



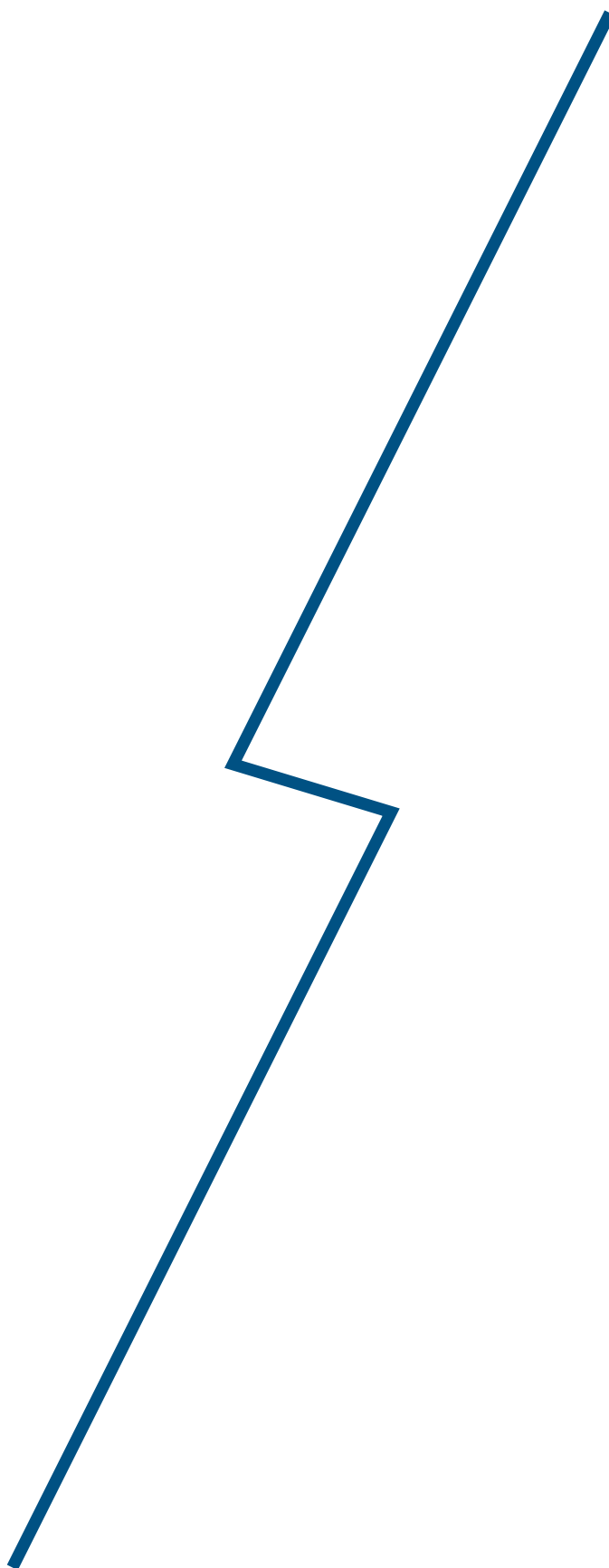
Annual Report

2014

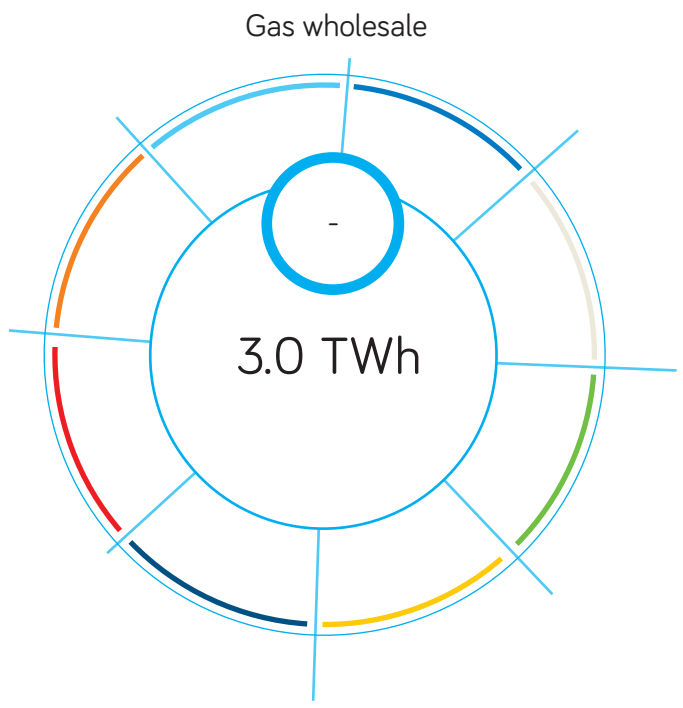
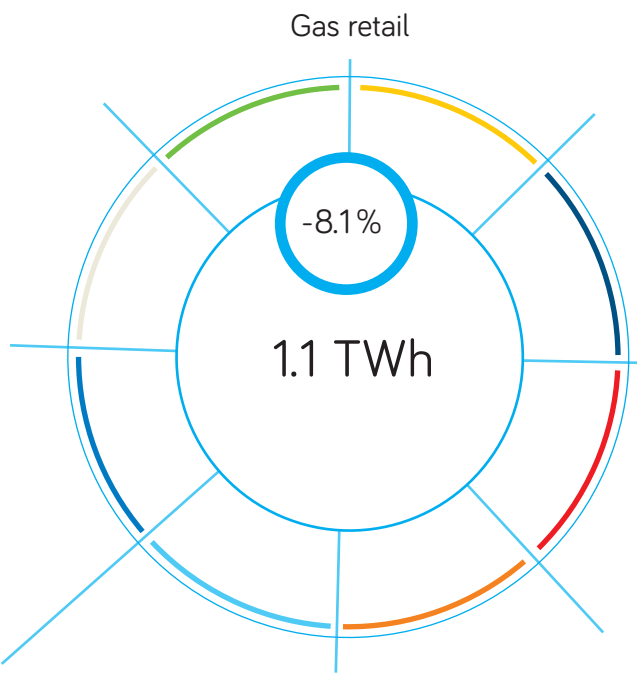
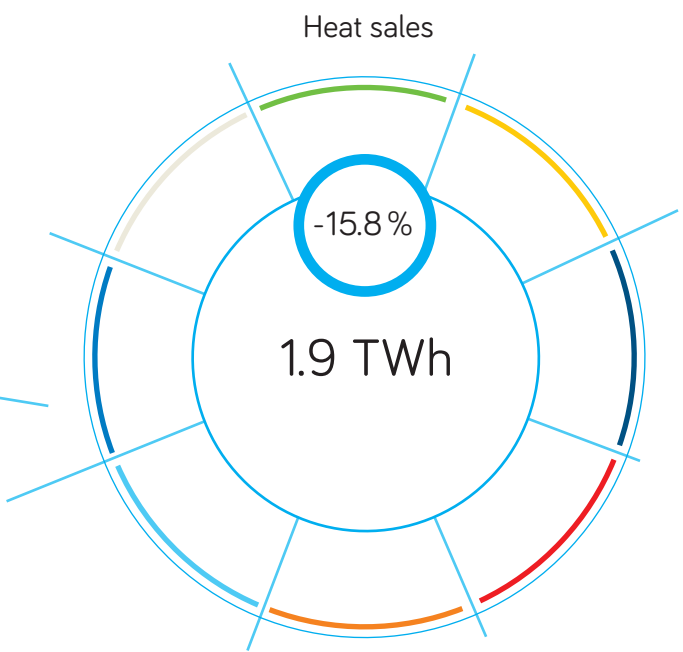
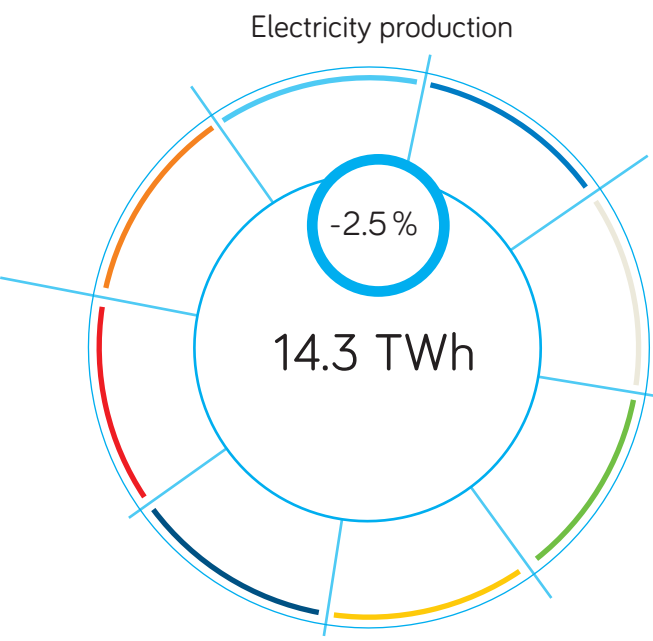
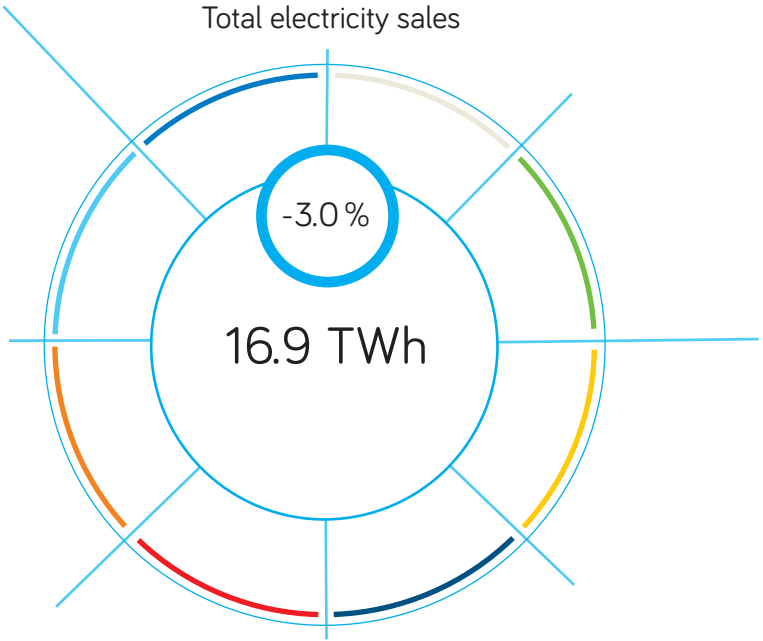


Annual
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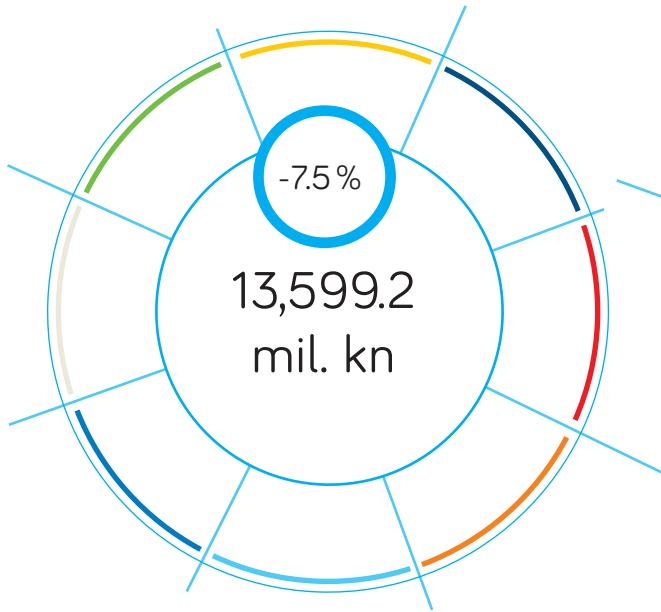
2014



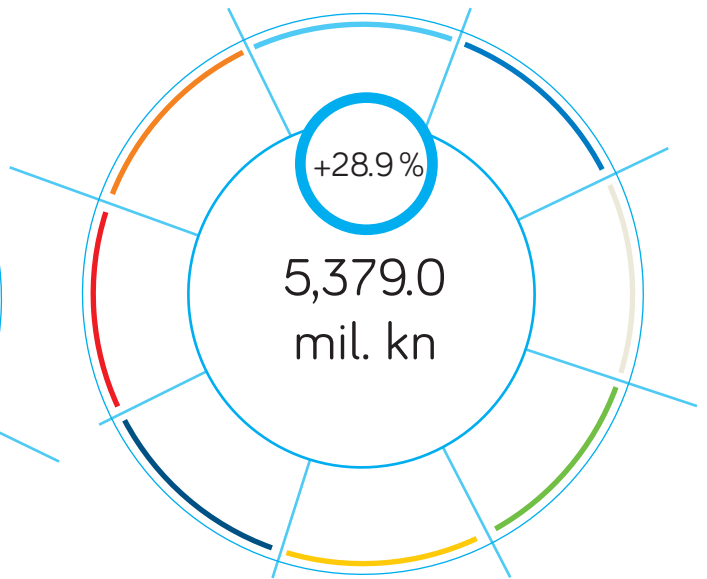
HEP Group 2014



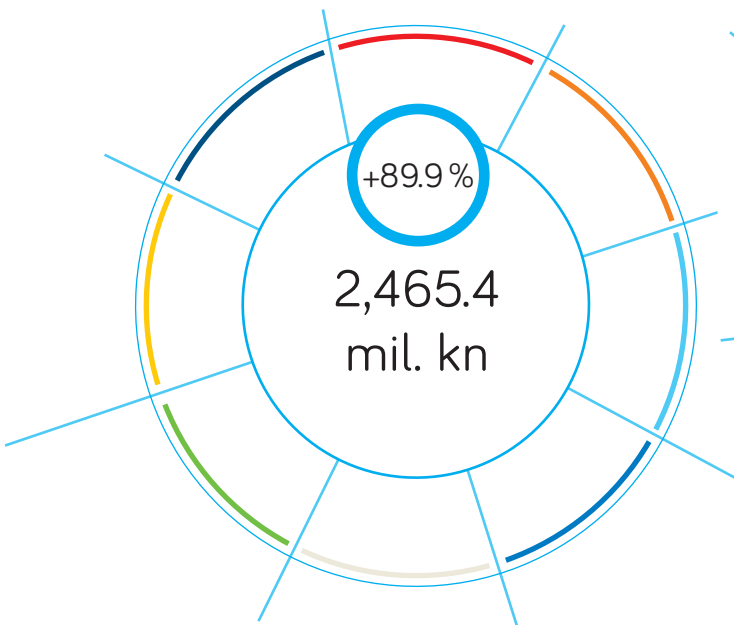
Operating income



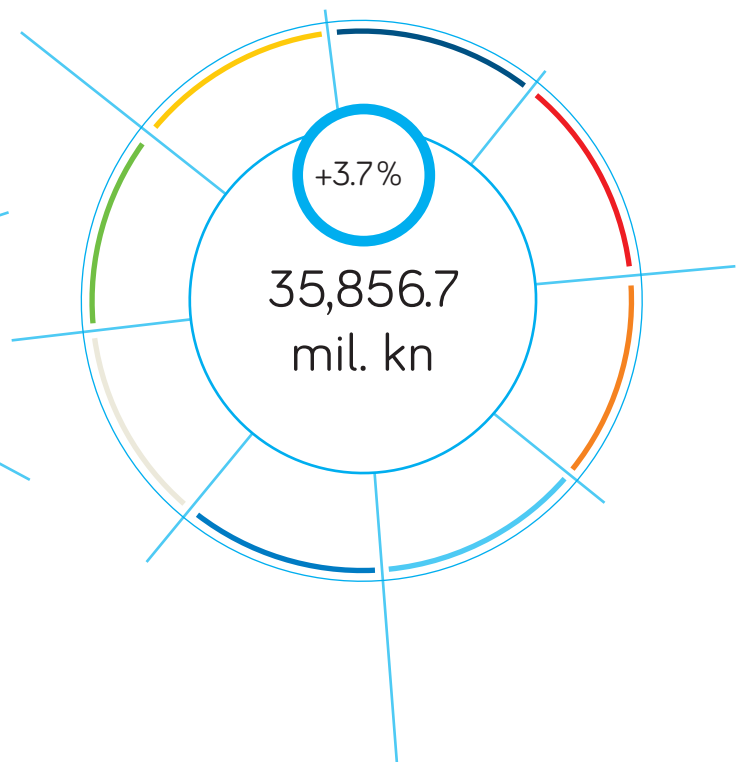
EBITDA



Group net profit



Total assets



Change
2014/2013 (%)

CONTENTS



	CHAIRMAN'S REPORT	6
	PRESIDENT'S REPORT	8
<hr/>		
1	COMPANY PROFILE	11
	Mission, vision and basic values	12
	HEP Group companies	14
	Legal framework	15
	Development – objectives, current and planned projects	19
	Membership in international organizations	24
	Short historical overview	25
<hr/>		
2	CORPORATE MANAGEMENT	27
	Governing bodies of HEP d.d.	28
	Members of governing bodies	30
	General Shareholders Assembly	32
	Audit	32
<hr/>		
3	BUSINESS OPERATIONS IN 2014	35
	Business environment	36
	Financial results achieved	37
	Results by activity	40
	Financial position	42
	Investments	43
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4	REPORT ON IMPACT ON STAKEHOLDERS	45
	Basic principles in relations with stakeholders	46
	Employees	47
	Customers	49
	Suppliers (public procurement)	54
	Community (donations)	56

5	ENVIRONMENT PROTECTION	61
	Policy and organization of nature and environmental protection function	62
	Legislation monitoring and implementation	63
	Basic indicators	64
	Major achievements in 2014	67
6	FINANCIAL STATEMENTS	71
	HEP Group – consolidated financial statements and auditor’s report	72
	HEP d.d. – financial statements	166
7	REPORTS BY HEP GROUP COMPANIES WITH FINANCIAL STATEMENTS	173
	HEP Proizvodnja d.o.o.	174
	HEP Operator distribucijskog sustava d.o.o.	183
	HEP Toplinarstvo d.o.o.	191
	HEP Plin d.o.o.	199
	HEP Opskrba d.o.o.	207
8	REPORTS BY OTHER HEP GROUP COMPANIES	217
	HEP Trgovina d.o.o.	218
	HEP Opskrba plinom d.o.o.	220
	HEP ESCO d.o.o.	222
	HEP Obnovljivi izvori energije d.o.o.	224
	Program Sava d.o.o.	225
	HEP Telekomunikacije d.o.o.	226
	HEP Odmor i rekreacija d.o.o.	227
	Ustanova HEP Nastavno obrazovni centar	228
	ADDRESS LIST	230

Chairman's report



Nikola Bruketa
Supervisory
Board Chairman

During fiscal year 2014, the Supervisory Board held ten meetings (one electronic session) in the period between two annual Assemblies. The Supervisory Board adopted the proposal submitted by the Management Board of HEP d.d. on appointing the auditor for the fiscal year 2014. BDO Croatia d.o.o. and Audit d.o.o. were jointly appointed auditors of Hrvatska elektroprivreda d.d. and its dependant companies.

During five meetings of the Audit Committee of Hrvatska elektroprivreda d.d., which also took part in the Company's operational supervision, numerous issues, in particular those regarding Company's financial reports, audit findings and activities of external auditor were discussed as well as the report on the work conducted by the Department of Internal Audit and Risk Management of HEP d.d. in 2014. The Supervisory Board supervised the conduct of Company affairs and carried out other work in accordance with the Companies Act, Articles of Association of the Company and Rules of Procedure of the Supervisory Board. It discussed and accepted information provided by the Management Board concerning overall conditions in the Company, business policy and relations with related companies, decisions significantly affecting the position of the Company, and general matters of the Company's future management. It also accepted the reports on the Company's business operations submitted during the business year and gave all necessary consents to decisions passed by the Management Board. The Supervisory Board analysed the execution of planned results and the implementation of fundamental objectives set by the Company's business policy for 2014. It also took active participation in monitoring the execution of the Work Programme of the Management Board for the term period 2014-2016 and meeting set key parameters of the Programme and planned activities.

Pursuant to the Decision adopted by the Croatian Government, the Supervisory Board revoked the appointment of the President of the Management Board Tomislav Šerić and the following Management Board members: Krunoslava Grgić Bolješić, Ivan Matasić and Perica Jukić on 12 September 2014. The Supervisory Board appointed Perica Jukić the new President of the Management Board of HEP d.d. on the same day. On 4 December 2014, Saša Dujmić and Tomislav Rosandić were appointed Board members. The Supervisory Board received the letter of resignation from Željko Štromar resigning from the position of a member of the Management Board on 28 March 2015 effective as of 31 March 2015.

At the proposal of the Company's Management Board, the Supervisory Board gave its consent for the Consolidated Economic Plan and the Investment Plan of HEP Group for 2015.

It also provided adequate prior consents regarding the following proposals:

- the engagement of an independent consultant for developing feasibility evaluation and providing the opinion regarding the possibility of connecting KKE Osijek 500 power plant onto the electric power system and relevant markets, and providing the consent for the execution of contracting procedure;
- the conclusion of the Amendment to the Agreement and the Agreement on Mutual Relations and Joint Financing of the Construction of Electric Power Facilities for Electricity Supply between HEP d.d. and HAC d.o.o.;
- the acceptance of the Plan of Company's Participation in Considering the Need for Increasing HEP d.d. Capital;
- the expression of intent for the conduct of the status change of merging APO d.o.o., a limited liability company with HEP d.d., joint-stock company;
- the expression of intent for the transfer of founders' rights of HEP-Education and Training Center onto HEP-Distribution System Operator d.o.o.;
- the engagement of consulting services for potential projects of strategic alliances, mergers and acquisitions in Croatia and the region, and the provision of consent for contracting the Framework Agreement by means of a public tender;
- the expression of interest for joint establishment of a limited liability company with RWE Hrvatska d.o.o.;
- adjustment of stock value of HEP d.d. in HEP-District Heating d.o.o.;
- emergency employment in 2015 by HEP d.d. and HEP Group companies;
- the correction of book value of thermal power plant assets pursuant to IAS 36;
- the write-off of bad debt and obsolete obligations of HEP Group as of 31 December 2014;
- the support to LNG Croatia d.o.o. for its application to CEF-Energy-2015-1 tender;
- the conclusion of the Purchase and Share Transfer Agreement of TE Plomin d.o.o. with RWE Generation SE.

The active role undertaken by the Supervisory Board in 2014 in the execution of HEP Group restructuring processes must be pointed out. It received regular reports from the Management Board of HEP d.d., expressed its opinions and provided recommendations to the Management Board focusing on enhancing operational efficiency and future strategic determinants of HEP Group in view of new circumstances emerging on the electricity market and taking an equal part in the competition.

By receiving regular reports and information from the Management Board of the Company, the Supervisory Board was continuously participating and following the activities regarding HEP Group's capital investment projects, annual investment plans and documents under which the strategic framework for investments was set.

Apart from regular reports submitted by the Management Board of HEP d.d. on operating performance and the business environment, the Supervisory Board also discussed other current topics: the selection of the financial adviser for the IPO preparation as a joint coordinator and the bookrunner, the delivery of the 2014 Investment Plan, the status of KKE Osijek 500, HPP Senj/Kosinj – Phase II, HPP Ombla, TPP Sisak C, TPP Plomin C and LNG Croatia, development of windpower plant projects in Croatia of business interest for HEP, the expressions of interest and the submission of initial data of RES projects, HEP Group restructuring project – transformation and implementation as well as the status of overall business relations and HEP's claims in other surrounding countries.

The review of business and financial reports found that the joint-stock company Hrvatska elektroprivreda and the group of its subsidiary companies had been conducting their affairs in accordance with the provisions of the Companies Act, Articles of Association, decisions of the Shareholders Assembly and the internal rules and regulations of the Company.

The Supervisory Board stated that the annual financial reports were drafted in line with the figures entered in the Company books, showing accurate property-related and operational state of affairs of the Company without expressing any objections to auditor's report on examining Company's annual financial statements and HEP Group's consolidated financial statements for 2014.

President's report



Perica Jukić, M.Sc.
President of the
Management Board

Taking a look at 2014, I would primarily like to express my satisfaction with the fact that HEP Group fully achieved its mission of safe and quality energy supply to its customers maintaining a high level of social responsibility. The Group achieved a record high net profit of HRK 2.5 billion. Thanks to our HRK 2 billion investments, we have retained the position of one of the biggest investors in Croatia.

Group's own generation facilities produced 14.3 TWh of electricity. Very good availability of power plants, transmission and distribution network was recorded with no significant disturbances in electricity, heat energy and gas supply. Improved financial performance and proactive liquidity management was recognized by rating agencies Standard & Poor's and Moody's, which repeatedly confirmed the 2013 HEP's positive outlook throughout 2014 despite negative forecasts of sovereign rating trends.

These very good business results were achieved in a demanding and volatile environment, characterized primarily by continuous unfavourable macroeconomic indicators, stronger electricity market competition resulting from the entry of alternative suppliers into household supply, and by changes in legal and regulatory framework important for energy sector operations. Challenging circumstances encouraged HEP Group to correct its development strategy, business objectives and to adjust its business system efficiently.

With the aim of retaining a dominant share of the Croatian electricity market, HEP implemented intensive measures for improving its services in 2014 as well as for developing and offering new, innovative products adjusted to customer requirements. HEP Supply remained the first choice of the biggest customers in Croatia. The competitiveness of its offer is proven by winning more than 76 percent of the total public procurement value in 2014.

Decreased income resulting from lower electricity sale was partly compensated by HEP's wholesale gas market operations. In February 2014, HEP was appointed the wholesale gas market supplier for the period from 1 April 2014 until 31 March 2017 pursuant to the Decision of the Croatian Government. As a result, HEP sells gas to suppliers under the public service obligation of gas supply under regulated terms for the needs of household customers.

The loss of income domestically is expected to be compensated by the expansion of business operations onto neighbouring markets. Preparatory activities conducted during 2014 ended up in the concrete result on the Slovenian market with HEP winning a five percent share of total electricity consumption until May 2015.

Our competitiveness is primarily the result of a very favourable structure of generation sources with hydropower plants accounting for about half the capacity. In light of their importance as the most profitable renewable energy source, HEP has embarked on a comprehensive multi-year hydropower plant refurbishment programme worth HRK 3.5 billion.

HEP intensified its RES-related business activities by expanding its portfolio in terms of power plant number and types. In April 2015, agreements for the construction of two wood biomass-fired cogeneration facilities in Osijek and Sisak were signed. These facilities will have the status of an eligible electricity producer. Such status was already acquired by nine photovoltaic power plants which were installed during 2014 onto the roofs of office buildings owned by HEP across Croatia and by small hydropower plant (mHE) Lešće. The construction of two other small hydropower plants, mHE Prančevići and Varaždin, had started, soon to be followed by the construction of mHE Peruča. In late January 2015, HEP published an invitation for all RES project leading partners in Croatia interested in selling their projects under development i.e. before the project's construction and production. Applied projects are being evaluated, which will serve as a basis for passing investment decisions on acquiring a certain number of said projects until end 2015. Having executed said activities, HEP as a leading energy company in Croatia will provide a powerful contribution to meeting national objectives harmonized with the EU energy and climate policies.

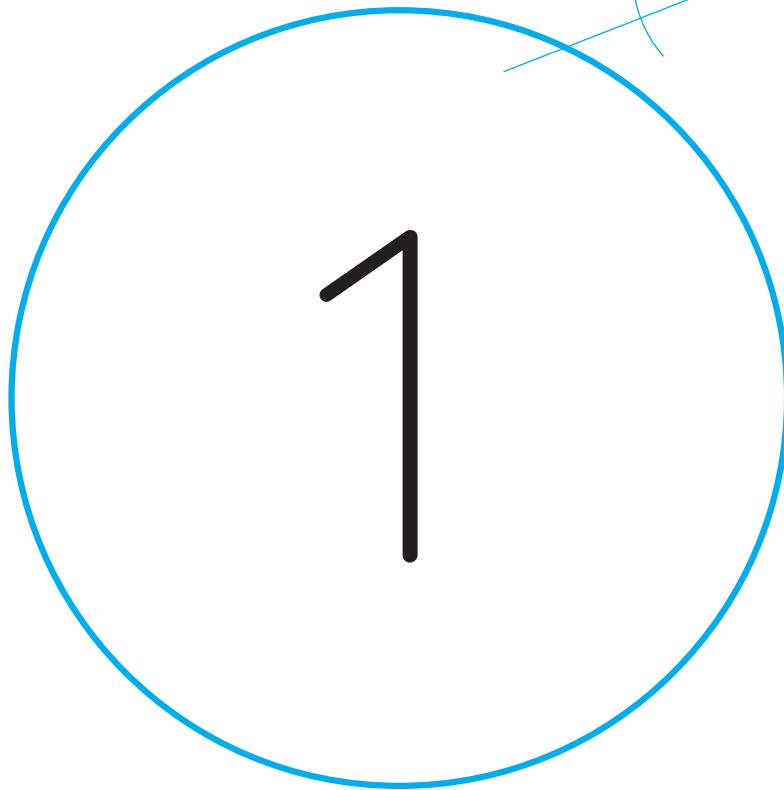
We have also been developing several conventional power plant projects, necessary primarily as a compensation for the existing units which will not meet stricter emission border values as of 1 January 2018. These are replacement, highly-efficient, natural gas-fired combined cogeneration power plants in Zagreb, Osijek and Sisak, while the Plomin site awaits its coal-fired replacement unit C, which was proclaimed the project of strategic importance for the Republic of Croatia under the Decision adopted by the Croatian Government of 15 May 2014 pursuant to the Croatian Strategic Investments Act. Following the negotiations with three bidders for the selection of the strategic partner for TPP Plomin C project, Marubeni from Japan was selected as a preferential bidder and the Exclusivity Agreement was signed in February 2015.

This report is being written during the third implementation phase of the HEP's Operational and Strategic Transformation Project, launched in 2014. There are three basic transformation directions: achieving cost efficiency as a condition for product competitiveness, the establishment of quality customer relations and meeting regulatory obligations in terms of HEP's harmonization with EU regulations. The project is expected to identify new business improvement possibilities, a stronger presence on new markets and the implementation of new technologies while increasing operating efficiency. The establishment of new business architecture and the optimization of business processes will result in significant long-term sustainable operating savings and ensure cost efficiency of HEP Group as a whole.

As the successful transformation of any business system is based on people, I would especially like to express my satisfaction with the success achieved by this Management Board in completing its priority task of establishing good relationships with social partners – trade unions. In light of the above and to mutual satisfaction, the new Collective Agreement for HEP Group was signed in November 2014, respecting HEP as the company of special importance and role for the Croatian economy.

We will continue to develop, intensely and responsibly, our primary task of making all our moves and decisions in line with the expectations expressed by our owner – the Republic of Croatia as well as all our customers. Regardless whether they include investment delivery, the price and quality of our products and services, environment or financial performance, I am convinced that all HEP employees possess sufficient experience, motive and dedication to achieve business success in all these areas.

COMPANY PROFILE





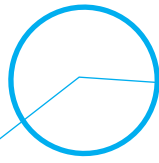
Mission

To provide secure and quality energy supply to customers, with a high degree of social responsibility.



Vision

HEP Group as a strong regional, modern and socially responsible company, recognized as an example of efficient energy generation and supply to customers.



Basic values

Competence and creativity

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

Quality and business excellence

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

Integrity

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

Environmental responsibility

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

Company profile

HEP GROUP COMPANIES

HEP d.d. (Hrvatska elektroprivreda d.d.) is the parent company of HEP Group, wholly owned by the state, the founder and sole (100%) owner of the subsidiary companies; it consolidates the management of HEP Group subsidiaries and is the owner of the assets which are contractually transferred to subsidiaries or daughter companies for management.

SUBSIDIARY COMPANIES WHOLLY OWNED BY HEP d.d.

HEP-Proizvodnja d.o.o. (HEP Generation) carries out the activity of electricity generation and heat production for district heating systems in the cities of Zagreb, Osijek and Sisak. **C.S. Buško Blato d.o.o.**, a daughter-company of HEP Proizvodnja d.o.o., is located in Bosnia and Herzegovina.

HEP – Operator distribucijskog sustava d.o.o. (HEP Distribution System Operator) is responsible for secure supply to tariff customers. The company distributes electricity taken from the transmission network, and conducts selling, metering, billing and payment collection for the electricity supplied. It is also responsible for maintenance and operation of the distribution network and plants.

HEP Opskrba d.o.o. (HEP Supply) supplies electricity, heat energy and gas.

HEP-Trgovina d.o.o. (HEP Trade) carries out the purchase and sale of electricity, the optimization of power plants' operation and trading intermediation on domestic and international markets. It has also been registered for gas supply. Its daughter companies **HEP Energija Ljubljana (Slovenia)**, **HEP Magyarorszag Energia KFT (Hungary)**, **HEP Trade d.o.o. Belgrade (Serbia)**, **HEP KS.sh.p.k Priština (Kosovo)** and **HEP Trade d.o.o. Mostar (B&H)** have the task of electricity trading in the markets of the countries of their establishment and in third markets.

HEP-Toplinarstvo d.o.o. (HEP District Heating) is active in heat production, distribution and supply in the cities of Zagreb, Osijek and Sisak and in a part of the Zagreb County. It has been registered as a heat energy buyer.

HEP-Plin d.o.o. (HEP Gas), headquartered in Osijek, distributes and supplies natural gas to customers.

HEP – Opskrba plinom d.o.o. (Gas Supply) carries out business activities of trade mediation on both domestic and foreign markets, fuel (gas) procurement contracting procedures and the sale for the needs of public service users, companies within HEP Group as well as other end customers, gas trade, gas supply and the provision of trading services.

HEP-ESCO d.o.o., a company providing energy services, develops, implements and finances market-based energy efficiency projects.

HEP – Obnovljivi izvori energije d.o.o. (HEP Renewable Energy Sources), a company for the organization and business management of the construction, operation, management and maintenance of facilities using RES for electricity and heat energy generation.

HEP – Asset Management d.o.o. (in the reporting period HEP-Leisure and Recreation d.o.o.) is the company in charge of the management of non-operating assets of HEP Group and the provision of tourism activities.

Plomin Holding d.o.o. develops local infrastructure and entrepreneurial projects in the vicinity of the Plomin power plant.

Program Sava d.o.o. (Programme Sava Ltd) is responsible for development and management of the multipurpose Programme for the Protection, Regulation and Use of the Sava River and its River Banks from the border with the Republic of Slovenia to the city of Sisak.

APO usluge zaštite okoliša d.o.o. (APO Environmental Services, merged with HEP d.d.) (its operations ceased in May 2015) is a consulting and engineering company specializing in environmental protection, especially hazardous and radioactive waste and radioactive material.

HEP - Nastavno-obrazovni centar, Velika (HEP Training and Education Center) is an educational institution which, in addition to providing live work training, conducts secondary school programmes for adults and organizes professional consultancy, seminars and courses.

COMPANIES IN MIXED OWNERSHIP

HEP Telekomunikacije d.o.o. (HEP Telecommunications), co-owned by HEP d.d., HEP-Distribution System Operator d.o.o. and Croatian Transmission System Operator d.o.o., established for providing IT and telecommunication support to HEP Group business operations.

TE Plomin d.o.o., co-owned by HEP d.d. and RWE Energie (50%:50%), operates the 210 MW power plant. (Under the Share Transfer Agreement and the Termination of Business Cooperation Agreement, the General Assembly of TE Plomin d.o.o. adopted the decision on amending the Articles of Association on 28 May 2015, under which HEP d.d. became the sole founder of the company).

LNG Hrvatska d.o.o., co-owned by HEP d.d. and Plinacro d.o.o. (50%:50%), established for the construction and management of the infrastructure necessary for receipt, storage and re-gasification of liquefied natural gas.

INSTITUTIONS

HEP Nastavno-obrazovni centar (Education and Training Centre) conducts secondary school programmes for adults and organizes professional consultancy, seminars and courses in addition to providing live work training.

Hrvatski centar za čistiju proizvodnju (Croatian Cleaner Production Center) aims at promoting the concept of cleaner production in Croatia. The services provided by the Center are designated for industry and service management sector, state administration, industry associations, educational institutions, financial organizations and the public.

INDEPENDENT TRANSMISSION OPERATOR

Hrvatski operator prijenosnog sustava d.o.o. (HOPS) (Croatian Transmission System Operator) has been unbundled from HEP Group pursuant to the Electricity Market Act and according to the ITO (Independent Transmission Operator) model.

COMPANY OUTSIDE HEP GROUP

NE Krško d.o.o. (Nuclear power plant Krško), Republic of Slovenia, co-owned by HEP d.d. and GEN Energija (50%:50%).

