).

New Acts and Regulations, harmonized with EU Guidelines and Directives, determined further restructuring and adjustments of operations of HEP Group. According to provisions of the Electricity Market Act and amendments of the Electricity Market Act, HEP d.d. and its subsidiaries continue to provide public energy services in the Republic of Croatia, namely: transmission, distribution and universal and guaranteed supply of electricity. Generation, supply (on open market) and trading of electricity are performed as market activities as defined by legislation regulating the energy activities and trading on energy markets. Supply of electricity on open market is performed in accordance with rules governing market relations, where the energy subjects freely negotiate quantities and prices on a free market basis. Supply of electricity as a universal and guaranteed service, is performed according to regulated conditions to the protected customers who have a right to such model of supply and choose it freely or automatically. Household customers are supplied with electricity as guaranteed public service, as well as part of protected customers that have not exercised their right to select the electricity supplier or are left without a supplier. Part of household customers exercised their right to choose their supplier. HEP d.d. and its subsidiaries are reorganizing the Group in accordance with changed Acts and Regulations and prescribed deadlines.

## 1. GENERAL (continued)

### Laws regulating the energy sector (continued)

In April 2012, the Government of the Republic of Croatia issued following Decisions: Tariff Model for Electricity Generation, with the exemption of protected customers, with no tariff items; Electricity Transmission Tariff Model, with no tariff items; Electricity Distribution Tariff Model, with no tariff items; and Electricity Supply Tariff Model, with the exemption of protected customers, with no tariff items. The Group has been applying above mentioned Tariff Models since 1 May 2012. On 30 September 2013 Decisions on Tariff Model for Electricity Generation, with the exemption of protected customers, with no tariff items and Electricity Supply Tariff Model, with the exemption of protected customers, with no tariff items ceased to have effect.

Electricity Market Act adopted in February 2013, determines that each customer has a right to freely choose a supplier, and household customers have a right to electricity supply as a universal service. Customers that have not exercised their right to select the electricity supplier or are left without a supplier, are using public guaranteed supply service. Pursuant to the provisions of the Electricity Market Act on 13 September 2013 the Croatian Energy Regulatory Agency (HERA) issued Methodology for determining tariff items for electricity supplies within the universal service and on 17 December 2013 HERA adopted the Methodology for determining the amount of tariff items for guaranteed electricity supplies.

From 1 October 2013, households supplied with electricity within the universal service, are charged in accordance with Methodology for setting tariff items for electricity supply within the universal service and the Decision of HEP Operator distribucijskog sustava d.o.o. on the amount of tariff items for electricity supply within universal service dated 1 October 2013, and from 1 January 2015 by Decision of HERA on the amount of tariff items for electricity supply in the context of universal service.

From the entry into force of the Act on Amendments to the Electricity Market Act, the decision on the amount of tariff items for electricity supply within the universal service is made by the HEP Operator distribucijskog sustava d.o.o. or HEP Elektra d.o.o. from 2 November 2016.

Customers using public guaranteed supply service were charged in accordance with the Methodology for setting prices for balancing electricity price charged to customers responsible for deviations and from 1 July 2014, in accordance with the Methodology for setting the tariff items for guaranteed electricity supply and the Decision of Croatian Energy Regulatory Agency on the amount of tariff items for guaranteed electricity supply.

## 1. GENERAL (continued)

### **General assembly**

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

Ivan Vrdoljak	Member	Member since 21 November 2012 until 3 March 2016
Tomislav Panenić	Member	Member since 4 March 2016 until 25 January 2017
Zdravko Marić	Member	Member since 26 January 2017

### **Supervisory Board**

#### *Members of the Supervisory Board in 2016*

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

#### *Members of the Supervisory Board in 2015*

Nikola Bruketa	President	President since 23 February 2012
Žarko Primorac	Member	Member since 23 February 2012
Ivo Uglešić	Member	Member since 23 February 2012
Igor Džajić	Member	Member since 19 September 2012
Mirko Žužić	Member	Member since 19 September 2012
Juraj Bukša	Member	Member since 5 June 2014
Jadranko Berlangi	Member	Member since 3 June 2008 to 31 May 2015
Dubravka Kolundžić	Member	Member since 1 June 2015

### **Management Board**

#### *Management Board in 2016*

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

#### *Management Board in 2015*

Perica Jukić	President	Member since 10 May 2013, President since 12 September 2014
Zvonko Ercegovac	Member	Member since 23 February 2012
Željko Štromar	Member	Member since 16 December 2013 to 31 March 2015
Tomislav Rosandić	Member	Member since 2 January 2015
Saša Dujmić	Member	Member since 4 December 2014

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

### ***Presentation of the consolidated financial statements***

The consolidated financial statements for 2016 have been prepared in accordance with the Accounting Act (Official Gazette 75/15, 120/16), the International Financial Reporting Standards ("IFRS"), as well as in accordance with the Ordinance on the structure and content of annual financial statements (Official Gazette 95/16).

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

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

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

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

### ***Adoption of new and revised International Financial Reporting Standards Standards and Interpretations effective in the current period***

- Amendments to IAS 19 Defined Benefit Plans: Employee Contributions – IAS 19 requires subjects to consider employee or third party contributions in accounting defined earning.
- 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

The effective date of the amendments is 1 January 2016. Earlier application is allowed.

- 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;
  - 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 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)

The application of the above-mentioned standards had no influence on the consolidated financial statements of the Company for 2016.

### ***New and revised IFRSs issued by the IASB but not effective***

- 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. IFRS 9 is effective for the annual period beginning on or after 1 January 2018, earlier applications are permitted. The application of this standard will have negligible affect the classification and measurement of financial instruments.
- 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. The Standard replaces IAS 11 and IAS 18. Standard is effective for the annual period beginning on or after 1 January 2018, earlier applications are permitted.

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

- The Standard allows a modified transfer model which does not require retroactive modifications. The Management performs detailed analysis on its possible effects on the Company's consolidated financial statements.

### ***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 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. The European Commission has decided not to implement this standard due to the fact that only small number of companies was within the scope of the standard.
- IFRS 16 Leases – the standard brings a new comprehensive model of identification of arrangements which have leases and their accounting treatment on the side of lessor and lessee. The standard will replace IAS 17 and interpretations of IFRIC 4, SIC 15 and SIC 27. IFRS 16 is effective for the annual period beginning on or after 1 January 2019. Earlier applications are permitted, but this is conditioned with the application of IFRS 15 unless already adopted. This standard brings significant changes to the accounting model of the lessee. Consequently, assets and liabilities will be recognised in the financial statements of the lessee in most contract that were formerly recognised as operating lease. This will result in an increase of assets and liabilities. The Management Board plans detailed analysis in the coming periods to determine effects on the consolidated financial statements of the Company.
- Amendments to IFRS 2 – classification and measurement of share based payment transactions (issued in June 2016).
- Amendments to IFRS 4 – Application of IFRS 9 Financial instruments with IFRS 4 Insurance agreements (issued in June 2016).
- 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).
- Clarifications to IFRS 15 Revenue from Contracts with Customers (issued in April 2016).
- Amendments to IAS 7 – part of its disclosure initiative (issued in January 2016)
- Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses (issued in January 2016).
- Amendments to IAS 40 – Transfer of real estate investments (issued December 2016.)
- Annual Improvements 2014-2016 Cycle (issued December 2016). They include:
  - IFRS 1 First application of IFRS,
  - IFRS 12 Disclosure of interests in other entities,
  - IFRS 28 Investments in associates and joint ventures

Amendments which relate to IFRS 12 are effective for periods starting on 1 January 2017, while amendments to IFRS 1 and IAS 28 are effective for the annual period beginning on or after 1 January 2018.

- IFRIC 22 Foreign currency transactions and advance considerations (issued December 2016).

The Company's management anticipates that the application of the above standards, amendments and interpretations, except for IFRS 16 as stated above, will have no material impact on the consolidated financial statements in the period of initial application.

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

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

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

### ***Principles and methods of consolidation***

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

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

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

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

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

### ***Reporting currency***

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

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

### ***Investments in joint arrangements***

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

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

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

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

Interest in joint ventures are measured using equity method.

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

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



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

### *Employee benefits*

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

	<b>2016 and 2015</b>
Pension insurance contributions	20%
Health insurance contributions	15%
Employment Fund contribution	1.7%
Occupational injury	0.5%

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

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

### *Jubilee awards*

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

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

### *Severance payments*

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

### ***Property, plant and equipment (hereinafter: PPE)***

Property, plant and equipment are measured at cost less accumulated depreciation and any impairment losses, except for land, which is carried at cost.

The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

PPE in use are depreciated using the straight-line method on the following bases:

	<b>2016 and 2015</b>
<b>Buildings</b>	
Hydroelectric power plants (flood gates and dams, buildings and other buildings as well as accompanying objects)	20 – 50 years
Thermal power plants (buildings and other structures)	33 – 50 years
Electricity transmission and distribution plants and facilities (transmission lines and buildings of transformer stations, switch-yard, dispatch centres and others)	20 – 40 years
Water and steam pipelines and other thermal power generation and transmission objects	33 years
Gas pipelines until 2014	20 – 25 years
Gas pipelines from 2014	40 years
Administrative buildings	50 years
<b>Plant and equipment</b>	
Hydroelectric power plants	10 – 33 years
Thermal power plants	6 – 25 years
Electricity transmission plants and facilities (electric parts of transformer stations and transformers; and electric parts of transmission lines)	15 – 40 years
Electricity distribution plants and facilities (electric parts of transformer stations and transformers, electric parts of distribution lines, measuring instruments, meters and other equipment)	8 – 40 years
Thermal power stations, hot-water pipelines and other equipment	15 – 30 years
Gas meters and other gas network equipment	5 – 20 years
Other equipment and vehicles	
IT equipment	5 – 20 years
Software licenses	5 years
Telecommunications equipment	5 – 20 years
Motor vehicles	5 – 8 years
Office furniture	10 years

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

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

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

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

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

### ***Impairment of PPE and intangible assets***

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

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

Recoverable amount is higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to that asset for which the estimates of future cash flows have not been adjusted.

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

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

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

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

### ***Intangible assets***

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

### ***Investment property***

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

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

### ***Finance and operating leases***

#### ***The Group as lessee***

The Group has no significant finance lease arrangements and there were no new significant operating lease arrangements concluded during 2016 and 2015. Operating lease payments are recognized as an expense in on a straight-line basis over the lease term.

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

### *Trade receivables and prepayments*

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

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

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

	2016 and 2015
Receivables ageing structure	Impairment percentage
31 - 60 days	1.5%
61 - 90 days	3%
91 - 180 days	9%
181 - 365 days	30%
Over one year	90%

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

### *Inventories*

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

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

Companies are obligated to have defined quantities of CO<sub>2</sub> emission rights at 30 April (yearly cycle). Due to withdrawal of IFRIC 3 *Emission Rights* and insufficient provisions of IFRS, the Group has analysed different accounting models for CO<sub>2</sub> emission rights, and among other EFRAG discussion papers. Occasionally, the Group trades with CO<sub>2</sub> emission rights. Due to that the Group recognize these emission rights as inventory. From April 2014, inventories include gas stock held for trading on the wholesale market and are stated at lower of cost and net realizable value. The Company measures inventories based on the weighted average price (Note 20).

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

Inventory costs for quantities of gas for direct delivery to customers are calculated using method of specific identification.

Cost comprise invoiced amount as well as all other costs directly attributable to bringing inventories to their present location and condition.

### ***Cash and cash equivalents***

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

### ***Borrowing costs***

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

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

### ***Foreign currencies***

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

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

Exchange differences arising on the settlement of monetary items, and on their retranslation, are stated in the consolidated income statement in the period in which they incurred. Exchange differences arising on retranslation of non-monetary assets carried at fair value are stated in the consolidated income statement as financial cost, except for exchange differences arising on the retranslation of non-monetary assets available for sale, for which gains and losses are recognized directly in equity. For such non-monetary items, any exchange gains or losses arising from retranslations are also recognized directly in equity.

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

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

### ***Taxation***

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

#### *Current tax*

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

#### *Deferred tax*

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

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and adjusted to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability will be settled or asset realized, based on tax laws that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

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

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

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

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

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

#### ***Financial assets***

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

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

#### *Effective interest method*

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

#### *Available-for-sale financial assets (AFS)*

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

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



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

### ***Financial assets (continued)***

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

### ***Loans and receivables***

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

### ***Impairment of financial assets***

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

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

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

In respect of AFS equity instruments, any increase in fair value subsequent to an impairment loss is recognized directly in revaluation reserve.

### ***Investments***

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

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

### ***Financial liabilities***

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

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

### ***Derecognition of financial liabilities***

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

### ***Derivative financial instruments***

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

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

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

### ***Provisions***

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

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

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

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

### ***Revenue recognition***

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

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

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

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

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

### **Revenue from connection fees**

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

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

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

### **Segment analysis**

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

### 3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

#### *Critical judgments when applying accounting policies*

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

#### *Useful lives of property, plant and equipment*

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

#### *Fair value of financial assets*

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

#### *Provisions for environment 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, 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 on 28 April 2006 issued a decree on the payment of funds for the decommissioning and disposal of radioactive waste and consumed nuclear fuel of the NPPK. Pursuant to Article 10, Par. 3 of the Law on the fund to finance the decommissioning and disposal of radioactive waste and consumed nuclear fuel from the Krško Nuclear Power Plant (Official Gazette 107/2007), on 24 December 2008 the Croatian government adopted an Ordinance on the amount, timeframe and method of payment of funds to finance the decommissioning and disposal of radioactive waste and consumed nuclear fuel from the Krško Nuclear Power Plant (Official Gazette 155/08) (Note 15).

Provision for decommissioning of thermal power plants represent present value of the estimated decommissioning costs of the Group's thermal power plants.

#### *Recognition of revenues from sale of electricity - households*

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

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

#### *Impairment of non-current assets*

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

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

Deferred tax assets are recognized for unused tax losses to the extent that it is probable that the related tax benefit will be realised against future taxable profits. Measurement of the amount of deferred taxes that can be recognised, requires a significant level of judgement which is based on the probable quantification of the time and level of future taxable profits, together with the future tax planning strategy. Carrying amount of deferred tax assets as at 31 December 2016 amounted to HRK 555,461 thousand, as at 31 December 2015 to HRK 650,681 thousand (Note 10).

#### *Actuarial estimates used in determining severance payments and jubilee awards*

The cost of defined benefits is determined using actuarial estimates. Actuarial estimates involve assumptions about discount rates, future salary increases and the mortality or fluctuation rates. Because of the long-term nature of those plans, there is uncertainty regarding those estimates. Provisions for jubilee awards and severance payments amounted to HRK 374,679 thousand as at 31 December 2016, and to HRK 420,425 thousand as at 31 December 2015 (Note 28).

#### *Consequences of certain court disputes*

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

#### 4. SEGMENT INFORMATION

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

	Electricity		Heating		Gas		Group	
	2016	2015	2016	2015	2016	2015	2016	2015
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Operating revenue	10.831.456	10.537.427	699.596	682.388	1.444.540	1.684.740	12.975.592	12.904.555
Other segment income	1.350.081	1.588.378	51.868	55.407	22.817	21.125	1.424.766	1.664.910
<b>Operating profit/loss</b>	<b>2.867.744</b>	<b>3.149.041</b>	<b>(162.625)</b>	<b>(290.676)</b>	<b>18.038</b>	<b>137.400</b>	<b>2.723.157</b>	<b>2.995.765</b>
Net financial expense							(132.796)	(600.041)
Corporate income tax							(545.359)	(455.667)
<b>Net profit</b>							<b>2.045.002</b>	<b>1.940.057</b>

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

	Total segment assets		Total segment liabilities	
	2016	2015	2016	2015
	HRK'000	HRK'000	HRK'000	HRK'000
Electricity	30,179,137	29,030,695	6,227,856	6,125,754
Heating	1,226,459	1,204,678	170,255	187,850
Gas	370,917	383,816	99,960	101,933
Unallocated	7,456,396	7,592,197	7,251,160	7,770,646
<b>Total Group</b>	<b>39,232,909</b>	<b>38,211,386</b>	<b>13,749,231</b>	<b>14,186,183</b>

#### 4. SEGMENT INFORMATION (continued)

##### Customer information

In 2016 electricity sales amounts to HRK 10,831,456 thousand (2015: HRK 10,537,427 thousand).

Heating energy sales for the year 2016 amounts to HRK 699,596 thousand (2014: HRK 682,388 thousand).

In 2016 gas sales in wholesale market amounts to HRK 1,102,728 thousand and gas sales to customers in the amount of HRK 341,812 thousand (2015 wholesale market: HRK 1,298,352 thousand; gas sales to customers HRK 386,388 thousand).

##### Geographical information

The Group operates in Europe, with countries that are members of the European Union and other countries that are not members of the European Union. Presented below is the territorial analysis of the revenue that the Group realized from continuing operations with external buyers of electricity:

	<b>2016</b>	<b>2015</b>
	In HRK'000	In HRK'000
Croatia	9,937,036	10,006,893
EU member states	789,423	365,132
Non - EU member states	104,997	165,402
	<b>10,831,456</b>	<b>10,537,427</b>



## 5. OTHER OPERATING INCOME

	2016 In HRK'000	2015 In HRK'000
Network/grid connection services	449,450	367,263
Revenues from court verdict for undelivered electricity NEK	-	328,925
Income from assets financed by network/grid connection fee	231,909	230,636
Reversal of impaired receivables (Note 21)	84,807	73,123
Services rendered	97,441	135,658
Capitalized assets	99,916	95,437
Penalty interests	40,592	74,243
Income from sale of materials	28,735	37,592
Income from sale of cross – border transmission capacity	60,616	58,508
Revenues from inter-compensation (HOPS) - cross-border	22,570	18,341
Reversal of severance payments based on termination of employment contract	-	21,915
Reversal of long-term provisions – vacation accrual	-	5,843
Reversal of long-term provisions for retirement benefits and jubilee awards	72,847	21,695
Reversal of long-term provisions – court costs	55,117	20,593
Reversal of other provisions	5,039	6,170
Recovery of receivables from pre-bankruptcy proceedings	5,433	17,363
Income in respect of the electricity payments reminders	3,538	5,082
Income in respect of court costs on claims	9,382	8,177
Income from sale of tangible assets	30,778	51,281
Recovery of written-off receivables	2,190	2,352
Income from subsidies, grants, reimbursements and compensation	11,930	-
Overcharged fee in previous year on CO2 emissions for electricity generation	9,486	255
Other income - NEK d.o.o.	5,813	4,977
Other	97,177	79,481
	<b>1,424,766</b>	<b>1,664,910</b>

In 2016 the Group realized income from network/grid connection services in the amount of HRK 449,450 thousand (2015: HRK 367,263 thousand) pursuant to IFRIC 18 (Transfers of assets from Customers).