LEGAL FRAMEWORK

EUROPEAN LEGAL FRAMEWORK

As a full EU member, Croatia bases its energy-related national legislative framework as well as its secondary legislation on the European energy-related legal framework. Under its EU accession of 1 July 2013, Croatia accepted the obligation of fully transposing EU regulations into its national legislature including not only the so-called 'third energy package' adopted in 2009 but also a number of other regulations affecting business operations of energy companies. Some of the regulations adopted by EU during 2014 which need to be transposed i.e. implemented by member states in a set time period include the following:

- Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC;
- Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC;

- Commission Delegated Regulation (EU) No 275/2014 of 7 January 2014 amending Annex I to Regulation (EU) No 1316/2013 of the European Parliament and of the Council establishing the Connecting Europe Facility;
- Commission Implementing Regulation (EU) No 1348/2014 of 17 December 2014 on data reporting implementing Article 8(2) and Article 8(6) of Regulation (EU) No 1227/2011 of the European Parliament and of the Council on wholesale energy market integrity and transparency.

THIRD ENERGY PACKAGE

Main objectives of the Third Energy Package include stronger market competition and liquidity, the improvement of network infrastructure operation, security of supply, customers' active role and the protection as well as the promotion of renewable energy sources.

Pursuant to obligations set under Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC, in line with the Electricity Market Act (Official Gazette 22/13) and the decision adopted by the Shareholders Assembly of HEP d.d (9 April 2013), HEP – Transmission System Operator d.o.o. commenced its business operations as of 1 July 2013 under the name of the Croatian Transmission System Operator d.o.o. in line with the Independent Transmission Operator model. Under the ITO model, it has been organized as an autonomous legal entity outside the structure of the vertically integrated entity. The certification procedure, which started in March 2014, has been conducted by the Croatian Energy Regulatory Agency (HERA). Its completion is expected in late 2015.

NATIONAL LEGAL FRAMEWORK

Apart from the Energy Development Strategy of the Republic of Croatia (2009), the underlying framework within which HEP d.d. and its subsidiaries, depending on their respective energy activities, conduct their business operations includes the following legislation:

- Energy Act
- Electricity Market Act
- Gas Market Act
- Heat Energy Market Act
- Regulation of Energy Activities Act
- Energy Efficiency Act

The Energy Act (Official Gazette 120/12, 14/14) regulates the measures for safe energy supply and efficient energy generation and use. It also defines legal acts under which the energy policy and energy system planning is regulated as well as the performance of energy activities on the market or as public services and the performance of energy activities by meeting environmental and energy efficiency measures.

THE ENERGY EFFICIENCY ACT (OFFICIAL GAZETTE 127/2014)

For the purpose of achieving set energy savings objectives in final energy demand, thus complying with the EU objective of a 20 percent lower primary energy until 2020, the Energy Efficiency Act was adopted in late 2014 thus transposing Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency, amendments of Directives 2009/125/EC and 2010/30/EU and repealing Directives 2004/8/EC and 2006/32/EC. Under said Act, the efficient use of energy is regulated as well as the adoption of local, regional and national plans for improving energy efficiency and its implementation. Energy efficiency measures are set as well as energy efficiency obligations, responsibilities of the energy regulatory entity, the transmission and distribution operator as well as the energy market in connection with energy transmission, transport and distribution, energy and/or water supply and in particular the activity of energy service, energy savings and user rights in energy efficiency implementation.

This Act aims at achieving objectives of sustainable energy development: reduced adverse environmental effects by the energy sector, increased security of energy supply, meeting energy user needs as well as international obligations undertaken by Croatia for reducing greenhouse gas emissions by stimulating energy efficiency measures in all energy consumption areas.

Having adopted the Third National Energy Efficiency Action Plan for the period 2014-2016 (31 July 2014), Croatia complied with the requirements set under Article 24 of Directive 2012/27/EU on energy efficiency and reporting requirements set under Directive 2012/31/EC on the energy performance of buildings. The third national energy efficiency action plan includes the proposed energy efficiency sector measures, which implementation will achieve the objective of reduced final energy demand, as well as energy generation (transformation), transmission and distribution measures which aim at achieving primary energy savings.

ELECTRICITY

The Electricity Market Act (Official Gazette 22/2013) regulates rules and measures for secure and reliable generation, transmission, distribution and supply of electricity as well as the organization of the electricity market as part of the EU electric power market. Furthermore, it regulates the rules for end-customer protection, electric power system organization and operation, open market access, setting universal service obligation and electricity customer rights including end-customer rights, separate business accounting, separate financial reports, network access rules, the principle of reciprocity and cross-border electricity transmission.

Under the Act, the transmission system operator must be organized and operated according to one of the three models envisaged by the Directive, unbundled when selecting the particular model, and certified by HERA. Furthermore, the Act also regulates criteria for the organizational and financial unbundling of the distribution system operator as well as the obligation to develop its own visual identity different from the remaining part of the vertically integrated entity.

Under said Act, a two-year period for the harmonization and adoption of new secondary legislation was set. To that effect, the following regulations were adopted in 2014:

- Electricity Origin Setting Methodology (HERA);
- Amendments to the Methodology for setting prices for billing balancing energy to entities responsible for deviations (HERA);
- A ten-year Croatian transmission network development plan for 2015-2024 (HOPS)

A significant number of regulations which should have been adopted within one year from the entry of the Act (March 2014) into effect had not been passed until end 2014. Some of them underwent the public consultation process, and their adoption is expected during 2015.

HEAT ENERGY

The Heat Energy Market Act (Official Gazette 80/13), the umbrella act for regulating heating activities in Croatia, experienced two changes in 2014. In January, Amendments to the Heat Energy Market Act (Official Gazette 14/14) were adopted, under which the inspection supervision of the implementation of said Act had been delegated to the inspectors of the Ministry of Economy. The second change was introduced with the entry of the Regulation on the Amendments of the Heat Energy Market Act (Official Gazette 102/14) into force in mid August, under which the activity of a heat energy buyer will be performed by their current heat energy supplier for all end heat energy customers who have not selected their heat energy buyer nor entered into the heat energy consumption contract. By adopting said Regulation, the Croatian Government provided assistance to heat energy end customer as well as heat energy entities in view of the slow process of establishing new contractual relations between heat energy buyers and end customers as well as the danger of heat energy supply interruptions during the 2014/2015 heating season due to the inability to meet legal time periods for contract conclusion.

In January 2014, the Regulation on the amount and the method for paying the concession fee for heat energy distribution and the concession for the construction of heat energy distribution facilities (Official Gazette 1/14) was passed. In May 2014, the Methodology for setting the amount of tariff item amounts for heat energy production (Official Gazette 56/14) and the Methodology for setting the tariff item amounts for heat energy distribution (Official Gazette 56/14) were adopted, under which the methodologies for calculating tariff items for heat energy production and distribution in the central heating system were set as well as elements for setting the allowed income, the procedure for submitting the request for

setting i.e. changing tariff item amounts, formulae for total income calculation, spreadsheet for monitoring cost and the calculation of allowed income of both the heat energy producer and the distributor. As of September 2014, four by-laws entered into effect:

- General Conditions for Heat Energy Distribution (Official Gazette 35/14) which regulate mutual relations, obligations and responsibilities of a heat energy supplier, distributor and end customers, terms of heat energy billing and invoicing, terms of heat energy supply restriction and shutdown, investments, reconstructions and maintenance of generation facilities and indoor installations, access to heat energy metering points and connection installations, procedure in case of unauthorized heat energy use, procedure in case of technical and other heat energy supply disturbances, procedure for re-allocating end customer heat energy, procedure for disconnecting the entire building/facility from the heating system, end customer protection measures, procedure for changing the heat energy distributor, method of informing end customers on heat energy consumption and cost, the obligation on the part of the heat energy buyer to inform end customers on every change of heat energy final price, the right to consumption data including the right and terms of distributing data to other heat energy buyers and legal protection.
- General Conditions for Heat Energy Supply (Official Gazette 35/14) which regulate mutual relations, obligations and responsibilities of a heat energy producer, distributor and supplier, terms of heat energy supply quality and security, terms of heat energy supply restriction and shutdown, terms of heat energy billing and invoicing, the procedure of changing the heat energy supplier and end customer protection measures.
- Heat Energy Distribution Grid Code (Official Gazette 35/14) which regulates the description, development, construction and maintenance of distribution network, management and supervision of distribution network, connection terms, construction of connections and connection on distribution network, rights and obligations of a distributor and a distribution network user, terms of metering supplied heat energy, data publishing and information exchange, service quality and security of heat energy supply, distribution network user protection measures and unauthorized use of heat energy.
- Rules on the method of supplied heat energy cost allocation and billing (Official Gazette 99/14) which regulate the installation of devices for local separation of supplied heat energy (heat cost allocators), heating output regulators (thermostatic radiator valves) and separate heat energy consumption meters (calorimeters) pursuant to the Heat Energy Market Act. The Rules also prescribe models of cost allocation and billing of supplied heat energy on a joint heat energy meter to heat energy customers - owners of self-standing functional units, registering heat energy via devices for local separation of supplied heat energy or metering it by a separate heat energy consumption meter.

GAS

The Gas Market Act (Official Gazette 28/13,14/14) regulates rights and obligations of energy entities present on the gas market and describes energy activities. In early February 2014, the Amendments to the Gas Market Act (Official Gazette 14/14) were published introducing the new gas market participant – a wholesale gas supplier under the public service. Under the Decision adopted by the Croatian Government, this role was taken over by HEP d.d. To this effect, the Croatian Government has adopted the following decisions:

- The Decision on appointing the wholesale gas market supplier (Official Gazette 29/14);
- The Decision on setting the obligation of natural gas sale by the natural gas producer to the wholesale gas market natural gas supplier (Official Gazette 29/14);
- The Decision on the gas price under which the natural gas producer shall sell natural gas produced in Croatia to the wholesale gas market supplier (Official Gazette 29/14);
- The Decision on the gas price under which the wholesale gas market supplier shall sell gas to supplier under the public service of gas supply to household customers (Official Gazette 29/14);
- The Decision on setting the priority in conducting the procedure of allocating the gas storage system capacity to the wholesale gas market supplier (Official Gazette 29/14).

As of early 2014, the implementation of new gas market regulation general acts adopted under the Gas Market Act provisions commenced:

- Transport System Grid Code (adopted by the transport system operator - Plinacro);
- Gas Distribution System Grid Code (HERA);
- Rules on Gas Storage Use (the gas storage system operator - PSP);
- Rules on Gas Market Organization (HROTE);
- General Conditions of Gas Supply (HERA);
- Methodology for setting tariff items for gas transport (HERA);
- Methodology for setting the tariff item amount for public service of gas supply and guaranteed supply (HERA);
- Methodology for setting tariff item amounts for gas distribution (HERA).

As of 1 January 2014, the implementation of the new entry-exit model commenced for the purpose of harmonizing Croatian regulations with the EU third energy package. It replaced the post stamp based model, under which tariff item amounts were equal for all transport system users regardless of the contracting level and type, and expressed in kuna for standard cube meter per day. The new model differentiates the entry and exit points. Accordingly, there are different capacity tariff items on each separate type of the transport system entry (interconnection, production, storage) as well as the transport system exit. Apart from the above, the new model also contains the tariff item for gas volume measured at transport system exits.

Under new acts, the following gas market novelties have been introduced:

- fundamental principles of switching a gas supplier;
- capacity trading on the secondary market, which provided gas suppliers with the possibility to trade transport system capacities within a gas year and thus optimize the cost of transport system capacity lease;
- gas trading at a virtual trading point, which provided gas suppliers with new possibilities of balancing balance responsible parties.

The implementation of the Transport System Grid Code as of 1 January 2014 showed the need for the improvement and amendment of some provisions. Thus, in May 2014, the transport system operator Plinacro adopted the new transport system grid code, in effect as of 1 June 2014. HROTE also adopted new rules on gas market organization in effect as of 11 February 2014, 16 June and 1 October 2014.

In December 2014, the new Transport System Grid Code, the new Rules on Gas Market Organization and the new Gas Distribution System Grid Code (Official Gazette 155/14) were announced and entered into force as of 1 January 2015. Under said general acts, new rules of allocating measured gas volumes at transport system exists/distribution system entry points were introduced as well as new transport system balancing rules. Under the new balancing model, the rule of allocating the actually consumed balancing energy was introduced to achieve the balancing energy market price as well as to ensure balancing energy bidders a daily submission of balancing energy bids. In the above said manner, each balance responsible party may balance gas volumes entering into and existing from the transport system for its balance groups, while any gas surplus or shortage can be sold or purchased by means of a transaction conducted at a virtual trading point.

DEVELOPMENT – OBJECTIVES, CURRENT AND PLANNED PROJECTS

DEVELOPMENT OBJECTIVES

Operational optimization means the adjustment of basic factors such as the business strategy, business model, organization, business processes, human resources, IT, management methods and efficiency of the entire business model. It consists of four basic elements:

- Operational optimization of HEP Group as a whole
- Increased efficiency of business processes
- Introduction of new control elements as well as new methods of work in key segments
- Harmonization with EU regulations.

Development investment cycle. Long-term investment decisions on the construction of new generation capacities and the reconstruction of the existing ones represent the key for making investments into HEP

generation capacities. HEP has a number of potential projects in various development stages, on the existing and new locations, by using various technologies. Projects are ranked according to feasibility and profitability criteria as well HEP's priority along with objectivised decision-making procedures and investment economic viability structuring.

Creating new market products and services. HEP will try to retain its dominant market share through its new products in all segments, the use of existing experiences and data from the customer database and introducing new services based on the smart grid principles.

Regional step forward. Losing a share of domestic market imposes the need for a stronger step forward into other markets, primarily regional ones.

ELECTRICITY GENERATION

While investments into existing generation capacities focus on increasing key, strategic generation facilities, investments into new generation capacities and technologies aim, through fuel energy diversification, at ensuring long-term reliability and availability of the Group's generation portfolio, which as a whole must meet terms of security of supply, competitiveness and sustainability now and in future. One of the key long-term development objectives based on sustainable development includes investments into RES.

The delivery of long-term business objectives by investing into the generation portfolio has been carried out in a dynamic energy sector environment, which has undergone significant changes in a relatively short period. Apart from the market and market risks, big and influential changes were brought about by the development of new technologies in the area of generation and infrastructural upgrade as well as by the establishment of the new regulatory framework. One of the key changes within the surrounding defining HEP Group operations was the change of the approach towards environment and climate changes, which resulted in the changed legislative framework.

The overview of electricity generation investments

- The construction of the new combi-cogeneration Unit C at Sisak TPP entered its final stage. Its trial operation is expected in the second half 2015.
- In accordance with the Strategic Investment Project Act of the Republic of Croatia and the Decision adopted by the Croatian Government of 15 May 2014, the TPP Plomin C (fuel-imported hard coal, 500 MW capacity) was declared the strategic project for the Republic of Croatia. Under the tender for the selection of the strategic partner, Japanese Marubeni was chosen. Negotiations started in September 2014. In February 2015, the Exclusivity Agreement was concluded under which the final negotiation phase is conducted only with one bidder for the purpose of agreement conclusion. The construction start is planned in 2016 following the finalisation of funding.
- TE-TO Osijek – the replacement of Unit A with the new CCCGT facility (500 MWe/160 MWt) – the feasibility study was completed, the administrative procedure accompanied by the adoption of the EIAS conducted and the location permit issued. The tender for the construction of Unit A, capacity under 500 MWe/160 MWt, was announced as a two-stage tender, under which the first stage included the expression of interest for participation thus proving bidders' qualification. During the second stage, qualified bidders were sent the invitation to submit their initial bids as a foundation for the process of negotiation with the most favourable bidder.
- EL-TO Zagreb – the replacement of Unit A with the new CCCGT facility (500 MWe/160 MWt) – the feasibility study was completed, the administrative procedure accompanied by the adoption of the EIAS conducted and the location permit issued. The next step includes the tender for the construction of the CCCGT Unit as well as other design and engineering activities on the site.
- HPP Kosinj/Senj 2 – the EIAS and the requirements set under Natura 2000 harmonized; other important basic design data renewed as a basis for preparing the project for location permit issuance
- Phase 2 of HPP Dubrovnik – the EIAS was completed in the part pertaining to the Republic of Croatia. The administrative procedure will be initiated upon the business model agreement with Elektroprivreda Republike Srpske. Investigation works of the Plat site were completed.
- In line with the decision on the required adjustment of the project environmental documentation by carrying out the appropriate assessment for successful and acceptable continuation of the HPP Ombla construction project, the additional research of biodiversity along a wider project area was arranged. In February 2015, the Appropriate Assessment of the Project for the environment was initiated.

- In September 2014, the international tender for two biomass-fired cogeneration plants (on the location of the existing thermal power plants in Osijek and Sisak) was announced. In April 2015, the supply and construction agreements were signed. Projects are funded by the KfW bank loan, and the supply of biomass (woodchip) has been secured under long-term contracts.
- In November 2013, the construction of small hydropower plant (mHE) Prančevići began. Its commissioning is expected in second half 2015. The construction of mHE Varaždin (a biological minimum generating set) also started, while mHE Peruča with its feed-in tariff RES status is undergoing the construction preparation phase. Documentation for the reconstruction of small hydropower plants CHE Fužine and HPP Zeleni vir is being developed.
- In March 2014, nine photovoltaic power plants were installed on HEP office buildings in several cities throughout Croatia.
- In January 2015, the public invitation for the expression of interest of lead members of RES projects in the phase of development or construction preparation was announced. 104 projects applied for HEP's potential acquisition. Apart from the above, HEP also considers several acquisitions from the portfolio of already built RES generation facilities.
- Other potential projects are also under consideration, including reversible hydropower plants and their potential of increasing the total value of HEP's generation portfolio. As this project is currently in the development stage, its further activities will be determined under the feasibility study.
- Hydropower plants are continuously being refurbished for the purpose of prolonging their life span, increasing operational reliability and availability, decreasing maintenance costs and achieving better generation characteristics. The most important projects carried out in 2014 included the revitalization of HPP Zakučac with the conducted trial operation of Unit B and the launch of the reconstruction (replacement) of Unit C.

ELECTRICITY DISTRIBUTION

Investments in energy infrastructure must ensure the retention of long-term value, enable stability of fuel supply and development of fuel market for the benefit of all participants.

During 2014, a number of substations and other facilities of the distribution network was constructed, reconstructed and/or rehabilitated.

Intensified modernization and the construction of the distribution network is planned for the following period focusing on covering electricity needs and connecting new customers, especially in large cities, tourist and industrial areas. Several separate investment programmes focusing on the recovery of voltage condition in the distribution system will continue as well as the introduction of modern metering devices for metering consumption and the harmonization with new norms.

Some significant capital investments made in 2014 include 110/10(20) kV Srđ substation, 110/10(20) kV Ferenščica substation (both with a high degree of completeness regarding a distribution part of the investment), 110/10(20) kV Sesvete substation, 110/10(20) kV Imotski substation, 110/10(20) kV Zadar East substation, 110/10(20) kV Medulin substation and 110/10(20) kV Rijeka substation.

Investments made in the replacement and regulation of metering points and connections are very important as they ensure regular meter replacement as well as the reconstruction of worn-out and technically outdated connections. Further development of the distribution network will ensure long-term monitoring of consumption development, electricity market development as well as the security of supply.

DISTRICT HEATING






In 2014, the works on connecting Zagreb districts of Dubrava, Ferenščica and Ravnice onto the central heating system continued. Works on the construction of the main hot water and steam lines under phase 1 – the rehabilitation of the heat water pipeline and the replacement of the heat water network in Knežija were fully completed. The rehabilitation of the hot water and steam pipelines has been carried out as well as the introduction of the remote control system of the heating network of the city of Osijek. The rehabilitation of the warm water stations and the network in the Sisak area of Caprag is underway as well as its connection onto the condensate return steam pipeline from Sisak TPP to Energana of the Ironworks Sisak.

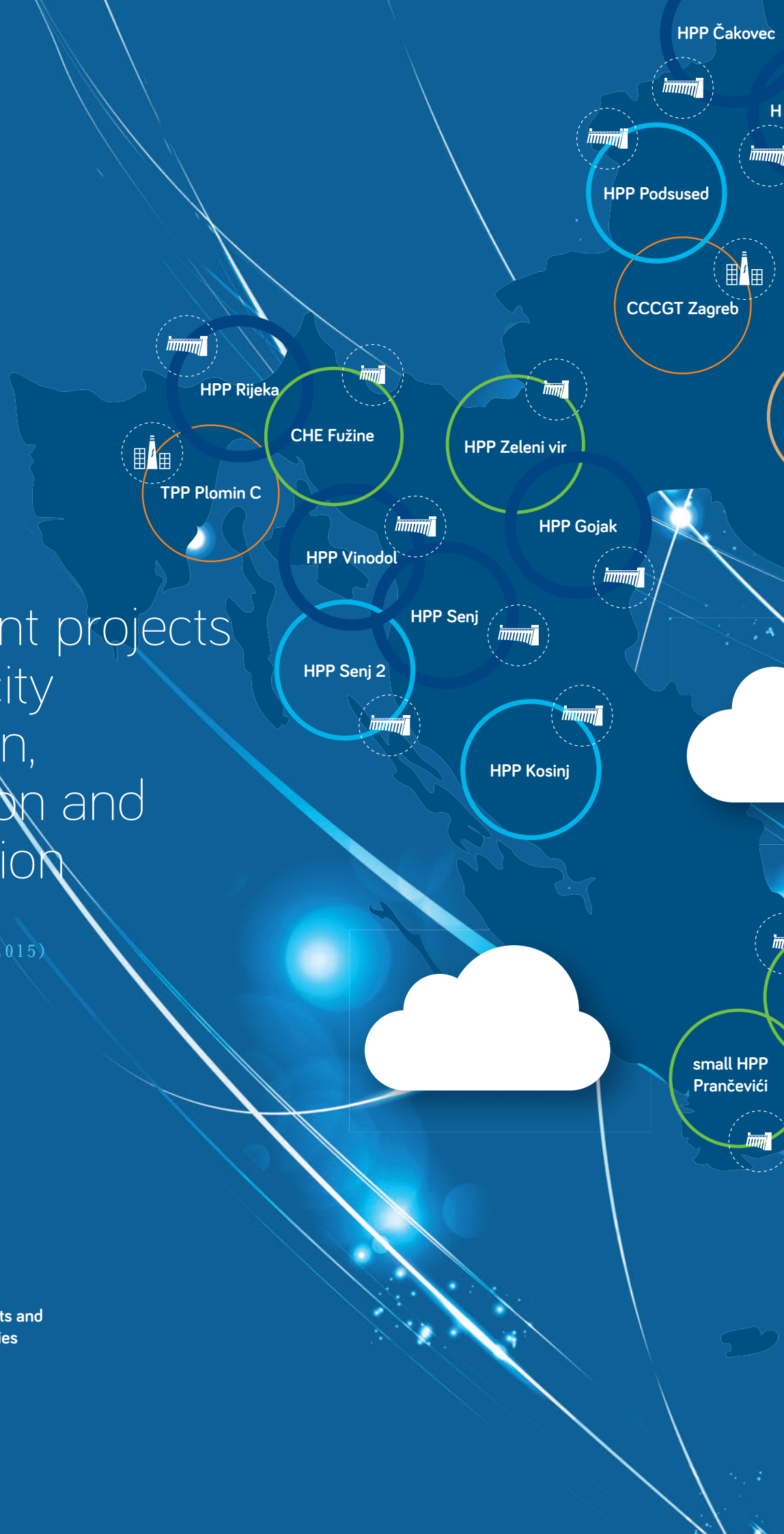
GAS

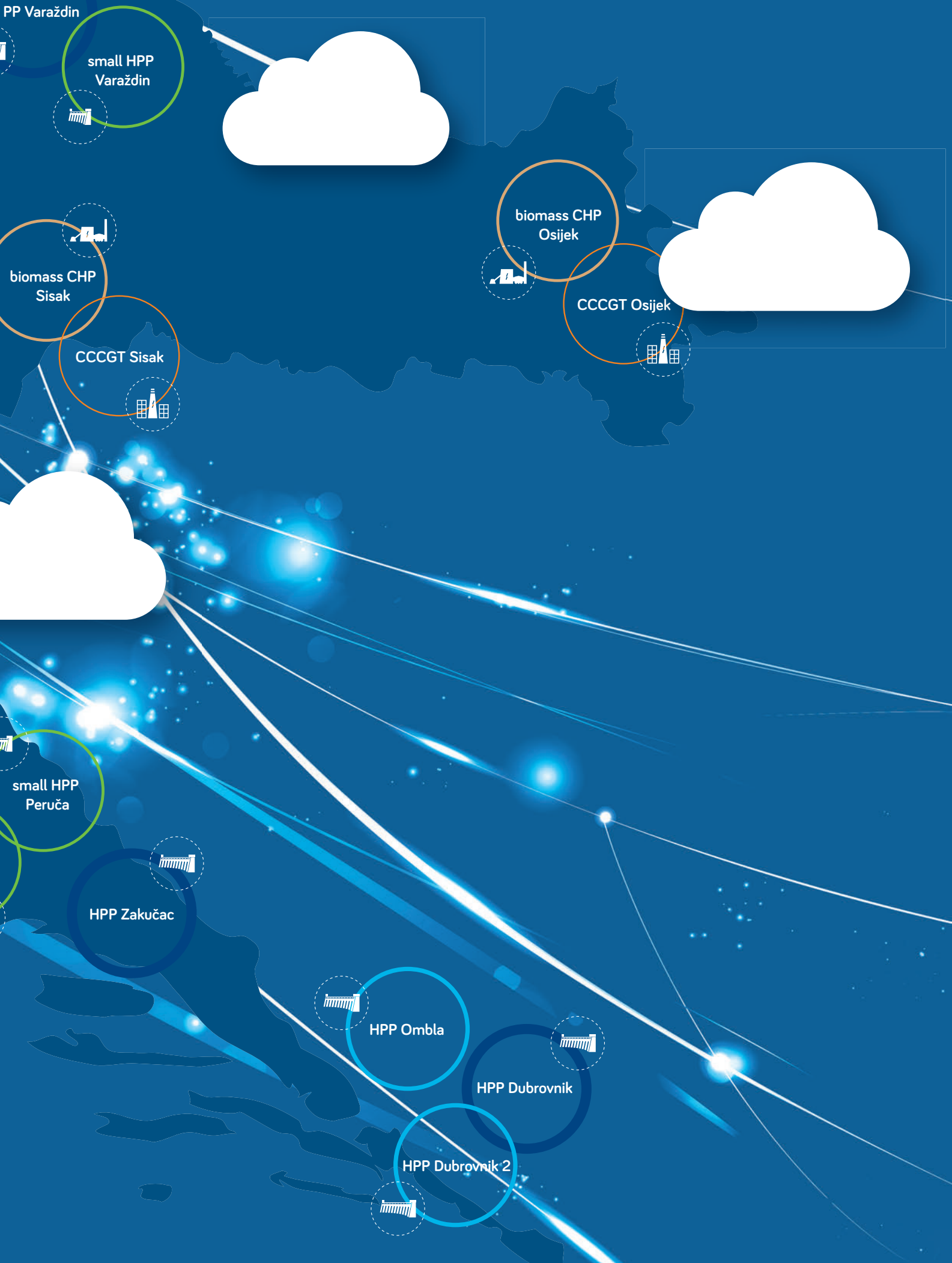
The construction of the gas network in Vuka and Kneževo settlements continued with a total of 45 km of the new gas network built.

Investment projects in electricity generation, preparation and construction

(AS OF 30 JUNE 2015)

-  hydropower plant
revitalisation
-  hydropower plant
construction
-  small hydropower
plants
-  thermal power plants and
cogeneration facilities
-  biomass
CHP plants





MEMBERSHIP IN INTERNATIONAL ORGANIZATIONS

HEP d.d. and HEP Group companies are collective and certain experts from HEP are individual members of a large number of international organizations, institutions and associations:

- **EURELECTRIC** (Union of the Electricity Industry)
- **IEEE** (The Institute of Electrical and Electronic Engineers)
- **CIGRE** (International Council on Large Electric Systems)
- **ICOLD** (International Commission of Large Dams)
- **IHA** (International Hydropower Association)
- **CIRED** (Congres International des Réseaux Electriques de Distribution)
- **CEEP** (Central Europe Energy Partners)
- **LWA** (Live Working Association)
- **EFET** (European Federation of Energy Traders)
- **IAEA** (International Atomic Energy Agency)
- **ENS** (European Nuclear Society)
- **UNICHAL** (International Union of Heat Distributors)
- **EUROHEAT & POWER** (international organization engaged in cogeneration, remote heating and cooling),
- **EWEA** (The European Wind Energy Association)
- **IIA GLOBAL** (Institute of Internal Auditors, Florida, USA), through HIIR – Institute of Internal Auditors of Croatia)
- **ISACA** (Information Systems Audit and Control Association); through the Croatian branch, ISACA Chapter Croatia)
- **ISSA** (International Social Security Association)
- **ECLA** (European Company Lawyers Association)

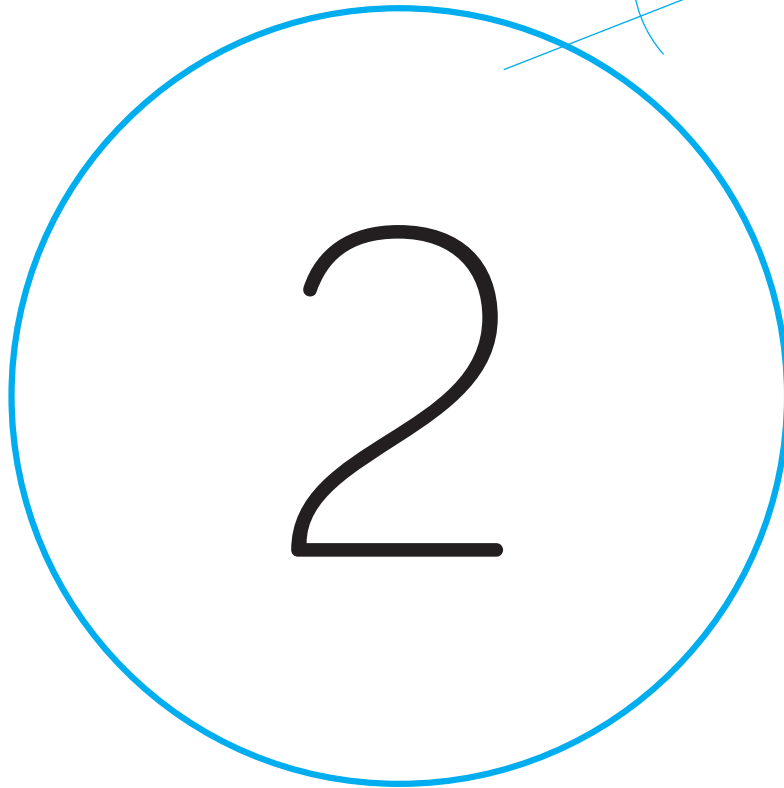
Our experts contribute to work of these organizations with their technical papers and materials, by participating in conferences, professional gatherings, symposia, workshops and seminars, circular e-mail discussions, work in bodies of these associations and in national committees. In this way, they share professional knowledge and experiences and are active members of the international energy community, directly and in an organized manner taking part in learning about, applying and creating the acquis. As such they are important participants in creating the national energy policy and legislation and in implementing activities of interest for HEP and its customers.

SHORT HISTORICAL OVERVIEW

1895 First alternating current electricity system in Croatia, Krka HPP - Šibenik

- 1912 Kraljevac HPP, among the largest hydro power plants at the time, built
- 1925 "Ante Šupuk i sin" (Ante Šupuk & Son), Šibenik, among UNIPEDE founders
- 1937 Vice Roy's Electrica Company founded
- 1941 State electrical company founded
- 1943 110 kV line Rakitje (Zagreb) - Brestanica (Slovenia) built
- 1945 Electrical company of Croatia founded
- 1954 Union of electricity companies of Croatia founded
Beginning of district heating: hot water pipeline for Končar factory from EL-TO Zagreb plant
- 1957 110kV Zagreb – Jajce (BiH) line went into service; synchronous operation of western and central system
- 1961 Business association of electricity distribution companies of Croatia founded
- 1962 First line of 220 kV network Zakučac HPP (Split) - Brinje – Mraclin (Zagreb)
- 1965 United electricity industry of Croatia founded
- 1974 Union of electricity organizations of Croatia founded
Gas distribution and supply commenced within Elektroslavonija Osijek
First 400 kV transformer station, Ernestinovo (Osijek), and first 400 kV line, Ernestinovo – Mladost, built
- 1981 Krško nuclear power plant put into operation
- 1990 Public enterprise Hrvatska elektroprivreda (HEP) founded**
- 1991 Heavy war destruction to power plants and facilities
- 1993 About 120 MW emergency diesel and gas power plants installed in Dalmatia
- 1995 Reconstruction and refurbishment of the Peruća dam completed (blasted in 1993)
- 1997 Eastern Slavonia reintegrated into the Croatian electricity system
- 1998 Gas -fired power plant (2x26 MW) put into operation at the EL-TO Zagreb site
- 2000 Plomin 2 TPP (210 MW) began commercial operation
- 2002 Hrvatska elektroprivreda d.d. restructured into HEP Group**
- 2003 Combined cycle cogeneration unit K (200 MWe/150 MWt) at TE-TO Zagreb put into operation
- 2009 Combined cycle cogeneration unit L (100 MWe, 80 MWt) at TE-TO Zagreb put into operation
- 2010 HE Lešće put into operation (42 MW)
- 2012 HEP d.d. issued bonds in the amount of USD 500 m
- 2013 Croatian Transmission System Operator unbundled from HEP Group according to ITO model
- 2014 The project of HEP Group transformation commenced
HEP d.d. became a wholesale gas market supplier

CORPORATE
GOVERNANCE



Corporate governance

In accordance with the HEP Group corporate governance model, HEP d.d. manages and partly performs tasks within corporate functions as well as directs, coordinates and monitors activities in dependant companies. Every member of the Management Board is an executive in charge of a corporate function. The main internal organization of HEP d.d. is based on corporate governance approach and on the powers the Company has over individual business activities.

GOVERNING BODIES OF HEP D.D. (FROM ARTICLES OF ASSOCIATION OF HEP D.D.)

THE MANAGEMENT BOARD OF THE COMPANY

The Management Board of the Company consists of 6 members, one of whom is appointed the president of the Management Board. The president is appointed and revoked by the Supervisory Board. The term of office of the president and members of the Management Board is 4 years.

For execution of its managerial tasks and powers, the Management Board performs the following work:

1. manages the business affairs of the Company,
2. establishes and implements the business policy, medium-term and long-term plans,
3. carries out decisions made by the Supervisory Board and the Shareholders Assembly, takes measures and issues instructions for their implementation,
4. passes internal rules and regulations of the Company and organizational rules,
5. represents and acts for the Company, and signs contracts within the framework of the law and these Articles of Association,
6. proposes decisions on matters falling in the scope of work of the Supervisory Board and Shareholders Assembly of the Company,
7. submits reports to the Supervisory Board on business policy and other principle issues regarding the future operations as well as on deviations from earlier predictions providing the reason; reports on the operational profitability and the profitability of using own capital; reports on business underway, especially income and state-of-affairs; activities which might be of a large significance for operational profitability and company's liquidity;
8. submits annual financial reports to the Company's Supervisory Board;
9. submits the report on the Company's state-of-affairs to the General Assembly once a year;
10. submits the written consolidated annual company report to the General Assembly;
11. appoints members of the Assembly and Supervisory Boards of the companies in which HEP d.d. has controlling interest or significant influence;
12. appoints and revokes Company's employees with special authorities and responsibilities;
13. passes staff and employment plans;
14. proposes and takes necessary measures and issues direct orders to ensure operations of the Company, especially the safety and operation of the power system;
15. performs other work tasks in line with the law and Company rules.

The Management Board of the Company may, subject to approval by the Supervisory Board, decide on:

1. establishing companies in this country and abroad,
2. sale and purchase of shares and stakes held by the Company in other companies, and sale of real property,
3. sale and purchase of and lien on real property exceeding HRK 20,000,000.00
4. borrowing and issuance of securities exceeding HRK 100,000,000.00
5. giving the power of attorney and waiving rights without compensation above HRK 5,000,000.00

SUPERVISORY BOARD

The Supervisory Board consists of 7 members. Six members are appointed and revoked by the Shareholders Assembly of the Company and one member is elected and revoked by workers pursuant to provisions of the Labour Act. The Decision adopted by the General Assembly on appointing and revoking members of the Supervisory Board enters into force on the day of its adoption. The term of office of the members of the Supervisory Board is four years. After the expiry of their term, the members of the Supervisory Board may be reelected. The members of the Supervisory Board elect the chairperson and a deputy chairperson among themselves.