## 6. PURCHASE COSTS

	<b>2016</b>	<b>2015</b>
	In HRK'000	In HRK'000
Cost of electricity	2,148,249	1,943,077
Gas cost	1,548,033	1,798,986
Fuel cost for sale on the wholesale market	1,246,442	1,352,038
	<b><u>4,942,724</u></b>	<b><u>5,094,101</u></b>

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

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

## 7. STAFF COSTS

	<b>2016</b>	<b>2015</b>
	In HRK'000	In HRK'000
Net salaries	1,069,123	1,078,947
Net salaries NEK d.o.o.	92,807	95,097
Taxes and contributions	704,001	711,389
Taxes and contributions NEK d.o.o.	38,512	38,398
	<b><u>1,904,443</u></b>	<b><u>1,923,831</u></b>

### Total staff costs:

	<b>2016</b>	<b>2015</b>
	In HRK'000	In HRK'000
Gross salaries	1,773,123	1,790,336
Gross salaries NEK d.o.o.	131,319	133,495
Reimbursement of costs to employees (Note 8)	119,205	117,937
Employee benefits (Note 8)	65,498	59,359
Unused vacation (Note 8)	9,800	-
	<b><u>2,098,945</u></b>	<b><u>2,101,127</u></b>

## 7. STAFF COSTS (continued)

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

	<b>2016</b> In HRK'000	<b>2015</b> In HRK'000
Gross salaries	28,523	27,198
Pension contributions	6,370	6,107
Other benefits	3,329	3,360
	<b>38,222</b>	<b>36,665</b>

### Remuneration for members of the Supervisory Board:

	<b>2016</b> In HRK'000	<b>2015</b> In HRK'000
Fees	192	192
Taxes and contributions	194	203
Other costs	18	17
	<b>404</b>	<b>412</b>

Reimbursement of costs to employees for 2016 includes commuting costs in the amount of HRK 72,711 thousand (2015: HRK 74,398 thousand), daily allowances and travelling expenses for 2016 in the amount of HRK 21,150 thousand (2015: HRK 19,581 thousand), additional health insurance for 2016 amounting to HRK 8,548 thousand (2015: HRK 7,507 thousand) and other similar expenses for 2016 in the amount of HRK 16,790 thousand (2015: HRK 16,451 thousand).

Employee benefit costs mostly include benefits under the Collective Agreement which amounts to HRK 46,890 thousand, and to a minor extent to solidarity support, family separation allowances, child benefits and other.

In 2016 there were no other payments to the Management Board members in addition to regular salaries and benefits in kind in the amount of HRK 2,721 thousand (2015: HRK 2,694 thousand).

## 8. OTHER OPERATING EXPENSES

	2016 In HRK'000	2015 In HRK'000
Maintenance costs	636,610	605,513
Impairment of trade receivables (Note 21)	107,276	170,915
Gas costs	126,178	154,122
Cost of services	296,732	295,829
Chargeable services and supplies	142,643	154,948
Cost of material	86,236	87,149
Compensation for lower quantities of gas than contracted	12,745	5,073
CO2 emission allowances cost	137,315	133,768
Value adjustment of inventory	13,209	15,898
Value adjustment of non-current tangible assets	108,256	47,507
Employee benefits (Note 7)	119,205	117,937
Other employees benefits (Note 7)	65,498	59,359
NE Krško – decommissioning expense	107,197	108,681
Taxes and contributions	90,980	87,339
Litigation provisions	25,244	25,313
Contributions and concession for water fees	64,785	71,517
Provision for unused vacation (Note 7)	9,800	-
Fee for the usage of power plant facilities	73,223	74,825
Compensation for water-purification and drainage	10,528	11,898
Property, plant and equipment write off	18,369	25,674
Cost of materials sold	15,049	30,012
Calculation and collection costs	29,111	30,004
Provisions for retirement benefits and jubilee awards	27,101	78,226
Provisions for severance payments based on the termination	342,964	-
Insurance premiums	12,612	16,186
Environmental protection fees	732	2,864
Compensation for damages	16,141	20,406
Bad debts write off	20,528	7,943
Provisions for decommissioning of fossil fuelled power plants	8,141	7,608
Other operating expenses NEK d.o.o.	245,275	216,761
Other	80,082	67,396
	<b>3,049,765</b>	<b>2,730,671</b>

## 9. FINANCIAL INCOME AND EXPENSES

	2016 In HRK'000	2015 In HRK'000
<b>Financial income</b>		
Foreign exchange gains	138,034	56,081
Interests	11,939	8,237
Fair value of cross currency swap (Note 25)	74,921	-
Dividend income	7,176	3,094
Other financial income	5	-
NEK d.o.o. – other financial income	798	3,067
Total financial income	<b>232,873</b>	<b>70,479</b>
<b>Financial expenses</b>		
Interests	(246,857)	(287,316)
Foreign exchange losses	(110,727)	(189,244)
Fair value of cross currency swap	-	(12,449)
Bond repurchase	-	(178,943)
Fair value of shares	-	(969)
NEK - Other financial expenses	(1,781)	(1,461)
Other financial expenses	(6,304)	(138)
Total financial expenses	<b>(365,669)</b>	<b>(670,520)</b>
<b>Net loss from financial activities</b>	<b>(132,796)</b>	<b>(600,041)</b>

## 10. CORPORATE INCOME TAX EXPENSE

	2016	2015
	In HRK'000	In HRK'000
Current tax	450,226	452,441
Deferred tax expense / (income) relating to the origination and reversal of temporary differences	95,133	3,226
<b>Corporate income tax expense</b>	<b>545,359</b>	<b>455,667</b>

Adjustments of deferred tax assets are shown as follows:

	2016	2015
	In HRK'000	In HRK'000
Balance at 1 January	650,681	653,907
Reversal of deferred tax assets	(112,497)	(47,609)
Recognition of deferred tax assets	17,277	44,383
Balance at 31 December	<b>555,461</b>	<b>650,681</b>

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

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

	2016	2015
	In HRK'000	In HRK'000
Profit before taxation	2,590,361	2,395,724
<b>Income tax at the applicable rate in the Republic of Croatia of (20%)</b>	<b>518,072</b>	<b>479,145</b>
Tax unrecognized income	(73,090)	(40,506)
Tax effect on permanent differences	95,133	3,226
Unrecognized deferred tax assets from companies operating with loss	5,244	13,802
<b>Tax expense for the year</b>	<b>545,359</b>	<b>455,667</b>
Effective tax rate	21%	19%

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

#### 10. CORPORATE INCOME TAX EXPENSE (continued)

The Group and its subsidiaries are subject to corporate income tax, according to the tax laws and regulations of the Republic of Croatia. Subsidiaries in the Group stated total tax losses in the amount of HRK 1,035,951 thousand (2015: HRK 1,444,665 thousand), while the Group stated total corporate income tax expense in the amount of HRK 450,226 thousand (2015: HRK 452,441 thousand) and deferred tax assets in the amount of HRK 95,133 thousand (2015: HRK 3,226 thousand).

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

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

Year of tax loss origination	Total tax loss stated by the Groupe	Year of expiry
	HRK'000	
2012	565,360	2017
2013	207,334	2018
2014	168,027	2019
2015	69,009	2020
2016	26,221	2021
	<u>1,035,951</u>	

Group companies which are continuously stating losses in their financial statements, are not recognizing deferred tax assets. HEP d.d. is realizing profit and has no tax losses carried forward to be utilized. According to the Croatian legislation, it is not possible to utilize tax losses at the Group level. Each individual company determines its tax liability.

As of 31 December 2016, the Group could not recognize deferred tax assets arising from tax losses carried forward in the amount of HRK 1,035,951 thousand.

# 10. CORPORATE INCOME TAX EXPENSE (continued)

In recent years Croatian Tax Authorities have not performed a review of the corporate income tax returns of HEP d.d. and its subsidiaries, except the short monitoring in 2013. In accordance with local regulations, 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 liabilities and penalties. The Company's Management is not aware of any circumstances that could lead to a potential material liability in this respect.

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

In HRK'000	Inventories write-off	Provisions for jubilee awards and retirement benefits	Depreciation over prescribed rates	Provision s for MTM bonds	PPE impairment	Tax losses carried forward	Other	Total
<b>As at 1 January 2015</b>	<b>42,243</b>	<b>82,414</b>	<b>6,908</b>	<b>-</b>	<b>477,881</b>	<b>-</b>	<b>44,461</b>	<b>653,907</b>
Credited to profit and loss for the year	2,832	10,791	2,105	16,375	(26,682)	3,242	(11,889)	(3,226)
<b>As at 31 December 2015</b>	<b>45,075</b>	<b>93,205</b>	<b>9,013</b>	<b>16,375</b>	<b>451,199</b>	<b>3,242</b>	<b>32,572</b>	<b>650,681</b>
Transfers to another account	-	(105)	-	-	-	-	18	(87)
Credited to profit and loss for the year	(2,399)	(17,788)	476	(10,570)	(56,621)	(1,902)	(6,329)	(95,133)
<b>As at 31 December 2016</b>	<b>42,676</b>	<b>75,312</b>	<b>9,489</b>	<b>5,805</b>	<b>394,578</b>	<b>1,340</b>	<b>26,261</b>	<b>555,461</b>



## 11. PROPERTY, PLANT AND EQUIPMENT

In HRK'000	Land and buildings	Fixtures and equipment	Assets under construction	Total
<b>COST</b>				
<b>As at 1 January 2015</b>	<b>37,910,992</b>	<b>43,912,045</b>	<b>4,188,741</b>	<b>86,011,778</b>
Transfers to another account	(156,753)	156,294	219	(240)
Additions	16,009	324,141	1,997,895	2,338,045
Additions NEK	-	100,899	519	101,418
Transfer from assets under construction	415,538	1,327,783	(1,788,095)	(44,774)
Inventory surpluses	13,523	16,334	-	29,857
Disposals	(117,081)	(373,617)	(12,705)	(503,403)
<b>As at 31 December 2015</b>	<b>38,082,228</b>	<b>45,463,879</b>	<b>4,386,574</b>	<b>87,932,681</b>
Transfers to another account	298,204	(303,614)	-	(5,410)
Additions	5,602	261,579	2,091,299	2,358,480
Additions NEK	-	-	208,761	208,761
Transfer from assets under construction	749,456	2,966,971	(3,767,586)	(51,159)
Transfer from assets under construction - NEK	112,456	127,405	(239,861)	-
Inventory surpluses	8,155	8,666	-	16,821
Disposals	(92,360)	(437,549)	(1,954)	(531,863)
<b>As at 31 December 2016</b>	<b>39,163,741</b>	<b>48,087,337</b>	<b>2,677,233</b>	<b>89,928,311</b>
<b>ACCUMULATED DEPRECIATION</b>				
<b>As at 1 January 2015</b>	<b>25,855,401</b>	<b>30,632,822</b>	-	<b>56,488,223</b>
Depreciation for the year	671,785	959,834	-	1,631,619
Depreciation for the year - NEK	-	213,765	-	213,765
Transfers to another account	(75,614)	75,580	-	(34)
Disposals	(113,300)	(364,966)	-	(478,266)
Inventory surpluses	6,349	(38,004)	-	(31,655)
<b>As at 31 December 2015</b>	<b>26,344,621</b>	<b>31,479,031</b>	-	<b>57,823,652</b>
Depreciation for the year	672,049	1,043,998	-	1,716,047
Depreciation for the year - NEK	25,179	104,703	-	129,882
Transfers to another account	49,912	(49,881)	-	31
Disposals	(62,047)	(437,798)	-	(499,845)
Inventory surpluses	4,743	(17,288)	-	(12,545)
<b>As at 31 December 2016</b>	<b>27,034,457</b>	<b>32,122,765</b>	-	<b>59,157,222</b>
<b>CARRYING AMOUNT</b>				
<b>At 31 December 2016</b>	<b>12,129,284</b>	<b>15,964,572</b>	<b>2,677,233</b>	<b>30,771,089</b>
<b>At 31 December 2015</b>	<b>11,737,607</b>	<b>13,984,848</b>	<b>4,386,574</b>	<b>30,109,029</b>

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

The Group owns a large number of properties, however titles to individual properties has not been fully resolved. The Group is in process of registering ownership over properties. Due to a large number of properties, there is a possibility that all properties of the Group are not registered in the Group's business ledgers. Also, there is a possibility that the Group's business ledgers include records of properties to which the Group has no title. The Management Board of the parent company adopted the Decision on measures and activities related to resolving the ownership status of properties of HEP d.d. and subsidiaries dated 27 June 2013. The Decision contains tasks and deadlines for the purpose of submitting proposals to the Land Registry Courts in order to register ownership rights. Activities on land-registry will be continued in 2017.

The Water Act that came into force on 1 January 2010, raised a question on the ownership and legal status of the Group's property - reservoirs and ancillary facilities used for generation of electricity from hydropower plants, which are, according to the Water Act defined as "Public water resources in general use as the property in ownership of the Republic of Croatia". The Group acquired above mentioned property through payment to previous owners, uniting an extremely large number of cadastral plots (land plots), which were submerged by the construction of the dam and therefore created reservoirs. 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.

## 12. INTANGIBLE ASSETS

	In HRK'000
<b>COST</b>	<b>Licences</b>
<b>Balance at 31 December 2014</b>	<b>656,402</b>
Transfers to another account	240
Additions	26,308
Transfer from assets under construction	44,774
Disposals	(1,108)
<b>Balance at 31 December 2015</b>	<b>726,616</b>
Transfers to another account	5,410
Additions	21,885
Transfer from assets under construction	51,159
Disposals	(7,295)
<b>Balance at 31 December 2016</b>	<b>797,775</b>
<b>ACCUMULATED AMORTIZATION</b>	
<b>Balance at 31 December 2014</b>	<b>579,356</b>
Transfers to another account	34
Amortization for the year	26,897
Disposals	(1,108)
<b>Balance at 31 December 2015</b>	<b>605,179</b>
Transfers to another account	(31)
Amortization for the year	42,337
Disposals	(7,296)
<b>Balance at 31 December 2016</b>	<b>640,189</b>
<b>CARRYING AMOUNT</b>	
<b>At 31 December 2016</b>	<b>157,586</b>
<b>At 31 December 2015</b>	<b>121,437</b>

### 13. INVESTMENT PROPERTY

As of 31 December 2016 and 2015 investment property comprise properties held for the purposes of earning rentals and/or capital appreciation, and are carried at fair value by reference to the best management estimate. The fair value comprise estimated market price at the end of the reporting period. All investment properties are owned by HEP d.d.

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

<b>At fair value</b>	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
Fair value	<b>236,778</b>	<b>236,153</b>
Net fair value adjustment	(5,914)	(795)
<b>Closing balance at fair value</b>	<b>230,864</b>	<b>235,358</b>
Investment property NEK	627	1,420
	<b>231,491</b>	<b>236,778</b>

#### 14. PREPAYMENTS FOR PROPERTY, PLANT AND EQUIPMENT

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Alstom Hrvatska d.o.o.	8,066	-
Arvos Ljungstroem GMBH	1,600	-
Končar KET	6,482	4,269
JSC Tehnopromexport –TE Sisak	58	58
Končar GIM	1,527	2,707
Litostroj Slovenia	85	160
VOITH Siemens Austrija	16	16
Končar inženjering Zagreb	350	2,605
Spegra Inženjering	1,046	2,224
Đuro Đaković Holding d.d.	2,754	19,810
Siemens	4,282	461
TPK Orometal d.d.	3,101	736
Other	7,340	4,834
	<b>36,707</b>	<b>37,880</b>

Prepayments for PPE relate to construction of production facilities.

## 15. INVESTMENT IN THE NUCLEAR POWER PLANT KRŠKO

### Investment background

Legal status of the Nuclear Power Plant Krško ("NE Krško") was regulated by inter-republic (between Slovenia and Croatia) 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 NE Krško in Slovenia, the other 50% was held by ELES d.o.o., Ljubljana, the legal successor of the Slovenian power utility.

In 1998, the Slovene government passed a decree transforming the NE Krško into a public company, NE KRŠKO d.o.o. ("NEK"), 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 NEK was cut off 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 NEK, usage and decommissioning, as well as a partnership agreement between HEP d.d. and ELES GEN d.o.o. This agreement was ratified by the Croatian parliament during 2002, and it came into force at 11 March 2003, following the ratification by the Slovenian parliament on 25 February 2003.

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

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

HEP d.d. started to receive electricity from NEK on 19 April 2003, and expects to receive 2,700-2,950 GWh annually up to year 2023, representing 15% 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 NEK 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 NEK as at 31 December 2003 amounted to SIT 84.7 billion (approximately: HRK 2.8 billion).

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

### **Current status**

#### **Payments to the Fund for Decommissioning of NEK**

Based on the Regulation on the amount, time and manner of payment of funds for the decommissioning and disposal of radioactive waste and used nuclear fuel of NEK, adopted by the Croatian Government on 24 December 2008, in the period from 2006 to 2016 HEP d.d. made payments to the Fund for Decommissioning of NEK in the amount of HRK 1,375,530 thousand. The amount of payment is determined by the Program of decommissioning from 2004. Actual annual liability in the amount of EUR 14,250 thousand is payable quarterly.

#### **Extension of useful life of NEK**

After NEK has obtained from the Slovenian nuclear safety administration a safety license to operate without any limitations in 2012, at the end of 2014 HEP and GEN Energija d.o.o. adopted a decision to extend the operational life of the plant until 2043. The decision to extend the operating life of NEK for 20 years was preceded with an investment feasibility study of long-term investments in the power plant.

#### **Resolution of an international arbitration dispute**

The Company has acquired the right to compensation for damages claimed from the Republic of Slovenia for undelivered electricity from NEK in the period from 1 July 2002 to 18 April 2003 in the amount of HRK 328,926 thousand (Note 5).

Compensation was paid in December 2015 and January 2016.

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

Joint operation in NEK is recognized in the financial statements by using the equity method (in 2014 the Group recognizes its share in assets, liabilities, revenues and expenses of NEK in its financial statements).

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

**15. INVESTMENT IN THE NUCLEAR POWER PLANT KRŠKO (continued)**

Extract from financial statements

In table below is shown an extract from financial statements of NEK in full (100%) amounts at 31 December 2016 and 2015:

	<b>31 Dec 2016</b>	<b>31 Dec 2015</b>
	In HRK'000	In HRK'000
Property, plant and equipment	2,400,731	2,270,953
Capital and reserves	3,339,824	3,374,393
Gross sales	1,229,413	1,372,011
Cash flow from operating activities	137,363	662,485
Profit for the year	3,396	-



## 16. INVESTMENT IN THE TE PLOMIN

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

Joint Venture Agreement from 1996 with RWE expired in May 2015. The Company signed with RWE termination of Joint Venture Agreement for TE Plomin II and the Agreement on the transfer of shares in TE Plomin II., and it became sole owner of the company TE Plomin d.o.o.

The Company paid all liabilities to RWE.