The Supervisory Board supervises the management of the Company's business affairs. It:

1. appoints and revokes the Management Board of the Company;
2. examines and reviews business records, documentation, cash records, securities and other documents related to the operations of the Company;
3. gives approval on annual financial reports made by the Management Board of the Company;
4. gives prior approval on the decisions of the Management Board where this is required by these Articles of Association;
5. submits reports to the Shareholders Assembly of the Company on the supervision carried out, especially with respect to financial operations and their consistency with business records
6. performs other activities set by the law and Company rules.

GENERAL SHAREHOLDERS ASSEMBLY

The Shareholders Assembly is composed of shareholders and/or their proxies. The Shareholders Assembly decides on matters determined by law and these Articles of Association, in particular:

1. passes the Articles of Association and their amendments;
2. appoints and revokes the members of the Supervisory Board;
3. makes decisions on the use of profit;
4. revokes members of the Management and Supervisory Boards of the Company;
5. appoints the auditor of the Company;
6. decides on increase or decrease in the capital stock of the Company;
7. decides on status changes and dissolution of the Company;
8. carries out other work in accordance with the law and these Articles of Association.

Members of governing bodies of Hrvatska elektroprivreda d.d. (HEP d.d.)

(Changes of the management structure occurring during the reporting period have been indicated in the Independent Auditor's Report on page 166)



MANAGEMENT
BOARD

Perica Jukić, M.Sc.
President of the Board
(as of 12 September 2014)

Born in 1969. Graduated from the Faculty of Mechanical Engineering and Naval Architecture in Zagreb in 1996, obtained his Master's degree in 2005 in cogeneration facilities and distribution of heat energy. He was employed by HEP Generation in 1996 first as an independent engineer in TE-TO Zagreb, and then as the Head of Generation and the facilities' director in 2008. Within this period, he worked as a generation engineer on commissioning of the new CCGT unit (Unit K in 2004) and as a process engineer involved in the Unit L project (2006-2009). In the period from 2009 until May 2013 he was the director of the Thermal Power Plants Department in HEP-Generation d.o.o. He was the Head of the joint HEP/RWE Operation and Maintenance Committee.



Saša Dujmić,
member (as of 4 December 2014)

Born in 1970. Graduated in 1995 from the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture in Split first acquiring the associate degree in electrical engineering and then in 2007 a bachelor's degree. He attends the graduate specialist study in Energy Sector Economy at the Faculty of Economics in Rijeka. He had been employed by HEP, Elektrodalmacija Split, since 1996 first as an engineer in the Facility Maintenance Department and then in the Preparation and Implementation Department. From 2012 until 2014, he was director of Elektrodalmacija Split of HEP Distribution System Operator. He has been a visiting fellow at the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture since 2007 in the course of Electrical Equipment Maintenance and Testing. He passed the state exam for performing particular tasks in facility construction at the Ministry of Environment and Physical Planning.



Zvonko Ercegovac,
member

Born in 1965. University specialist in economics (2008) and graduate electrical engineer (electrical energy programme) (2005). In 1992, a graduate degree in electromechanical engineering. State exam in the area of electrical engineering passed at the Ministry of Construction and Environmental Protection in 1993. Before being appointed a member of the Management Board, director of Supply Department, HEP Gas from 1989, preceded by the position of a protection engineer and the head of Sales and Customer Relations. From 2006 to 2010, a member of the HERA Council.



Tomislav Rosandić,
member (as of 2 January 2015)

Born in 1975. Graduated in 1997 from the Faculty of Economics, University of Zagreb in the field of managing company's finances. He was employed by Cibala banka first as a securities analyst, and then as the director of the Retail Department. From 2000 until 2002, he was a branch manager of Zagrebačka banka, and a member of the Management Board of Dilj d.d. for a year. From 2003 until 2005, he presided over the Management Board of Dilj d.d., a member of Nexe Group. In 2005, he became the CFO of the Group, and then a member of the Management Board and its CFO. Before having been appointed a member of the Management Board of HEP d.d., he was a member of the Management Board and the CFO of Eurocable Group d.d. from 2012 until 2014. He has been a deputy chairman of the Supervisory Board of Slatinska banka. He has been a certified investment advisor since 2003, and a certified member of supervisory boards since 2007.

GENERAL SHAREHOLDERS ASSEMBLY

GENERAL SHAREHOLDERS ASSEMBLY 2014

The annual meeting of the General Shareholders Assembly was held on June 5, 2014. The Assembly reviewed consolidated and unconsolidated annual financial statements of HEP d.d. and HEP Group for 2013 including Independent Auditor's Report and the Annual Report on the state of affairs and operations of HEP d.d. and HEP Group in 2013 and the report of the Supervisory Board on the supervision conducted over HEP d.d. conduct of operations in 2013.

GENERAL SHAREHOLDERS ASSEMBLY 2015

The annual meeting of the General Shareholders Assembly was held on June 11, 2015. The Assembly reviewed consolidated and non-consolidated annual financial statements of the Company and HEP Group for 2014 including the Independent Auditor's Report, the Annual Report on the state of affairs and operations of HEP d.d. and HEP Group in 2014 and the report of the Supervisory Board on the supervision conducted in 2014. The Assembly adopted the Decision on the use of operating profits made in 2014. The Assembly adopted the Decision under which the acts of the Management and Supervisory Boards of HEP d.d. for 2014 were ratified.

A U D I T

INDEPENDENT AUDITOR

At the meeting held on June 5, 2014 the General Assembly appointed the auditing firms BDO Croatia d.o.o. and Audit d.o.o. Zagreb the auditor of HEP d.d., related companies and consolidated financial statements for HEP Group for the year ended December 31, 2014.

INTERNAL AUDIT AND RISK MANAGEMENT

The Internal Audit and Risk Management Department, as a pivotal function of HEP d.d., is responsible for the corporate function of internal audit and risk management. As such, it is a part of the internal supervision of HEP Group.

The Department carries out internal audits in line with the annual internal audit work programme. The purpose and the objective of internal audits and reports is to provide the management with a reasonable guarantee of security, efficiency and effectiveness of the business system and processes, reliability and accuracy of information, compliance of business operations with laws, regulations and HEP Group's internal rules, plans, programs and business policy.

The reports systematically provide the assessment of the revised state of affairs and business processes as well as the internal control systems. Reports on the conducted internal audits were regularly submitted to the Management Board, the Supervisory Board and the Audit Committee of HEP d.d. as well as responsible management. The Department provides recommendations for enhancing business processes, assists the Management Board of HEP d.d. and the responsible management of HEP Group in improving internal controls and mitigation of operating risks.

Pursuant to the Audit Act, the Internal Audit and Risk Management Department falls under the jurisdiction of the Audit Committee. During 2014, the Audit Committee held four meetings discussing, among others, essential topics regarding internal audit performance. This has significantly contributed to further development of the internal audit in HEP Group and facilitated the strengthening of the principle of its independence within HEP Group.

The Department submits semi-annual and annual reports on its work to the Management Board of HEP d.d., the Supervisory Board and the Audit Committee of HEP d.d. on a regular basis and pursuant to the Internal Audit Rulebook.

The internal audit operating tasks have been defined under the Internal Audit Rulebook, which has been harmonized with IPPF (International Professional Practices Framework published by the inter-

national IIA Global Association). This has significantly improved the work of the Department as well as the process of monitoring the implementation of recommendations in all internal audits according to the Departmental Annual Plan. The Rulebook is based on the basic internal audit principles (integrity, objectivity, confidentiality, expertise) and guarantees a quality normative framework required for the professional execution of internal audit activities.

HEP BUSINESS
OPERATIONS IN 2014



HEP Business operations in 2014

BUSINESS ENVIRONMENT

In 2014, the mission of HEP Group has been completely fulfilled: secure and good-quality supply of energy to customers has been achieved along with a high level of social responsibility.

The Croatian economy went through the sixth year of recession, with a further 0.4% GDP fall. Electricity prices on referential power exchanges in the surrounding area continued to be low in 2014, which despite the gas price decrease put pressure on a further decrease of generation in HEP's thermal power plants. In order to reasonably amortize the effects of unfavourable business surrounding and the strengthening of competition on the electricity and gas market, the Group has been continually focused on increasing cost and process efficiency, which, with favourable hydrological conditions, resulted in a significant financial result.

Reduced operating expenses by HRK 1.9 bn together with reduced operating income by HRK 1.1 bn led to the increase of operating income by HRK 826.8 m. Group's net profit totals at HRK 2.5 bn, compared to the last year's profit of HRK 1.3 bn. The biggest contribution to consolidated results of the Group was achieved by electricity, which was followed by gas, whereas the loss was recorded by district heating activity.

Lower income from electricity compared to 2013 is the result of the reduced price for households within the universal service and for business customers within the guaranteed supply as of 1 October 2013 as well as the reduced average price for HEP Supply customers due to adjustments made to meet the competitive environment accompanied by decreased consumption in Croatia and a loss of a market share. The loss of a market share encouraged HEP Group to create new products and services for its customers, to focus the marketing campaign on strengthening HEP's brand and a number of other activities for improving the quality of customer relations aimed at retaining the leading position on the electric power market. In late 2013, households were offered an innovative package of electricity supply services called Hepi.

Lower income from heat and gas retail sales is the result of higher average air temperatures during winter. HEP Group has expanded its gas supply service beyond the area covered by its distribution network in eastern Slavonia by offering its existing electricity customers the gas supply as well.

Under the Decision adopted by the Croatian Government, Hrvatska elektroprivreda d.d. has been appointed the wholesale gas supplier in the period from 1 April 2014 until 31 March 2017. As the wholesale gas supplier, as of 1 April 2014, it sells gas under regulated conditions to suppliers under the public service obligation of supplying gas to households and ensures a reliable and secure gas supply. In March 2014, HEP d.d. concluded the contract with 35 household suppliers. In 2014, HEP Group recorded income from this business activity of HRK 689.6 m.

In 2014, total electricity turnover (sale domestically and abroad) amounted to 19 TWh, of which 14.3 TWh was generated in power plants fully or partially owned by HEP Group, while the remaining portion was procured on the market. 16.9 TWh was allocated for the needs of domestic customers and covering the network losses, while 2.1 TWh was sold on neighbouring markets. Gross domestic electricity consumption was reduced by 2.2 percent.

Due to lower generation in thermal power plants and lower procurement of electricity, reduced costs of electricity and fuel procurement additionally strengthened Group's liquidity, so all trade payables were settled within due periods, whereas the investments were funded by own means without the need for new long-term debts.

HEP Group continued to be one of the biggest investors in Croatia in 2014 with its HRK 2 billion investments. The replacement of equipment, reconstructions and refurbishments of the existing generating facilities and the distribution network were continuously conducted.

In the process of choosing a strategic partner for the construction and management of Unit C of the thermal power plant Plomin, HEP chose Marubeni from Japan as the preferential bidder in September 2014 and signed the Exclusivity Agreement on 25 February 2015.

In line with the current practice, future decisions on planning and delivering investment projects will also be made exclusively on the basis of the objective procedure of determining HEP's priority interests and ranking projects according to criteria of feasibility and cost-effectiveness.

Ratings by Standard and Poor's ('BB-' with a positive outlook) and Moody's ('Ba2' with a positive outlook) are in compliance with financial market demands and facilitate favourable indebtedness on the capital market. The confirmation of the rating grade with a stable outlook reflects HEP's financial results, supported by strengthened liquidity and favourable hydrological conditions throughout the previous year.

HEP Group has been carrying out the Project of Operative and Strategic Transformation which will, in light of the new business structure and the optimization of business processes, lead to significant long-term operating sustainable savings and ensure cost efficiency of HEP Group as a whole as well as strengthen its market competitiveness. Essential structural changes are also conducted with an aim of harmonizing business and mutual business relations with energy regulations.

ACHIEVED FINANCIAL PERFORMANCE

According to financial indicators, HEP Group is one of the biggest business entities in the Republic of Croatia. The long lasting recession and economic slow-down had been causing reduced energy consumption in Croatia for a number of years, the trend which continued in 2014.

Due to favourable hydrological conditions in 2014, the record-high hydro generation of electricity was achieved. Generation in gas-fired thermal power plants was lowered due to high costs of generation in comparison with the prices of electricity on the wholesale market, while the electricity procurement on the market was also reduced due to losing a part of customers, which switched to alternative suppliers resulting in lower sales. All the above impacted the costs of electricity procurement, which were decreased by HRK 986.2mn (45.1%) and the costs of energy fuel, decreased by HRK 1,093.1m (40.0%). Although operating income was reduced due to the decrease in electricity sale, a significantly higher reduced costs led to the increase of operating revenue of HRK 3.2 bn (HRK 2.4 bn in 2013). The increase in profit was affected by gas wholesale as well as a slightly higher export of electricity surpluses generated in hydro power plants. HEP Group's net profit totals at HRK 2,465.4 m, of which HRK 2,462.3 m is attributable to equity holders of the parent.

Consolidated profit and loss account (abridged)					HRK m
	2012	2013	13/12 (%)	2014	14/13 (%)
Operating income	14,019.6	14,694.9	+4.8	13,599.2	-7.5
Operating cost	13,670.3	12,321.3	-9.9	10,398.7	-15.6
Operating profit	349.3	2,373.6	+579.6	3,200.4	+34.8
Group net profit	35.8	1,298.2		2,465.4	+89.9
Net profit attributable to equity holders of the parent	27.1	1,292.3		2,462.3	+90.5

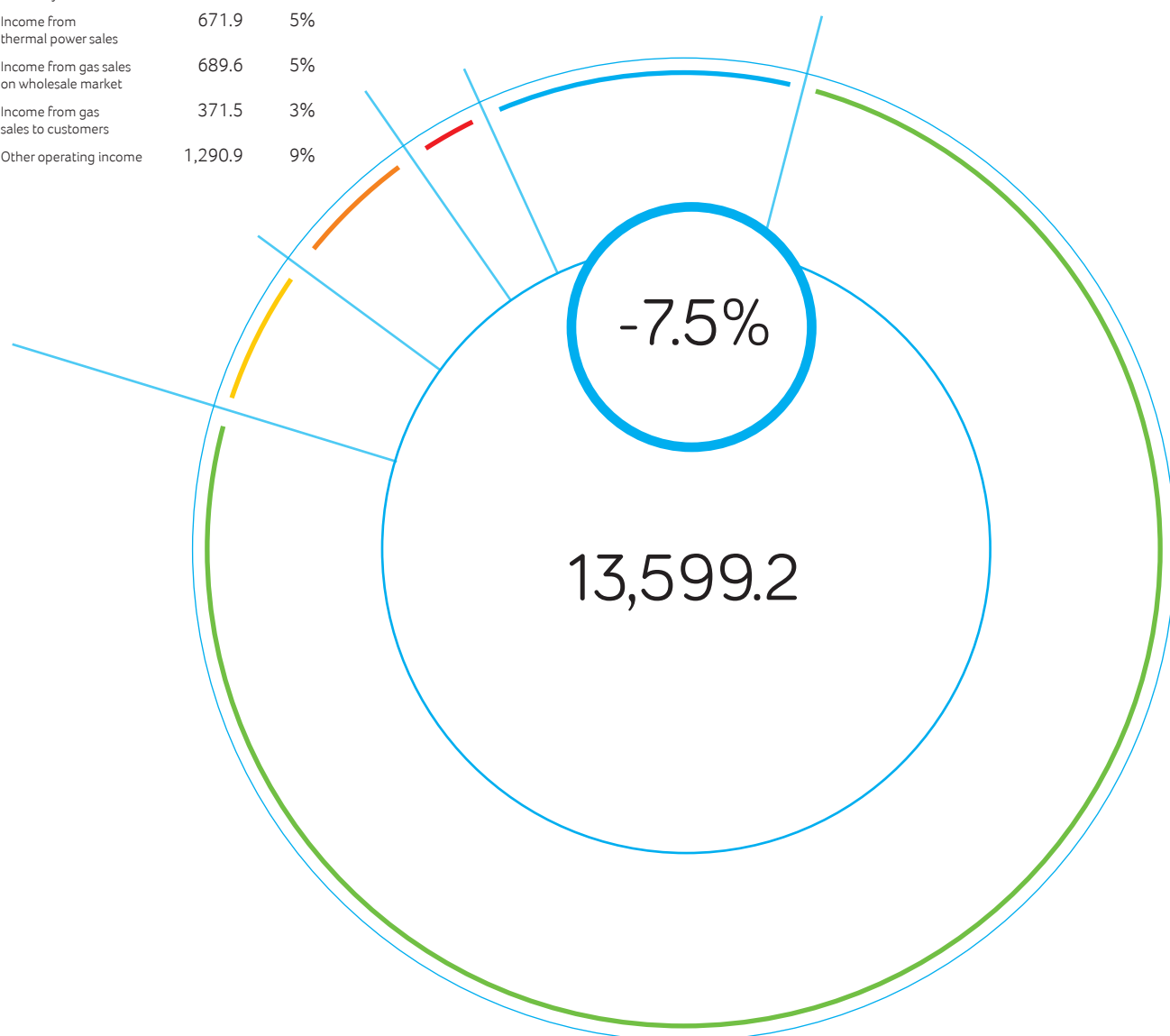
Operating

INCOME

In 2014, Group's operating income was HRK 13,599.2 m. This is a decrease of HRK 1,095.7 m (7.5%) in comparison with 2013. The decrease of operating income is primarily the result of lower income from electricity sale to Croatian buyers. Income from electricity sale accounts for 78% of Group's operating income. An 11.5% decrease in comparison with the previous year is the result of a lower consumption and the loss of a part of the Croatian market as well as a decrease of sale prices. While the income from domestic activity reduced, the income from exporting the electricity surplus increased compared to the previous year. Income from heat energy sale, which accounts for 5% of operating income was lower due to a 12% lower consumption. The income from the wholesale of gas totals at HRK 689.6 m, and accounts for 5% of total income. The income from gas sale on the retail market accounts for 3%, an 8.5% decrease compared to 2013. Other business income was reduced by 18.2% in total compared to the previous year. This decrease is primarily the result of income from cancelling provisions, income from default interest from electricity, heat and gas customers, extraordinary income and income from market functions of the Croatian Transmission System Operator.

OPERATING COST (HRK m)

Income from electricity sales	10,575.3	78%
Income from thermal power sales	671.9	5%
Income from gas sales on wholesale market	689.6	5%
Income from gas sales to customers	371.5	3%
Other operating income	1,290.9	9%



Operating COST

Group's operating costs decreased in 2014 by HRK 1,922.6 m to HRK 10,398.7 m. Energy fuel for electricity and heat energy generation as well as electricity procurement account for 27% of total costs and amount to HRK 2,842.7 m, which is a total decrease of HRK 1,953.3 m or 40.7% compared to 2013, as a result of the following factors:

due to extremely favorable hydrology, hydro power plants generated the total of 8.4 TWh of electricity, which is 3.8% more than in 2013;

procurement of electricity on the market decreased by 1.5 TWh, due to lower sales of electricity to Croatian buyers;

due to high generation cost and lower heat consumption, electricity generation in thermal power plants and heat energy generation decreased by 1.2 TWh and 0.3 TWh, respectively resulting in 38.6 percent less consumed gas;

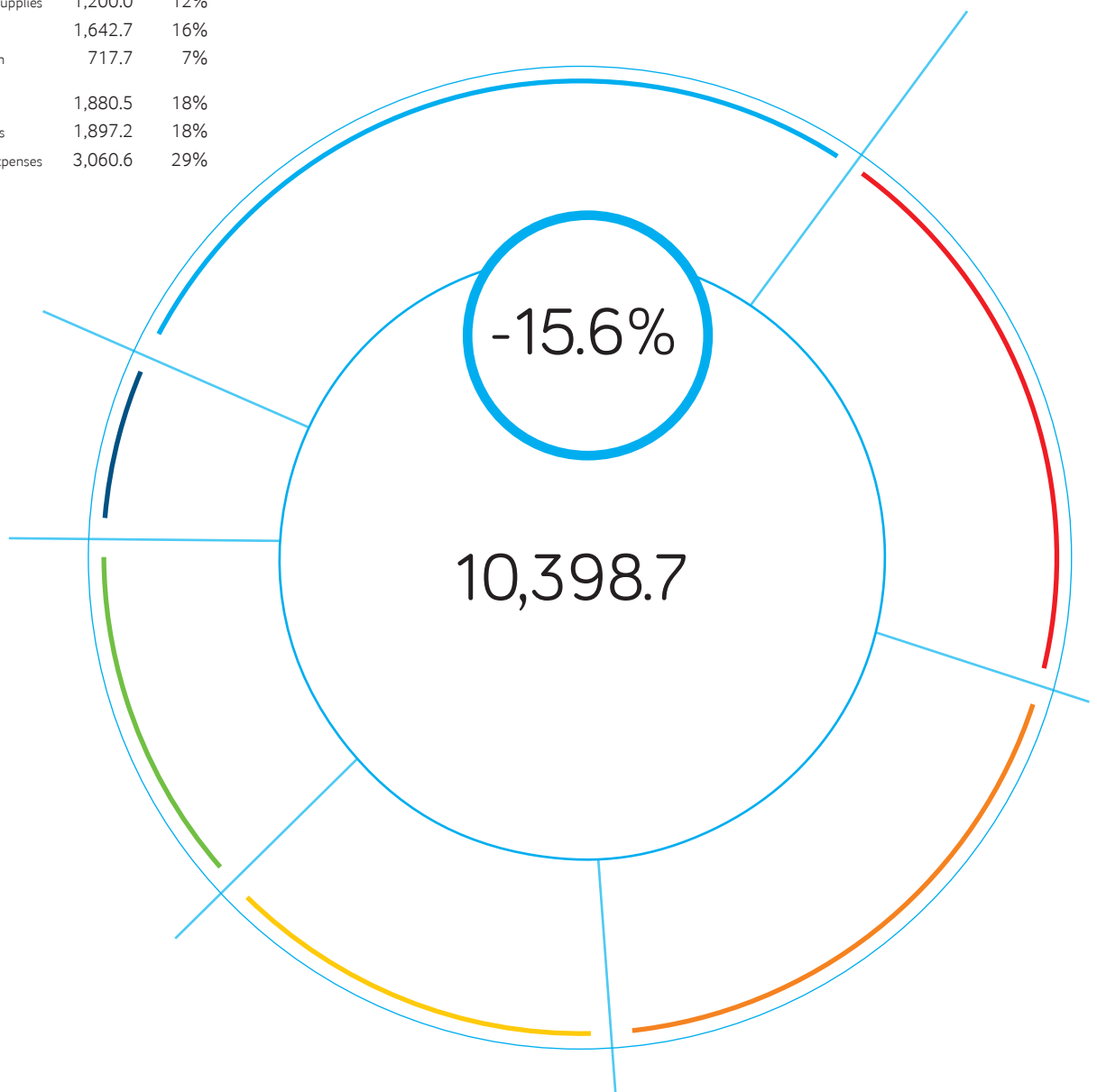
26.1% lower prices for imported electricity;

lower prices of energy fuel (9.6% for gas and 4.1% for coal)

In comparison with 2013, other business expenses reduced in total by 17.1% due to decreased cost of paid out severance pays, costs of fees, concessions and emissions as well as the value adjustment of short-term assets. Staff expenses increased by 0.6% due to the increase in the number of employees resulting from the essential replacement of retired workers as a result of the 2013 restructuring.

OPERATING COSTS (HRK m)

Cost of electricity supplies	1,200.0	12%
Fuel costs	1,642.7	16%
Cost of gas sales on wholesale market	717.7	7%
Staff costs	1,880.5	18%
Depreciations costs	1,897.2	18%
Other operating expenses	3,060.6	29%



RESULTS BY ACTIVITIES

BUSINESS RESULT

	HRK m								
	electricity			heat energy			gas		
	2013	2014	14/13	2013	2014	14/13	2013	2014	14/13
Operating income	13,428.4	11,767.1	-12.4%	830.4	741.8	-10.7%	436.1	1,090.2	+150%
Profit (loss) from operations	2,543.0	3,265.3	+28.4%	-166.6	-135.1	-18.9%	-2.8	70.2	

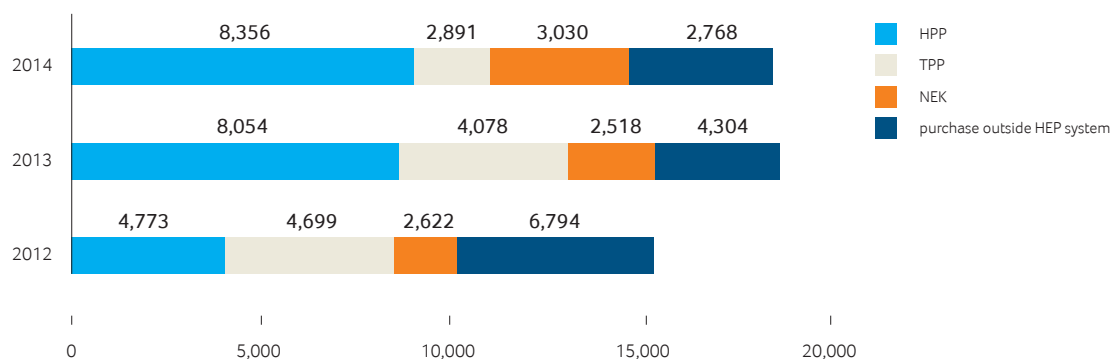
The biggest part of operating income (86.5%) as well as Group's total operating income was recorded from electricity business. The growth of profit from this activity, despite lower income, was the result of a significant reduction of generation and electricity procurement costs as well as another very favourable hydrological year with the all-time hydro generation record. The district heating business accounts for 5.5% of income and records the loss from operations of HRK 135.1 m. In comparison with the previous year, the loss was reduced due to lower costs of heat energy generation. The share of gas wholesale and retail activities in the operating income totals at 8.0%, recording the profit from operations of HRK 70.2 m.

ELECTRICITY

Electricity generation, transmission, distribution and supply are carried out by HEP Group along the entire area of Croatia. HEP Group is the biggest supplier of electricity. In 2014, the profit from operations amounted to HRK 3,265.3 m.

The income from the sale of electricity totals at HRK 10,575.3 m, 93% of which account for the supply of Croatian customers and 7% for sales outside Croatia.

ELECTRICITY SALE AND PROCUREMENT (GWh)

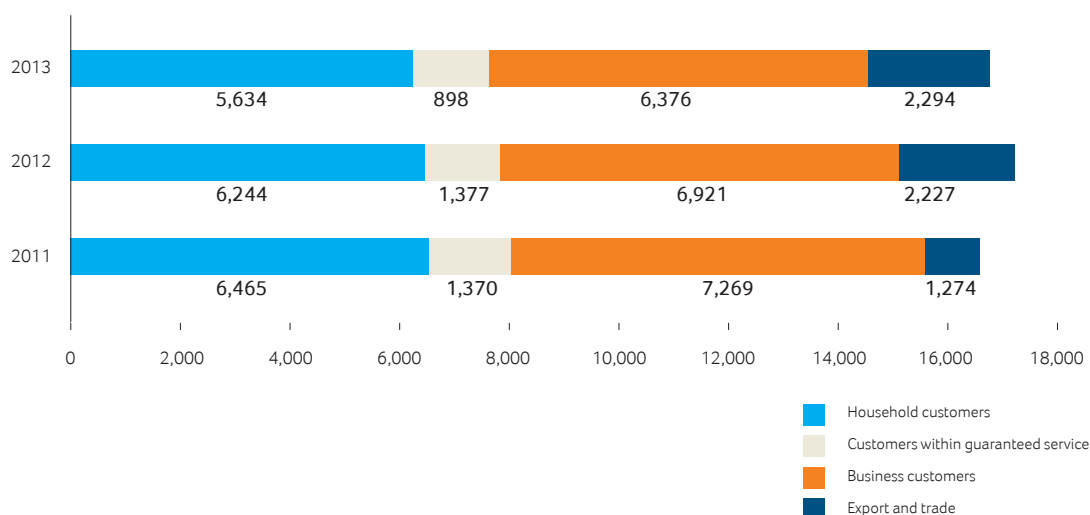


Power plants wholly or partially owned by the Group generated 14.3 TWh of electricity, which is 84% of total electricity turnover recorded by the Group in 2014. Due to good hydrology, the cost structure of electricity sources was very favourable with historically highest hydro generation of 8,356 GWh of electricity produced, a 47 GWh increase in comparison with the highest generation recorded in 2010. Due to cost optimization of electricity generation, generation in gas-fired thermal power plants was lower resulting in 29.1% less electricity generated in comparison with 2013. A total of 2,768 GWh was procured outside the system, which is 35.7% less than during the previous year, of which 913 GWh was purchased by HROTE for the generation from renewable energy sources and cogenerations within the incentive system.

12.9 TWh of electricity was sold to domestic customers, which is an 11.2% decrease, i.e. 1.6 TWh less compared to the previous year, of which 0.6 TWh less sold to household customers and 1.0 TWh to business customers. HEP's sale to domestic customers accounts for 86.8% of total electricity sale in Croatia in 2014. In the structure of electricity sale to domestic customers, a share of household customers accounts for 46.6% (5,634 GWh), business customers 49.4% (6,376 GWh) and business customers within guaranteed supply 7.0% (898 GWh). Foreign sale totals at 2,294 GWh, which is 3.0% more than in 2013.

Apart from lower electricity sale to domestic customers, the decrease of income from electricity was affected by lower sale prices for the supply of household customers within the universal service and business customers within the guaranteed supply, reduced as of 1 October, 2013. Since July 1 2014, business customers within the guaranteed supply have a higher price due to the implementation of the new methodology, under which the Croatian Energy Regulatory Agency sets the prices, which made the customers choose other market suppliers offering lower prices, resulting in a 34.8% lower price within the guaranteed supply in comparison with the previous year.

ELECTRICITY SALE (GWh)



DISTRICT HEATING

Generation, distribution and heat energy supply are conducted in the area of Zagreb, Osijek, Velika Gorica, Zaprešić, Samobor and Sisak. In 2014, the generation of heat energy and process steam amounted to 2.2 TWh, which is 12.8% less than in 2013. It was affected by decreased consumption due to warm winter. The sale of heat energy amounted to 1.9 TWh or 15.5%, which is less than in 2013. The annual consumption of household and commercial customers was lower by 15.0% and 17.0%, respectively. In 2014, district heating business recorded loss from operations of HRK 135.1 m. Compared to 2013, the loss was lower by HRK 31.5 m primarily due to lower fuel and heat energy procurement costs, lower fuel prices as well as lower heat energy consumption.

GAS

HEP Group conducts the activity of retail gas distribution and customer supply. As of 1 April 2014, it has also conducted the activity of a wholesale market supplier. With regard to said business activities, the profit from operations amounted to HRK 70.2 m, whereas in 2013 there was a loss of HRK 2.8 m recorded. The business of gas distribution and supply of retail customers is conducted in the following counties: Osijek-Baranja, Virovitica-Srijem and Požega-Slavonia. Having liberalised the gas market, HEP Gas started supplying customers on other distribution areas (Zagreb, Varaždin, Bjelovar, Zadar).

Income from gas distribution and supply of retail customers amounted to HRK 371.5 m, which is 8.5% less than in 2013 due to decreased consumption and a slightly lower selling price. The consumption of retail customers reduced by 8.1% in comparison with the previous year due to warm winter. The sale of gas to household customers was lower by 17.3%, whereas the sale of gas to business customers increased by 6.1% due to increased sale across the HEP Gas distribution area and the sale to new customers in other distribution areas.

Pursuant to the decision of the Croatian Government, Hrvatska elektroprivreda d.d. was appointed the supplier on the wholesale gas market in the period between 1 April 2014 until 31 March 2017. As the wholesale gas market supplier and under regulated conditions, it will sell gas to suppliers under the obligation of the public service of supply to household customers and ensure a reliable and secure gas supply. The 2014 income from gas wholesale amounted to HRK 689.6 m.

FINANCIAL POSITION

CONSOLIDATED BALANCE SHEET (ABRIDGED)

	December 31 2013		December 31 2014		Change 14/13 (%)
	HRK m	share	HRK m	share	
Long-term assets	30,701.9	89%	30,779.2	86%	+0.3
Short-term assets	3,869.5	11%	5,077.6	14%	+31.2
Total assets	34,571.4	100%	35,856.7	100%	+3.7
Capital and reserves	19,845.6	57%	22,077.6	62%	+11.2
Long term provisions	808.4	2%	902.8	3%	+11.7
Long term liabilities	10,064.5	29%	8,991.8	25%	-10.7
Short term liabilities	3,853.0	11%	3,884.6	11%	+0.8
Total capital and liabilities	34,571.4	100%	35,856.7	100%	+3.7

ASSETS

The value of HEP Group's total assets at the end of 2014 was HRK 35.9 bn and it increased by HRK 1,285.3 m. Long-term assets account for 86% of Group's asset value, an increase of HRK 77.2 m in terms of the investment in the preparation and the construction of new energy facilities, connection of customers as well as the replacement, reconstruction and refurbishment of existing energy facilities.

Due to electricity price trends on the regional wholesale market and the impact of these prices on the competitiveness of electricity generation in thermal power plants, indicators were determined for lowering the asset value of buildings and thermal power plant facilities in line with the International Accounting Standard 36. The correction of accounting value of thermal power plants was conducted pursuant to their current value, which on 31 December 2014 amounted to HRK 2.4 bn, as well as the changes in earlier reporting periods.

The value of short-term assets is HRK 5.1 bn and it increased by HRK 1,208.1 m due to the increase of cash and cash equivalents by HRK 819.1m, the increase in inventories by HRK 458.9 m, whereas accounts receivables and other short-term accounts receivables decreased by HRK 69.9 m. The most significant item in short-term assets is accounts receivables of HRK 1.9 bn, which increased due to gas wholesale receivables. The inventories amounted to HRK 1.6 bn and they were increased due to the increase of CO₂ emission unit inventories and gas wholesale inventories in the underground gas storage Okoli.

CAPITAL AND LIABILITIES

At the end of 2014, capital and reserves amounted to HRK 22.1 bn with an increase of HRK 2,230.0 m in comparison with 2013, due to achieved profit. This increased the share of this item in the Group's total assets from 57% to 62%.

Long-term provisions were increased by HRK 94.4 m, mainly due to increased provisions for severance pays and anniversary awards.

Long-term liabilities amounted to HRK 8,991.8 m, accounting for 25% of the Group's total liabilities and capital. They were decreased by HRK 1,072.7 m due to decreased long-term loan and bond related liabilities as well as decreased SWAP transaction liabilities. In 2014, there were no new long-term loans. Short-term liabilities amounted to HRK 3,884.6 m, an increase of HRK 31.6 m compared to the beginning of the year. Liabilities for current maturity of long-term loans, liabilities for taxes and contributions as well as other short-term liabilities were increased. Liabilities towards banks were decreased as all short-term loans were paid off in the first half of the year. The debt/equity ratio was lowered to 22.7% in comparison with the end of the previous year when it was 30.4%.

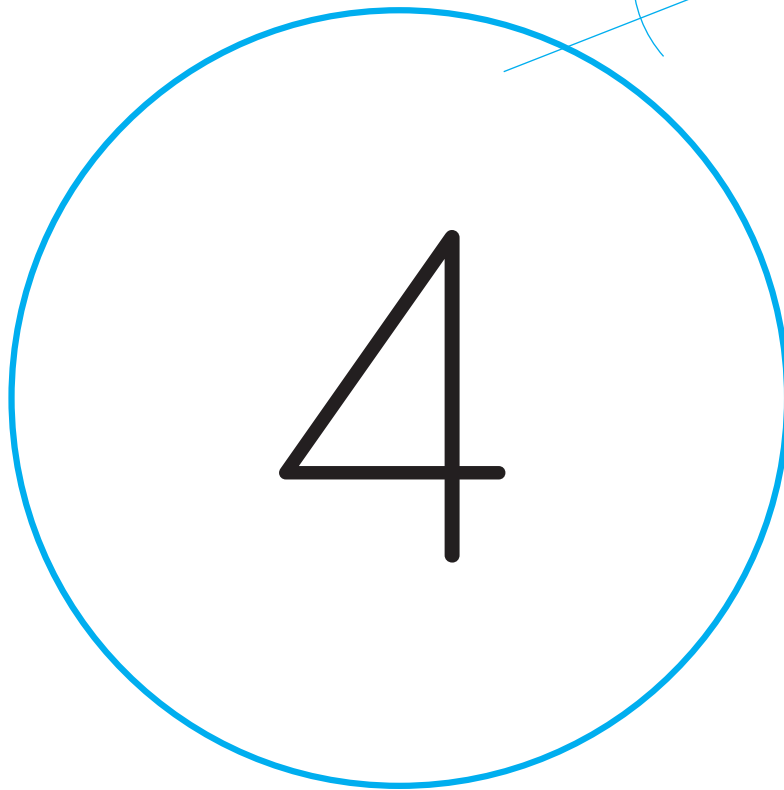
INVESTMENTS

In 2014, the Group made investments in the amount of HRK 2,042.5 m. Main investments focused on the reconstruction and the modernization of generation facilities and electric power system plants, the construction of new generation energy facilities and the reconstruction of the existing ones and the construction of new transmission and distribution network infrastructure.

Apart from the above, investments were made into district heating and gas distribution energy systems as well as into the upgrade of IT infrastructure and the preparation for the construction of the electric vehicle charging station infrastructure.

Investments				HRK m
	2012	2013	2014	2014/2013
Investments in property, plants and equipment	2,598.3	2,166.9	2,042.5	-5.7%

REPORT ON IMPACT
ON STAKEHOLDERS



Report on impact on stakeholders

HEP conducts its business in compliance with the law and ethical standards, on the principles of sustainable development and social responsibility, based on the following documents:

- Code of Ethics (available at: <http://www.hep.hr/hep/odgovornost/etickiKodeks.pdf>)
- Code of Ethics of the Croatian Chamber of Economy
- Code of Corporate Governance (Zagreb Stock Exchange and HANFA)

BASIC PRINCIPLES IN RELATIONS WITH STAKEHOLDERS

To achieve our **mission** and to fulfill our **vision**, we align all our business operations with expectations **of all stakeholders**, adhering to the following **principles**:

OWNER

- To achieve optimum business effects and an appropriate profit for the owner.

CUSTOMERS

- To satisfy the needs and expectations of the customers, providing value for money. To act in a professional and correct manner in accordance with best practices and generally accepted values, building trust in our actions.

EMPLOYEES

- To appreciate employee interests and competencies and to develop a reward and promotion system. To secure and constantly apply state-of-the art work safety measures and to encourage life-long learning, cooperative spirit and professionalism.

BUSINESS PARTNERS

- To foster and build relations with business partners, respecting their quality and professionalism. To carry out public procurement processes in a correct manner and to prevent any possible irregularity.

SOCIETY, LOCAL COMMUNITIES

- To respect cultural, religious, traditional and any other material or spiritual characteristics in cooperating with the local communities in which we are active, creating a friendly environment.

EMPLOYEES

NUMBER AND STRUCTURE OF EMPLOYEES

On December 31 2014, 10,904 out of the total of 11,006 employees were employed on a permanent basis and 97 on a temporary basis (of which 86 trainees on a temporary basis), while 5 employees were on unpaid leave.

NUMBER OF EMPLOYEES BY HEP GROUP COMPANY (DECEMBER 31, 2014)

HEP Group company	No of employees		Change
	2013	2014	2014 – 2013
HEP-Operator distribucijskog sustava d.o.o.	7,531	7,627	96
HEP-Proizvodnja d.o.o.	2,182	2,184	2
HEP d.d.	460	451	-9
HEP-Toplinarstvo d.o.o.	347	345	-2
HEP-Plin d.o.o.	134	143	9
HEP-Opskrba d.o.o.	75	73	-2
Crpna stanica Buško blato d.o.o.	42	42	0
HEP-Trgovina d.o.o.	23	27	4
HEP-Telekomunikacije d.o.o.	0	26	26
HEP-ESCO d.o.o.	22	22	0
APO d.o.o.	20	17	-3
HEP-Nastavno obrazovni centar Velika	12	12	0
HEP-Odmor i rekreacija d.o.o.	12	12	0
HEP-Obnovljivi izvori energije d.o.o.	9	9	0
Program Sava d.o.o.	8	8	0
HEP-Opskrba plinom d.o.o.	0	8	8
HEP Group TOTAL*	10,877	11,006	129

*Without HOPS

QUALIFICATION STRUCTURE

Qualification	2013	2013 (%)	2014	2014 (%)
DSc and MSc	199	1.8	203	1.84
BSc	1,693	15.6	1,824	16.57
Assoc. degree	874	8.0	881	8.00
Secondary sch.	4,858	44.7	4,939	44.88
Element. sch. / semi skilled	492	4.5	478	4.34
Highly skilled	1,501	13.8	1,446	13.14
Skilled	1,267	11.7	1,241	11.28
Total	10,877	100%	11,006	100%

AGE STRUCTURE

Years of age	No of employees
do 20	7
20-25	68
25-30	398
30-35	702
35-40	1,316
40-45	1,526
45-50	1,707
50-55	2,042
55-60	2,171
60-65	1,069
Total	11,006

EMPLOYMENT AND TRADE UNION RELATIONS

Five trade unions are active in HEP Group: Croatian Electricity Trade Union - HES, Independent Trade Union of Employees of Hrvatska elektroprivreda – NSR, Vocational Trade Union of Workers in Hrvatska elektroprivreda - TEHNOS, Autonomous Trade Union in Power Industry, Chemistry and Non-Metal Industry of Croatia – EKN and the Croatian Trade Union for Distribution Workers – HEDISS (registered on 19 April, 2012). Employment and rights of employees of HEP Group companies are regulated under work rules of the companies and the Collective Agreement for HEP Group.

On April 26, 2013 the new Collective Agreement (Bulletin 303 of April 26, 2013) was concluded between HEP Group and two representative trade unions, in effect from April 1, 2013 until March 31, 2014.

The currently valid Collective Agreement (Bulletin 321 of 6 October 2014) has been concluded for the period from 1 October 2014 until 30 June 2016. In the period not covered by the valid collective agreement (from 1 April 2014 until 30 September 2014), work relations and employment rights in HEP Group companies were regulated under the Company's Operating Rules.

Pursuant to Article 153 of the Collective Agreement, the parties to the Collective Agreement set up the Joint Commission for the interpretation of the Agreement provisions. The commission met periodically, in accordance with the provisions of the Collective Agreement and depending on the requests for interpretation they received.

The employers of HEP Group companies with elected workers' councils fulfilled their obligations toward workers' councils in compliance with the sections 149-151 of the Labour Act (Official Gazette 93/14) relating to obligations to inform, consult and allow the participation in decision-making of workers' councils on matters important for employees.

HUMAN RESOURCE MANAGEMENT

HEP Group has been implementing modern practices of HR management focused on employing and developing competent workers who will represent the company's competitive value in its operations on the open market.

Standardized processes of employing new workers and selecting scholarship recipients as well as introducing new employees to their work tasks i.e. monitoring their knowledge acquisition for independent work were set up. They function in a manner which facilitates the selection of best candidates as well as their fast and successful adaptation to work environment.

Having considered the need for permanent life-long employee education which will contribute to developing their professional knowledge and skills necessary for efficient operation and enable the follow-up as well as the implementation of cutting-edge trends in all HEP Group operational parts, HEP allocates significant financial resources to education, professional development in Croatia and abroad (conferences, seminars, courses) and specialist trainings required by work needs.

The HR Department has been conducting in-house educations in social skills development and business correspondence intended for authorized staff, interns and all interested employees.

For the purpose of keeping a single education record and unifying data and report development for the requirements of HEP Group, the Records of Education software application has been implemented.

HEALTH AND WORK SAFETY

Under the law, the implementation of protective measure is the responsibility of the Employer. The responsibility within the organizational units lies on employer's authorized officers on behalf of the employer. As required by law, in each organizational unit there is one or more safety specialists, depending on the number of employees. Safety specialists provide their professional assistance to the employer and its authorized officers in the implementation and improvement of safety at work and protection of health of employees.

In 2014, there were 159 work injuries in HEP Group, 25 serious and 134 light ones.

New employees or workers who changed their work position undergo safe work education in line with legal obligations. Other trainings are conducted according to expressed needs by areas and plants, internally or externally by authorized companies, depending on the type of training. Hazardous machines and devices specified in the List of Machines as well as the fire alarm and suppression systems are tested according to testing schedule and deadlines as required by law.

CUSTOMERS

NUMBER OF CUSTOMERS

The number and structure of electricity, district heating, process steam and natural gas customers is shown in reports by HEP Group companies.

RELATIONS WITH ELECTRICITY CUSTOMERS – HEP DSO

HEP Distribution System Operator d.o.o. (HEP DSO) is a company that provides the network use service to all customers connected to the distribution network. HEP DSO is also the provider of the public service of electricity supply to customers within the universal and guaranteed supply. Through its public service of supply (universal and guaranteed supply), HEP DSO supplied 2.1 million metering points in late 2014. The Company has continually been raising the quality level of the services provided to its customers and improving its distribution network for the purpose of increasing the quality level of supplied electricity to all distribution network users.

The web site of HEP DSO provides its customers with the possibility of obtaining most relevant information on one place. All other questions can be submitted to a single e-mail address. The 'My Account' application facilitates the submission of meter readings as well as provisional calculations, the overview of historical consumption and payment data. Customers can also view all announced interruptions in electricity supply for the entire Croatian territory.

Apart from on-line, customers can communicate with employees of local distribution areas by free phone numbers. Meter readings can be submitted at any time to a free telephone answering machine at 0800 0555. In addition to these channels of communication, in each distribution area customers can communicate directly with employees with the purpose of submitting meter readings, getting information or filing a complaint.

All household customers can pay their electricity bills without any extra charge at all FINA and Croatian Postal Service offices. Customers can also pay their bills without an extra charge by a standing order agreed with a commercial bank or a credit card company with which HEP DSO has concluded the contract for this service.

RELATIONS WITH ELECTRICITY CUSTOMERS - HEP SUPPLY

In conducting its business operations, HEP Supply tries to meet the increasing customer and market requirements. While emphasizing new solutions and innovative products, special attention is paid to service quality and customer relations.

According to the research conducted by the Croatian Association for Energetics (February 2015), more than two thirds of the respondents thinks that HEP Supply offers the best price and service quality ratio available on the market. This has been emphasized by the research conducted by PWC Consultancy, according to which HEP Supply has the best contact center compared to other alternative market suppliers. All the above is the result of permanent learning and education of all its employees.

Special attention is paid to customer service quality with 96% of all customer queries being resolved on their first call. Customers can also contact HEP Supply on the free phone number 0800 5255, by sending an e-mail to opskrba@hep.hr, and by calling the Billing and Invoicing Department. In 2014, the Contact Center of HEP Supply recorded more than 145,000 incoming calls and replied to more than 17,000 customer e-mails. All information regarding the account balance, due liabilities and other issues are available non-stop on My Account application. Apart from the above, the customer is supplied with additional information through HEP Supply web page, the newsletter and its Facebook page.

HEP Supply's Contact Center provides a complete service for its Hepi product intended for a household customer: information provision, request submission, contract drafting and control, printing, entering contracts into billing application and customer complaint resolution. More than 9,500 queries were sent to hepi@hep.hr. The Contact Center replied to more than 81,000 phone calls regarding Hepi.

145,000

inbound calls
to the Contact
Centre



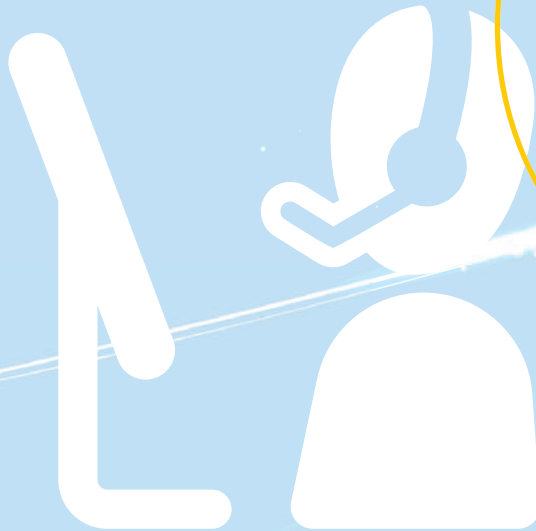
HEP Supply Customer relations

2014

17,000



e-mail replies
to customer
queries



67%

of respondents believe that HEP Supply offers the best service price/quality ratio on the market (the research conducted by the Energy Association of Croatia in February 2015)



96%

of customer queries resolved on first call



700

key customers participated at the Meeting with HEP Supply Customers



Key accounts are taken care by sales advisers, trained for dealing with such an important customer portfolio, with almost daily communication and at mutual initiative. Traditional annual Meetings with HEP Supply customers were organized in 2014 in Split, Rijeka, Osijek and Zagreb. They gathered more than 700 key customers. Customers are very keen on participating in these meetings as they provide first-hand information regarding new products and services as well as electricity market trends and development.

RELATIONS WITH HEAT ENERGY CUSTOMERS (HEP DISTRICT HEATING)

HEP District Heating has set the satisfaction of heat energy end customers as its primary business goal. Therefore, particular attention is paid to improving the communication and providing additional services to its end customers. In 2014, HEP District Heating tried to provide its end customers with indepth information regarding the provisions of the Heat Energy Market Act, under which a number of obligations has been prescribed for all market participants.

Along with the July 2014 bill, HEP District Heating sent to all its heat energy end customers in Zagreb, Osijek, Sisak, Velika Gorica, Samobor and Zaprešić letters concerning two most important obligations set under the Heat Energy Market Act: the obligation on adopting the decision on entering into the heat energy consumption agreement and the obligation on entering the heat energy consumption agreement with a heat energy distributor.

Supporting the creation of the market environment for doing business, HEP District Heating informed its end customers of the possibility of concluding the heat energy consumption agreement with another legal or physical person entered into the heat energy distributor registry published on HERA's web site. Said letters also contain contact phone numbers and e-mail addresses through which end customers can communicate daily with HEP District Heating employees regarding Act provisions.

Additional information and professional advice regarding the installation of heat cost allocators are provided to end customers through dedicated phone lines and e-mail addresses.

In view of new heat energy price elements and a new design of the heat energy bill as of September 2014, as yet another obligation resulting from the Act and by-laws regulating the heat business, HEP District Heating sent to all its end customers information on changes along with their September 2014 bills as well as new prices for their district heating systems.

HEP District Heating has established great cooperation with other heat energy market stakeholders – the Ministry of Economy, HERA, city councils, media and others to provide the public with timely information of current events and changes on the heat energy market. In the cooperation with residential building managers, four forums were held discussing the topic of the Heat Energy Market Act with the participation of over 1000 representatives of residential building co-owners as well as presentations held in Zagreb, Osijek, Sisak, Velika Gorica, Varaždin, Karlovac, Vukovar and Slavonski Brod.

RELATIONS WITH GAS CUSTOMERS (HEP GAS)

Customer gas supply had been continuous throughout the year with short gas supply interruptions due to planned network work or the connection of new customers, which was timely announced by direct written notes and in the media.

Customer gas supply is conducted in line with the General Conditions for Natural Gas Customer Supply. Gas supply volumes were timely read and billed.

As the majority of customers are supplied in line with the public service provision principles, purchased gas was billed according to regulated prices set by the Croatian Government. During 2014, the selling price for households remained unchanged, while most business customers experienced monthly changes (due to constant changes of the purchase price relying on oil, gas and USD currency trends). This made the billing of supplied gas more difficult. The collection of payment from entrepreneurial customers was aggravated.

COMPLAINT COMMISSIONS

As required by the Consumer Protection Act, commissions are in place for customer complaints in 21 distribution areas of HEP DSO, in HEP-District Heating d.o.o. and HEP-Gas d.o.o. Commissions are composed of representatives of individual HEP companies or areas and representatives of consumer associations. HEP Supply has tried to resolve all customer complaints amicably. In case of any disputes, it uses five certified mediators.

NUMBER OF COMPLAINTS DISCUSSED BY HEP DSO COMMISSIONS – 2014

Billing	Faulty meter	Connection/ disconnection	Voltage conditions	Other	TOTAL
total 278	total 11	total 4	total 2	total 34	total 329
accepted 45	accepted 4	accepted 0	accepted 0	accepted 5	accepted 54
rejected 233	rejected 7	rejected 4	rejected 2	rejected 29	rejected 275

NUMBER OF COMPLAINTS DISCUSSED BY HEP-DISTRICT HEATING COMMISSIONS – 2014

Quality of supply services (regarding meter reading, billing, collection)	Quality of heat energy (tempera- ture on customer premises, temperature of hot water, steam parameters)	Change in connected load	Change at metering point (separation, linking, relocation of installations, etc.)	Redistribution of supplied heat volume	Other	TOTAL
total 4	total 0	total 0	total 0	total 0	total 1	total 5
accepted 0	accepted 0	accepted 0	accepted 0	accepted 0	accepted 0	accepted 0
rejected 4	rejected 0	rejected 0	rejected 0	rejected 0	rejected 1	rejected 5

NUMBER OF COMPLAINTS DISCUSSED BY HEP-GAS COMMISSIONS - 2014

total	35
accepted	0
rejected	35

SUPPLIERS (PUBLIC PROCUREMENT)

The primary business objective in this area is to build a reliable system of public procurement, characterized by predictability, better competition, efficient and effective management of resources, procurement based on the 'value for money' principle and orderly procedure conduct (timely procurement). To achieve these objectives, HEP continued to provide activities and measures for transparency strengthening throughout 2014, providing more information to prospective tenderers focusing on giving equal opportunity to all those wishing to participate in the public procurement procedure.

All public procurement procedures within HEP Group are posted on HEP website. In 2014, HEP d.d. expanded the scope of information available on the web portal for procurement procedure announcement. Apart from basic information, tender documentation as well as the selected and revoked decisions are now also published. These decisions are published in the E-Procurement Bulletin of the Republic of Croatia.

In accordance with provisions of the Public Procurement Act, HEP Group members, which are subject to the Public Procurement Act, publish information on awards and performance of framework agreements and contracts made on the basis of an appropriate public procurement procedure on HEP website.

One of the most significant activities for enhancing the entire procurement business operations of HEP Group is the development of the Procurement and Contracting Rules of HEP Group, in effect as of 19 January 2015. The adoption of this internal document has significantly contributed to the enhancement and balancing of procurement processes and ensured the compliance with basic public procurement principles, which will result in a better organisation and harmonization of business processes as well as the development of a reliable public procurement system.

Number of procurement procedures carried out in 2014 by HEP Group companies

HEP Group company	Number of public procurement processes in 2014
HEP d.d.	99
HEP-Proizvodnja d.o.o.	213
HEP-Operator distribucijskog sustava d.d.	284
HEP-Plin d.o.o.	14
HEP-Toplinarstvo d.o.o.	62
HEP-Obnovljivi izvori energije d.o.o.	2
HEP-Upravljanje imovinom d.o.o.	1
HEP Opskrba d.o.o.	1
HEP NOC d.o.o.	3
TOTAL	879

The Procurement Department of HEP d.d. conducted 55 public procurement procedures, 20 of which were high value and 35 low value ones.

In 2014, eight negotiated public procurement procedures were conducted for importing equipment, spare parts and services required for the work of individual HEP Group facilities. All these procedures were conducted with foreign suppliers in English (with the accompanying Croatian versions).

The Procurement Department primarily conducts the procurement for other users i.e. Departments of HEP d.d. and/or subsidiaries, which includes the conclusion of contracts and framework agreements.

THE MOST SIGNIFICANT SUPPLIERS IN 2014*

Supplier	Subject Matter
Brodomerkur d.d.	Meters, power transformers, cable accessories
Cotra d.o.o.	Concrete bearers, meters, wooden chestnut pillars, wooden impregnated pillars, power transformers, cable accessories
ZP Brodomerkur d.d. and Brodometalurgija d.o.o.	Concrete pillars
Autokuća Štarkelj d.o.o.	Cargo and passenger vehicles by groups
HP Hrvatska pošta d.d.	Postal services
Grand auto d.o.o.	Cargo and passenger vehicles by groups
Wellmax d.o.o.	Aluminium-steel and steel-graphite ropes, connection and metering cabinets for homes and power plants
Končar-Inženjering za energetiku i transport d.d.	Power transformers – 110/21 and 110/10.5(21) kV, 20 and 40 MVA
Allianz Zagreb d.d.	Insurance programme for Hrvatska elektroprivreda d.d. and its daughter companies
Elcon d.o.o.	Meters, connection and metering cabinets for homes and power plants
Elektrocentar Petek d.o.o.	Meters
Autocommerce Hrvatska d.o.o.	Cargo and passenger vehicles by groups
Croatia zdravstveno osiguranje d.d.	Supplemental health insurance
Brodometalurgija d.o.o.	Meters
Plastometalik	Connection and metering cabinets for homes and power plants
Električar d.o.o.	Connection and metering cabinets for homes and power plants
Porsche Croatia d.o.o.	Electric and passenger cars by groups
Autogrifon d.o.o.	Electric vehicles by groups

(The overview of the most significant suppliers with which HEP d.d. concluded contracts and framework agreements in line with public procurement procedures conducted by the Procurement Department of HEP d.d.)

In view of the large number of public procurement subject matters, HEP has been continuously improving its procurement business by developing internal rules, single templates for public procurement procedures, adopting internal implementation instructions and integrating the subject matter at the HEP Group level.

COMMUNITY (DONATIONS)

AID TO FLOODED POPULATION IN 2014

HEP helped the Eastern Slavonia residents, hurt by the catastrophic flood on 17 May 2014 by multiple various donations. The sum of one million kuna was donated to the Croatian Red Cross for the residents of the flooded areas. One million kuna was donated by HEP DSO to municipalities of Gunja, Drenovci and Vrbanja to fund necessary rehabilitation works on electrical installations in flooded residential buildings of said area. A dedicated donation to household electricity customers was used for settling electricity costs of HRK 1.7 million. HEP also paid for electricity costs of about one million kuna incurred by container homes housing those people who were hurt by floods. HEP also funded the rehabilitation of the playground in the village of Gunja.

PUBLIC TENDER FOR AWARDING GRANTS

In 2014, HEP conducted the fourth public tender for donations titled 'Light along the Mutual Path'. All those participating in the tender (registered associations, clubs and institutions with head offices in Croatia) could apply their projects or work programmes for 2014 in the following areas: youth, culture and heritage, science, community or environment. In line with the terms, a total of 1,976 projects or annual work programmes applied. Having evaluated the project quality and originality, a degree of its usefulness for local or wider community as well as the donation utilization efficiency, HEP selected 373 projects or work programmes, which implementation was subsidized by donations of HRK 2.5 million.

DEMINE ASSISTANCE

A 2 million kuna donation was awarded to the Croatian Mine Action Center for demining the south of Croatia under the safety criteria set by the annual demining plan of the Croatian Government. By awarding its donations to the Croatian Mine Action Center since 2011, HEP has made a significant contribution to achieving one of the priority national projects, important for the safety of people as well as for the economic development of the mine infested areas.

ZelEn

ZelEn is certified electricity generated solely from HEP's renewable sources, a unique product offered by HEP Supply to its customers. Funds collected through the sale of ZelEn are allocated exclusively to energy efficiency and RES projects integrated in the facilities which will achieve measurable effects of reduced greenhouse gas emissions. Having conducted the 2014 tender, the first donation was awarded to the Children's Home Ivana Brlić Mažuranić from Lovran for its energy efficiency project.

OTHER (MULTI-YEAR PROGRAMMES)

Since 1995, HEP has been awarding students who achieve best results in national mathematics and physics contests and since 2005 to best students of vocational electrical schools.

Since 1998, HEP has been participating in the Eco School Project which has been implemented by the Foundation for Environmental Education of the Council of Europe. HEP is the sponsor of the following ECO Schools: Electromechanical Vocational School Varaždin, Konjščina, Stanovi Zadar, Ivo Lola Ribar Labin, Vladimir Nazor Pazin, Kostrena, Kalnik elementary schools and Cvrčak and mrav kindergarten, Tribalj

On the occasion of the Earth Day, April 22, Degenia Velebitica, an annual award for the best piece of environmental journalism, has been presented since 1999. The founders of the award are the Environmental Journalists Section of the Croatian Journalists Society and APO Environmental services, a member of HEP Group. HEP regularly supports the work of HEP's Pensioners Association and HEP's Croatian Homeland War Veterans Association by giving donations.

in **1995**



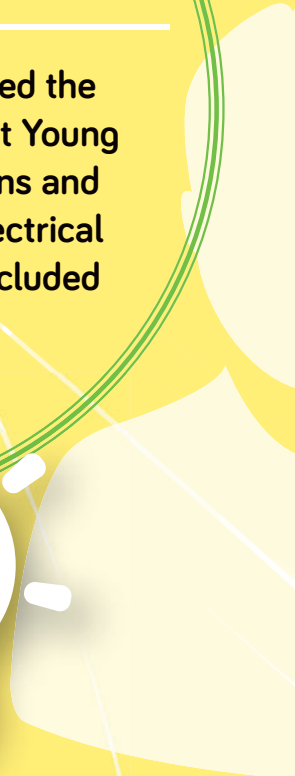
HEP established the Award for Best Young Mathematicians and Physicists (electrical technicians included in 2005)

Pupils
Award

606



awards from
1995 until 2014





1.5



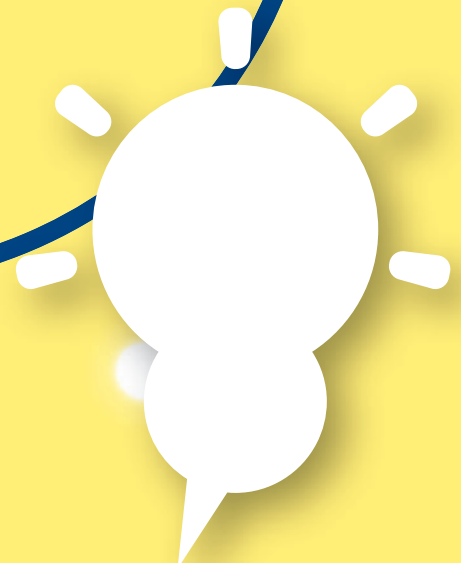
million kuna
in total was
awarded to
pupils



8th



Grand Prix by the Croatian
Public Relations Association
(March 2015) for the best
communication project
in corporate social
responsibility in 2014



ENVIRONMENTAL
PROTECTION



Environmental protection

POLICY AND ORGANIZATION OF NATURE AND ENVIRONMENTAL PROTECTION FUNCTION

During 2014, several new and amended environmental legal regulations were adopted, which marked the continuation of activities stemming from the Croatian Accession to EU and the harmonization with EU directives. These new regulations are becoming a part of HEP business policy.

HEP continuously monitors and analyzes the impact of its business processes on the environment. The most important indicators of such impacts are emissions of air pollutants and the quantity of production waste. The company reports on all environmental components to relevant institutions, units of local self-government and the interested public in a timely and objective manner. Employees working in the nature and environmental protection department attend seminars and workshops to obtain information about duties and activities arising from environmental and nature protection legislation.

Technical support to these employees is provided by the Sustainable Development and Quality Improvement Department of HEP d.d. and members of HEP teams: the Team for the Coordination and Standardization of Environmental Business Procedures, the Team for the Implementation of the Kyoto Protocol provisions and the Team for Obtaining the Environmental Permits. The fundamental objective of the Team for the Coordination and Standardization of Environmental Business Procedures is to analyse and evaluate environmental activities in HEP Group emphasizing planning, coordination, internal communication and proposals for improving environmental activities. Due to the significant affect it has on HEP Group operations, planning the work of the existing generation facilities and the construction of new ones, the Team for the Implementation of the Kyoto Protocol provisions was set up with its underlying objective of establishing the greenhouse gas emission trading system within HEP Group and controlling the work of the sector and companies within the system during the third trading period (from 2013 until 2020) as well as preparing HEP Group for the post 2020 period.

Environmental permits are a precondition for the continuous operation of the existing and one of the preconditions for obtaining the usability permit for the reconstruction of the existing and the construction of new thermal power plants of nominal heat energy exceeding 50 MW. As the procedure for obtaining environmental permits formally commenced in 2007, the fundamental task entrusted to the Team in charge of obtaining environmental permits in the cooperation with authorized personnel of the Ministry for Environmental Protection and Nature was to develop requirements as well as technical and technological solutions and make plans and plants' harmonization programmes within set time periods viable in view of the plants' life span.

MONITORING AND IMPLEMENTATION OF LEGISLATION

OBTAINING ENVIRONMENTAL PERMITS

The procedure for obtaining environmental permits for the existing thermal power plants exceeding 50 MW continued. During 2014, four out of nine HEP's existing facilities were issued the Environmental Permit. These are: the Osijek Facility of HEP-District Heating d.o.o., TE-TO Osijek cogeneration plant, TPP Sisak and KTE Jertovec of HEP Generation d.o.o. Procedures conducted by the Ministry of Environmental and Nature Protection regarding other plants are underway. The Environmental Permit was also issued to the replacement unit TPP Plomin C.

GREENHOUSE GAS EMISSION TRADING

Croatia has become a part of the European Union Emission Trading Scheme (EU ETS) at the beginning of the third trading period (from January 1, 2013 until December 31, 2020). Through its membership in the EU ETS, HEP has undertaken the obligation of buying greenhouse gas emissions on the market in the volume of verified CO₂ emissions occurring as a consequence of electricity and a portion of heat energy generation, burning fossil fuels in thermal facilities of nominal thermal power exceeding 20 MW. Purchased emission units must be submitted by traders onto the Accounts of plant operators opened in the EU Greenhouse Gas Inventory – the Croatian part, until 30 April each for the previous calendar year. The system of CO₂ emission trading in HEP Group was officially set up in November 2012 pursuant to the Decision of the Management Board of HEP under which the obligations of individual organisational units within HEP Group were set.

The first year of HEP's participation in EU ETS finished successfully as a result of excellent cooperation among departments and companies of HEP Group, carried out by inter-departmental commission (founded in March 2013) primarily for providing guidelines to HEP Trade in charge of buying and selling emission units in HEP Group.

As the emission prices are influenced by a number of factors (market supply and demand ratio, weather conditions, economy and politics), the PLEXOS market simulator was used for projecting CO₂ emission volumes as well as planning funds for emission purchase.

WATER FRAMEWORK DIRECTIVE – BASIS FOR INTEGRAL WATER MANAGEMENT

The foundation for the EU integral water management was set by the Water Framework Directive (2006/60/EC), which provisions were transposed by the Republic of Croatia into its Water Act and its resulting secondary legislation. The integral water management includes water protection and the evaluation of ecosystem services, sustainable water usage, eutrophication and water pollution reduction as well as flood and ice risk assessment and management. The Water Area Management Plan stemming from the Water Act remains in force until 2015. The list of candidates with individual water body status was made as its part to be confirmed through the Water Bodies Management Plan for the period 2016–2021. The announcement of the water body status and the determined water level is a prerequisite for setting objectives which need to be developed by implementing measures i.e. it affects the operation of the existing and the construction of future generation facilities, as well as the achievement of goals to be defined under the low-carbon strategy and the objectives set under the RES Action Plan for the period 2014–2020.

EUROPEAN ECOLOGICAL NETWORK NATURA 2000

Areas of the National Ecological Network in Croatia encompass internationally important bird habitats as well as areas important for other wild species and biotypes pursuant to the Bird Protection Directive (Council Directive 79/409/EEC; 2009/147/EC) and the Directive on the conservation of natural habitats of wild flora and fauna (Council Directive 92/43/EEC). In light of its particular geographical position, Croatia has numerous biological variety of species and biotypes thus making the size of its territory in the National Ecological Network and the NATURA 2000 proposal one of the largest in Europe.

In the period between 2009 until today, HEP has repeatedly, in a written and oral communication with state bodies competent for the preservation of biological diversity, indicated the possible real obstacles

and limitations in the operation of the existing and the construction of planned electric facilities, to which the company has not received a satisfactory reply. Since 2007, the year of establishing the National Ecological Network, HEP has not constructed a single new significant investment project on the area of the ecological network. Therefore, real limitations regarding the execution i.e. increased project costs will be seen and quantified only after some of these projects have gone through the process of environmental impact assessment.

MEETING LEGAL REQUIREMENTS

To educate and inform the employees about obligations resulting from legal environmental regulations in a timely manner, HEP Group has been systematically following and monitoring, in the form of monthly reports and annual printed bulletins, as well as preparing overviews of legal requirements in environmental and nature protection of importance for operations and business of all HEP Group companies since 2000. During 2014, improvements were continued as well as a further integration of new modules into the internal IT system of environmental protection (INFOZOK) aimed at integrating environmental data, improving the management of processes affecting the environment and a better quality of planning activities and costs needed for the implementation of environmental measures.

BASIC INDICATORS

During 2014, HEP continued to monitor air pollutant emissions – sulfur dioxide (SO₂), nitrogen oxides (NO_x), carbon monoxide (CO), carbon dioxide (CO₂) and particulates as required by the air quality legislation, as well as the quantities of hazardous and non-hazardous waste generated within HEP and the concentration of hazardous substances in waste water.

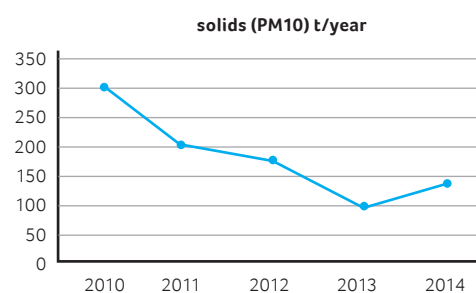
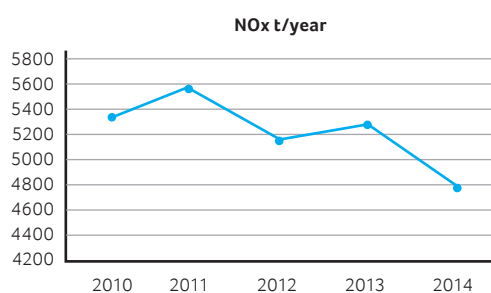
AIR EMISSIONS

Pollutant air emissions come predominantly from HEP's large combustion plants – thermal power plants Plomin 1, Plomin 2, TE-TO Zagreb, EL-TO Zagreb, TE-TO Osijek, TPP Sisak, TPP Jertovec and TPP Rijeka, while the remaining part of the pollutant emissions result from heating boiler rooms of HEP District Heating d.o.o and own business premises of HEP DSO.

Compared to 2013, the year 2014 witnessed a decrease of all air emissions from thermal facilities as a result of increased, environmentally friendlier share of natural gas compared to fuel oil as well as a shorter operation of thermal generation facilities. The emission of solid particles is the only exception as they increased due to the use of stored inventory of liquid fuel, which must be utilized by HEP thermal facilities no later than end 2015. As of January 1, 2012 HEP has been procuring only a low-sulphur fuel for the operation of its thermal and cogeneration plants.

EMISSION OF AIR POLLUTANT SUBSTANCES BY HEP GROUP SOURCES (2010-2014)

Year	NO _x t/year	SO ₂ t/year	solids (PM10) t/year	CO ₂ t/year
2010	5,318	8,277	313	3,899,372
2011	5,574	9,621	220	4,035,541
2012	5,156	8,055	179	3,726,274
2013	5,286	6,025	93	3,490,584
2014	4,779	3,747	145	2,947,102
2014/2013 (%)	-9.6	-37.8	55.2	-15.6



WASTE

During 2014, secondary legislation under the Sustainable Waste Management Act (Official Gazette 94/13) was adopted, which provisions need to be implemented by the existing waste management system in HEP. The years-long trend of improving waste management system continued in 2014 by investing in existing and new temporary waste storages and in employee education. All HEP Group companies and plants continued to build and equip temporary storages for waste and secondary raw materials and furnish them with tanks for separate waste collection. The electronic management of waste data using the Waste Management application continued in all plants.

In 2014, a total of 1,964 tons of hazardous waste and 109,698 tons of non-hazardous waste was produced within HEP Group. Increased quantities of generated hazardous and non-hazardous waste compared to 2013 are the result of written-off equipment and material, the new fleet and the cleaning of liquid fuel containers and oil sumps. All generated waste was handed over to authorized collectors, exporters or processors for further processing and final disposal.

TOTAL QUANTITY OF HAZARDOUS AND NON-HAZARDOUS WASTE GENERATED (2010-2014)

Year	Hazardous waste (t)	Non-hazardous waste (t)
2010	1,152	93,185
2011	1,574	116,236
2012	2,259	103,519
2013	1,565	101,705
2014	1,964	109,698
2014/2013 %	25.5	7.9



EXPENSES FOR ENVIRONMENTAL AND NATURE PROTECTION

In 2014, total expenses for nature and environmental protection incurred by HEP Group companies amounted to HRK 154.13 m. The cost of regular operations regarding environmental protection increased due to HEP's involvement in the EU greenhouse gas emission trading system. The most significant investments in 2014 were the projects of improving the waste management system in HEP's plants as well as the nature and the environment protection projects.