### Extract from financial statements

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

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Property, plant and equipment	257,646	205,779
Capital and reserves	182,089	181,584
Gross sales	626,734	645,363
Operating profit	9,902	15,910
Net profit	2,901	3,357
Cash flows from operating activities	76,278	115,347

**16. INVESTMENT IN THE TE PLOMIN (continued)**

	<b>2016</b> In HRK'000	<b>2015</b> In HRK'000
<b>Opening balance</b>	-	<b>29,202</b>
Equity payoff	-	(25,853)
Liabilities for dividend / Dividend payment	-	(4,054)
Increase for current year's profit	-	962
Exchange differences	-	(257)
<b>Closing balance</b>	<b>-</b>	<b>-</b>

**17. LONG TERM LOANS AND DEPOSITS**

	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
Loans given	57,373	28,947
Impairments	-	(12)
Current portion of long-term loans given	(28,400)	(330)
<b>Long-term portion</b>	<b>28,973</b>	<b>28,605</b>

## 17. LONG TERM LOANS AND DEPOSITS (continued)

Loans given to non-related parties:

	Year of loan approval	Repayment period	Loan amount	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
City of Dubrovnik	2013	5 years	5,707	2,512	2,707
City of Pregrada	2006	10 years	1,358	136	271
Did d.o.o. LNG	2007	4 years	1,010	129	129
Hrvatska	2015	5 years	63,600	54,596	25,840
<b>Total</b>				<b>57,373</b>	<b>28,947</b>
Impairment				-	(12)
Current portion				(28,400)	(330)
<b>Long-term portion</b>				<b>28,973</b>	<b>28,605</b>

## 18. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Available-for-sale investments	288,493	244,845
Other investments	7,445	1,065
	<b>295,938</b>	<b>245,910</b>

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

	2016 In HRK'000	2015 In HRK'000
<b>Opening balance</b>	<b>244,845</b>	<b>191,611</b>
Changes in fair value of available-for-sale investments	43,648	53,127
Investment in shares	-	107
<b>Closing balance</b>	<b>288,493</b>	<b>244,845</b>

# 18. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS (continued)

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

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
<b>Available-for-sale investments:</b>		
Jadranski Naftovod d.d.	286,099	242,915
Viktor Lenac d.d.	177	115
Đuro Đaković d.d.	5	5
Kraš d.d.	4	3
Pevec d.d.	555	312
Jadran d.d.	364	364
Industrogradnja grupa d.d.	490	490
Optima Telekom d.d.,	296	223
Institut IGH d.d.,	172	98
Međimurje beton d.d.	153	154
HTP Korčula d.d.	71	59
Lanište d.o.o.	72	72
Other	35	35
	<b>288,493</b>	<b>244,845</b>

# 18. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS (continued)

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
<b>Other investments</b>		
Geopodravina d.o.o.	200	200
LNG Hrvatska d.o.o.	865	865
Novenerg d.o.o.	380	-
Cropex	6,000	-
	<b>7,445</b>	<b>1,065</b>
	<b>295,938</b>	<b>245,910</b>

## 18. AVAILABLE-FOR-SALE AND OTHER INVESTMENTS (continued)

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

In 2016 and 2015 fair value was determined by a market value from Zagreb Stock Exchange as of 31 December. The market price of one share of Jadranski Naftovod as of 31 December 2016 was HRK 5,300 and as of 31 December 2015 was HRK 4,500. By fair valuation of the investment in Jadranski Naftovod as of 31 December 2016 total amount of investment was increased by HRK 43,184 thousand (2015: increased by HRK 54,037 thousand). The fair valuation in 2016 and 2015 was recognised through equity (revaluation reserves). For 18% (2015: 20%) of the increase in the value of investments, reserves were decreased and the deferred tax liability increased.

On 1 June 2010, HEP d.d. and Plinacro d.o.o. had concluded the Articles of Incorporation of LNG Hrvatska d.o.o., a liquefied natural gas company. Recapitalization was conducted in 2011 and subscribed capital was increased from HRK 20 thousand to HRK 220 thousand and in 2012 to HRK 1,730 thousand. HEP d.d. has a 50% stake in the company, and Plinacro d.o.o. has other 50%. As registered at Commercial court, on 4 February 2013 LNG Hrvatska d.o.o. was recapitalized by Plinacro d.o.o. in the amount of HRK 22,600 thousand. Subscribed capital of LNG Hrvatska d.o.o. is stated in the amount of HRK 24,330 thousand.

Based on the pre-bankruptcy settlement agreements with debtors for electricity, heating and gas sold, the Group has become a stakeholder in those companies in the total amount of HRK 2,145 thousand.

## 19. OTHER NON-CURRENT ASSETS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Housing loan receivables	17,590	21,818
Energy efficiency receivables – long-term portion	23,836	15,460
Derivative financial instruments	-	70,900
Other non-current assets	5,515	7,617
	<b>46,941</b>	<b>115,795</b>

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

## 20. INVENTORIES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Inventories of fuels and chemicals	150,627	129,118
Electric materials	330,917	320,381
Spare parts	194,400	197,320
Construction material	24,974	32,699
Gas inventory for wholesale	379,488	439,951
CO <sub>2</sub> emission units	222,957	297,128
Other inventories	74,967	62,473
Nuclear fuel and other material - NEK d.o.o.	260,113	229,941
	<b>1,638,443</b>	<b>1,709,011</b>
Value adjustment of obsolete materials and spare parts	(233,075)	(219,722)
	<b>1,405,368</b>	<b>1,489,289</b>

## 21. TRADE RECEIVABLES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Electricity – Corporate customers	1,422,648	1,473,439
Electricity – Households	489,270	478,274
Export of electricity	67,886	32,770
Heating, gas and services	791,301	805,186
Connection to transmission network	-	27,292
Receivables from NEK d.o.o.	15,057	8,951
Other	63,826	66,749
	<b>2,849,988</b>	<b>2,892,661</b>
Impairment of bad and doubtful receivables	(896,396)	(1,045,598)
	<b>1,953,592</b>	<b>1,847,063</b>

## 21. TRADE RECEIVABLES (continued)

Aging structure of unimpaired trade receivables:

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Undue	1,336,879	1,206,160
Up to 30 days	333,439	349,305
31-60 days	118,850	125,892
61-90 days	55,159	51,797
91-180 days	56,141	62,379
181-365 days	43,773	41,659
More than 365 days	9,351	9,871
	<b>1,953,592</b>	<b>1,847,063</b>

Movements in impairments were as follows:

	2016 In HRK'000	2016 In HRK'000
<b>Balance at 1 January</b>	<b>1,045,598</b>	<b>974,179</b>
Impairment of trade receivables (Note 8)	107,276	170,915
Derecognition of previously impaired trade receivables	(171,671)	(26,373)
Reversal of impairments (Note 5)	(84,807)	(73,123)
<b>Balance at 31 December</b>	<b>896,396</b>	<b>1,045,598</b>

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

## 22. OTHER SHORT-TERM RECEIVABLES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Receivables for corporate income tax	60,522	210,936
Prepayments	5,863	5,359
Receivables from the State for employees	9,714	6,435
Claims for overcharged water management fee	5,914	-
Demand and term deposits with maturity over 3 months	111,191	99,166
Demand and term deposits with maturity over 3 months NEK	275,980	417,904
Receivables from HEP-ESCO d.o.o. for Energy efficiency project	9,813	13,063
Loan receivables from companies with participating interest	25,752	-
Receivables for sold flats	6,464	6,499
Receivables from OIE - HROTE	34,774	30,548
Received bills of exchange	27,456	-
Derivative financial instruments (Note 25)	96,196	-
Other receivables NEK	2,369	2,031
Other short-term receivables	58,909	43,812
	<b>730,917</b>	<b>835,753</b>

## 23. CASH AND CASH EQUIVALENTS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Current accounts – Foreign currency	938,761	497,566
Current accounts - HRK	216,798	427,145
Current accounts for special purposes	31,686	30,706
Petty cash - HRK	260	271
Short term deposits - up to 90 days	1,314,216	1,419,032
Daily deposits	441,633	118,393
Cash Funds	75,322	-
Current account – HRK and foreign currency - NEK	170	53
	<b>3,018,846</b>	<b>2,493,166</b>



## 24. EQUITY AND RESERVES

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

### Reserves

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Opening balance	100,836	54,947
Other comprehensive income/(loss)	39,457	45,889
	<b>140,293</b>	<b>100,836</b>

### Retained earnings

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Opening balance	4,132,208	2,201,265
Other changes	-	(5,357)
Exchange losses arising on translation of foreign operations	(18,984)	(4,196)
Land surpluses	-	1,401
Dividends paid	(607,000)	-
Profit / (loss) for the year	2,045,002	1,939,095
	<b>5,551,226</b>	<b>4,132,208</b>

## 25. LIABILITIES FOR ISSUED BONDS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Nominal value of bonds in the country issued in 2007	92,946	186,410
Discounted value	84	(84)
Current maturity on bonds	(93,030)	(93,380)
	<b>-</b>	<b>92,946</b>
Value of bonds issued abroad in 2012	498,617	3,008,746
Bond repurchase (83.37%)	-	(2,806,955)
Exchange differences	(5,046)	296,826
Current portion of bonds	(493,571)	-
<b>Bonds issued in 2012</b>	<b>-</b>	<b>498,617</b>
Nominal value of bonds from 2015 issued abroad	3,656,047	3,703,533
Exchange differences	(37,511)	3,455
Discounted value	7,892	(50,941)
	<b>3,626,428</b>	<b>3,656,047</b>
Accrued bond expenses	(20,255)	(23,727)
<b>Bonds issued in 2015</b>	<b>3,606,173</b>	<b>3,632,320</b>
<b>Total liabilities for issued bonds</b>	<b>3,606,173</b>	<b>4,223,883</b>

### Bonds issued in the Republic of Croatia

Bonds issued at the end of 2007 amounting to HRK 700,000 thousand are repayable in 15 semi-annual instalments, commencing three years from the date of issue, and are bearing fixed interest of 6.50 percent. The 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 annual interest of 6%. Bonds are listed at Luxembourg stock - exchange and they are actively traded.

## **25. LIABILITIES FOR 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 converted in EUR for all period of bond duration, respectively until its outermost maturity date at 9 November 2017.

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

### *Refinancing*

In October 2015, bonds issued in 2012 were refinanced from the new bond issue and repaid 83.37% of the principal respectively USD 416,852 thousand. The amount of outstanding principal on bonds issued in 2012, on 31 December 2016 amounted to USD 83,148 thousand.