EXPENSES FOR ENVIRONMENTAL AND NATURE PROTECTION IN HEP GROUP IN 2014 (IN HRK 000)

Environmental protection	Cost of regular operations	Investments
Air and Climate	56,023	69
Waste Waters	3,392	195
Waste	8,640	4,083
Soil and Underground Water Protection	1,488	64
Noise and Vibrations	19	0
Nature and Landscape Protection	6,143	4725
Radiation Protection	38	0
Research and Development	41	1140
Others (mostly fees in regular operations)	67,720	348
Total 2014	143,504	10,625
Total 2013	84,180	16,904
2014/2013 (%)	70	-37

MAJOR ACHIEVEMENTS IN 2014

AIR QUALITY PROTECTION

- To meet limit values for emissions of nitrogen oxides (NO_x) following the expiry of the transitional period of harmonization with the Industrial Emissions Directive pursuant to the provisions of the EU Accession Agreement (following 1 January 2018), the construction of the DeNO_x facility started in the second unit of TPP Plomin. The investment value is EUR 17.3 million.
- Pursuant to provisions of the Recovery programme for reducing solid emissions from EL-TO Zagreb, air quality measurements began at the Bijenik mobile station. Under the Recovery Programme, the obligation of measuring sulfur dioxide SO₂ and solids PM10 was set in the four year period as well as the verification of measured data, which will be conducted by a company licenced by the Ministry of Environmental and Nature Protection.
- TE-TO Zagreb carried out the replacement of the device for measuring the air pollution emissions on the main stack (200 m).
- Elektra Požega started the replacement of the existing boiler units by more efficient facade-mounted gas boilers, which will result in reduced fuel consumption and reduced air pollution emissions.

WATER PROTECTION

- TE-TO Zagreb has been conducting the reconstruction of oily water separation within the fuel liquid management.
- A part of the internal drainage system of TPP Sisak has been rehabilitated to achieve structural stability and functionality i.e. its watertightness. The drainage system rehabilitation included the main collector, drainage of mixed, process, sanitary, run-off rain and oily waste waters as well as a septic tank. The device for measuring the waste water flow and the device for measuring the flow of collected and discharged cooling water from the plant have been installed.
- Elektroslavonija Osijek started the rehabilitation of run-off river and sanitary waste waters at its Zeleno polje site.
- The waste water drainage system of Bokanjac Elektra Zadar Facility was connected onto the public system of drainage.

WASTE MANAGEMENT AND SOIL PROTECTION

- Temporary waste storage development continued in HEP's facilities. New containers for a separate collection of waste and waste oil as well as their accompanying bundwalls were procured.
- For the purpose of preventing the leakage of turbine oil from the outdoor tank into the ground, TE-TO Osijek installed a waterproof bundwall. To prevent chemical leaks into the ground when pouring it from cisterns into storage tanks, the tank area has been established.
- To protect own facilities and increase water quality, HEP hydropower plants continued to remove and dispose the debris, which stops at entry points and facility grids during high water levels. Although not the producers of such waste and not being legally bound, HEP fully finances the cleaning of water flows and driftwood waste management. Annually, 2500 to 4500 tonnes of waste is stopped by grids.
- Elektra Zabok and Elektra Sisak recorded extraordinary events of transformer oil leakages into the ground due to unauthorized entries into transformer warehouses. Soil remediation in both cases was entrusted to authorized companies licenced by the Ministry for Environmental and Nature Protection. To prevent unauthorized entries into transformer warehouses and oil leakages into the ground, protective measures have been upgraded (fencing and concreting of warehouse foundation, separator installation).

ENVIRONMENTAL PROTECTION

- Invasive species (egeria densa and zebra mussel) continued to be removed for the purpose of protecting equipment as well as preserving biological diversity of the Drava river in HEP Generation's hydrogeneration area North.


A stylized graphic featuring two white clouds at the top. A blue dotted line curves from the left cloud, passes behind the number '130', and ends at a power plant icon on the right. The power plant icon consists of a black tower with a lightning bolt symbol and a grid-like structure to its right.

130

million kuna worth DeNOx facility
will be built in the second unit of
TPP Plomin

Environmental protection

2014

A black silhouette of a stork standing on a nest made of logs. The entire graphic is enclosed within a yellow circular border.

903

stork nests are located on
HEP distribution network
pillars (out of a total of
1,100 to 1,300 in Croatia)

154.13

million kuna in total was invested by HEP Group
in the protection of environment and nature



2,500-4,500

tonnes of river debris waste stopped
annually by HEP hydropower plant
traps;

HEP fully funds its disposal



- Under the Agreement on cooperation in conducting protection measures of the protected white stork (*Ciconia Ciconia*), concluded between the Ministry of Culture and HEP in 2004, HEP DSO has permanently been conducting measures for white stork protection. During 2014, activities relating to bird protection against MV electric shocks were conducted, especially in areas of increased risk according to data collected during 2013. Pursuant to legal obligations, MV lines data located in the preservation areas significant for birds was gathered to define the most risky areas and establish a more quality monitoring of injuries and a more efficient implementation of bird protection measures against being injured by electricity.

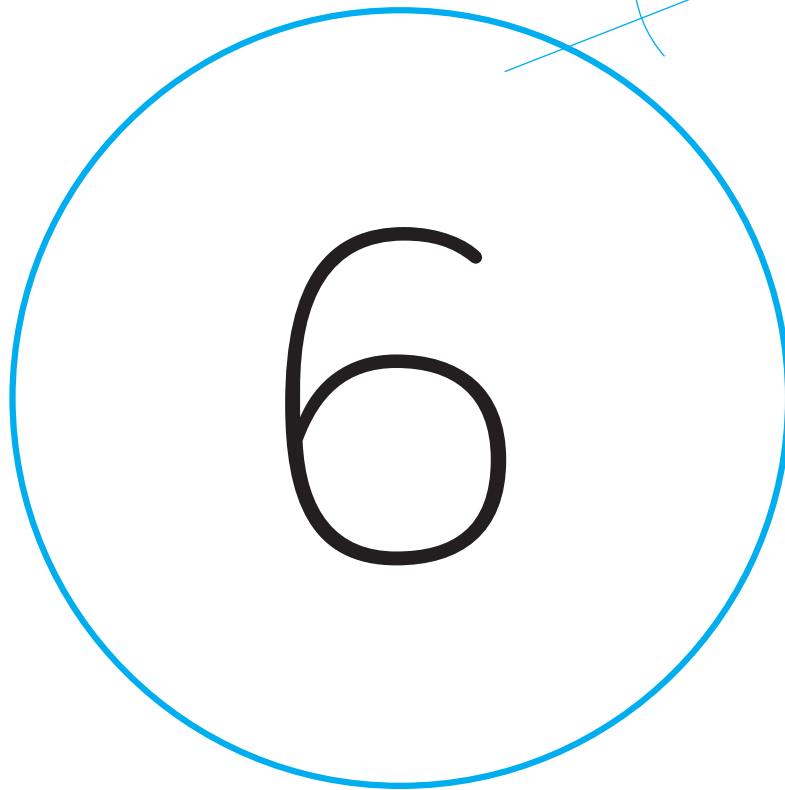
OTHER

- The construction of the heat accumulator is currently underway in TE-TO Zagreb. It will increase the efficiency of all generation units on said site. The reconstruction of the Unit C turbogenerator regulation system was conducted as well as the cooling reconstruction of Voith joint shafts on the grid water circulation pumps. The above will contribute to increased operating efficiency of Unit C as well as to lower fuel consumption and its effect on individual environmental components.
- TE-TO Osijek conducted the modification and reconstruction of raw water heating system for the purpose of improving the utilization degree of waste heat energy.
- TPP Rijeka replaced outdoor lights by more efficient ones.
- In the hydrogeneration area North, the removal of accumulated deposits from the accumulation lake of HPP Varaždin continued for maintaining safety and reaching initial accumulation levels.
- HEP District Heating continued the project of the main hot water pipeline revitalization in Zagreb, Osijek and Sisak. The revitalization has been conducted by implementing the pre-insulated pipe technology which will result in decreased heat losses, increased reliability of supply, reduced fuel consumption and lower air pollution emissions.

CERTIFICATION

- Integrated environment management systems according to ISO 14001 as well as the quality management according to ISO 9001 were introduced during 2014 in generation facilities of hydropower area south and HPP Dubrovnik. Thus, all thermal and hydro generation facilities of HEP Generation d.o.o. will be harmonized with ISO quality and environment standards.
- In October 2014, TÜV SÜD certified the electricity generation from renewable energy sources in all HEP hydropower plants during 2013. HEP Supply has been selling to all its customers the new ZelEn product since 2013 by using the certificate as a certificate of origin of RES generation, so-called green energy.
- In 2014, all 21 distribution areas of HEP DSO re-certified their environment management systems according to ISO 14001, which were first introduced and certified in 2012.

FINANCIAL STATEMENTS



HRVATSKA ELEKTROPRIVREDA D.D. ZAGREB

Consolidated financial statements

**Independent Auditor's Report
as of 31 December 2014**

Responsibility for the consolidated financial statements	73
Independent auditor's report	74
Consolidated Statement of Comprehensive Income	76
Consolidated Balance Sheet/Consolidated Statement of Financial Position	78
Consolidated Statement of Changes in Equity	80
Consolidated Cash Flow Statement	81
Notes to the Consolidated Financial Statements	83

The Management Board of Hrvatska elektroprivreda d.d., Zagreb, Ulica grada Vukovara 37, (hereinafter: "HEP d.d." or "the Company") is responsible for ensuring that the annual consolidated financial statements for the year 2014 are prepared in accordance with the Accounting Act (Official gazette No 109/07, 54/13) and the International Financial Reporting Standards effective in the European Union, to give a truthful and objective view of the Company's consolidated financial position, consolidated results of operations, consolidated changes in equity and consolidated cash flows 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 drawn up consolidated financial statements under the assumption that the Company is a going concern.

In preparing these financial statements, the Board is responsible for:

- the selection of suitable accounting policies that are then applied consistently;
- reasonable and prudent judgments and estimates;
- following applicable financial reporting standards, and that any material departures are disclosed and explained in the consolidated financial statements; and
- preparing the consolidated financial statements on the going concern basis unless such and assumption is not appropriate.

The Board is responsible for keeping proper accounting records, which shall at any time and with reasonable accuracy reflect the Company's consolidated financial position and results of operations and their compliance with the Accounting Act (Official Gazette No 109/07, 54/13) and the International Financial Reporting Standards. The Board is also responsible for safeguarding the Company's assets and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

Signed on behalf of the Board:

Perica Jukić
President of the Board

Hrvatska elektroprivreda d.d.
Ulica grada Vukovara 37
10000 Zagreb
Republic of Croatia
30 April 2015

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Hrvatska elektroprivreda (HEP) d.d.

1. We have conducted an audit of the accompanying annual consolidated financial statements of Hrvatska Elektroprivreda d.d. (hereinafter: "HEP d.d." or "the Company") which comprise the Consolidated Balance Sheet / Consolidated Statement of Financial Position as at 31 December 2014; Consolidated Statement of Comprehensive Income; the Consolidated Statement of Changes in Equity; the Consolidated Cash Flow Statement for the year ended, and a summary of principal accounting policies and other notes with explanations.

Responsibility of the Company's Management

2. The Company's Management is responsible for the preparation and fair presentation of the enclosed Consolidated Financial Statements according to the International Financial Reporting Standards in effect in the European Union and for internal controls that Management identifies are relevant to prepare the consolidated financial statements free from any significant misstatements whether due to fraud or error.

Auditor's responsibility

3. Our responsibility is to express an opinion on the enclosed consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the consolidated financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the said circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

4. In our opinion, the enclosed consolidated financial statements, in all materially significant aspects, give a true and fair view of the consolidated financial position of Hrvatska elektroprivreda (HEP) d.d., as at 31 December 2014 and of HEP d.d.'s consolidated financial performance and consolidated cash flows for 2014 in accordance with the Croatian Accounting Act and International Financial Reporting Standards that are effective in the European Union.

Emphasis of matter

5. As described in Note 28 to the consolidated financial statements in the Consolidated Balance Sheet / Consolidated Statement of the Financial Position as at 31 December 2014, the Company has entered liability for a clearing debt to the amount of HRK 759,089 thousand regarding payment under a letter of credit on the basis of consent by the Ministry of Finance with the use of funds pursuant to an interbank agreement. As there is no other document that regulates relations between the Company and the Ministry of Finance regarding the clearing debt up to the date of our independent auditor's report, it has not been clearly defined as either a loan or government subsidy.

Opinion compliance with other legal or regulatory requirements

6. The Management Board is responsible for the preparation of these annual consolidated financial statements for the year ended 31 December 2014 in the prescribed form based on the Statute of the structure and Content of Annual Consolidated Financial Statements (Official Gazette 38/08, 12/09, 130/10) ("Standard Annual Consolidated Financial Statements"). Financial information presented in Company's Standard Annual Consolidated Financial Statements is in accordance with the information presented in Company's Annual Consolidated Financial Statements presented on pages 4 to 95 for which we expressed our opinion as presented in the paragraph above 'Opinion.'

Disclaimer of opinion on compliance of the Annual Report

7. The Management Board is responsible for the preparation of the Company's Annual Report. Pursuant to Article 17 of the Accounting Act, we are obliged to give our opinion on the compatibility of the Company's Annual Report with the Company's Annual Consolidated Financial Statements. In our opinion, pursuant to the conducted audit of the Company's Annual Consolidated Financial Statements and in comparison with the Company's Annual Report for the year ended 31 December 2014, the financial information presented in the Company's Annual Report and approved by the Management Board on 30 April 2015 is in compliance with the financial information presented in the Company's Annual Consolidated Financial Statements presented on pages 4 to 95 for which we have expressed our opinion as stated in the paragraph 'Opinion' above.

Zagreb, 30 April 2015

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

Zdenko Balen, Member of the Board
Ines Rožić, Certified Auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić, Member of the Board
Dubravka Tršinar, Certified Auditor

Consolidated Statement of Comprehensive Income

FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	2014	2013
		HRK '000	HRK '000
			Restated
Income from electricity sales	4	10,575,290	11,947,939
Income from thermal power sales	4	671,946	763,461
Income from gas sales on wholesale market	4, 34	689,575	-
Income from gas sales to customers	4	371,490	406,167
Other operating income	4,5	1,290,873	1,577,350
Total operating income		13,599,174	14,694,917
Cost of electricity supplies		(1,200,023)	(2,186,214)
Fuel costs		(1,642,692)	(2,609,803)
Costs of gas sales on wholesale market	34	(717,721)	-
Staff costs	6	(1,880,519)	(1,868,718)
Depreciations costs	10, 11	(1,897,190)	(1,836,801)
Other operating expenses	7	(3,060,580)	(3,819,773)
Total operating expenses		(10,398,725)	(12,321,309)
Profit from operations		3,200,449	2,373,608
Financial income	8	433,671	62,541
Financial expenses	8	(556,577)	(873,287)
Net financial expenses		(122,906)	(810,746)
Profit before tax		3,077,543	1,562,862
Profit	9	(612,119)	(264,658)
Profit for current year		2,465,424	1,298,204
Attributable to:			
Equity holder		2,462,332	1,292,256
Non-controlling interest		3,092	5,948
		2,465,424	1,298,204

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

Consolidated Statement of Comprehensive Income (continued)
For the year ended 31 December 2014

	2014	2013
	HRK '000	HRK '000
		Restated
Profit for the current year	2,465,424	1,298,204
Other comprehensive income		
Foreign currency translation differences	81	401
Fair valuation of JANAF shares	52,330	(3,429)
Total items which are transferred into profit and loss account	52,411	(3,028)
Other comprehensive income / (loss), net	52,411	(3,028)
Total comprehensive income for the current year	2,517,835	1,295,176
Total comprehensive income attributable to:		
Equity holder	2,514,662	1,288,827
Non-controlling interest	3,173	6,349
	2,517,835	1,295,176

The accompanying notes are an integral part of these consolidated financial statements.
Signed on behalf of the Company on 30 April 2015.

Perica Jukić
President of the Board

Consolidated Balance Sheet /Consolidated Statement of Financial Position

AS AT 31 DECEMBER 2014

ASSETS	Note	31 December 2014	31 December 2013	1 January 2013
		HRK '000	HRK '000	HRK '000
			Restated	Restated
Long-term assets				
Property, plant and equipment	10, 14	25,334,813	25,318,021	25,121,211
Capital works in progress	10	4,188,741	4,076,885	3,929,074
Intangible assets	11	77,046	69,433	73,968
Investment property	12	236,153	233,057	233,917
Prepayment for tangible assets	13	41,486	57,766	72,318
Long-term loans and deposits	16	4,533	6,160	514
Assets available for sale and other investments	17	192,676	125,166	129,353
Other long-term assets	18	49,804	58,812	67,318
Deferred tax assets	9	653,907	756,647	724,929
		30,779,159	30,701,947	30,352,602
Short-term assets				
Inventories	19	1,613,297	1,154,404	1,250,037
Trade receivables	20	1,864,680	1,800,076	1,873,245
Other short-term receivables	21	519,682	654,169	317,996
Cash and cash equivalents	22	1,079,900	260,844	605,024
		5,077,559	3,869,493	4,046,302
TOTAL ASSETS		35,856,718	34,571,440	34,398,904

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

Consolidated Balance Sheet/Consolidated Statement of Financial Position (continued)
As at 31 December 2014

CAPITAL and LIABILITIES	Note	31 December 2014	31 December 2013	1 January 2013
		HRK '000	HRK '000	HRK '000
			Restated	Restated
Share capital	23	19,792,159	19,792,159	19,792,159
Capital reserves	23	54,947	2,617	6,046
Retained earnings	23	2,201,265	18,809	(1,207,682)
Equity attributable to equity holder		22,048,371	19,813,585	18,590,523
Non-controlling interest	15	29,202	31,977	47,283
Total equity		22,077,573	19,845,562	18,637,806
Long-term borrowings	24	1,262,036	1,722,010	1,839,630
Long-term liabilities toward the state	25	21,690	24,451	27,544
Long-term provision	26	902,779	808,382	661,411
Bonds issued	27	3,194,986	3,278,893	3,335,608
Other long-term liabilities	28	4,499,502	5,038,526	4,911,633
Deferred tax liability		13,573	654	1,511
Total long-term liabilities		9,894,566	10,872,916	10,777,337
Trade payables	32	1,590,745	1,580,440	2,492,729
Current portion of long-term bonds issued	27	93,380	93,380	593,380
Current portion of long-term borrowings	24	416,349	208,838	132,084
Short-term borrowings	29	8,981	692,654	410,843
Taxes and contributions payable	30	361,095	165,670	347,817
Interest payable		38,263	41,132	45,574
Liabilities to employees	31	151,240	145,940	140,568
Other short-term payable	32	1,224,526	924,908	820,766
Total current liabilities		3,884,579	3,852,962	4,983,761
TOTAL CAPITAL AND LIABILITIES		35,856,718	34,571,440	34,398,904

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

Signed on behalf of the Company on 30 April 2015
Perica Jukić
President of the Board

Consolidated Statement of Changes in Equity

FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital	Capital reserves	Retained earnings/ transferred (loss)	Equity attributable to the equity holder of the parent	Non- controlling interest	Total equity
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Effect of restatement	-	-	(1,326,597)	(1,326,597)	-	(1,326,597)
Balance at 1 January 2013 Restated	19,792,159	6,046	(1,207,682)	18,590,523	47,283	18,637,806
Transferred losses	-	-	(271)	(271)	-	(271)
Transferred losses - NEK	-	-	(75,081)	(75,081)	-	(75,081)
Surpluses of land	-	-	1,622	1,622	-	1,622
Profit for the current year	-	-	1,292,256	1,292,256	5,948	1,298,204
Translation differences	-	-	-	-	401	401
Fair value - JANAF shares	-	(3,429)	-	(3,429)	-	(3,429)
Total comprehensive income for the current year	-	(3,429)	1,292,256	1,288,827	6,349	1,295,176
Non-controlling interest	-	-	-	-	(8,707)	(8,707)
Distribution of dividend RWE	-	-	-	-	(12,948)	(12,948)
Balance at 31 December 2013	19,792,159	2,617	10,844	19,805,620	31,977	19,837,597
Restatement	-	-	7,965	7,965	-	7,965
Balance at 1 January 2014 Restated	19,792,159	2,617	18,809	19,813,585	31,977	19,845,562
Effect of restatement - NE Krško	-	-	2,135	2,135	-	2,135
Allocation of retained earnings	-	-	(284,918)	(284,918)	-	(284,918)
Surpluses in land	-	-	2,907	2,907	-	2,907
Income in current year	-	-	2,452,411	2,452,411	3,092	2,455,503
Income in current year - NEK	-	-	9,921	9,921	-	9,921
Translation differences	-	-	-	-	81	81
Fair value JANAF shares	-	52,330	-	52,330	-	52,330
Total comprehensive income for the current year	-	52,330	2,462,332	2,514,662	3,173	2,517,835
Non-controlling interest	-	-	-	-	(5,948)	(5,948)
Balance at 31 December 2014	19,792,159	54,947	2,201,265	22,048,371	29,202	22,077,573

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

Signed on behalf of the Company on 30 April 2015

Perica Jukić

President of the Board

Consolidated Cash Flow Statement

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK '000	HRK '000
		Restated
Cash flow from operating activities		
Profit in current year	2,465,424	1,298,204
Income tax expense recognised in profit	509,764	296,377
Net financial expense	122,906	810,746
Gain from real estate fair valuation	(3,954)	(4,907)
Decrease of other long-term assets	(49,311)	(20,179)
Fair value adjustment JANAf shares	52,330	(3,429)
Loss on fair value adjustment of derivatives	393,281	(391,808)
Depreciation – real estate, plant & equipment & intangible assets	1,897,190	1,836,801
Increase/ value adjustment of receivables	56,689	25,811
Increase / value adjustment of inventories	19,892	47,987
Increase/(decrease) provisions	94,397	115,744
Operating cash flows before movements in working capital	5,558,608	4,011,347
Increase trade receivables	(121,293)	67,305
Decrease in inventories	(478,785)	30,418
(Increase) /decrease other short-term assets	(60,454)	(162,397)
(Decrease / increase trade liabilities	(67,470)	(639,960)
Increase other short-term liabilities	798,242	(50,994)
(Decrease) other long-term liabilities	(607,062)	93,642
Cash generated from operations	5,021,786	3,349,361
Paid income tax / Income tax return	(465,018)	(364,946)
Interest paid	(404,220)	(378,355)
NET CASH (USED FOR) /OPERATING ACTIVITIES	4,152,548	2,606,060
INVESTMENT ACTIVITIES		
Interest received	13,210	13,817
Acquisition of property, plant and equipment	(2,042,535)	(2,166,937)
Property, plant and equipment sold	20,845	33,507
Change in the non-controlling interest and dividend payment to RWE	(5,948)	(21,655)
NET CASH USED IN INVESTMENT ACTIVITIES	(2,014,428)	(2,141,268)

Consolidated Cash Flow Statement (continued)
For the year ended 31 December 2014

	2014	2013
	HRK '000	HRK '000
		Restated
FINANCING ACTIVITIES		
Gains from long-term loans	58	23,955
Gains from short-term loans	-	478,000
Repayment of long-term loans	(258,958)	(134,547)
Repayment of bonds issued	(93,380)	(593,380)
Repayment of short-term loans	(681,866)	(583,000)
Allocation of dividend to the parent	(284,918)	-
NET CASH USED IN FINANCING ACTIVITIES	(1,319,064)	(808,972)
NET INCREASE/(DECREASE) OF CASH AND CASH EQUIVALENTS	819,056	(344,180)
CASH AND CASH EQUIVALENTS AT START OF YEAR	260,844	605,024
CASH AND CASH EQUIVALENTS AT END OF YEAR	1,079,900	260,844

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

Signed on behalf of the Company on 30 April 2015

Perica Jukić
 President of the Board

Notes to the Consolidated Financial Statements – HEP d.d.

FOR THE YEAR ENDED 31 DECEMBER 2014

GENERAL

The 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 Note 35.

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

All the Group’s activities are governed by applicable laws, regulations and decisions issued by the Croatian Government.

As at 31 December 2014, the Group employed 12,061 workers (31 December 2013: 11,877).

As at 31 December NEK d.o.o. employed 646 workers (2013.: 635)

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

ENERGY LAWS

The Croatian Parliament (Sabor) on 19 October 2012 adopted Energy Act regulating energy activities and on 8 February 2013 Sabor passed the Electricity Market Act. The Gas Market Act was adopted on 22 February 2013 and the District Heating Energy Act in turn was adopted on 21 June 2013. The new laws and by-laws determine the further restructuring of the HEP Group and the adjustment of operations in line with European Union guidelines and directives.

The HEP d.d. and subsidiary companies its services continue to perform as by law determined public services: the transmission, distribution and supply of electricity which is performed as a universal service and a guaranteed service.

The generation, supply and trading of electricity are performed as market activities as is defined by regulations which regulate energy activities and trading on energy markets.

The supply of electricity is performed according to rules by which are regulated market relations, where the energy subjects freely contract the quantity and price of electricity delivered. The supply of electricity which is performed as a universal service and as a guaranteed service is performed according to regulated conditions to buyers who have the right to such mode of supply and choose it freely or utilize it automatically. Buyers in the household category are supplied with electricity within the system of a public service commitment as do privileged customers who did not utilize the right to choice a suppliers or have remained without a supplier. Some customers in the household category have exercised the right to choose a supplier.

HEP d.d. and subsidiary companies make adjustments to Group’s organization structure according to changed regulations and time-limits prescribed by these regulations.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

GENERAL (continued)

ENERGY LAWS (CONTINUED)

In April 2012, the Government of the Republic of Croatia (RH) adopted a Decision on The Electricity Generation Tariff Model, with the exemption of privileged customers, with no tariff item amounts; The Electricity Transmission Tariff Model, with no tariff item amounts; The Electricity Distribution Tariff Model, with no tariff amounts; and the Electricity Supply Tariff Model, with the exemption of eligible customers, with no tariff amounts. The Group has been applying the tariff models since 1 May 2012; Decision on the amount of tariff items for electricity generation with the exception of privileged customers, without tariff items and the tariff system for the supply of electricity with the exception of privileged customers without tariff items which were applicable until 30 September 2013.

In February 2013 the Electricity Market Act was adopted which determines that each customer has the right to freely choose a supplier, and customers in the household category have the right to electricity supplies as an universal service. Customers, who did not utilize the right to choose a supplier or have remained without a supplier, consume the service of guaranteed supply which is performed as a public service. Pursuant to the provisions of the Electricity Market Law on 13 September the Croatian Electricity Regulatory Agency (HERA) adopted the Methodology for determining tariff items for electricity supplies within the framework of a universal service and on 17 December 2013 HERA adopted the Methodology for determining the amount of tariff items for guaranteed electricity supplies.

As of 1 October 2013 electricity supplies for households within the framework of universal services are subject to tariff items for electricity and supplies and fees in accordance with the Methodology for determining the amount of tariff items for electricity supplies within universal services and a decision by HEP Operator distribucijskog sustava d.o.o. on the amount of tariff items for electricity supplies within the framework of universal services dated 1 October 2013.

Customers supplied with electricity as a guaranteed supply, pay for supplies to the amount of tariff items in accordance with the Methodology for determining the prices for calculated electricity balancing, subject to reliable discrepancies. As of 1 July 2014 tariff items for electricity supplies in accordance with the Methodology for determining amounts of tariff items for guaranteed electricity supplies and a HERA decision on the amount of tariff items for guaranteed electricity supplies dated 12 June 2014 are applied for supplies to customers within the framework of guaranteed supplies.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

GENERAL (continued)

GOVERNANCE AND MANAGEMENT

GENERAL ASSEMBLY

The General Assembly consists of members representing shareholder interests:

Ivan Vrdoljak	Member	Since 21 November 2012
---------------	--------	------------------------

Supervisory Board

Members of the Supervisory Board in 2014

Nikola Bruketa	President	Member since 23 February 2012	2012
Žarko Primorac	Member	Member since 23 February 2012	2012
Ivo Uglešić	Member	Member since 23 February 2012	2012
Ante Ramljak	Member	Member since 23 February 2012	2012
Igor Džajić	Member	Member since 19 September	2012
Juraj Bukša	Member	Member since 5 June	2014
Jadranko Berlengi	Member	Member since 3 June	2008

Supervisory Board in 2013

Nikola Bruketa	President	Member since 23 February 2012	2012
Žarko Primorac	Member	Member since 23 February 2012	2012
Ivo Uglešić	Member	Member since 23 February 2012	2012
Ante Ramljak	Member	Member since 23 February 2012	2012
Igor Džajić	Member	Member since 19 September	2012
Mirko Žužić	Member	Member since 19 September	2013
Jadranko Berlengi	Member	Member since 3 June	2008

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

GENERAL (continued)

GOVERNANCE AND MANAGEMENT (CONTINUED)

Management Board in 2014

Perica Jukić	President	Member since 10 May 2013, President since 12 September 2014
Tomislav Šerić	President	Member since 10 May 2013 to 12 September 2014
Zvonko Ercegovac	Member	Member since 23 February 2012
Ivan Matasić	Member	Member since 23 February 2012 to 12 September 2014
Krunoslava Grgić-Bolješić	Member	Member since 23 February 2012 to 12 September 2014
Željko Štromar	Member	Member since 16 December 2013 to 31 March 2015
Saša Dujmić	Member	Member since 4 December 2014

Management Board in 2013

Tomislav Šerić	President	Member since 10 May 2013
Zlatko Koračević	President	Member to 10 May 2013
Zvonko Ercegovac	Member	Member since 23 February 2012
Ivan Matasić	Member	Member since 23 February 2012
Krunoslava Grgić-Bolješić	Member	Member since 23 February 2012
Perica Jukić	Member	Member since 10 May 2013
Rodoljub Lalić	Member	Member to 10 May 2013
Željko Štromar	Member	Member since 16 December 2013

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

PRESENTATION OF FINANCIAL STATEMENTS

The financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") effective in the European Union.

The IFRS issued by the Committee for Financial Reporting Standards appointed by the Government of the RH (Official Gazette 136/09, 8/10, 18/10, 27/10, 65/10, 120/10, 58/11, 140/11, 15/12, 118/12, 45/13, 69/13, 73/13), which were effective until Croatia entered the European Union, are in accordance with the IFRS established by the European Commission and instruments in the Official Gazette of the European Union.

Financial statements are prepared on the basis of historical costs with the exception of certain financial instruments that are stated in revaluated amounts. The financial statements are stated in thousands of Croatian Kuna ('000 HRK), as the official operating currency that represents the Group's principal business operations.

BASIS OF ACCOUNTING

The Group maintains its accounting records in Croatian and the reporting currency is the Croatian Kuna in accordance with Croatian laws and accounting principles and practices observed by enterprises in Croatia. The accounting records of the subsidiaries in Croatia and abroad are maintained in accordance with the requirements of the respective local jurisdictions.

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

STANDARDS, INTERPRETATIONS AND SUPPLEMENTS ISSUED BY THE IASB AND ADOPTED IN THE EUROPEAN UNION THAT ARE IN FORCE

As of 31 December 2014, the Company adopted the amended IASB standards listed below and a comparison of data has been presented. The adopted standards did not influence the principal as of 1 January 2014:

- **IFRS 10 “Consolidated Financial Statements,”** issued in May 2011 and supplemented in 2012 replaces the preceding IAS 27 version (2008) “Consolidated and Separated Financial Statements” effective for the annual period beginning on or after 1 January 2014);
- **IFRS 11 “Joint Arrangements,”** issued in May 2011 and supplemented in 2012 replaces the preceding IAS 31 “Interest in Joint Ventures,” (effective for the annual period beginning on or after 1 January 2014);
- **IFRS 12 “Disclosure of Interests in Other Entities,”** issued in May 2011 and supplemented in 2012 (effective for the annual period beginning on or after 1 January 2014);
- **IAS 27 “Unconsolidated Financial Statements,”** (amended and supplemented in 2011), consolidated requirements previously described in IAS 27 (2008) are revised and contained in IFRS 10 “Consolidated Financial Statements,” (IAS 27 in force (amendment and supplement in 2011) is applied to the annual period beginning on or after 1 January 2014);
- **IAS 28 “Investments in Associates and Joint Ventures,”** (amended and supplemented in 2011). This version replaces IAS 28 (2003) “Investments in Associates,” (IAS 28 in force (amended and supplement in 2011) is applied to the annual period beginning on or after 1 January 2014);
- **IFRS 21 “Levies,”** – issued in May 2013, (effective for the annual period beginning on or after 1 January 2014);
- **Supplements to IAS 32** – Clearance of financial assets and financial liabilities (effective for the annual period beginning on or after 1 January 2014);
- **Amendments and supplements to IAS 39** – Eligible Hedge Items (effective for the annual period beginning on or after 1 January 2014).

STANDARDS, INTERPRETATIONS AND SUPPLEMENTS THAT HAVE NOT COME INTO FORCE AS YET

On the date these financial statements were approved the following amended standards and interpretations had been issued but were not in force as at 31 December 2014:

- **IFRS 9 Financial Instruments** – in July 2014, IASB issued a final version of IFRS 9 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 affect the classification and measurement of financial instruments.
- **IFRS 14 Regulatory Deferral Accounts** – this standard relates to subjects that operate on regulated markets and are applying IFRS for the first time. IFRS 14 is effective for the annual period beginning on or after 1 January 2016. The Company prepares its Financial Statements in accordance with IFRS and does not apply this standard.
- **Amendments and supplements to IAS 19 Employee Benefits** – IAS 19 requires subjects to consider employee or third party contributions in accounting defined earning. This amendment is effective for the annual period beginning on or after 1 July 2014. The Company does not expect this amendment to be relevant to the Company.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- Annual Improvements 2010-2012, effective as of 1 July 2014 and it is not expected that they will have any significant impact on the Company. They include:
 - IFRS 2 Share-based Payment
 - IFRS 3 Business Combinations
 - IFRS 8 Operating Segments
 - IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets
 - IAS 24 Related Party Disclosures
- Annual Improvements 2011-2013, effective as of 1 July 2014 and it is not expected that they will have any significant impact on the Company. They include:
 - IFRS 3 Business Combinations
 - IFRS 13 Fair Value Measurement
 - IAS 40 Investment Property
 - 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.

Management anticipates that the application of other standards, amendments and interpretations will not have a materially significant impact on the financial statements in the period of their initial application.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

BASIS FOR THE PREPARATION OF THE GROUP'S FINANCIAL STATEMENTS

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

PRINCIPLES AND METHOD OF CONSOLIDATION

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

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group

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

Non-controlling interests in the net assets of consolidated subsidiaries in these financial statements are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling share of changes in equity since the date of the combination.

REPORTING CURRENCY

The Group's consolidated financial statements are prepared in Croatian Kuna.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

INVESTMENTS IN ASSOCIATED

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

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

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

Any excess of the cost of acquisition over the Group’s share of the fair value of the identifiable net assets of the associate at the date of acquisition is recognised as goodwill. Goodwill is included in the net book value of investments and is tested for impairment as part of investment. Any deficiency of the cost of acquisition below the Group’s share of the fair value of the identifiable net assets of the associate at the date of acquisition is credited to profit and loss in the period of acquisition. Where the Group transacts with its associate, profits and losses are eliminated to the extent of the Group’s interest in the relevant associate.

INVESTMENT IN JOINTLY CONTROLLED ENTITIES

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

Certain individual financial statements by companies, for investment by jointly controlled companies assets and liabilities are recorded in accordance to the share in joint management (Note 13 Investment in NEK d.o.o.).

Where a Group entity directly undertakes its activities under joint venture arrangements, the Group’s share of jointly controlled assets and any liabilities jointly incurred with other ventures are recognised in the financial statements of the relevant entity and classified according to their nature. Liabilities and expenses incurred directly in respect of interests in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Group’s share of the output of jointly controlled assets, and its share of joint venture expenses, are recognised when it is probable that the economic benefits associated with the transactions will flow to / from the Group and their amount can be measured reliably. Joint venture arrangements that involve the establishment of a separate entity in which each venture has an interest are referred to as jointly controlled entities. The Group reports its interests in jointly controlled entities using full consolidation.

The Group reports its interests in jointly controlled entities using full consolidation for TE Plomin d.o.o. and accounts for assets and liabilities based on its share in joint control.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

COSTS OF CONTRIBUTIONS AND OTHER EMPLOYEE BENEFIT COSTS

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

The Group is obliged to pay contributions to pension and health insurance funds in Croatia in accordance with legislative regulations. This obligation applies to all staff hired on the basis of employment contract. The contributions are paid at a certain percentage determined on the basis of gross salary.

	2014 and 2013
Pension insurance contributions	20%
Health insurance contributions as of 1 April 2014	15%
Employment fund contributions	1.7%
Occupational injuries	0.5%

CONTRIBUTIONS FOR HEALTH INSURANCE

As of 1 May 2012 to 31 March 2014 a rate of 13% applied and then as of 1 April that rate was 15%.