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

### *The new bond issue*

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

### *Cross currency swap*

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

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

## ***Derivative financial instruments***

### **Cross currency swap**

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

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

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

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

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

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

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

On 31 December 2016, using this measuring method, the Company stated fair value of assets by bonds issued in 2012 in the amount of HRK 96,196 thousand (Note 22) (31 December 2015: HRK 70,900 thousand), (Note 19).

On 31 December 2016, using this measuring method, the Company stated fair value of liabilities by bonds issued in 2015 in the amount of HRK 32,251 thousand (31 December 2015: HRK 81,876 thousand), (Note 29).

## 26. LONG-TERM LOAN LIABILITIES

	Interest rates	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Domestic bank loans			
	Floating	827,728	1,219,772
Foreign bank loans	Fixed	237,817	90,296
Finance leases	Fixed	13,202	16,066
<b>Total</b>		<b>1,078,747</b>	<b>1,326,134</b>
Deferred loan originated fees		(2,152)	(3,382)
<b>Total long-term loans</b>		<b>1,076,595</b>	<b>1,322,752</b>
Current portion of long-term loans		(408,711)	(383,525)
Current portion of finance lease (Note 33)		(3,120)	(2,984)
<b>Long-term portion</b>		<b>664,764</b>	<b>936,243</b>

In 2016, the Company contracted loans with domestic and foreign banks with floating and fixed interest rates ranging from 0.47% to 5.6%

Loans from domestic banks are secured by bills of exchange and promissory notes. At 31 December 2016, the Group doesn't have any liabilities covered by *sovereign loan guarantees*.

### New financing sources

For the financing of the investment plan and the regular operations in 2016 the Group used own funds and funds from loans in use.

### Loans in use

During 2016, the Group still had available funds from long-term loan approved in 2008 by KfW Entwicklungsbank in the amount of EUR 50,000 thousand for the financing of energy efficiency and renewable energy projects. As of 31 December 2016, KfW loan balance was EUR 31,5 million, and the amount of EUR 18,5 million were unutilised.

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

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

	(In HRK'000)
2017	411,831
2018	432,452
2019	138,952
2020	61,174
2021	34,338
	<hr/>
	<b>1,078,747</b>
	<hr/>

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

The primary goal related to risks resulting from covenants is to protect the Group from possible defaults, respectively early maturity of loan liabilities.

The agreed covenants are monitored and calculated based on the projected Balance sheet and the Income statement. The Group prepares preliminary calculations of the covenants in the upcoming mid-term period, and is following their trends.

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

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

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

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

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

As of 31 December 2016 covenants were not breached and the Group has met all contractual financial indicators.

The Group's total exposure to loan liabilities subject to covenant conditions as of 31 December 2016 amounts to EUR 70,588 thousand.

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

	31 Dec 2016	31 Dec 2015
<b>Currency</b>		
EUR	142,733	173,690

For the purpose of providing solvency reserves for the following mid-term period, the Company has concluded with domestic banks multi-purpose overdraft agreements in the total amount of HRK 1,0 billion. Funds from agreed overdrafts the Company may use as short-term loans, as well as for issuance of guarantees, letters of credit and letters of intention in accordance with the Group needs.

During 2016, due to good liquidity, the Group did not conclude short-term loans from preapproved mid-term multipurpose overdraft agreements. Also, the Group has signed reverse factoring agreement in the amount of EUR 50 million with maturity until 31 December 2017.

As of 31 December 2016, the Group has available the amount of up to HRK 699,3 million from short-term financing sources.

After the balance sheet date, the Government of the Republic of Croatia issued a consent on the basis of which the overdrafts of banks were prolonged for 3 years and the total amount of available short-term funds amounts to HRK 1,392 million.

## 27. LONG-TERM LIABILITIES TO THE STATE

Long-term liabilities to the State amounted to HRK 15,901 thousand in 2016 (2015: HRK 18,774 thousand) and relate to the sale of apartments to employees in accordance with the State program that was discontinued in 1996. According to the law regulating housing sales, 65% of the proceeds from the sale of apartments to employees were payable to the State at such time as the proceeds were collected. According to the law, HEP d.d. has no liability to allocate the funds until they are collected from the employee.

## 28. LONG-TERM PROVISIONS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Provisions for court disputes	337,899	367,772
Provisions for severance payments	329,693	374,550
Provisions for jubilee awards	44,986	45,875
Provisions for decommissioning of fossil fuelled power plants	161,438	128,297
Provision for electricity purchased from wind power plants	21,631	21,631
Provisions for severance payments, jubilee awards and other - NEK	35,053	31,376
	<b>930,700</b>	<b>969,501</b>

Provisions for decommissioning of fossil fuelled power plants in the amount of HRK 161,438 thousand represent discounted value of the estimated decommissioning costs of the Group's fossil fuel power plants.



## 28. LONG-TERM PROVISIONS (continued)

Movements in provisions during the presented period were as follows:

	Legal disputes	Provisions for severance payments	Jubilee awards	Decommission- ing of FFPPs	Other	Total
	In HRK'000	In HRK'000	In HRK'000	In HRK'000	In HRK'000	In HRK'000
<b>At 1 January 2015</b>	<b>363,052</b>	<b>319,691</b>	<b>44,806</b>	<b>120,689</b>	<b>54,541</b>	<b>902,779</b>
Additional provisions	25,260	77,566	8,538	7,608	-	118,972
Decrease in provisions (amounts paid)	(16,922)	(2,977)	(4,901)	-	(1,534)	(26,334)
Decrease in provisions based on estimates	(3,618)	(19,730)	(2,568)	-	-	(25,916)
<b>At 31 December 2015</b>	<b>367,772</b>	<b>374,550</b>	<b>45,875</b>	<b>128,297</b>	<b>53,007</b>	<b>969,501</b>
Additional provisions	25,870	29,789	2,031	33,141	3,677	94,508
Decrease in provisions (amounts paid)	(10,650)	(3,856)	(857)	-	-	(15,363)
Decrease in provisions based on estimates	(45,093)	(70,790)	(2,063)	-	-	(117,946)
<b>At 31 December 2016</b>	<b>337,899</b>	<b>329,693</b>	<b>44,986</b>	<b>161,438</b>	<b>56,684</b>	<b>930,700</b>

### *Provisions for court disputes*

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

HEP Proizvodnja d.o.o. is in litigation with Zagrebački Holding d.o.o., with provisions amounting to HRK 38,045 thousand in 2016 and relate to dispute for fee for wastewater treatment plant.

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

## 28. LONG-TERM PROVISIONS (continued)

### 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 take into account the overall electro-energy security in the Republic of Croatia, and the fact that the Company has constructed and invested significant funds in these facilities, that the Company maintains the mentioned facilities and is the owner of all equipment necessary for the management and functionality of the said hydroelectric 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.

In addition, during 2015 the Ministry of Agriculture initiated a procedure for amending and change of the Water Act. As part of this process, and bearing in mind all the above, the Company has submitted suggestion for amendment and change of the provisions of the Water Act with the aim of clarifying the property-ownership rights and ownership of the Republic of Croatia on electricity production facilities built by legal entities in majority ownership of the Republic of Croatia. The Ministry of Economy has also sent its consent to the initiative of the Company for amending and change of the Water Act.

In 2016 and 2017, the Company continued its activities in order to address the issue of ownership of hydroelectric power plants and reported to the Ministry of Environmental Protection and Energy on the mentioned issue.

## 28. LONG-TERM PROVISIONS (continued)

### *Provisions for severance payments and jubilee awards*

Movements in the present value of the defined employees benefits during the current period were as follows:

	<b>Retirement benefits</b>	<b>Jubilee awards</b>	<b>Total</b>
	In HRK'000	In HRK'000	In HRK'000
<b>At 1 January 2015</b>	<b>319,691</b>	<b>44,806</b>	<b>364,497</b>
Cost of services	13,309	2,308	15,617
Interest expense	14,140	1,706	15,846
Benefits paid	(8,993)	(6,829)	(15,822)
Past service cost	29,823	1,394	31,217
Actuarial (losses)	6,580	2,490	9,070
<b>At 31 December 2015</b>	<b>374,550</b>	<b>45,875</b>	<b>420,425</b>
Cost of services	12,636	2,393	15,029
Interest expense	8,636	1,161	9,797
Benefits paid	(11,639)	(5,830)	(17,469)
Past service cost	3,267	474	3,741
Actuarial (losses)	(57,757)	913	(56,844)
<b>At 31 December 2016</b>	<b>329,693</b>	<b>44,986</b>	<b>374,679</b>

## 28. LONG-TERM PROVISIONS (continued)

The following assumptions were used in preparing the calculations:

- The termination rates ranges from 0% to 5,66% and is based on the statistical fluctuation rates for the Group in the period from 2006 to 2016.
- The probability of death by age and sex is based on 2010-2012 Croatian Mortality Tables published by the Croatian Bureau of Statistics. It is assumed that the population of employees of the Group represents average with respect to mortality and health status.
- It is assumed that there will be no annual salary growth.
- Present value of the obligation was determined using a 2.8% discount rate for all Group members.

## 29. OTHER LONG-TERM LIABILITIES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Deferred income – assets financed by third parties	3,280,668	3,505,750
Long-term liabilities for assets financed from clearing debt	863,450	842,162
Cross currency swap (Note 25)	32,251	81,876
Other long-term liabilities	13,978	15,182
	<b>4,190,347</b>	<b>4,444,970</b>

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

At 31 December 2016, the Company stated clearing debt liability in the amount of HRK 863,450 thousand (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.

### 30. TRADE PAYABLES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Domestic trade payables	1,490,580	1,510,348
Foreign trade payables	169,824	73,293
Foreign trade payables - EU	97,937	136,569
Trade payables - NEK d.o.o.	28,997	20,700
	<b>1,787,338</b>	<b>1,740,910</b>

### 31. TAXES AND CONTRIBUTIONS

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
VAT liability	106,110	105,430
Utility and other fees	17,190	37,326
Contributions on salaries	21,527	22,738
Contributions and taxes for employees material right	8,878	29,530
Other	4,045	4,264
	<b>157,750</b>	<b>199,288</b>

### 32. LIABILITIES TO EMPLOYEES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Net salaries	79,092	79,744
Contributions	36,379	40,435
Severance payments for retirements	4,303	60,718
Severance payments for termination of employment contracts	-	12,406
Net salaries NEK d.o.o.	15,176	11,601
Other	20,319	21,606
	<b>155,269</b>	<b>226,510</b>

### 33. OTHER NON-CURRENT LIABILITIES

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
Prepayments received for connection fees	380,208	357,756
Other prepayments	128,914	116,202
Accrued expenses for unused vacations	71,304	61,504
Accrued income from electricity sale to households	22,077	33,539
Liabilities for calculated solidarity fee	14,612	13,980
Liabilities for fees for renewable energy sources	46,457	46,704
Accrued severance payments to employees	342,964	31,851
Accrued interest expenses	2,122	-
Accrued expenses for CO <sub>2</sub> emissions	137,289	133,740
Other accrued expenses	3,682	12,844
Current portion of liabilities for finance lease (Note 26)	3,120	2,984
NEK d.o.o. liabilities	5,045	44,420
Other	16,186	23,182
	<b>1,173,980</b>	<b>878,706</b>

Correction of household income as at 31 December 2016 was obtained by calculating the logarithmic curve using network losses of 7,87%, while for the year ended 31 December 2015, stated percentage of loss used in the calculation was 8,39%. The result is an increase in revenue for 2016 in the amount HRK 11,462 thousand in comparison to the previous year, and stated liability for accrued income in the amount of HRK 22,077 thousand (2015: HRK 33,539 thousand).

Pursuant to The Act on Air Protection (Official Gazette No. 130/2011, 47/14) and the accompanying ordinances in the area of greenhouse gas emissions, HEP d.d. has been classified as the obligator of the EU ETS system. The Group obtained permits for greenhouse gas emissions for all nine plants and monitor emissions from facilities in accordance with the approved monitoring plan and is submitting verified reports to the Environmental Protection Agency by 31 March each year, on the total CO<sub>2</sub> emissions for the previous calendar year. Based on the submitted report, and not later than 30 April of the current year, the Group is obligated to submit quantities of emission units to the EU Registry in the amount equal to the verified total greenhouse gas emissions from the facilities in the previous calendar year, according to verified report.

HEP's EU-ETS plants submitted to the EU Registry emission units in the quantities of verified emissions for 2013, 2014, 2015 and 2016.

### 33. OTHER NON-CURRENT LIABILITIES (continued)

Pursuant to the above, the cost of greenhouse gas emissions fee consists of the amount of CO<sub>2</sub> emitted (equivalent) and the price of emission units which the Group calculates on accruals (accrued expenses) and expenses of the period during the year in which the greenhouse gases emissions.

### 34. RELATED PARTY TRANSACTIONS

The Company holds 50% of shares in Krško Nuclear Power Plant d.o.o. (NEK). Although investment in NEK is recognized in the financial statements as joint operation, due to the fact that NEK is a separate legal entity, transactions between NEK and HEP d.d. are also presented within related party transactions. 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 arisen from related party transactions are presented in the table below:

	31 Dec 2016 In HRK'000	31 Dec 2015 In HRK'000
<b>NEK</b>		
Liabilities for purchased electricity	52,444	41,802
Costs of purchased electricity	609,026	664,425

Management remunerations are explained in the Note 7.

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

In HRK'000	Sales revenue		Purchase cost	
	2016	2015	2016	2015
<b>Companies partially owned by the State</b>				
Hrvatske Željeznice	101,658	107,502	1,307	2,185
INA-Industrija nafte d.d.	158,780	152,362	1,049,732	1,278,937
Prirodni Plin d.o.o.	-	-	-	-
Plinacro d.o.o.	1,377	1,456	149,952	103,603
Croatia osiguranje d.d.	2,839	4,449	1,775	2,074
Hrvatska pošta d.d.	12,147	14,069	39,331	21,785
Hrvatske šume d.o.o.	3,751	3,481	3,042	3,469
Jadrolinija d.o.o.	609	514	580	851
Narodne novine d.d.	2,346	3,663	3,639	3,682
Hrvatska radio televizija	11,713	16,394	1,514	1,422
Plovput d.d.	327	270	164	164
Croatia Airlines d.d.	974	1,096	6	2
Petrokemija Kutina d.d.	17,631	20,924	257	197
Ministry of Foreign Affairs	481	969	-	-
Ministry of Defence	21,192	21,726	-	-
Ministry of the Interior	23,236	19,090	-	-
Elementary and high schools	76,890	83,648	18	18
Judicial institutions	9,126	8,660	126	75
Colleges and universities	31,294	37,652	1,201	1,820
Legislative, executive and other bodies of Republic of Croatia	27,836	27,014	4,031	4,335
Health institutions and organizations	100,785	109,853	193	718
HROTE d.o.o.	157,687	38,055	655,880	573,697
Others	9,635	13,518	7,353	18,249
<b>TOTAL</b>	<b>772,314</b>	<b>686,365</b>	<b>1,920,101</b>	<b>2,017,283</b>



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

In HRK'000	Receivables		Liabilities	
	31 Dec 2016	31 Dec 2015	31 Dec 2016	31 Dec 2015
<b>Companies partially owned by the State</b>				
Hrvatske Željeznice	27,589	28,735	177	400
INA-industrija nafte d.d.	19,923	16,269	119,264	138,417
Plinacro d.o.o.	152	119	31,228	22,950
Croatia osiguranje d.d.	242	302	427	656
Hrvatska pošta d.d.	1,448	1,249	8,120	2,381
Hrvatske šume d.o.o.	1,029	361	13	2
Jadrolinija d.o.o.	123	91	25	487
Narodne novine d.d.	411	459	645	778
Hrvatska radio televizija	2,525	2,850	23	35
Plovput d.d.	58	8	51	51
Croatia Airlines d.d.	109	109	-	-
Petrokemija Kutina d.d.	3,176	3,773	82	152
Ministry of Defence	4,356	4,366	-	-
Ministry of the Interior	4,648	3,587	-	-
Elementary and high schools	15,531	14,658	-	-
Judicial institutions	1,495	1,254	-	-
Colleges and universities	5,519	9,979	-	-
Legislative, executive and other bodies of Republic of Croatia	5,404	4,442	-	-
Health institutions and organizations	19,881	17,261	-	-
HROTE d.o.o.	80,128	33,354	127,841	100,680
Others	18,567	21,731	18,892	19,212
<b>TOTAL</b>	<b>212,314</b>	<b>164,957</b>	<b>306,788</b>	<b>286,201</b>

### **35. CONTINGENT LIABILITIES AND COMMITMENTS**

#### **Court disputes**

In 2016 the Group has recorded provisions for court disputes for which it considers it is unlikely that they will be ruled in favour of HEP d.d. and subsidiary companies.

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

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

#### **Operating commitments**

As part of regular investment activities, at 31 December 2016 the Group had concluded agreements for investments in various facilities and equipment that has commenced but has not been completed. In 2016, the value of the most significant contracted investments in progress amounted to HRK 1,380,746 thousand (2015: HRK 1,474,040 thousand).

#### **Environmental and nature protection**

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

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

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

A request has been submitted to the Ministry of Environmental and Nature Protection (today: the Ministry of Environment and Energy) to unify environmental protection conditions (environmental permits). All nine of the HEP's plants with power inputs >50 MWt have come up with solutions on the unified environmental and energy protection (environmental permit solutions) - TE Plomin 1, TE Plomin 2, TE Rijeka, TE-TO Zagreb, EL-TO Zagreb, TE-TO Sisak, KTE Jertovec, TE-TO Osijek and Pogon Osijek HEP-Toplinarstvo.

The CO<sub>2</sub> emissions trading system was officially set up pursuant to the Decision of the Management Board of HEP d.d. under which, obligations, responsibilities and deadlines for meeting obligations for individual departments and companies within HEP's emission trading system are set. Croatian Environment Agency has opened nine "Accounts" of plant operators in the EU Greenhouse Gas Inventory. HEP successfully fulfilled its legal obligations for submission of emission units to the EU Greenhouse Gas Inventory for 2015 and for 2016 HEP entered information verifying CO<sub>2</sub> emission, which were after confirmation by Croatian officials submitted onto all nine Accounts of plant operators with the relevant quantities that corresponded the verified CO<sub>2</sub> emissions.

In 2016, non-financial sustainability report for 2015 for the HEP Group in accordance with Global Reporting Initiative (GRI 4) guidelines is finished. Sustainability Report was published on the website of HEP in Croatian and English language. Implementation of Environment management system in accordance with ISO 14001 in HEP's generation facilities is finished in 2015 and during 2016 internal audits were carried out at HEP-Proizvodnja d.o.o. and HEP-ODS d.o.o., as well as recertification procedures in facilities where it was necessary to extend the certificates.

In 2016, it is continued establishment of environmental information system (INFOZOK) with a goal of unifying data relating to environmental and nature protection. INFOZOK is upgraded with modules for data collection about usage and monitoring of water quality, managing data on environmental permits and analyzes of legal regulations in the field of environmental protection

#### **Gas supply at wholesale market**

By a Decision of the Government of the Republic of Croatia in April 2014, HEP d.d. was defined as a gas supplier on the wholesale market in a period until April 2017. Pursuant to the above Decision from the Croatian Government, the Company has rented 70% of warehouse capacities in underground gas storage facilities. 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. By the Act on Amendments to the Gas Market Act the Company is determined as suppliers on the wholesale gas Market from April 1, 2017 to March 31, 2018. Pursuant to the provisions of the Act on Amendments to the Gas Market Act, the gas storage system operator allocated to the Company 3,050 kWh or 60% of storage capacity in the underground gas storage facility.