The Group's companies are obliged to withhold pension insurance contributions from the employees' gross salaries.

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

PENSION ALLOWANCES AND JUBILEE AWARDS

The Group pays employees jubilee awards and one-off retirement bonuses upon retirement. The obligations and expenses for these payments are determined with the application of the method of forecasting credit units. The method of forecasting credit units for each period of seniority is observed as the basis for additional units of eligibility to allowances and each unit is measured separately until the realisation of final liabilities. This liability is determined at the current value of forecasted future monetary outflow with the application of the discount rate which is similar to the interest rate of state bonds in the RH 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 in the Company.

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014**

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

**PENSION ALLOWANCES AND JUBILEE
AWARDS (CONTINUED)**

SEVERANCE PACKAGES

A Collective Agreement has been in force as of 1 October 2014 (which relates to all members of the HEP Company), pursuant to which each employee is eligible for a severance package upon retiring amounting to 1/8 of the average gross monthly wage of employees for the three months prior to retiring and for each completed year of continual employment in the Company. That Collective Agreement is valid until 30 June 2016.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are carried at cost less accumulated depreciation and any impairment losses, except for land, which is carried at cost. The estimated useful lives, residual values and depreciation methods are reviewed at each year's end, and each change in the estimate is counted on the basis of new expectations and has the effect in the current and the future periods. Property, plant and equipment in used are depreciated using the straight-line method on the following bases:

	2014 and 2013
Buildings	
Hydroelectric power plants (flood gates and dams, buildings and other buildings as well as accompanying structures)	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 other)	20 – 40 years
Water and steam pipelines and other thermal power generation	33 years
Gas pipelines	20 – 25 years
Administrative buildings	50 years
Plant and equipment	
Hydroelectric power plants	10 – 33 years
Thermal power plants	6 – 25 years
Electricity transmission plants and facilities (electric parts of transformer stations and 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 license	5 years
Telecommunications equipment	5 – 20 years
Vehicles	5 – 8 years
Office furniture	10 years

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

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

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

Any gains or losses arising from the disposal or withdrawal of property, plant and equipment is determined as the difference between the proceeds of gains on sale and the carrying amount of the asset and they are credited or charged, respectively, to the income statement.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

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

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

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

A recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

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

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

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

INTANGIBLE ASSETS

Intangible fixed assets include patents, trademarks and licenses and are carried at cost less accumulated depreciation. Depreciation is provided on a straight-line method over a period of 5 years (licences and IT programmes).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INVESTMENT PROPERTY

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

Investment in property ceases to be recognised, i.e. removed due to sale or permanent withdrawal from use when no future economic benefits are expected from the disposal. Any gain or loss arising on de-recognition of the property (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period in which the property ceases to be recognized.

FINANCE AND OPERATING LEASES

THE GROUP AS A LESSEE

The Group has no significant finance lease arrangements and no significant operating lease arrangements were entered during 2014 and 2013. The Group recognises amounts payable under operating leases are recognised as an expense on a straight-line basis over the term of the relevant lease, unless there is another systematic basis that would be more representative of the time pattern of the user's benefit.

TRADE RECEIVABLES AND PREPAYMENTS

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

Management conducts a value adjustment for bad of doubtful accounts based on a review of the total age structure of the receivables and based on a review of significant, individual amounts included in the receivables.

As the collectability of certain receivables over a longer period is not certain, the Group makes a reasonable assessment of allowance for irrecoverable amounts:

Age of receivables	Percentage if impairment 2014 and 2013
31 – 60 days	1.5%
61 – 90 days	3%
91 -180 days	9%
181-365 days	30%
More than 1 year	90%

Legally disputed receivables and receivables from subjects in the process of pre-bankruptcy settlement (principal debt and interest) are fully provided, regardless of the number of past due days and the provision is charged to expenses.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INVENTORIES

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

Since 2013 inventories include CO₂ emission units, with the inclusion of the RH into the European system of trading with emission units of green-house gasses (EU ETS), Hrvatska elektroprivreda as a producer of electricity and heating energy is obliged to purchase emission units of green-house gasses that correspond to verified CO₂ emission produced by burning fossil fuel in thermal power plants which then emit CO₂.

Since April 2014 stocks consist of gas for sale on wholesale markets and are stated at the lower value of the cost of supply determined on the basis of the average weighted price. (Notes 18 and 31)

The costs of stocks of gas sold directly to customers are calculated using the method of specific identification of their individual costs.

Cost comprises the invoiced amount as well as all other costs directly attributable to bringing inventories to their location and the condition of being readily available for use. The average weighted price method is used to determine the cost of inventories

CASH AND CASH EQUIVALENTS

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

BORROWING COSTS

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

All other borrowing costs are recognised in the statement of income in the period in which they are incurred. Short-term borrowings and supplier loans are recorded at original amount granted less repayment. Interest expense is charged to income statement on an accrual basis.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

FOREIGN CURRENCY TRANSACTIONS

Individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group entity are expressed in Croatian Kuna (HRK), which is the functional currency of the Group and the currency presented in the consolidated financial statements.

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

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

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

TAXATION

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

CURRENT TAX

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

DEFERRED TAX

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

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

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the amount in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

TAXATION (CONTINUED)

CURRENT AND DEFERRED TAX PERIODS

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

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

FINANCIAL ASSETS

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

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

EFFECTIVE INTEREST METHOD

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

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

FINANCIAL ASSETS AVAILABLE FOR SALE

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

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

FINANCIAL ASSETS (CONTINUED)

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

LOANS AND RECEIVABLES

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

DECREASE IN VALUE OF FINANCIAL ASSETS

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

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

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

Previously entered losses subsequent to impairment of principal instruments available for sale are not cancelled through the income statement and any increase in fair value subsequent to an impairment loss is recognised directly in equity.

INVESTMENTS

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

FINANCIAL LIABILITIES

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

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

CESSATION OF RECOGNISING FINANCIAL LIABILITIES

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

DERIVATIVE FINANCIAL INSTRUMENTS

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

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

PROVISIONS

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

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014****2. SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (continued)****USE OF ESTIMATES IN PREPARING
THE FINANCIAL STATEMENTS**

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

RECOGNITION OF INCOME

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

Income from the sale of electricity is recognised according to the best Management estimate of the actual energy consumed based on the energy data and tariff items under the cost-recovery models called Electricity Transmission Tariff Model with no Tariff Amounts and The Electricity Distribution Tariff Model, with no Tariff Amounts; and the Electricity Supply Tariff Model, with the exemption of eligible customers, with no tariff amounts until 30 September 2013 and the Methodology for determining of the amounts of tariff items for the supply of electric energy in the frame of universal service since 1 October 2013. Recognition of income is based on Decision of the Government of the Republic of Croatia on the level of tariff items from April 2012 and the Decision of HEP Operator distribucijskog sustava d.o.o. on the level of tariff items for the supply of electric energy in the frame of universal service from September 2013. Customers supplied with electricity as a guaranteed supply pay for supplies to the amount of tariff items in accordance to the Methodology for determining prices to calculate electricity balanced subjects responsible for discrepancies and as of 1 July 2014 they are subject to tariff items for electricity in accordance with the Methodology for defining tariff items amounts for guaranteed electricity supplies and the decision by the Croatian Electricity Regulatory Agency (HERA) of the amount of tariff items for guaranteed electricity supplies date 12 June 2014. Income from the supply of electricity for customers who have selected a supplier are recognised at the price that is in accordance with the Methodology of count of electric energy for privileged buyers in the category of entrepreneurs of the HEP Opskrba and is based on data of sales achieved to buyers with contracted electricity prices and supply fees that are based on the Methodology to calculate electricity prices for supply to buyers by HEP Opskrba, which was adopted by the Supervisory Board of HEP Opskrba. For buyers in the household category, the Decision by HEP d.d. Management of 15.11.2013 is applied – Approval of new product for household customers from HEP Supply which approves the release of the HEPI tariff model on the market.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INCOME FROM CONNECTION FEES

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

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

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

SEGMENTAL DISCLOSURES

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

CRITICAL JUDGEMENT FOR THE APPLICATION OF ACCOUNTING POLICIES

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

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

USEFUL LIVES OF PROPERTY, PLANT AND EQUIPMENT

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

FAIR VALUE ADJUSTMENT OF FINANCIAL ASSETS AND INTEREST SWAP

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

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 Nuclear Power Plant Krško.

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

IMPAIRMENT BASED ON HIGHER OR LOWER CALCULATED INCOME

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

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

CRITICAL JUDGEMENT FOR THE APPLICATION OF ACCOUNTING POLICIES (CONTINUED)

IMPAIRMENT BASED ON HIGHER OR LOWER CALCULATED INCOME (CONTINUED)

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

IMPAIRMENT OF LONG-TERM ASSETS

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

AVAILABILITY OF TAXABLE INCOME FOR WHICH ASSETS FROM DEFERRED TAXES CAN BE RECOGNISED

A deferred tax asset is recognized only to the extent that it is probable that the related tax benefit will be realized. In determining the amount of deferred taxes that can be recognised are required, which are based on the probable quantification of time and level of future taxable profits, together with the future tax planning strategy. The carrying amount of deferred tax assets at 31 December 2014 amounted to HRK 653,907 thousand and at 31 December 2013 it amounted to HRK 756,647 thousand (see Note 9).

ACTUARY ESTIMATES USED TO CALCULATE ALLOWANCES FOR RETIREMENT

The cost of defined benefits is determined using actuarial estimates. Actuarial estimates involve assumptions about discount rates, future salary increases and the mortality or fluctuation rates. Because of the long-term nature of those plans, there is uncertainty surrounding those estimates. Provisions for retirement bonuses and jubilee awards at 31 December 2014 amounted to HRK 364,497 thousand and HRK 271,527 thousand as at 31 December 2013. (see Note 26).

CONSEQUENCES OF CERTAIN LEGAL DISPUTES

There are a number of legal disputes that have arisen from the regular course of its operations. Provisions are recorded if there is a current liability resulting from a past event (taking into account all available evidence, including the opinion of legal experts) where there is a likelihood of an outflow of resources will be required to settle the obligation and if this can be reliably estimated (see Note 26).

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014**

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

CRITICAL JUDGEMENT FOR THE APPLICATION OF ACCOUNTING POLICIES (CONTINUED)

FAIR VALUE OF SHARES IN JANAF AND INVESTMENT PROPERTY

In 2014 and 2013 the Company valued its shares in the Adriatic Oil Pipeline (JANAF) at fair value. The fair value in 2014 and 2013 was determined based on a notification of Central Clearing Deposit Agency regarding open balances as of 31 December. The market value of shares in JANAF at 31 December 2014 amounted to HRK 3,499 (2013: HRK 2,290) resulting in an increase of shares by HRK 65,262 thousand (2013: decrease by HRK 4,318 thousand, see Note 15). The fair value in 2014 and 2013 was included in reserves. A value adjustment of 20% was recorded for the increased value of the investment through an increased value of investment and decrease in provisions and increased in deferred tax liabilities.

VALUE ADJUSTMENT

TAKING OVER PROPERTY FROM HAC D.O.O.

During the period between 2007 and 2009 HEP d.d. and HAC d.o.o. signed an agreement of mutual relations and joint financing of electricity complexes necessary for electricity supplies in relation to the Construction Law, the Public Roads Law, Energy Law, and Law on Electricity Market as a mutual interest. For the purpose of regulating undefined relations between the contractual parties and taking over the said electricity complex, Supplements to the Agreement were prepared whereby the Company takes over the electricity complex constructed by HAC d.o.o. within the construction of public roads in accordance with the provisions of the Roads Law.

Pursuant to the signed Agreement to take over the electricity complex between HEP d.d. and HAC d.o.o. dated 25 March 2015, HEP d.d. has recorded business events in its accounts for 2014 in accordance with Point 42 of the IRS 8 and restated them for previous periods.

INVESTMENTS IN NE KRŠKO D.O.O.

Pursuant to the published International Financial Reporting Standards (IFRS) 11 "Joint Arrangements" which replaced International Accounting Standard (IAS) 31 "Interest in Joint Venture," joint venture in NE Krško d.o.o. according to International Financial Reporting Standard 11 is classified as a joint arrangement. The Company recognises its share in each asset and each liability, income and expense for its share in the joint arrangement of NEK d.o.o. The Company conducted a value adjustment of investments in NE Krško d.o.o. previously calculated by the method of share and difference between method of share and method of accounting assets and liabilities stated as a debit to retained profit.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

VALUE ADJUSTMENT

FAIR VALUE OF SHARES IN THERMAL POWER PLANTS

Pursuant to Defined indicators for the impairment of assets and calculation of value of impairment in accordance with IRS 36 the carrying amount of the value of thermal power plants was conducted which at 31.12.2014 were valued at HRK 2,389,405,851.93. The value adjustment consists of the value of buildings and equipment and plants.

For the reason noted, value adjustments were conducted for previous reporting periods.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

RESTATEMENTS IN THE FINANCIAL STATEMENTS AS AT 1 JANUARY 2013

	Note	Amount in the consolidated financial statements prior to restatement	Amount in the consolidated financial statements after restatement	Effect of restatement increase / (decrease)
		HRK '000	HRK '000	HRK '000
Consolidated Statement of Financial Position at 1 January 2013				
Property, plant and equipment	10	25,304,113	25,121,211	(182,902)
Current investments	10	3,915,002	3,929,074	14,072
Investment in NE Krško	14	1,754,419	-	(1,754,419)
Deferred tax assets	9	224,904	724,929	500,025
Total long-term assets		31,775,826	30,352,602	(1,423,224)
Inventories	19	981,641	1,250,037	268,396
Other short-term receivables	21	243,614	317,996	74,382
Total short-term assets		3,703,524	4,046,302	342,778
TOTAL ASSETS		35,479,350	34,398,904	(1,080,446)
Retained profit	23	118,915	(1,207,682)	(1,326,597)
Principal subscribed to the owner		19,917,120	18,590,523	(1,326,597)
Total capital		19,964,403	18,637,806	(1,326,597)
Liabilities for taxes and contributions		179,441	347,817	168,376
Other short-term liabilities		381,375	820,766	439,391
Total short-term liabilities		4,737,610	4,983,761	246,151
TOTAL CAPITAL and LIABILITIES		35,479,350	34,398,904	(1,080,446)

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

RESTATEMENTS IN THE CONSOLIDATED FINANCIAL STATEMENTS AS AT 31 DECEMBER 2013

	Note	Amount in the consolidated financial statements prior to restatement	Amount in the consolidated financial statements after restatement	Effect of restatement increase / (decrease)
		HRK '000	HRK '000	HRK '000
Consolidated Statement of Comprehensive Income for the year ended 31 December 2013				
Costs of electricity supplies		2,670,155	2,186,214	(483,941)
Fuel costs		2,609,803	2,735,799	125,996
Staff costs		1,739,964	1,868,718	128,754
Depreciations costs	10,11	1,799,217	1,836,801	37,584
Other operating costs		3,498,481	3,693,777	195,296
Total operating expenses		12,317,620	12,321,309	(3,689)
Profit from operations		2,377,297	2,373,608	(3,689)
Profit before tax		1,566,551	1,562,862	(3,689)
Corporate income tax		(265,396)	(264,658)	738
Profit for current year		1,301,155	1,298,204	(2,951)
Capital to the owner		1,295,207	1,292,256	(2,951)
		HRK '000	HRK '000	HRK '000
Consolidated Statement of Financial Position for the year ended 31 December 2013				
Property, plant and equipment	10	25,504,613	25,318,021	(186,592)
Current investments		4,062,813	4,076,885	14,072
Property investment		231,285	233,057	1,772
Prepayments for tangible assets	13	57,288	57,766	478
Investment in NE Krško		1,754,419	-	(1,754,419)
Deferred tax assets	9	255,885	756,647	500,763
Total long-term assets		32,125,873	30,701,947	(1,423,926)
Inventories		903,236	1,154,404	251,168
Trade receivables		1,780,129	1,800,076	19,947
Other short-term receivables		490,930	654,169	163,239
Cash and cash equivalents		260,755	260,844	89
Total short-term assets		3,435,050	3,869,493	434,443
TOTAL ASSETS		35,560,923	34,571,440	(989,483)

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

Retained earnings	23	1,415,473	18,809	(1,396,664)
Principal subscribed to the owner		21,210,249	19,813,585	(1,396,664)
Total capital		21,242,226	19,845,562	(1,396,664)
Liabilities for long-term loans		1,686,418	1,722,010	35,592
Long-term provisions		781,797	808,382	26,585
Other long-term liabilities		5,037,592	5,038,526	934
Total long-term liabilities		10,809,805	10,872,916	63,111
Liabilities toward suppliers		1,485,965	1,580,440	94,475
Liabilities for short-term loans		672,338	692,654	20,316
Liabilities for taxes and contributions	30	35,540	165,670	130,130
Liabilities to employees		135,168	145,940	10,772
Other short-term liabilities		836,531	924,908	88,377
Total short-term liabilities		3,508,892	3,852,962	344,070
TOTAL CAPITAL I LIABILITIES		35,560,923	34,571,440	(989,483)

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

4. SEGMENT INFORMATION

The Group generates income from its operations in a single geographical area – the Republic of Croatia. The Group's reportable segments are separated as follows: electricity (generation, transmission, distribution and sale of electricity), heating (distribution and sale of heating power), and gas (distribution and sale of gas).

Each segment's operating profit or loss include all revenue and expenses directly attributable to the reporting business segments. Information about segment financial income, expense and income tax is not provided on a segment level, as the segments are disclosed based on operating profit.

	Electricity		Heating		Gas		Group	
	2014.	2013.	2014.	2013.	2014.	2013.	2014.	2013.
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Income from core activity	10,575,290	11,947,939	671,946	763,461	1,061,065	406,167	12,308,301	13,117,567
Other income allocated to segments	1,191,846	1,480,459	69,886	66,928	29,141	29,963	1,290,873	1,577,350
Income / losses from operations	3,265,346	2,543,025	(135,068)	(166,615)	70,171	(2,802)	3,200,449	2,373,608
					Net financial expenses		(122,906)	(810,746)
					Profit tax		(612,119)	(264,658)
					Net profit		2,465,424	1,298,204

Segment assets consist primarily of property, plant and equipment, receivables, cash and inventories. Segment liabilities consist of trade and other payables. Non-segment assets and liabilities consist of assets and liabilities that cannot be reasonably attributed to the reporting business segments. Total unallocated assets include investments in NE Krško, 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	
	2014	2013	2014	2013
	HRK '000	HRK '000	HRK '000	HRK '000
		Restated		Restated
Electricity	27,807,534	27,706,562	6,613,995	6,481,463
Heating	1,184,190	1,227,066	203,167	178,558
Gas	389,202	347,338	104,419	153,035
Unallocated	6,475,792	5,290,474	6,857,564	7,912,822
Group Total	35,856,718	34,571,440	13,779,145	14,725,878

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

INFORMATION ON THE LARGEST CUSTOMERS

Income from the sale of electricity in 2014 amounted to HRK 10,575,290 thousand (2013: HRK 11,947,939 thousand).

Income from the sale of district heating energy in 2014 amounted to HRK 671,946 thousand (2013: HRK 763,461 thousand).

Income from the sale of gas in 2014 on the wholesale market amounted to HRK 689,575 thousand and the sale to customers amounted to HRK 371,490 thousand (2013: sale of gas to customers: HRK 406,167 thousand).

TERRITORIAL BUSINESS ANALYSIS

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

	2014	2013
	HRK '000	HRK '000
		Restated
Croatia	9,815,887	11,236,233
European Union member states	604,645	330,581
Other non-European Union countries	154,758	381,125
	10,575,290	11,947,939

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

5. OTHER OPERATING INCOME

	2014	2013
	HRK '000	HRK '000
		Restated
Service for connection to network	352,047	349,864
Income of assets to finance connections fees	234,482	233,050
Subsequent collection of receivables previously with the provision made (Note 20)	99,549	90,064
Services rendered	112,187	132,106
Capitalised assets	88,905	95,988
Default interest	58,664	107,097
Income from the sale of materials	39,510	40,812
Income from the sale of cross-border transmission capacity	75,731	61,041
Income compensations mechanisms HOPS – foreign market	35,747	40,044
Income from cancellation of costs for severance pays on the basis of cancellation of employment contract	-	204,712
Reversal of long-term provisions – vacation	70	11,489
Reversal of long-term provisions for retirement benefits and jubilee awards	4,696	62,666
Reversal of long-term provisions – court costs	42,487	25,259
Income from reversal of other provisions	20	28,529
Income of excises to the invoiced electric energy and gas	29,546	16,749
Income in respect of the electricity bill reminders	5,334	5,493
Income from balancing energy	8,389	-
Income in respect of court costs on claims	1,012	7,022
Inventory surplus – fixed assets	7,654	3,079
Income from sale of tangible assets	1,603	5,375
Recovery of receivables previously written-off	8,906	6,000
Other operating income - NEK d.o.o.	5,094	-
Other	79,240	50,911
	1,290,873	1,577,350

In 2015 the Group generated income from grid connection services in the amount of HRK 352,047 thousand (2013: HRK 349,864 thousand) based on IFRIC 18 (Transfer of Assets From Customer).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

6. STAFF COSTS

	2014	2013
	HRK '000	HRK '000
		Restated
Net salaries	1,038,540	1,052,623
Net salaries in NEK d.o.o.	94,546	85,983
Costs of taxes and contributions on salaries	703,240	687,340
Costs of taxes and contributions on salaries - NEK d.o.o.	44,193	42,772
	1,880,519	1,868,717

TOTAL STAFF COSTS:

	2014	2013
	HRK '000	HRK '000
		Restated
Gross salaries	1,741,780	1,739,962
Gross salaries NEK	138,739	128,755
Allowances for staff costs (Note 7)	112,542	128,388
Material rights of employees (Note 7)	73,244	518,370
	2,066,305	2,515,475

REMUNERATION FOR MEMBERS OF THE BOARD AND EXECUTIVE DIRECTORS IN THE GROUP:

	2014	2013
	HRK '000	HRK '000
		Restated
Gross salaries	24,034	22,230
Costs of taxes and contributions on salaries	5,439	4,976
Other allowances	3,354	2,635
	32,827	29,841

Allowances for staff costs include transport allowances amounting to HRK 72,539 thousand (2013: HRK 76,613 thousand), daily travel allowance and travelling expenses amounting to HRK 18,024 thousand (2013: HRK 17,368 thousand), supplementary health insurance amounting to HRK 6,770 thousand (2013: HRK 13,219 thousand) amounting HRK 15,209 thousand (2013: HRK 21,155 thousand).

Employee benefit costs include benefits under the Collective Agreement which mostly relate to the costs for severance pays on the basis of the termination of employment contracts amounting to HRK 49,974 thousand and a smaller portion for solidarity support, severance pays, jubilee awards, compensations for the detached life, allowance to children, etc.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

7. OTHER OPERATING EXPENSES

	2014	2013
	HRK '000	HRK '000
		Restated
Maintenance costs (service and material)	600,137	550,142
Value provision of trade receivables (Note 20)	221,014	277,866
Gas costs	224,733	361,296
General and administrative expenses	252,775	259,342
Collective services and material	130,910	106,409
Cost of materials	89,895	83,888
Compensation for less taken -over quantities of gas than contracted	2,611	144,859
Purchase of emission units of CO	108,972	98,661
Excises for electric energy and gas	29,546	16,841
Value adjustment of inventories	16,993	48,347
Compensations of staff costs (Note 6)	112,542	128,388
Other material employee benefits (Note 6)	73,244	518,370
NE Krško – decommissioning expenses according to government decision	108,719	107,937
Contributions, taxes and fees to the state	85,221	87,121
Litigation provisions	29,668	196,837
Contributions and concession for water	67,198	71,310
Provision for unused annual leave	17,677	552
Fee for the usage of power plant facilities	87,654	76,043
Compensation for water-purification and drainage	14,893	16,301
Write-off of long-term tangible assets	21,318	32,150
Purchase value of sold materials	25,777	29,870
Calculation and collection costs	34,372	36,973
Provisions for retirement bonuses and jubilee awards	97,666	3,065
Provisions for severance pays on the basis of employment contract cancellation	53,568	133,092
Insurance premiums	22,584	23,943
Environment protection contributions	3,319	4,591
Damages and indemnifications	12,929	19,556
Written-off unused receivables	12,510	13,691
Provision for decommission of thermo-electric power plants	7,920	8,427
Value adjustment for long-term tangible assets	73,518	195,296
Costs of fuel - NEK	134,385	125,996
Costs of services - NEK d.o.o.	147,278	-
Other operating costs - NEK d.o.o.	75,364	-
Other costs	63,670	42,613
	3,060,580	3,819,773

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

8. FINANCIAL INCOME AND EXPENSES

	2014	2013
Financial income	HRK '000	HRK '000
		Restated
Foreign currency exchange gains	22,437	47,608
Interest	13,210	13,817
Fair value swap (Note 27)	393,281	-
Income from dividend	3,000	1,116
Other financial income – NEK d.o.o.	1,743	-
Total financial income	433,671	62,541
Financial expenses		
Interest	(400,378)	(378,883)
Foreign currency losses	(152,571)	(59,685)
Depreciation of deferred interest	(3,833)	(3,804)
Fair value swap	-	(391,808)
Fair value of shares	(202)	(36,136)
Other financial expenses	(5,647)	(7,304)
Financial expenses	(562,631)	(877,620)
Capitalised borrowing costs	6,054	4,333
Total financial expenses	(556,577)	(873,287)
Net losses from financing activities	(122,906)	(810,746)

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

9. INCOME TAX

	2014	2013
	HRK '000	HRK '000
		Restated
Current tax	509,764	296,377
Deferred tax related to generating and removing temporary difference	102,355	(31,719)
Corporate income tax	612,119	264,658

Value adjustment of differed tax is as follows:

	2014	2013
	HRK '000	HRK '000
		Restated
Balance at 1 January	756,647	224,904
Effect of restatement	-	500,763
Reversal of deferred tax assets	(155,853)	(115,401)
Deferred tax assets recognition	53,113	146,381
Balance at 31 December	653,907	756,647

Deferred tax assets have arisen on the tax not recognized provisions for jubilee awards and regular severance pays, value provisions which are not tax recognized and other provisions. The reconciliation between income tax and profit reported in the income statement is set out below:

	2014	2013
	HRK '000	HRK '000
		Restated
Profit before taxation	3,077,543	1,562,862
Income tax at the Republic of Croatia rate of 20%	615,509	312,572
Tax non recognized income	(138,582)	(40,564)
Tax effect of permanent differences	102,355	(31,719)
Tax effect of losses brought forward from previous years	(768)	(17,097)
Unrecognised deferred tax asset on losses carry forward	33,605	41,466
Tax expense for the current year	612,119	264,658

The Group and its subsidiary Companies are subject to income tax separately, according to the tax laws and regulations of the Republic of Croatia. Other subsidiaries in the Group including HEP d.d. reported total tax losses of HRK 1,528,456 thousand (2013: HRK 1,476,528 thousand), while the Group recorded a total income tax expense of HRK 509,764 thousand (2013: HRK 296,377 thousand) and reported deferred tax assets in the amount of HRK 102,355 thousand (2013: HRK 31,719 thousand).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

9. INCOME TAX (continued)

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

Tax losses	Total tax loss for the Group	Year of expiry
2010	152,800	2015
2011	434,935	2016
2012	565,360	2017
2013	207,334	2018
2014	168,027	2019
	1,528,456	

As of 31 December 2014 and 2013 the Group did not recognise deferred tax assets arising from tax losses carried forward at certain subsidiaries because the availability of future taxable profit against which the unused tax losses can be utilized is not certain.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

9. INCOME TAX (continued)

The Croatian Tax Administration has not performed a review of the Company's income tax returns and its subsidiaries, except a shortened monitoring in 2013. In accordance with local regulations, the Tax Administration may at any time inspect the books and records of the Company within 3 years following the year in which the tax liability is reported and may impose additional tax assessments and penalties. Management is not aware of any circumstances that may give rise to a potential material liability in this respect.

The tables below present a summary of changes in deferred tax assets during the year:

HRK '000	Value adjustment of inventory	Provisions for jubilee and retirement benefits	Depreciation at rates above statutory rates	Provisions for the MTM upon bonds	Value adjustment of long-term tangible assets	Other	Total
At 1 January 2013	29,946	115,086	4,112	3	500,048	75,734	724,929
Entered (debited) / in favour of the income statement	8,598	(47,734)	1,275	78,359	715	(9,495)	31,717
At 31 December 2013	38,544	67,352	5,387	78,362	500,763	66,239	756,647
Entered (debited) / in favour of the income statement	3,699	15,062	1,521	(78,362)	(22,882)	(21,778)	(102,740)
At 31 December 2014	42,243	82,414	6,908	-	477,881	44,461	653,907

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

PROPERTY, PLANT AND EQUIPMENT

HRK '000 ACQUISITION VALUE	Land and buildings	Inventory and equipment	Current investments	Total
at 1 January 2013	35,847,411	35,732,868	3,915,002	75,495,281
Restated at 1 January 2013	-	1,048,202	-	1,048,202
Restated - NEK d.o.o.	1,073,567	4,769,370	14,072	5,857,009
Balance at 1 January 2013, restated	36,920,978	41,550,440	3,929,074	82,400,492
Transfers	14,917	(16,194)	-	(1,277)
Additions	15,030	115,911	2,032,485	2,163,426
Provisions for legal disputes	-	-	4,642	4,642
Current investments	539,876	1,314,060	(1,872,068)	(18,132)
Inventory surplus	3,916	4,322	-	8,238
Disposals	(46,501)	(235,843)	(17,248)	(299,592)
At 31 December 2013	37,448,216	42,732,696	4,076,885	84,257,797
Transfers	1,700	(1,694)	-	6
Additions	22,011	123,351	1,893,731	2,039,093
Current investments	521,174	1,277,754	(1,825,274)	(26,346)
Inventory surplus	3,707	3,646	236	7,589
Disposals	(92,338)	(262,510)	(6,165)	(361,013)
Increased assets - NEK d.o.o. NEK	6,522	38,802	49,328	94,652
At 31 December 2014	37,910,992	43,912,045	4,188,741	86,011,776
ACCUMULATED DEPRECIATION				
At 1 January 2013	23,114,175	23,161,991	-	46,276,166
Effect of restatement 1 January 2013	-	128,548	-	82,434
Effect of restatement HEP Proizvodnja d.o.o.	661,047	1,839,078	-	2,500,125
Restated - NEK d.o.o.	789,228	3,656,140	-	4,445,368
At 1 January 2013, restated	24,564,450	28,785,757	-	53,350,207
Depreciation costs	720,421	1,053,833	-	1,774,254
Transfers	5,116	(5,408)	-	(292)
Disposals	(43,716)	(224,588)	-	(268,304)
Inventory surplus	745	2,591	-	3,336
HEP Proizvodnja d.o.o.	(23,462)	27,152	-	3,690
At 1 January 2013, restated	25,223,554	29,639,337	-	54,862,891
Decrease assets HEP Proizvodnja d.o.o.	10,115	63,403	-	73,518
Depreciations costs	680,388	948,798	-	1,629,186
Depreciations costs - NEK	24,328	221,511	-	245,839
Transfers	1,034	(341)	-	693
Removed from books	(84,018)	(243,521)	-	(327,539)
Inventory surplus	-	3,635	-	3,635
At 31 December 2014	25,855,401	30,632,822	-	56,488,223
CARRYING AMOUNT				
At 31 December 2014	12,055,591	13,279,223	4,188,741	29,523,555
At 31 December 2013, restated	12,224,662	13,093,359	4,076,885	29,394,906

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

PROPERTY, PLANT AND EQUIPMENT (continued)

Due to political developments in Croatia since 1990, certain local municipal land registers have not been fully established. The Group is in the process of registering its title to land and buildings through the local courts in Croatia. To this date no disputes have been lodged related to the Group's ownership.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

INTANGIBLE ASSETS

	HRK '000
ACQUISITION VALUE	Intangible assets
Balance at 1 January 2013, restated	614,353
Transfers	1,277
Additions	3,511
Current investments	18,132
Disposals	(10,282)
Balance at 31 December 2013, restated	626,991
Transfers	(6)
Additions	3,442
Current investments	26,346
Disposals	(371)
Balance at 31 December 2014	656,402
ACCUMULATED DEPRECIATION	
Balance at 1 January 2013, restated	540,385
Transfers	273
Depreciation in current year	24,963
Disposals	(8,063)
Balance at 31 December 2013, restated	557,558
Transfers	2
Depreciation in current year	22,165
Disposals	(369)
Balance at 31 December 2014	579,356
CARRYING AMOUNT	
Balance at 31 December 2014	77,046
Balance at 31 December 2013, restated	69,433
Balance at 1 January 2013, restated	73,968

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

PROPERTY INVESTMENT

As of 31 December 2014 investment properties comprise properties held for the purpose of generating earnings from rental and/or capital appreciation, and are carried at fair value based on market price of the Management Board. Fair value comprises the estimated market value at the end of the reporting period. All investment properties are owned by the HEP d.d.

At fair value	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Fair value adjustment	231,285	233,917	234,760
Depreciation costs	(269)	(366)	(366)
Net change in value on the basis of fair value adjustment	3,378	(6,192)	(331)
Other changes	157	3,926	(146)
Closing balance at fair value	234,551	231,285	233,917
Property investment - NEK d.o.o.	1,602	1,772	-
Closing balance	236,153	233,057	233,917

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

PREPAYMENT FOR TANGIBLE ASSETS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
JSC Tehnopromexport – TE Sisak	17,727	25,182	49,659
Končar GIM	5,550	10,311	15,528
Litostroj Slovenia	284	2,174	2,444
VOITH Siemens Austria	689	1,887	2,288
Končar inženjering Zagreb	1,002	2,732	-
Spegra Inženjering	-	2,836	-
Đuro Đaković holding	1,844	4,361	-
Končar Inženjering d.d. - TE Sisak	-	-	622
Siemens	1,130	1,999	-
Other	13,260	6,284	1,777
	41,486	57,766	72,318

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

14. INVESTMENT IN NE KRŠKO

BACKGROUND

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

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

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

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

The agreement also clearly defined the liabilities for the RH to care for half the radioactive and consumed nuclear fuel from NE Krško. Each country is obliged to secure half the necessary resources to finance the costs of preparing a programme of decommissioning and costs to implement the programme. Each side shall set aside the said funds for that purpose in a specific fund to the amount specified in the decommissioning programme. Pursuant to the valid Programme for the decommissioning of NE Krško and disposal of radioactive waste and consumed nuclear fuel, HEP d.d. is obliged to make deposits to the Fund to the amount of ERU 14,250 thousand.

HEP d.d. started to receive electricity from NPPK on 19 April 2003, and expects to receive 2,700-2,950 GWh annually up to 2023, representing 15% of electricity consumption in Croatia.

By the end of 2003, the provisions of the Agreement were implemented according to which HEP d.d. and NPPK waive mutual receivables for damages and withdraw all claims arising there from up to 30 June 2002, including the disputed liabilities for electricity purchase and amounts due with respect to the previously calculated contribution for financing the decommissioning of the power plant and funds to cover the losses from previous years. After implementing the changes, the capital of NPPK as at 31 December 2003 amounted to SIT 84.7 billion (approximately: HRK 2.8 billion). Still there are some outstanding off-balance receivables from HEP d.d. to NPPK and Slovenia from the past, which do not have any influence on the current business relations but are related to compensating for damages that the Company is seeking from the Republic of Slovenia for undelivered electricity from NE Krško for the period 1.7.2002-18.4.2003. The matter was referred to international arbitration in 2005 before the International Centre for the Resolution of Investment Disputes in Washington.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

14. INVESTMENT IN NE KRŠKO (continued)

CURRENT STATUS

Payment to the Fund for the Decommissioning of NE Krško

According to the above stated Agreement, the decommissioning of NPPK will be a joint obligation of both parties. Each party will provide half of the funds necessary to prepare the decommissioning plan and to cover the cost of implementation of the plan adopted by the Croatian government on 24.12.2008. As of 2006 and until the end of 2014 Hrvatska elektroprivreda paid the amount of HRK 1,159,652 thousand to the Fund to finance the decommissioning of NE Krško. The amount of the payment is defined by the 2004 Decommissioning Programme. The current annual liabilities of EUR 14,250 thousand to the Fund are paid in quarterly.

EXTENSION OF USEFUL LIFE

After NE Krško obtained a licence in 2012 from the Republic of Slovenia related to the nuclear safety without any limitations, at the end of 2014 HEP and GEN Energija adopted a decision to extend the life of the plant until 2043. The decision to extend the operating life of NE Krško for 20 years was preceded with an investment feasibility study of long-term investments in the power plant.

ACCOUNTING MONITORING OF JOINT INVESTMENTS IN NE KRŠKO

Investments in NEK until 2014 were calculated according to the method of shares.

Pursuant to International Financial Reporting Standard (IFRS) 11 – Joint Arrangements, which replaced International Accounting Standard (IAS) 31 – Interest in Joint Ventures, the joint operations of NE Krško d.o.o. are classified as jointly controlled.

The Company recognises its share in each asset and in each liability, in income and expenses in accordance with its share in the joint management.

The transfer from accounts monitoring of investments in NEK d.o.o. from the method of shares in accounts of assets and liabilities pursuant to share, in the financial statements for 2014 the Company has entered the following changes: impairment of investments calculated according to the method of shares, recognised its share in each asset and in each liability and income and expenses of NEK d.o.o., stated the difference between the value of shares that the Company ceased to recognise and recognised assets and liabilities debited to the retained profit from the preceding period (as at 31.12.2013: HRK 75,080 thousand).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

14. INVESTMENT IN NE KRŠKO (continued)

EXCERPT FROM THE FINANCIAL STATEMENTS

The table below shows an excerpt of the financial statements for NE Krško d.o.o. in 100% amounts as at 31 December 2014 and 2013:

	31 December 2014	31 December 2013
	HRK '000	HRK '000
Property, plant and equipment	2,495,642	2,823,284
Capital and reserves	3,382,788	3,358,677
Gross income from sales	1,494,330	1,468,111
Cash flow from operating activities	401,719	560,324
Profit in current year	19,842	2,080

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014**

15. INVESTMENT IN TE PLOMIN

In November 1996, HEP d.d. entered into a Joint Venture Agreement with RWE Energie Aktiengesellschaft, Germany ('RWE') regarding the completion and operation of TPP Plomin II. Consequently, a joint venture, TE Plomin d.o.o. ('Plomin') was formed in December 1996. Partners to this joint investment hold a 50% share in the capital of the new company. A number of agreements were entered into, which regulate the mutual relations and relations with the new Groups.

Pursuant to the 1996 Agreement of shares in assets, HEP d.d. invested property, plant and equipment previously obtained for the project valued at DEM 50,000 thousand (HRK 179,138 thousand) as its share in TE Plomin d.o.o. An amount of HRK 50 thousand was allocated as share capital and HRK 179,088 thousand and the remainder for reserves.

Pursuant to the agreement of joint venture, RWE invested the same amount of money during the construction period. The initial cash contribution of HRK 50 thousand was allocated to share capital and the remainder to reserves. The capital RWE invested was to be returned 15 years after the start of operations, or 30 April 2000. The Agreement between HEP and RWE ceases to be valid pursuant to its provisions as HEP has decided to exploit its right which entails that 15 years after the power plant is put into operation it takes over RWE's share that it has in TE Plomin d.o.o.

An agreement of the transfer of business shares is expected to be concluded between 30.4. and 31.5.2015.

In 2014 the return of invested capital was not paid to RWE as agreed and in 2013 the return on capital amounted to HRK 12,948 thousand. As at 31 December 2014 a further HRK 26,060 thousand remained unpaid (2013: HRK 25,979 thousand).

Payment is expected on 30.4.2015.

Pursuant to Plomin's Articles of Association, RWE has the right to an annual dividend for the duration of the joint arrangement at an annual rate of 14% to 17% depending on the number of hours of peak exploitation of the availability of the power plant during the year. RWE invested capital is included in unpaid capital as is that share of unpaid cumulative interest during the construction phase.

During the period of construction, the accrued cumulative interest on the RWE capital amounted to HRK 54,717 thousand (EUR 7,536 thousand) and is payable on a straight-line basis during the period of exploitation. As at 31 December 2014 accrued undistributed interest amounted to HRK 5,116 thousand (2012.: HRK 8,846 thousand).

RWE has the right to an annual refund of capital invested (through preferential dividend) from Plomin's net profit. In 2014 that dividend amounted to 17% as it did in 2013. In 2014 the dividend for 2013 was not paid pursuant to a decision by the Company but is stated in the figure of short-term liabilities and amounts to HRK 5,948 thousand (Note 32). The dividend for 2012 was not paid out in 2013 pursuant to a decision by Company but is stated in the short-term liabilities and amounts to HRK 8,707 thousand. Payment is expected on 30.4.2015.

The said dividend has priority in relation to HEP d.d.'s share, considering that HEP d.d.'s share will be used to pay interest to RWE for 2000 and HEP d.d. did not realise its share of profit in Plomin.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

15. INVESTMENT IN TE PLOMIN (continued)

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

EXCERPT FROM THE FINANCIAL STATEMENTS

In the consolidated financial statements the Group has presented its share in TE Plomin on the method of complete consolidation:

	31 December 2014	31 December 2013
	HRK '000	HRK '000
Property, plant and equipment	187,183	286,116
Capital and inventories	195,310	211,115
Gross income from sales	747,784	782,951
Income from regular operations	30,323	13,102
Net income	3,092	5,948
Cash flow from business operations	24,197	20,677

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
Opening balance of non-controlling share	31,977	47,283	62,847
Capital payment	-	(12,948)	(12,922)
Liabilities for dividend / Dividend pay out	(5,948)	(8,707)	(11,514)
Increase for the current year profit	3,092	5,948	8,707
Exchange difference	81	401	165
Closing balance	29,202	31,977	47,283

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

16. LONG-TERM LOANS AND DEPOSITS OFFERED

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Receivables from loans	4,743	6,379	808
Value adjustment	(74)	(83)	(158)
Current dues on long-term loans	(136)	(136)	(136)
Long-term portion	4,533	6,160	514

Loans to unrelated parties are states as follows:

	Date loan approved	Repayment	Loan amount	31 December 2014	31 December 2013	1 January 2013
				HRK '000	HRK '000	HRK '000
					Restated	Restated
City of Dubrovnik	2013.	5 years	5,707	4,207	5,707	-
City of Pregrada	2006.	10 years	1,358	407	543	679
Did d.o.o.	2007.	4 years	1,010	129	129	129
Total				4,743	6,379	808
Value adjustment				(74)	(83)	(158)
Current dues				(136)	(136)	(136)
Long-term portion				4,533	6,160	514

17. INVESTMENTS AVAILABLE FOR SALE AND other investments

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Investments available for sale	191,611	124,101	128,288
Other investments	1,065	1,065	1,065
	192,676	125,166	129,353

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

17. INVESTMENT AVAILABLE FOR SALE AND other investments (continued)

Changes to investments available for sale are stated as follows:

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Balance at start of the year	124,101	128,288	120,605
Fair value of shares in Jadranski Naftovod d.d. & Viktor Lenac through income statement	65,230	(4,286)	7,470
Fair value of investments through income statement	(73)	-	-
Investments in shares	2,353	99	213
	191,611	124,101	128,288
	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Investments available for sale:			
Jadranski Naftovod d.d.	188,878	123,616	127,935
Viktor Lenac d.d.	128	166	133
Đuro Đaković d.d.	5	5	5
Kraš d.d.	2	2	2
Pevec d.d.	312	312	213
Jadran d.d.	365	-	-
Industrogradnja grupa d.d.	490	-	-
Optima Telekom d.d.,	1,099	-	-
Institut IGH d.d.,	178	-	-
Međimurje beton d.d.	104	-	-
HTP Korčula d.d.	50	-	-
	191,611	124,101	128,288
Other investments			
Geopodravina d.o.o.	200	200	200
LNG Hrvatska d.o.o.	865	865	865
	1,065	1,065	1,065
	192,676	125,166	129,363

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014**17. INVESTMENTS 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. According to the Management Decision, the Jadranski Naftovod shares were designated as available for sale. The shares were subscribed at the Central Depository Agency on 19 March 2009. In 2014 and 2013 fair value was determined by notification of the Central Clearing Deposit Agency as of 31 December. The market value of shares in JANAF as at 31 December 2014 amounted to HRK 3,499 and in 2013: HRK 2,290. The fair value adjustment of investments in JANAF as at 31 December 2014 increased the value of investments by HRK 65,262 thousand (2013: increased by HRK 4,318 thousand). The fair value adjustment in 2014 and 2013 was conducted through inventories. Inventories were reduced by the 20% increase in the value of investments and increased deferred tax liabilities.

On 1 June 2010 HEP d.d. and Plinacro d.o.o. concluded the Articles of Incorporation of LNG Hrvatska d.o.o., a liquefied natural gas company. In 2011 it increased the share capital from HRK 20 thousand to HRK 220 thousand, and in 2012 to HRK 1,730 thousand so HEP is the owner of a portion or an amount of 50%, and the Plinacro d.o.o. is the owner of the other part of the portion. The Company was additionally capitalized by Plinacro d.o.o. with an amount of HRK 22,600 thousand as is recorded at the Commercial Court, dated 4 February 2013. The share capital of LNG Hrvatska d.o.o. amounts to HRK 24,330 thousand. Pursuant to a pre-bankruptcy settlement with creditors for electricity, heating energy and gas sold and exchanged receivables for shares in companies facing difficulties in operations, the Group took over shares in 7 companies with a total value of HRK 2,145 thousand.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

18. OTHER LONG-TERM ASSETS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Housing loan receivables	25,572	29,672	33,649
Energy efficiency receivables – long-term portion	10,992	19,003	24,616
Accrued cumulative interest – RWE	1,283	5,116	8,846
Other long-term assets	11,957	5,021	207
	49,804	58,812	67,318

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

Pursuant to the provisions of association interest is calculated on the entire capital invested by RWE Power during the construction phase of the power station at a rate of 17% (intercalary interest). Intercalary interest is calculated on the total amount of EUR 7,536 thousand or the equivalent to HRK 55,653 thousand and has been entirely recognised as deferred expense subject to straight-line depreciation over a period of 15 years.

Repayment of interest is done along with the repayment of invested funds from RWE Power and it started after the electric power plant was finished. In 2014 the total amount repaid was EUR 502 thousand equivalent to HRK 3,817 thousand (2012: EUR 502 thousand, equivalent to HRK 3,809 thousand). Complete payment of interest is due to be made on 30.4.2015.

As at 31 December 2014 deferred expenses for the interest amounted EUR 168 thousand or the equivalent of HRK 1,283 thousand (2013: EUR 670 thousand or HRK 5,116 thousand). Currency exchange differences are included in the financial income or expense for the year in they arise.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

19. INVENTORIES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Inventories of fuel and chemicals	292,215	425,168	526,542
Electrical material	298,635	276,886	217,167
Spare parts	191,943	176,671	221,934
Building material	38,193	94,694	87,378
Inventories of gas for wholesale	432,559	-	-
CO2 emission units	219,270	67,613	-
Other inventories	64,812	47,777	66,206
Inventories of nuclear fuel and other material - NEK d.o.o.	281,135	251,168	268,396
	1,818,762	1,339,977	1,387,623
Impairment of obsolete materials and spare parts	(205,465)	(185,573)	(137,586)
	1,613,297	1,154,404	1,250,037

In 2013 the assessment of inventories was changed in a way that provisions were set aside for material stocks according to the age structure as follows: material stocks of 2 to 3 years – 30% of value; material stocks 3 to 4 years – 60% of value and material stocks of more than 4 years -100% of value. This excludes criteria of the effect of turnover of unmarketable stocks.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

20. TRADE RECEIVABLES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Electricity – corporate customers	1,410,548	1,563,413	1,606,227
Electricity – households	445,353	478,131	478,424
Electricity – foreign sales	33,699	26,026	53,207
Heating, gas and services	846,967	531,501	502,643
Connection to transmission network	2	57,022	41,233
Trade receivables - NEK d.o.o.	42,501	19,947	-
	59,791	41,526	83,190
	2,838,859	2,717,566	2,764,924
Impairment of bad and doubtful receivables	(974,179)	(917,490)	(891,679)
	1,864,680	1,800,076	1,873,245

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

20. TRADE RECEIVABLES (continued)

Age structures of traded receivables not impaired are stated as follows:

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Undue	1,194,793	1,025,984	1,015,832
Up to 30 days	363,326	427,207	437,422
31-60 days	122,393	150,482	161,682
61-90 days	59,883	64,919	75,704
91-180 days	59,278	87,281	89,315
181-365 days	55,330	32,657	71,078
More than 365 days	9,677	11,546	22,212
	1,864,680	1,800,076	1,873,245

Impairment adjustments for reduced value are stated as follows:

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Balance at 1 January	917,490	891,679	781,600
Value adjustment trade receivables (Note 7)	221,014	277,866	250,972
Removals from accounts of previously written-off receivables	(64,776)	(161,991)	(21,338)
Amounts collected with the provision made (Note 5)	(99,549)	(90,064)	(119,555)
At 31 December	974,179	917,490	891,679

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

21. OTHER SHORT-TERM RECEIVABLES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Receivables from VAT	-	64,421	142,908
Prepayment for working capital	3,544	638	706
Receivables from the state for employees	4,387	35,634	15,366
Receivables from interest	340	3,123	2,995
Demand and term deposits over 3 months	209,950	90,075	21,220
Demand and term deposits over 3 months - NEK	216,160	191,514	63,831
Receivables upon short-term loan from non-related companies	10,500	90,000	-
Receivables from MF for overpaid VAT upon import	-	39,853	-
Accounted income from sale of electric energy to households	-	58,207	-
Other receivables - NEK	2,005	2,032	10,551
Other short-term receivables	72,796	78,672	60,419
	519,682	654,169	317,996

The Company in August 2013 concluded a contract for a short-term loan with legal entities with public authorities for an amount of HRK 90,000 thousand for a period of one year with an interest rate at the level of the discount rate of the HNB and repayment was made in 2014.

In November 2014 the Company concluded a contract for a short-term loan with the company in the RH amounting to HRK 10,500 thousand for a period of 180 days with an interest rate at the level of the discount rate of the HNB and the repayment was executed in 2015.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

22. CASH AND CASH EQUIVALENTS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Kuna currency account	448,172	150,543	156,084
Foreign currency accounts	193,425	39,227	118,482
Reserved cash	21,473	9,222	7,403
Kuna cashier	231	281	280
Deposits with a maturity of 90 days	30,012	4,685	159,225
Short-term term deposits (daily)	386,551	56,797	163,550
Transactions in foreign currency - NEK	36	89	-
	1,079,900	260,844	605,024

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

23. CAPITAL AND RESERVES

When the Company was first registered on 12 December 1994, the Company's share capital was registered in German marks (DEM) to the amount of 5,784,832 thousand DEM. The following registration on 19 July 1995 the share capital was stated in Croatian Kuna and amounted to HRK 19,792,159 thousand. Shareholder capital consists of 10,995,644 regular shares with a nominal value of HRK 1,800.

RESERVES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Starting balance of reserves	2,617	6,046	(438,957)
Transferred from retained profit	-	-	438,957
Other comprehensive income / (losses) - JANAF	52,330	(3,429)	6,046
Capital reserves	54,947	2,617	6,046

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Starting balance	18,809	(1,207,682)	516,807
Restatement	-	-	(1,326,597)
Increase/decrease retained profit - NEK	2,135	(75,081)	-
Other increases	2,907	3,368	13,964
Transfer to capital reserves	-	-	(438,957)
Payment of profit to owner	(284,918)	-	-
Profit / (Loss) in current year	2,462,332	1,298,204	27,101
	2,201,265	18,809	(1,207,682)

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

24. LIABILITIES FROM LONG-TERM LOANS

	Interest rate	31 December 2014	31 December 2013	1 January 2013
		HRK '000	HRK '000	HRK '000
			Restated	Restated
Loans with domestic banks	EURIBOR+ (1.00%- 5.35%)	1,640,285	1,853,007	1,961,548
Loans with foreign banks	Fixed 2.71%	23,183	23,588	25,585
Financial leasing	Fixed 5.6%	22,362	25,898	-
Loan - RWE		-	1,279	5,055
Loan - NEK		-	35,592	-
Total		1,685,830	1,939,364	1,992,188
Davison of charges for loans		(4,611)	(5,841)	(20,474)
Total long-term liabilities for loans		1,681,219	1,933,523	1,971,714
Current dues		(416,349)	(208,838)	(132,084)
Current dues on financial leases (Note 32)		(2,834)	(2,675)	
Long-term portion		1,262,036	1,722,010	1,839,630

Loans of domestic banks are assured by bills of exchange and debentures. As at 31.12.2014 the Group no longer has any loans guaranteed by the RH.

NEW SOURCES OF FINANCING

For the financing of the investment plan and the regular operations in 2014 the Group used its own sources as well as the loan assets in use.

CURRENT LOANS IN USE

In 2014 the long-term loan approved by KfW Entwicklungsbank amounting to 50 million EUR continued to be used to finance energy efficiency and renewable energy projects. The balance of the loan with od KfW Bank as at 31 December 2014 amounted to 3.1 million EUR, or the unused portion of the loan amounting to 46.9 million EUR.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

24. LIABILITIES FOR LONG-TERM LOANS (continued)

The repayment schedule of the principal on long-term loans due in the next five years:

2015	419,183
2016	389,900
2017	389,784
2018	383,017
2019	85,490
After 2019	13,845
	1,681,219

The terms of some loans include restrictive financial and business conditions according to which the Group needs to satisfy the prescribed level of the following indicators: net value of assets (own capital), debt coverage and net total liabilities for loans.

As at 31 December 2014 the Group satisfied the contracted financial indicators.

Below is an overview of long-term loans states in foreign currency (in thousands):

Currency	31 December 2014	31 December 2013	1 January 2013
EUR	219,596	245,703	263,349

25. LONG-TERM LIABILITIES TOWARD THE STATE

Long-term liabilities toward the state amounting to HRK 21,690 thousand in 2014 (2013: HRK 24,451 thousand) relate to the sale of apartments to employees in accordance with the state programme that was abolished in 1996. According to the law regulating housing sales, 65% of the proceeds from the sale of apartments to employees were payable to the state at such time as the proceeds were collected. According to the law, HEP d.d. has no liability to remit the funds, unless and until they are collected from the employee.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

26. LONG-TERM PROVISIONS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Provisions for legal disputes	363,052	375,870	204,292
Provisions for retirement bonuses	319,691	231,911	285,739
Provisions for jubilee awards	44,806	39,616	45,408
Provisions for decommissioning thermal power plant	120,689	112,769	104,341
Provisions for downloaded electricity from wind power plants	21,631	21,631	21,631
Provisions for retirement bonuses and jubilee awards & other benefits - NEK	32,910	26,585	-
	902,779	808,382	661,411

The thermal power plant decommissioning provision amounting to HRK 120,689 thousand represents a discounted value of the estimated decommissioning costs of the Group's thermal power plants. Movements in the present value of defined benefit obligations in the current period were as follows:

	Provisions for legal disputes	Provisions for severance packages	Provisions for jubilee awards	Provisions for decommissioning thermal power plants	Other	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January 2014	375,870	231,911	39,616	112,769	48,216	808,382
Transferred	-	-	-	-	-	-
New provisions	29,667	93,820	5,924	7,920	6,325	143,656
Decrease in provisions (amounts paid)	(26,258)	(1,652)	(721)	-	-	(28,631)
Decrease in provisions according to valuation	(16,227)	(4,388)	(13)	-	-	(20,628)
As at 31 December 2014	363,052	319,691	44,806	120,689	54,541	902,779

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

26. LONG-TERM PROVISIONS (continued)

LEGAL DISPUTES

The Company makes provisions for legal disputes where it is assessed the unlikely outcome in favour of HEP d.d. The total amount of provisions at 31 December 2014 amounted to HRK 363,052 thousand (2013: HRK 375,870 thousand).

The most significant of these is a dispute in which HEP Proizvodnja d.o.o. and HEP d.d. HEP Proizvodnja d.o.o. as the plaintiff have instituted a complaint against Zagrebački Holding d.o.o. for which provisions have been provided in 2014 to the amount of HRK 76,130 thousand and related to compensation for water purification plants.

The most important provision relates to the court case related to HEP Peruća which was started in 1995, for which a first instance ruling in 2012 went in favour of the plaintiff. In regard to the complexity of the valuation and the estimation of proofs on behalf of the court, as well as the high value of the procedure amounting to HRK 330,000 thousand and of the possibility of a partial success in favour of the plaintiff, assets are provided for at a level of 50% of the value of the dispute amounting to HRK 165,000 thousand. Other significant disputes relate to Kartner sparkass amounting to HRK 9,903 thousand, the City of Dubrovnik amounting to HRK 4,345 thousand, the Konavle Municipality amounting to HRK 3,760 thousand and Dubrovnik-Neretva County amounting to HRK 1,966 thousand.

THE WATER MANAGEMENT ACT

According to an interpretation by the State Prosecution, the Law on Waters that came into force on 4.1.1996 and the new Law on Waters that came into force on 1.1.2010, bring into question the property-legal status of the asset for electricity production from the hydro-electricity plant because the land on which the hydro-electric plant was constructed on is classified as 'Public Water Resources' which by its legal nature is considered to be real estate for common use owned by the RH 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 RH relating the right of registering ownership of hydroelectric power plants in favour of RH. There is no common legal practise regarding this issue.

The Company has disputed the interpretation of the Law on Waters seeing that this refers to real estate that was entered in the Company's balance sheet during the process of transition 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.

The Company filed a recommendation to the Constitutional Court to institute proceedings to check the compliance of Article 23, Par. 4 of the Law on Waters with the Constitution and upon conclusion of the procedure to annul the said provision.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

26. LONG-TERM PROVISIONS (continued)

PROVISIONS FOR SEVERANCE PACKAGES AND JUBILEE AWARDS

Changes to the current identified liabilities pursuant to employee benefits in the current period are states as follows:

	Severance packages	Jubilee awards	Total
	HRK '000	HRK '000	HRK '000
As at 1 January 2014	231,911	39,616	271,527
Current service costs	11,364	2,248	13,612
Interest costs	11,857	1,635	13,492
Benefits paid	(14,525)	(7,068)	(21,593)
Past service costs	1,347	227	1,574
Actuary costs (losses)	77,737	8,148	85,885
As at 31 December 2014	319,691	44,806	364,497

The following assumptions were used to prepare the calculation:

- The termination rate is 6.08 % and is based on statistical fluctuation rates for the Group in the period from 2006 to 2014.;
- The mortality rate by age and gender is based on Croatian Mortality Tables 2000-2002 published by the Croatian Bureau of Statistics. It is assumed that the population of employees of the Group represents the average with respect to mortality and health status;
- We assumed the annual salary will not increase.
- The present value of the obligation was determined using a discount rate of 4% per annum for all members of the Group.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

27. LIABILITIES FOR ISSUED BONDS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Nominal value of bonds in the country	279,790	373,170	966,550
Discounted value	(170)	(286)	(814)
Current maturity on bonds	(93,380)	(93,380)	(593,380)
	186,240	279,504	372,356
Nominal value of bonds abroad	2,999,389	2,963,252	2,955,595
Currency exchange differences	9,357	36,137	7,657
	3,008,746	2,999,389	2,963,252
Total liabilities for issued bonds	3,194,986	3,278,893	3,335,608

BONDS ISSUED IN THE COUNTRY

Bonds issued in 2006 amounting to HRK 500,000 thousand with a maturity in November 2013 were entirely paid out. Bonds amounting to HRK 700,000 thousand issued at the end of 2007 are being repaid in 15 six-monthly instalments, with a grace period of three years after the issue date and bear a fixed interest rate of 6.50%. The bonds were listed on the Zagreb Stock Exchange.

BONDS ISSUED ABROAD

In November 2012 the Company issued bonds amounting to USD 500,000 thousand on the international capital market. The bonds carry a maturity of 5 years and are entirely due in November 2017 and bear a fixed interest rate of 6.00%. HEP d.d. bonds are listed on the Luxembourg Stock Exchange market and are regularly traded.

For the purpose of securing currency risks an agreement was concluded of value exchange (swap).

27. LIABILITIES FOR ISSUED BONDS (continued)

CURRENCY SWAP

For the purpose of protection against currency exchange risk, i.e. changes in the value of the dollar, the Company concluded an agreement of currency swap by which the dollar liability for bonds issued abroad and denominated into euro for the entire time of the duration of the bonds, i.e. until their maturity on 9 November 2017.

According to the agreement the six-monthly interest rate paid by the company is fixed at 6.53%, while the interest rate that the Company seeks from the contracting party based on the swap is equal to the fixed rate at which the bonds were issued and amounts to 6.00%.

The Company connects the fair value of the currency swap to the calculation of the Mark-to-Market "MTM" value and at 31.12.2014 it amounted to HRK 1,473 thousand, liabilities amounting to HRK 391,808 thousand were removed and the amount of HRK 393,281 thousand is recorded as a financial expense. (Note 8.).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

28. OTHER LONG-TERM LIABILITIES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Deferred income for property financed by third parties	3,738,553	3,975,988	4,220,301
Long term liabilities for assets financed by clearing debt	759,089	668,377	689,792
Long-term debt under interest rate swap (Note 27)	-	391,808	-
Other	1,860	2,353	1,540
	4,499,502	5,038,526	4,911,633

Deferred revenue is related to fixed assets contributed by customers and others without charge. The revenue is recognized into income over the same periods as the related assets are depreciated, which applies to contracts for connection to the network concluded by 30 June 2009. After 1 July 2009 the connection fee is recognized as income in the amount of funds received from the customer in the period when the customer is connected to the grid or when permanent access to the delivery of the service is given.

At 31 December 2013 the Group reported a liability in the amount of HRK 759,089 thousand in respect of a clearing debt (2013: HRK 668,377 thousand) regarding a payment under a letter of credit on the basis of the Consent of the Ministry of finance with the use of the funds pursuant to an interbank agreement. As there is no other document that would regulate the relationship between the Company and the Ministry of finance regarding the clearing debt, it has not been clearly defined as either a loan or a government subsidy.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

29. LIABILITIES FOR SHORT-TERM BORROWINGS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Borrowings with domestic banks and subsidiaries of foreign banks, denominated in various currencies under the following terms:	-	295,000	400,000
Interest rate per EURIBOR/TZ Min. Fin. + margin (2.75%-3.20%)	-	-	-
secured by bills of exchange	-		
Other short-term borrowings	-	369,664	3,261
Short-term portion of loan - RWE	8,981	7,674	7,582
Short-term loan	-	20,316	-
	8,981	692,654	410,843

By July 2014 the Group had repaid all the existing short-term loans. However, for the purpose of providing for solvency reserves in the following medium-term period, during the year the Company concluded multi-purpose general contracts with domestic banks with a total amount of HRK 1.0 billion.

The Company can use the funds from the said framework for short-term loans, to issue guarantees, assets, and letters of intent in accordance with the Group's needs.

From the above mentioned medium-term multi-purpose framework in 2014, the Group did not have any need to conclude any short-term loans due to good liquidity.

At the end of June 2014, the Group settled all liabilities to suppliers through reverse (supplier) factoring. After the said return the Group possesses the entire amount from the framework agreement on reverse (supplier) factoring available until 31 December 2015.

As at 31.12.2014, the Group had HRK 1,328 million at its disposal for short-term sources of financing.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

30. LIABILITIES TAXES AND CONTRIBUTIONS

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Liabilities for VAT	120,567	-	-
Liabilities for income tax	180,250	130,129	302,222
Utilities and other fees	30,731	13,641	17,519
Contributions on salaries	22,570	18,650	20,111
Other	6,977	3,250	7,965
	361,095	165,670	347,817

31. LIABILITIES TOWARD EMPLOYEES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Liabilities for net salaries	79,123	71,589	75,220
Liabilities for contributions	39,397	37,749	39,179
Liabilities for net salaries - NEK d.o.o.	10,620	10,772	-
Other	22,100	25,830	26,169
	151,240	145,940	140,568

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

32. LIABILITIES TOWARD SUPPLIERS AND OTHER SHORT-TERM LIABILITIES

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
LIABILITIES TOWARD SUPPLIERS			
Liabilities toward suppliers in the country	1,401,253	1,126,964	2,246,352
Liabilities toward suppliers abroad	68,243	187,926	246,377
Liabilities toward suppliers in the EU	105,355	171,075	-
Liabilities toward suppliers - NEK d.o.o.	15,894	94,475	-
	1,590,745	1,580,440	2,492,729

	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
OTHER SHORT-TERM LIABILITIES			
Deferred income and received advances for connections	330,859	287,181	216,610
Liabilities for other advances received	121,033	116,797	98,344
Accrued expenses for unused vacation days	71,436	53,828	64,827
Deferred income from sale of el. energy to households	40,467	-	19,426
Liabilities for renewable sources	45,128	47,541	11,477
Accounted costs of severance pays to employees	231,123	177,555	249,174
Interest	122,926	44	755
Costs of CO2 emission units	111,806	98,508	-
Liabilities to HAC	77,775	77,775	77,775
Other costs	1,703	5,126	28,324
Liabilities for non-controlling part (Note 15)	14,807	8,707	-
Current portion of financial lease (Note 24)	2,834	2,675	-
Liabilities - NEK d.o.o.	39,999	10,602	-
Other liabilities	12,630	38,569	54,054
	1,224,526	924,908	820,766

Correction of income from households as at 31 December 2013 was obtained by the count of logarithmic curve using the losses in the network of 8.68% in the amount of HRK 58,207 thousand while for the year ended 31 December 2012 the percent of loss was 8.85%. The result is the increase of revenue in the amount of HRK 77,632 thousand in respect to the previous year: cancellation of liability for accounted income in the amount of HRK 19,425 thousand was made and recorded in the receivables to the amount of HRK 58,207 thousand (Note 21).

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

33. RELATED PARTY TRANSACTIONS

The Group has a 50% ownership in the capital of NPPK (NE Krško d.o.o.). Electricity produced at NE Krško is delivered to HEP d.d. at 50% of the total quantities produced at a price which is determined in accordance with the total production costs of NE Krško.

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

	31 December 2014	31 December 2013
	HRK '000	HRK '000
NE Krško d.o.o.		
Liabilities for purchased electricity	62,830	63,373
Cost of purchased electricity	747,165	727,855

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

33. RELATED PARTY TRANSACTIONS (continued)

HRK '000	Income from sales		Costs of supply	
	2014	2013	2014	2013
Enterprises controlled partially by the state				
Croatian Railways	104,993	137,709	3,297	67,997
INA-Oil Industry (Parent)	131,359	156,430	983,943	54,506
Natural Gas	0	0	457,863	2,002,330
Plinacro	2,274	2,298	73,949	64,278
Croatia Osiguranje – Insurance Co	5,136	5,618	14,223	17,543
Croatia Post	20,226	23,210	22,493	44,539
Croatian Forests	3,260	5,529	5,464	2,261
Jadrolinija	650	870	658	4,031
Official Gazette	2,385	1,618	3,932	4,438
Croatian Radio Television	13,127	13,735	1,158	1,194
Plovput	446	578	349	165
Croatia Airlines	768	981	6	66
Petrokemija Kutina	18,537	3,488	61	82
Ministry of Foreign and European Affairs	455	513	-	-
Defence Ministry	22,182	24,358	-	-
Interior Ministry	13,074	26,510	-	-
Primary and secondary schools	78,055	88,078	-	-
Judicial institutions	8,188	13,758	74	173
Universities and Institutes of Technology	27,792	33,610	1,172	3,715
Legislative, executive and other government bodies	26,129	29,040	5,426	6,345
Health institutions and organisations	112,742	122,821	1,168	3,194
Other users	11,342	16,619	5,124	6,577
TOTAL	603,120	707,371	1,580,360	2,283,434

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

33. RELATED PARTY TRANSACTIONS (continued)

HRK '000	Amount of receivables		Amount of liabilities	
	31 December 2014	31 December 2013	31 December 2014	31 December 2013
Majority state owned companies				
Croatian Railways	31,811	79,781	541	39,792
INA-Oil Industry (Parent)	14,544	18,298	163,640	11,075
Natural Gas	-	-	-	153,148
Plinacro	125	400	11,446	8,670
Croatia Osiguranje – Insurance Co	705	611	2,779	5,119
Croatia Post	1,282	3,211	2,725	8,786
Croatian Forests	474	530	4	49
Jadrolinija	49	57	581	1,274
Official Gazette	289	163	838	1,226
Croatian Radio Television	2,653	2,399	39	147
Plovput	24	74	165	51
Croatia Airlines	95	217	-	-
Petrokemija Kutina	3,675	9,488	13	-
Defence Ministry	4,311	4,090	-	-
Interior Ministry	2,069	6,592	-	-
Primary and secondary schools	16,526	20,491	-	-
Judicial institutions	1,838	4,532	-	-
Universities and Institutes of Technology	4,161	4,619	-	-
Legislative, executive and other government bodies	5,131	5,572	-	-
Health institutions and organisations	20,202	27,855	-	-
Other users	21,623	4,191	10,317	3,513
TOTAL	131,587	193,171	193,088	232,850

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

34. UNCERTAIN EVENTS AND COMMITTED LIABILITIES

LEGAL DISPUTES

In 2014 the Group recorded provisions for legal 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 valued at costs in 1994 to the amount of HRK 1,243,970 thousand. During the Company's transition in 1994 into a shareholding company, this amount was not included in the net value of assets.

OPERATING LIABILITIES

As part of its regular investment activities, at 31 December 2014 the Group had contract for investments that were started by not competed for various buildings and equipment. In 2014 the value of contracted unfinished works for the most significant projects amounted to around HRK 1,411,115 thousand (2013: HRK 1,300,391 thousand).

ENVIRONMENT PROTECTION

HEP continually monitors and analyses the impact of its business operations on the environment. The most important indicators of this are the monitoring of air-borne pollutant emissions and waste that occurs and HEP ensures the timely and objective reporting to the relevant institutions, local government units and the public. Employees involved in environment and nature protection receive additional training through seminars and workshops where they are informed of the obligations and activities resulting from legal environmental regulations in the areas of environment and nature protection.

The Company's Accounting Monitoring of Costs and Investments in Environmental Protection system (RETZOK) introduced in 2004 facilitates monitoring requirements for environment and nature protection. A request has been submitted to the Ministry of Environment and Nature Protection to unify environment protection conditions. Some thermal-power plants have obtained environment licences - TE Sisak, TE-TO Osijek, KTE Jertovec and Pogon Osijek HEP-Toplinarstva d.o.o., procedures are still underway for other plants...

The system of CO₂ emissions trading in HEP Company was officially set up in 2012 pursuant to the Decision of the Management Board of HEP under which obligations, responsibilities and time-limits for meeting obligations of individual departments and companies within HEP's emission trading system are set. The Agency for Environment Protection has opened nine Accounts of plant operators in the EU Greenhouse Gas Inventory. HEP has successfully fulfilled its legal obligations and submission of emission units to the EU Greenhouse Gas Inventory for 2013 and in 2014 entered information verifying CO₂ emission which were confirmed by Croatian officials and these emission units were submitted onto all nine Accounts of plant operators with the relevant quantities that corresponded the verified CO₂ emissions. In 2014 activities were started to prepare non-financial statements for 2013 and 2014 for the HEP Group in accordance with Global Reporting Initiative (GRI 4) guidelines.

The system is continually being introduced regarding environment management system in accordance with ISO 14001 in distribution areas of HEP structures.

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014**

34. UNCERTAIN EVENTS AND COMMITTED LIABILITIES

In 2014 the process of introduction the environment protection IT system in HEP Group continued with the objective of combining data related to environment and nature protection. INFOZOK was upgraded with modules for data collection of the use and monitoring of the quality of water and monitoring data on environment licences.

Investments into environment protection and energy efficiency projects were submitted to the Environment Protection Fund at the HEP Group level resulting in incentive corrective factors leading to a reduction of 50% of allowances for the emission of air-borne pollutants.

Environment protection management in accordance with ISO 14001 is continually being introduced in all HEP production structures.

In 2013 the process of introduction the environment protection IT system in HEP Group continued with the objective of combining data related to environment and nature protection.

RESTRUCTURING OF HEP OPERATOR PRIJENOSNOG SUSTAVA D.O.O. (CROATIAN TRANSMISSION SYSTEM OPERATOR D.O.O.)

The Electricity Market Act (Official Gazette 22/2013) came into force on 2.3.2013 (hereinafter: the Act). Regulatory acts prescribed the Act need to be adopted within twelve months of the Act entering into force and regulatory acts prescribed by the Energy Act (Official Gazette 120/2012) within six months of the Act entering into force.

Pursuant to the provisions of the Act (Official Gazette 22/2013) HEP d.d, as the ruling company within the vertical structure of an integrated subject and the owner of the transmission system, conducted the restructure of the transmission system operator pursuant to the provisions of the Act and undertook all activities to fulfil the requirement to divide the transmission system operator with the aim of having it certified.

The General Assembly of HEP d.d. on 9 April 2013 adopted the decisions to divide the transmission operator system on the model of ITO - Independent Transmission Operator

In July 2013, registration procedures were conducted to transform HEP Operator prijenosnog sustava (now: Croatian Transmission System Operator d.o.o., abbreviated HOPS d.o.o.) with the objective of restructuring it in accordance with the ITO model "Independent Transmission Operator" pursuant with the Electricity Market Act and decision of the HEP d.d General Assembly.