The Wholesale Market Provider (HEP d.d.) sells gas to public service providers for the needs of household customers under regulated conditions and is obliged to provide reliable and secure gas supply.

### 36. SUBSIDIARIES

As at 31 December 2016 the Company had the following subsidiaries in its ownership:

Subsidiary	Country	Ownership interest in %	Principal activity
HEP-Proizvodnja d.o.o.	Croatia	100	Electricity generation and heating
Hrvatski operator prijenosnog sustava d.o.o.	Croatia	100	Electricity transmission
HEP-Operator distribucijskog sustava d.o.o.	Croatia	100	Electricity distribution
HEP ELEKTRA d.o.o.	Croatia	100	Electricity supply
HEP Opskrba d.o.o.	Croatia	100	Electricity supply
HEP–Toplinarstvo d.o.o.	Croatia	100	Thermal power generation and distribution
HEP–Plin d.o.o.	Croatia	100	Gas distribution
TE Plomin d.o.o.	Croatia	100	Electricity generation
HEP ESCO d.o.o.	Croatia	100	Financing of energy efficiency projects
Plomin Holding d.o.o.	Croatia	100	Development of infrastructure in area around Plomin
CS Buško Blato d.o.o.	BiH	100	Maintenance of hydro power plants
HEP–Upravljanje imovinom d.o.o.	Croatia	100	Accommodation and recreation services
HEPNOC Velika	Croatia	100	Accommodation and training
HEP –Trgovina d.o.o.	Croatia	100	Electrical energy trading and optimization of power plants production
HEP Energija d.o.o. Ljubljana	Slovenia	100	Electricity trading
HEP -MagyarorszagEnergiakft	Hungary	100	Electricity trading
HEP- Trade d.o.o. Mostar	BIH	100	Electricity trading
HEP KS sh.p.k, Priština	Kosovo	100	Electricity trading
HEP- Trade d.o.o. Beograd	Serbia	100	Electricity trading
Program Sava d.o.o.	Croatia	100	Spatial planning, design, construction and supervision
HEP Opskrba plinom d.o.o.	Croatia	100	Gas distribution
HEP-Telekomunikacije d.o.o.	Croatia	100	Telecommunication services
Hrvatski centar za čistiju proizvodnju	Croatia	100	Teaching and counseling 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 (Note 1). 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 d.o.o. changed its name to Program Sava d.o.o. za usluge. In 2015, the company APO d.o.o., for environmental protection was merged with the Company and the company HEP OIE d.o.o. was merged to the company HEP Proizvodnja d.o.o. The ownership of the company HEP NOC Velika in 2015 was transferred to HEP Operator distribucijskog sustava d.o.o.

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

### 37. FINANCIAL RISK MANAGEMENT

#### **Capital risk management**

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

#### **Gearing ratio**

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

	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
Debt	5,269,370	5,640,015
Cash and cash equivalents	(3,018,846)	(2,493,166)
Net debt	2,250,524	3,146,849
Equity	25,483,678	24,025,203
Net debt to equity ratio	<b>9%</b>	<b>13%</b>

#### **Significant accounting policies**

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

#### **Categories of financial instruments**

	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
<b>Financial assets</b>		
Available-for-sale	295,938	245,910
At fair value through profit or loss	96,196	70,900
Loans and receivables (including cash and cash equivalents)	5,454,059	4,956,580
Other non-current assets	70,399	73,500
<b>Financial liabilities</b>		
At fair value through profit or loss	32,251	81,876
Non-current liabilities	5,161,943	6,036,244
Other current liabilities	2,844,932	2,315,955

### 37. FINANCIAL RISK MANAGEMENT (continued)

#### *Financial risk management objectives*

The Treasury function within the Group provides to the companies support 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 companies through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

#### *Market risk management*

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

#### *Foreign currency risk management*

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

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

	<b>Assets</b>		<b>Liabilities</b>	
	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000	<b>31 Dec 2016</b> In HRK'000	<b>31 Dec 2015</b> In HRK'000
European Union EUR	236,444	239,017	733,424	751,030
USD	10,496	10,738	12,814	3,775

### 37. FINANCIAL RISK MANAGEMENT (continued)

#### *Foreign currency sensitivity analysis*

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

	2016	2015
	In HRK'000	In HRK'000
EUR change effect		
<b>Gain or loss</b>	375,606	390,924
USD change effect		
<b>Gain or loss</b>	1,662	(4,869)

### 37. FINANCIAL RISK MANAGEMENT (continued)

#### ***Interest rate risk management***

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

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

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

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

- Profit for the year ended 31 December 2016 would decrease by HRK 3,866 thousand (2015: HRK 5,963 thousand) based on exposure to interest rate risk. This is mainly attributable to the Group's exposure to interest rates on its floating interest rate loans representing 15,52% of all interest-bearing loans (2015: 21,33%); and
- the Group's sensitivity to interest rates would decrease during current period mainly due to decrease in floating interest rate.

#### ***Credit risk management***

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

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

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



### 37. FINANCIAL RISK MANAGEMENT (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 Group manages liquidity risk by maintaining adequate reserves, loans from banks, and other sources of financing, and by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

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

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

#### *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
<b>31 Dec 2016</b>							
Interest free		4,943,768	589,005	250,529	81,441	-	5,864,743
Floating interest	0.45%	25,923	-	-	36,230	-	62,153
Fixed interest		-	-	-	-	-	-
<b>Total</b>		<b>4,969,691</b>	<b>589,005</b>	<b>250,529</b>	<b>117,671</b>	<b>-</b>	<b>5,926,896</b>
<b>31 Dec 2015</b>							
Interest free		4,343,494	803,872	55,069	46,927	68,923	5,318,285
Floating interest	3.00%	-	-	775	26,254	-	27,029
Fixed interest		-	-	-	-	-	-
<b>Total</b>		<b>4,343,494</b>	<b>803,872</b>	<b>55,844</b>	<b>73,181</b>	<b>68,923</b>	<b>5,345,314</b>

### 37. FINANCIAL RISK MANAGEMENT (continued)

#### *Liquidity risk management (continued)*

##### **Maturity of non-derivative financial liabilities**

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

	Weighted average effective interest rate	Less than 1 month	1 - 3 months	3 -12 months	1 - 5 years	Over 5 years	Total
		HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>31 Dec 2016</b>							
Interest free		1,144,789	611,756	86,834	875,105	32,251	2,750,735
Floating interest	2.09%	70,981	29,634	297,689	693,488	-	1,091,792
Fixed interest	4.84%	313	626	837,098	963,718	3,850,940	5,652,695
<b>Total</b>		<b>1,216,083</b>	<b>642,016</b>	<b>1,221,621</b>	<b>2,532,311</b>	<b>3,883,191</b>	<b>9,495,222</b>
<b>31 Dec 2015</b>							
Interest free		1,077,052	744,376	23,429	949,204	-	2,794,061
Floating interest	2.31%	73,876	30,315	308,418	863,662	-	1,276,271
Fixed interest	5.03%	0	632	319,220	1,453,234	4,066,660	5,839,746
<b>Total</b>		<b>1,150,928</b>	<b>775,323</b>	<b>651,067</b>	<b>3,266,100</b>	<b>4,066,660</b>	<b>9,910,078</b>

The Group has access to sources of financing. The total unused amount at the end of the reporting period was HRK 839,370 thousand. The Group expects to meet its other obligations from operating cash flows and proceeds from matured financial assets.

### 37. FINANCIAL RISK MANAGEMENT (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 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 analyses the financial instruments subsequently measured at fair value, classified within 3 groups according to IFRS 13:

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

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.

### 37. FINANCIAL RISK MANAGEMENT (continued)

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

	1 <sup>st</sup> level HRK '000	2 <sup>nd</sup> level HRK '000	3 <sup>rd</sup> level HRK '000	Total HRK '000
<b>2016</b>				
Available-for-sale assets	295,938	-	-	<b>295,938</b>
Derivative financial assets	-	-	96,196	<b>96,196</b>
Derivative financial liabilities	-	-	32,251	<b>32,251</b>
Investment property	-	231,491	-	<b>231,491</b>
<b>2015</b>				
Available-for-sale assets	245,910	-	-	<b>245,910</b>
Derivative financial assets	-	-	70,900	<b>70,900</b>
Derivative financial liabilities	-	-	81,876	<b>81,876</b>
Investment property	-	236,778	-	<b>236,778</b>

### 38. OTHER DISCLOSURES

The auditors of HEP Group's financial statements provided services in the amount of HRK 730 thousand (in 2015: HRK 730 thousand). Services in 2016 and 2015 mainly relate to audit costs, review of condensed interim financial information and audits of regulatory reports prepared for regulatory needs.

### 39. EVENTS AFTER THE CONSOLIDATED STATEMENT OF FINANCIAL POSITION DATE / (CONSOLIDATED BALANCE SHEET DATE)

After the consolidated statement of financial position date / (consolidated balance sheet) date, there were no events relevant to be published in the consolidated financial statements of the Company for 2016.

### 40. APPROVAL OF THE FINANCIAL STATEMENTS

These consolidated financial statements were approved by the Management Board and authorized for issue on 28 April 2017.

Signed on behalf of the Company on 28 April 2017:

Tomislav Rosandić  
Management Board  
member

Zvonko Ercegovic  
Management Board  
member

Saša Dujmić  
Management  
Board member

Perica Jukić  
President of the  
Management Board