Assets that the HEP Operator prijenosnog sustava d.o.o. used were transferred to its ownership and any receivables due were transferred to the HEP Operator prijenosnog sustava d.o.o.'s capital

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

S U P P L Y A T W H O L E S A L E G A S M A R K E T

Since April 2014 HEP d.d. by a Decision of the Government of the Republic of Croatia was determined as a supplier on wholesale market of gas in a period until April 2017. Pursuant to the above the Croatian Government rented 70% of warehouse capacities in underground gas storage facilities.

The supplier on the wholesale market (HEP d.d.) sells gas to suppliers in public service for the purposes of buyers from the household category at regulated conditions and is obliged to provide for a reliable and secure supply of gas.

	HRK '000
Income from the sale of Gas	
Income from the sale of gas to suppliers - unrelated companies	689,575
Income from the sale of gas – related companies	94,542
Other income regarding sale of gas	16,763
Total income from the sale of gas	800,880
Costs related to the sale of gas	
Costs of gas sold	553,159
Fees for storage capacities	80,008
Fees for use of transport system	84,554
	717,721
Other costs related to the sale of gas	19,555
Total costs related to the sale of gas	737,276

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

35. SUBSIDIARIES

As at 31 December 2014, the Company in its ownership had the following subsidiaries:

Subsidiary	Country	Interest in (%)	Main activity
HEP-Proizvodnja d.o.o.	Croatia	100	Electricity generation and heating
Hrvatski operator prijenosnog sustava d.o.o.	Croatia	100	Electricity transmission
HEP-Operator distribucijskog sustava d.o.o.	Croatia	100	Electricity distribution
HEP-Opskrba d.o.o.	Croatia	100	Electricity supply
HEP-Toplinarstvo d.o.o.	Croatia	100	Thermal power generation and distribution
HEP-Trgovina d.o.o.	Croatia	100	Electrical energy trading and optimising power plant operations
HEP-Plin d.o.o.	Croatia	100	Gas distribution
TE Plomin d.o.o.	Croatia	50	Electricity generation
APO d.o.o., usluge zaštite okoliša	Croatia	100	Environmental protection services and radioactive waste management
HEP ESCO d.o.o.	Croatia	100	Financing energy efficiency projects
Plomin Holding d.o.o.	Croatia	100	Development of infrastructure in area around Plomin
CS Buško Blato d.o.o.	BiH	100	Maintenance of hydro power plants
HEP-Odmor i rekreacija d.o.o.	Croatia	100	Accommodation and recreation service
HEP-NOC Velika	Croatia	100	Accommodation and training
HEP-Obnovljivi izvori energije d.o.o.	Croatia	100	Electricity generation
Program Sava d.o.o.	Croatia	100	Area arrangement, design, building and monitoring
HEP-Trgovina d.o.o. Ljubljana	Slovenia	100	Electrical energy trading
HEP- Magyarorszag Energia KFT	Hungary	100	Electrical energy trading
HEP-Trade d.o.o., Mostar	BiH	100	Electrical energy trading
HEP-Trade d.o.o., Beograd	Serbia	100	Electrical energy trading
HEP – KS sh.p.k.	Kosovo	100	Electrical energy trading
HEP-Telekomunikacije d.o.o.	Croatia	100	Telecommunications
HEP – Opskrba plinom d.o.o.	Croatia	100	Gas supply

The majority of these subsidiaries were formed for the purpose of reorganization and re-structuring the core business activities driven by the new energy legislation, which came into effect as of 1 January 2002, as indicated in Note 1. and HEP- Telekomunikacije d.o.o. in 2013.

HEP-RVNP d.o.o. has changed its name in 2014 into Program Sava d.o.o.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS

CAPITAL RISK MANAGEMENT

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

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

Gearing ratio

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

	31 December 2014	31 December 2013
	HRK '000	HRK '000
Debt	4,975,732	5,995,775
Cash and cash equivalents	(1,079,900)	(260,844)
Net debt	3,895,832	5,734,931
Equity	22,077,573	19,845,562
Net debt to equity ratio	18%	29%

SIGNIFICANT ACCOUNTING POLICIES

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

CATEGORIES OF FINANCIAL INSTRUMENTS

	31 December 2014	31 December 2013
	HRK '000	HRK '000
Financial assets		
Financial assets available for sale	192,676	125,166
Loans and receivables (including cash and cash equivalents)	3,385,074	2,534,330
Other long-term assets	54,337	64,971
Financial liabilities		
Long-term liabilities	5,749,390	6,390,110
Short-term liabilities	2,316,043	2,854,940

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS (continued)

FINANCIAL RISK OBJECTIVES

The function of the treasury within the HEP Group provides companies with services to the business, co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Group through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

MARKET RISK

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

Foreign currency risk management

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

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

	Assets		Liabilities	
	31 December 2014	31 December 2013	31 December 2014	31 December 2013
	'000	'000	'000	'000
European Union (EUR)	23,260	4,900	626,788	729,763
USD	30	-	5,954	158

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS (continued)

FOREIGN CURRENCY SENSITIVITY ANALYSIS

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

	2014	2013
	HRK '000	HRK '000
EUR exchange impact		
Profit or loss	462,391	553,624
USD exchange impact		
Profit or loss	3,393	91

**Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014****36. FINANCIAL INSTRUMENTS (continued)****INTEREST RATE RISK MANAGEMENT**

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

INTEREST RATE SENSITIVITY ANALYSIS

The sensitivity analysis has been determined based on the interest rate exposure of the Group to financial instruments at the date of the balance sheet/statement of financial position. For floating rates, the analysis is prepared assuming the amount of liability outstanding at the balance sheet / 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 2014 would decrease/increase by HRK 8,201 thousand (2013: HRK 12,349 thousand), based on exposure to interest rate risk. This is mainly attributable to the Company's exposure to interest rates on its variable rate borrowings, which accounted for 33.12% of the Company's debt (2013: 41.63%);
- The Group's sensitivity to interest rates has decreased during the current period mainly due to the reduction in variable rate of debt instruments.

LOAN RISK MANAGEMENT

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

The Group does not have any significant credit risk exposure to any single counterparty or any company of counterparties having similar characteristics. The Group defines counterparties as having similar characteristics if they are related entities.

Credit risk with respect to trade receivables is primarily related to domestic corporate receivables, specifically where services are provided to economic concerns, which are in a difficult financial position. Overdue receivables from households are limited due to Company's ability to disconnect such customers from the power supply network.

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS (continued)

LIQUIDITY RISK MANAGEMENT

The 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, banking facilities and other sources of financing, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

LIQUIDITY AND INTEREST RISK TABLES

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

MATURITY OF NON-DERIVATIVE FINANCIAL ASSETS

	Weighted average effective interest rate	Less than 1 month	1 – 3 months	3 -12 months	1 – 5 years	Over 5 years	Total
		HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
2014							
Non-interest bearing		2,366,041	801,454	337,149	39,131	910	3,544,685
Floating interest rate instruments		131	-	-	-	-	131
Fixed interest	6.00%	62	10,618	522	-	-	11,202
Total		2,366,234	812,072	337,671	39,131	910	3,556,018
2013							
Non-interest bearing		914,345	787,697	206,655	409,260	2,224	2,320,181
Floating interest rate instruments	7.00%	535	1,018	92,331	-	-	93,884
Total		914,880	788,715	298,986	409,260	2,224	2,414,065

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

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS (continued)

LIQUIDITY RISK MANAGEMENT (CONTINUED)

MATURITY OF NON-DERIVATIVE FINANCIAL LIABILITIES

	Weighted average effective interest rate	Less than 1 month	1 – 3 months	3 – 12 months	1 – 5 years	Over 5 years	Total
	%	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
2014							
Non-interest bearing		1,980,663	862,644	89,568	846,629	118,889	3,898,403
Floating interest rate instruments	2.60	81,010	54,902	323,469	1,440,009	-	1,899,390
Fixed interest	6.50	-	956	312,552	3,634,269	14,526	3,962,303
Total		2,061,673	918,502	725,589	5,920,907	133,415	9,760,096
2013							
Non-interest bearing		1,481,347	628,489	28,808	1,075,760	5,704	3,220,108
Floating interest rate instruments	3.17	14,585	49,118	824,881	1,656,115	78,835	2,623,534
Fixed interest	6.46	473	45,774	315,464	3,921,980	25,510	4,309,201
Total		1,496,405	723,381	1,169,153	6,653,855	110,049	10,152,843

The Group has access to financing facilities, the total unused amount of which is HRK 1,687,895 thousand at the reporting date. The Group expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

36. FINANCIAL INSTRUMENTS (continued)

FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value of financial assets and financial liabilities are defined as follows:

- Fair value of financial assets and financial liabilities that are traded on active markets under standard terms are defined at the price quoted on the market;
- Fair value of other financial assets and other financial liabilities (excluding derivative instruments) are defined in accordance with the model to determine prices and based on analysis of discounted cash flows using the price on previous transactions on the market and the price that is offered for similar instruments;
- Fair value of derivative instruments is calculated at listed prices. Where these prices are not available, an analysis of discounted cash flows is used with the application of the valid curve of income for the period of the duration of the instrument for unoptional derivatives, while optional derivatives are based on the model to determine the price of options. Termed currency contracts are valued using the quoted forward currency exchange and curve of income from quoted interest rates for contracts with similar maturities. Interest swap is valued at the current value estimated for future cash flows and discounted on the basis of valid income curves from quoted interest rates.

INDICATORS OF FAIR VALUE RECOGNISED IN THE STATEMENT OF FINANCIAL POSITION

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

1. Level 1 observable indicators – indicators of fair value derived from (unrestated) prices quoted in active markets for identical assets and liabilities are identical;
2. Level 2 observable indicators – indicators of fair value derived from data other than quoted prices from Level 1 for observable assets or liabilities (i.e. their prices) or indirectly (derived from the price); and
3. Level 3 indicators – indicators derived from valuation techniques using as input data on the assets or liabilities that are not based on available market data (unobservable input).

	Level 1	Level 2	Level 3	Total
	HRK '000	HRK '000	HRK '000	HRK '000
2014				
Assets available for sale	192,676	-	-	192,676
Fair value of swap	-	-	1,473	1,473
Investment in real estate	-	-	234,551	234,551
2013				
Assets available for sale	125,166	-	-	125,166
Fair value of swap	-	-	391,808	391,808
Investment in real estate	-	-	231,285	231,285

The measurement of fair value of the currency swap is connected with the value "Mark-to-market" ("MTM") according to the calculation of business banks and also that the value is Restated at each reporting date through the profit and loss account.

Notes to the Consolidated Financial Statements (continued)
For the year ended 31 December 2014

34. APPROVAL OF THE FINANCIAL STATEMENTS

These Consolidated financial statements were approved by the Board and authorised for issue on 30 April 2015.

Signed on behalf of the Company on 30 April 2015. :

Perica Jukić
President of the Board

HEP GROUP – CONSOLIDATED FINANCIAL STATEMENTS
TOGETHER WITH INDEPENDENT AUDITOR'S REPORT

HEP d.d. – Financial statements

INDEPENDENT AUDITOR'S REPORT

TO THE SHAREHOLDERS OF HRVATSKA ELEKTROPRIVREDA (HEP) D.D.

1. We have conducted an audit of the accompanying annual financial statements of Hrvatska Elektroprivreda d.d. (hereinafter: "HEP d.d." or "the Company") which comprise the Balance Sheet / Statement of Financial Position as at 31 December 2014; Statement of Comprehensive Income; the Statement of Changes in Equity; the Cash Flow Statement for the year ended, and a summary of principal accounting policies and other notes with explanations.

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT

2. The Company's Management is responsible for the preparation and fair presentation of the enclosed Financial Statements according to the International Financial Reporting Standards in effect in the European Union and for internal controls that Management identifies are relevant to prepare the financial statements free from any significant misstatements whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

3. Our responsibility is to express an opinion on the enclosed financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the said circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

4. In our opinion, the enclosed financial statements, in all materially significant aspects, give a true and fair view of the financial position of Hrvatska elektroprivreda (HEP) d.d., as at 31 December 2014 and of HEP d.d.'s financial performance and cash flows for 2014 in accordance with the Croatian Accounting Act and International Financial Reporting Standards that are effective in the European Union.

EMPHASIS OF MATTER

5. As described in Note 1 to the financial statements, pursuant to a contract of financial leasing to subsidiaries HEP d.d. has offered property, plant and equipment for rental. The said rentals carry an interest to the level that HEP d.d. obtained from external sources to finance the construction of the said property. The receivables noted are expressed in their nominal value due to the specific organisation structure of the HEP Company.
6. As described in Note 26 to the financial statements HEP d.d. has entered a liability for a clearing debt to the amount of HRK 759,089 thousand regarding payment under a letter of credit on the basis of consent by the Ministry of Finance with the use of funds pursuant to an interbank agreement. As there is no other document that regulates relations between the Company and the Ministry of Finance regarding the clearing debt up to the date of our independent auditor's report, it has not been clearly defined as either a loan or government subsidy.
7. HEP d.d. has prepared the financial statements in accordance with the International Financial Reporting Standards and in accordance with requirements specified by Croatian laws and regulations and as such has expressed its investments in dependent and associated companies as investment expenses. HEP d.d. has also prepared a consolidated financial statement for the company and its subsidiaries which was compiled on 24 April 2015. For the purpose of obtaining a better understanding of HEP d.d. and the HEP Company, the Consolidated Financial Statements should be read together with the financial statements.

OPINION COMPLIANCE WITH OTHER LEGAL OR REGULATORY REQUIREMENTS

8. The Management Board is responsible for the preparation of these financial statements for the year ended 31 December 2014 in the prescribed form based on the Statute of the structure and Content of Annual Financial Statements (Official Gazette 38/08, 12/09, 130/10) ("Standard Annual Financial Statements"). Financial information presented in Company's Standard Annual Financial Statements is in accordance with the information presented in Company's Annual Financial Statements presented on pages 5 to 95 for which we expressed our opinion as presented in the paragraph above 'Opinion'.

DISCLAIMER OF OPINION ON COMPLIANCE OF THE ANNUAL REPORT

9. The Management Board is responsible for the preparation of the HEP d.d.'s Annual Report. Pursuant to Article 17 of the Accounting Act, we are obliged to give our opinion on the compatibility of HEP d.d.'s Annual Report with HEP d.d.'s Annual Financial Statements. In our opinion, pursuant to the conducted audit of HEP d.d.'s Annual Financial Statements and in comparison with HEP d.d.'s Annual Report for the year ended 31 December 2014, the financial information presented in HEP d.d.'s Annual Report and approved by the Management Board on 30 April 2015 is in compliance with the financial information presented in HEP d.d.'s Annual Financial Statements presented on pages 5 to 95 for which we have expressed our opinion as stated in the paragraph 'Opinion' above.

Zagreb, 30 April 2015

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

Zdenko Balen,
Member of the Management Board
Darko Karić, Certified Auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić,
Member of the Management Board
Dubravka Tršinar, Certified Auditor

Statement of Comprehensive Income – HEP d.d.

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK '000	HRK '000
Income from electricity sales	7,236,373	11,000,616
Income from electricity sales – related companies	151,366	231,965
Income from gas sales	689,575	-
Income from gas sales HEP – Gas – related companies	94,542	-
Operating income – related companies	952,705	1,205,014
Other operating income	166,446	196,426
Total operating income	9,291,007	12,634,021
Electricity supplies	(704,439)	(1,714,262)
Fuel costs – NEK d.o.o.	(134,385)	(125,995)
Electricity supplies – related companies	(598,714)	(720,972)
Costs of gas sales	(553,159)	-
Costs related to gas sales	(164,562)	-
Staff costs	(226,237)	(211,541)
Depreciation costs	(364,655)	(316,551)
Costs of allowances for the generation, transmission and distribution of electricity – related companies	(4,948,470)	(8,346,845)
Other operating expenses	(679,697)	(651,142)
Total operating expenses	(8,374,318)	(12,087,308)
Profit from operations	916,689	546,713
Financial income	2,147,192	1,067,217
Financial expenses	(1,635,353)	(838,318)
Net profit from financial activities	511,839	228,899
Profit before tax	1,428,528	775,612
Income/Expenses on profit tax	(209,556)	(27,871)
	1,218,972	747,741

Statement of Comprehensive Income – HEP d.d. (continued)
For the year ended 31 December 2014

~	2014	2013
	HRK '000	HRK '000
Profit of the current year	1,218,972	747,741
Other comprehensive income		
Fair value adjustment of investment in Jadranski Naftovod d.d.	52,330	(3,429)
Total items to be transferred to profit and loss account	52,330	(3,429)
Other comprehensive income /(loss) net	52,330	(3,429)
Total comprehensive profit for current year	1,271,302	744,312,161

Signed on behalf of the Company on 30 April 2015
 Perica Jukić
 President of the Board

Balance sheet / statement of financial position – HEP d.d.

AS AT 31 DECEMBER 2014

ASSETS	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Property, plant and equipment	3,263,523	3,418,320	3,460,562
Capital works in progress	391,867	413,890	327,168
Intangible assets	16,435	13,397	13,042
Investment property	15,491	10,305	8,010
Prepayment for tangible assets	4,287	6,418	13,035
Investment and receivables from TE Plomin	254,278	256,404	300,820
Investment in subsidiaries	5,325,094	4,026,353	6,398
Investment available for sales and other investments	192,223	125,166	129,353
Long-term loans and deposits	4,404	6,031	385
Receivables on long-term leases from related parties	14,501,373	14,457,420	14,724,461
Receivables on long-term loans from related parties	94,929	110,729	126,529
Receivables on sub-leases from related parties	1,044,070	1,160,963	1,393,054
Other receivables	1,281	1,456	1,091
Deferred tax assets	19,679	104,766	51,633
Total long-term assets	25,128,934	24,111,618	20,555,541
Inventories	954,414	341,148	286,686
Trade receivables	392,907	64,404	35,282
Current maturity of long-term receivables from related companies for rental	1,086,428	1,080,257	1,109,084
Current maturity of long-term rentals from related parties	154,219	125,355	150,969
Other short-term receivables	39,990	315,962	26,577
Receivables from related companies	4,074,125	5,457,238	8,474,013
Short-term financial investments NEK d.o.o.	216,160	191,514	63,831
Cash and cash equivalents	730,693	83,190	497,096
Total short-term assets	7,648,936	7,659,068	10,643,538
TOTAL ASSETS	32,777,870	31,770,686	31,199,079

Balance Sheet/Statement of Financial Position – HEP d.d. (continued)
As at 31 December 2014

CAPITAL and LIABILITIES	31 December 2014	31 December 2013	1 January 2013
	HRK '000	HRK '000	HRK '000
		Restated	Restated
Share capital	19,792,159	19,792,159	19,792,159
Capital reserves	54,947	2,617	6,046
Retained earnings	3,265,948	2,329,760	1,657,099
Total capital	23,113,054	22,124,536	21,455,304
Bonds issued	3,194,986	3,278,893	3,335,608
Long-term loans	1,242,508	1,697,507	1,834,576
Long-term liabilities toward the state	972	1,026	1,075
Other long-term liabilities	764,777	1,066,770	697,153
Long-term liabilities to related companies	5,758	5,758	161,854
Provisions	255,781	244,314	39,909
Deferred tax liabilities	13,573	654	1,511
Total long-term liabilities	5,478,355	6,294,922	6,071,686
Trade payables	577,709	452,498	718,879
Current portion of long-term bonds issued	93,380	93,380	593,380
Current portion of long-term loans	416,349	208,838	132,084
Liabilities for short-term borrowings	0	684,925	402,826
Liabilities for taxes	91,813	224,296	351,073
Interest payable	38,247	41,110	45,439
Liabilities toward related companies	2,658,833	1,507,607	1,302,276
Liabilities toward employees	16,868	16,781	5,437
Other liabilities	293,262	121,793	120,695
Total short-term liabilities	4,186,461	3,351,228	3,672,089
TOTAL CAPITAL I LIABILITIES	32,777,870	31,770,686	31,199,079

Signed on behalf of the Company on 30 April 2015:

Perica Jukić

President of the Management Board

REPORTS BY HEP
GROUP COMPANIES



HEP Proizvodnja d.o.o.

HEP-Proizvodnja continued to improve core generation activities within HEP Group in 2014 in line with the Company's registration for electricity and heat energy generation meeting the needs and costs of HEP's portfolio of electricity, heat energy and process steam supply to its customers.

The enhancement of HEP generation business activities includes a wide scope of technical and technological, economic and legal activities from the following priority business areas:

- planning, preparation and execution of the construction of new and the revitalization of the existing hydropower plants, thermal power plants and cogeneration plants;
- prevention and corrective maintenance according to plants condition and the needs of the Croatian electric power system; operational planning and management of generation as well as fuel procurement, storage and consumption optimization;
- provision of ancillary services to HOPS, provision and activation of power and energy regulation reserves;
- certification of the guarantee of green energy origin as well as electricity generation within the incentive system; execution of environmental and work safety measures and activities;
- contribution to improvements of the Croatian energy regulations and the cooperation with the Croatian bodies and institutions.

From the energy point of view, the year 2014 was above average in terms of hydrology with total recorded generation of 9,805 GWh, of which hydro accounted for 8,356 GWh and thermal production for 1,450 GWh. Lower production in thermal and cogeneration plants was the result of the market-wise more favourable electricity import for the needs of HEP customers compared to high thermal and cogeneration cost due to high fuel prices – natural gas, extremely favourable hydrology in terms of hydro generation and a significant increase of generation from RES in Croatia, primarily by wind farms. Heat energy production remained at the last years level, while the fuel consumption optimization was based on reduced unit production i.e. increased operation of boiler units for the needs of heat consumption of district heating systems in Zagreb, Osijek and Sisak. Appropriate availability and permanent operation along with a somewhat lower generation was characteristic for both Plomin TPP units. In 2014, special attention was paid to the optimization of the fuel reserves structure and volume for thermal power and cogeneration plants considering the economic and environmental justification of substituting fuel oil with natural gas.

By appropriately maintaining its heat and electricity generation facilities, HEP Generation retained a high availability level of almost all its generation units in 2014. Apart from some minor difficulties, planned regular maintenance of generation units was carried out as well as the reactive maintenance in cases of breakdown repairs and operational disturbances.

For the purpose of ensuring the safety of the Croatian electric power system control, generation facilities operated by HEP Generation provided the complete provision of regulation and reserve capacity services by the transmission system operator (HOPS). Good cooperation in the operation and maintenance of generation units outside Croatian borders (Buško blato, Trebišnjica) was established.

The issuance of the 'green energy' certificate for all hydropower plants continued.

HEP Generation and HEP District Heating signed the contract on heat energy sale and the use of the distribution network for tariff and eligible customers.

In 2014, HEP Generation continued the analysis of other consumption based on the metering points at the interface with the distribution network, which direct effects are expected during 2015.

A high level of cooperation with relevant bodies and energy sector institutions (MINGO, MZOIP, HERA, HROTE) was retained as well as with foreign and domestic equipment producers and service providers.

Director

Nikola Rukavina

GENERATING PLANTS

Hydro power plants	Available capacity (MW) / (-MW pumping regime)	Hydro power plants	Available capacity (MW)
Storage		Run-of-river	
HE Zakučac	522*	HE Varaždin	92.46
RHE Velebit	276 (-240)	HE Dubrava	79.78
HE Orlovac	237	HE Čakovec	77.44
HE Senj	216	HE Gojak	55.5
HE Dubrovnik	108+120	HE Rijeka	36.8
HE Vinodol	90	HE Miljacka	24
HE Peruća	61.2	HE Jaruga	7.2
HE Kraljevac	46.4	HE Golubić	6.54
HE Đale	40.8	HE Ozalj	5.5
HE Sklope	22.5	HE Krčić	0.34
CS Buško blato	7.5/4.2/(-10.2/-4.8)	HE Lešće	41.2
CHE Fužine	4.6/(-5.7)	HE Lešće ABM	1.09
HE Zavrelje	2		
RHE Lepenica	0.8 (-1.2)		
HE Zeleni vir	1.7		

CS: pumping station CHE: pumped storage RHE: reversible pump turbine

* The capacity following the Unit A revitalization has still not been confirmed by acceptance testings.

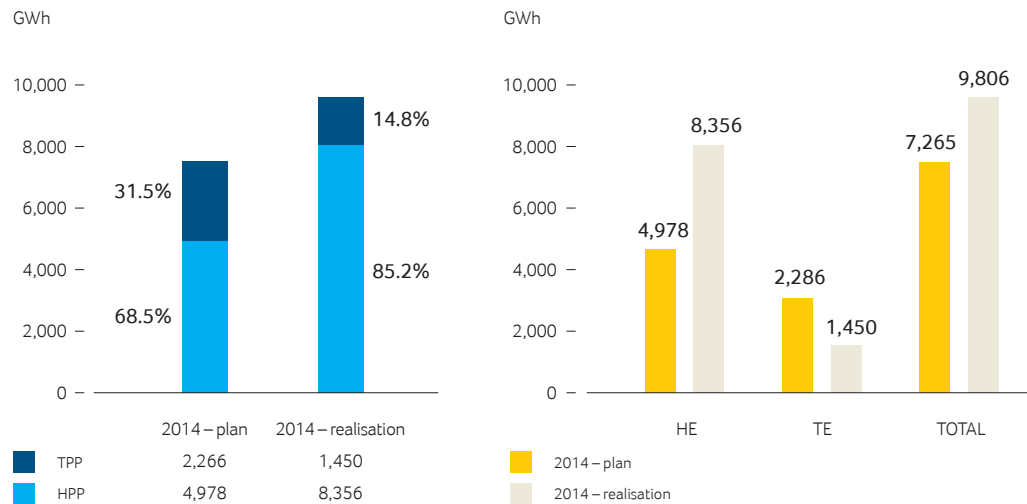
** During revitalization of HE Dubrovnik, shared 50%-50% generation was agreed

Thermal power plants	Net available capacity (MW,MWT,T/H)	Fuel
TE Sisak	396 / 0 / 96	oil/natural gas
TE-TO Zagreb	422 / 743 / 360	oil/natural gas
TE Rijeka	303	oil
TE Plomin (A)	105	coal
EL-TO Zagreb	88.8 / 347 / 377	oil/natural gas
TE-TO Osijek	90 / 139 / 150	oil / natural gas/extra light oil
KTE Jertovec	74	natural gas/extra light oil
TE PLOMIN (B)*	192	coal

* Owned by TE Plomin d.o.o. (HEP : RWE Power - 50% : 50%); HEP-Proizvodnja d.o.o. – O&M contract

ELECTRICITY GENERATION IN 2014

In 2014, HEP Generation power plants produced the total of 9,805.6 GWh of electricity. Hydro and thermal generation accounted for 8,355.8 GWh or 85.2 percent and 1,449.8 GWh or 14.8 percent, respectively. Compared to the 2014 planned generation, total recorded generation was 35 percent higher including 68% higher hydro and 37% lower thermal generation.



HEAT ENERGY PRODUCTION IN 2014

In 2014, HEP Generation CCGT plants generated a total of 2,058,100 MWh of heat energy, which is 14.2% less than planned in 2014. Compared to the generated 2,314,043 MWh the year before, heat generation decreased by 11.1 percent.

Process steam generation amounted to 729,217 tonnes, which is 10.1% less than planned in 2014 (811,231 t). The generation in 2013 recorded 824,250 tonnes.

Heat production in 2014 was 1,450,662 MWh or 15.7% less than planned in 2014 (1,721,645 MWh). The 2013 generation was 1,655,170 MWh.

AVAILABILITY OF POWER PLANTS RUN BY HEP GENERATION FOR 2014 INCLUDING TE PLOMIN D.O.O.

Availability of all generating plants i.e. HEP power plants measured as the ratio of availability hours (availability hours = operation + reserve in relation to total number of hours minus planned overhauls) is 97.7%, which exceeds availability in 2013 by 0.6%.

FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the Owners of the company HEP Proizvodnja d.o.o.:

1. We have audited the accompanying annual financial statements of the company HEP Proizvodnja d.o.o., Zagreb, Ulica grada Vukovara 37, (hereinafter "the Company") for the year ended 31 December 2014, which comprise the Balance Sheet / Statement of Financial Position as at 31 December 2014, Statement of Comprehensive Income, Statement of Changes in Equity and the Cash Flows Statement for the year then ended; and the accompanying Notes to the Financial Statements which concisely set out the principal accounting policies and other disclosures.

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT FOR FINANCIAL STATEMENTS

2. The Company's Management is responsible for the preparation and fair presentation of the enclosed Financial Statements according to the International Financial Reporting Standards in effect in the European Union and for internal controls that Management identifies are relevant to prepare the financial statements free from any significant misstatements whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

3. Our responsibility is to express an opinion on the enclosed Financial Statements based on the audit performed. We conducted our audit in accordance with International Standards of Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatements. An audit includes performing of procedures to obtain audit evidence supporting the amounts and disclosures in the Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements in the Financial Statements, whether due to fraud or error. In making these risk assessments, the auditor considers internal controls relevant to the Company's preparation and fair presentation of the Financial Statements in order to conduct audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Company's Management, as well as evaluating the overall presentation of the Financial Statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

4. In our opinion, the enclosed financial statements, in all material aspects, give a true and fair view of the financial position of the Company as at 31 December 2014, and its financial performance and cash flows for 2014 in accordance with the Accounting Act and International Financial Reporting Standards effective in the European Union.

EMPHASIS OF MATTER

5. We draw attention to the fact that at 31 December 2014 the Company stated losses above the amount of capital and amounting to HRK 1,088,009 thousand. Pursuant to the Law on Financial Operations and Pre-bankruptcy Settlement Proceedings, the Company does not meet the required criteria of capital adequacy. The Company's continued operations under the going concern principal depends on the Company's ability to secure sufficient resources to settle obligations in a timely manner, to secure adequate sources on financing and to commence doing business at a profit. In order to achieve this as described in Note 1 to the Financial Statements, a member of the Company has obliged to offer financial support to the Company and the Company's Management has made an effort to improve current operations and the Company's financial position.

6. As described in the Note 1, to the enclosed financial statements, HEP d.d. has leased property, plant and equipment to its subsidiaries under finance lease agreements. The leases bear interest to the extent that the HEP d.d. has acquired external financing to construct the underlying assets. These liabilities are stated at their nominal value because of the specifics of the HEP Group.

OPINION ON COMPLIANCE WITH OTHER LEGAL OR REGULATORY REQUIREMENT

7. The Company's Management is responsible for the preparation of the Company's annual financial statements for the year ended 31 December 2014 in the prescribed format on the basis of the Regulation on the Structure and Content of the Annual Financial Statements (National gazette No 38/08, 12/09, 130/10) ("Standard Annual financial statements"). The financial information set out in standard Company's Annual Financial Statements are identical to the information stated in the Company's Annual Financial Statements shown on pages 5 to 60 which are the subject of our opinion as set out in section Opinion, above.

OPINION ON COMPLIANCE OF ANNUAL REPORT

8. The Company's Management is responsible for the preparation of the Company's Annual statement. As a result of the provisions of article 17 of the Accounting Act, we are obliged to express an opinion on adjustment of the Company's Annual statement with the Company's Annual Financial Statements. In our opinion and on the basis of the performed audit of the Company's Annual Financial Statements and a comparison with the company's Annual Statement for the year which ended 31 December 2014, the financial information set out in the Company's Annual Statement and approved for issuance by the Company's Management on 15 April 2015, are in accordance with the financial information set out in the company's Annual Financial Statements shown on pages 5 to 60 which were the subject of our opinion, as set out in section Opinion.

In Zagreb, 24 April 2015

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

Zdenko Balen,
Member of the Management Board

Darko Karić, Certified Auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić,
Member of the Management Board

Dubravka Tršinar, Certified Auditor

HEP Proizvodnja d.o.o., Statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK thousand	HRK thousand
		Restated
Income from fee for production of electric energy and other income - related companies	3,929,747	4,867,049
Other operating income	38,277	37,281
	3,968,024	4,904,330
Energy for manufacturing, materials and spare parts	(1,337,602)	(2,268,994)
Service expenses	(303,091)	(317,175)
Personnel expenses	(345,522)	(337,451)
Depreciation	(237,160)	(233,959)
Administrative expenses – related companies	(96,312)	(94,658)
Other operating expenses	(433,013)	(828,430)
	(2,752,700)	(4,080,667)
Profit from operating activities	1,215,324	823,663
Financial income	472	484
Financial expenses	(68,213)	(79,314)
Net loss from financial activities	(67,741)	(78,830)
Profit from regular operations before taxation	1,147,583	744,833
Corporate income tax	(232,560)	(150,686)
Profit/(Loss) for the business year	915,023	594,147

HEP-Proizvodnja d.o.o.,
Statement of comprehensive income
for the year ended 31 December 2014 (continued)

	2014	2013
	HRK thousand	HRK thousand
		Restated
Profit for the current year	915,023	594,147
Other comprehensive income or loss for the current year		
Total comprehensive profit for the current year	915,023	594,147

Signed on behalf of the Company on 24 April 2015
 Nikola Rukavina,
 Director

HEP Proizvodnja d.o.o., Balance sheet / Statement of financial position

AS AT 31 DECEMBER 2014

ASSETS	31 December 2014	31 December 2013	1 January 2013
"	HRK thousand	HRK thousand	HRK thousand
		Restated	Restated
Intangible assets	13,764	16,874	17,735
Property, plant and equipment	3,843,159	3,749,262	3,944,670
Investments in progress	2,418,733	2,412,498	2,082,059
Investments in properties	38,651	38,655	38,739
Prepayments for property, plant and equipment	50,848	63,263	69,447
Investments in subsidiaries	8	8	8
Receivables from the sale of apartments	8,356	10,471	11,861
Deferred tax assets	541,242	585,061	557,029
Total long-term assets	6,914,761	6,876,092	6,721,548
Inventories	313,630	417,009	604,414
Other short-term assets	6,525	36,927	115,778
Receivables from related companies	1,953,235	2,013,635	1,282,025
Trade receivables	2,341	2,080	3,034
Current portion of long-term receivables	2,451	2,299	2,749
Cash and cash equivalents	37,885	8,294	5,886
Total short-term assets	2,316,067	2,480,244	2,013,886
TOTAL ASSETS	9,230,828	9,356,336	8,735,434

HEP-Proizvodnja d.o.o.,
Balance sheet / Statement of financial position
as at 31 December 2014 (continued)

CAPITAL AND LIABILITIES	31 December 2014	31 December 2013	1 January 2013
	HRK thousand	HRK thousand	HRK thousand
		Restated	Restated
Subscribed capital	20	20	20
Accumulated loss	(1,088,029)	(1,420,430)	(2,014,577)
Total capital	(1,088,009)	(1,420,410)	(2,014,557)
Long-term liabilities to related companies	6,053,033	6,080,579	6,259,281
Long-term provisions	300,795	278,941	266,730
Other long-term liabilities	6,721	7,714	8,799
Total long-term liabilities	6,360,549	6,367,234	6,534,810
Trade payables	250,281	361,519	707,294
Liabilities to related companies	2,970,480	3,366,070	3,135,450
Current portion of long-term liabilities to related companies	237,160	233,959	248,323
Other short-term liabilities	500,367	447,964	124,114
Total short-term liabilities	3,958,288	4,409,512	4,215,181
TOTAL CAPITAL AND LIABILITIES	9,230,828	9,356,336	8,735,434

Signed on behalf of the Company on 24 April 2015
Nikola Rukavina,
Director

HEP Operator distribucijskog sustava d.o.o.

HEP-Operator distribucijskog sustava d.o.o. (HEP DSO - distribution system operator) is the largest limited liability company within HEP Group. HEP DSO performs electricity distribution and supply as public services i.e. regulated activities.

Apart from its core activities, HEP DSO also performs non-core ones, which primarily regard the construction of electric power facilities and network connections. Its supporting activities facilitate the delivery and records of business events as well as their changes, operational analyses, operational IT support and other auxiliary activities within core and non-core operations.

As the company operates within the constantly changing legal and regulatory framework, its operations are carried out along with the ongoing harmonization and enhancement of business processes. The underlying legal framework is set by the Energy Act, the Electricity Market Act, the Act on the Regulation of Energy Activities and their by-laws as well as other general regulations defining company operations. The most significant secondary legislation includes the General Terms of Electricity Supply, the Methodology for Setting Tariff Item Amounts for Electricity Supply within the Universal Service, the Methodology for Setting Tariff Item Amounts for Guaranteed Electricity Supply, the Rulebook on the Electric Power Network Connection Fee and the Connection Power Increase Fee as well as the Electric Power System Grid Code.

During 2014, a number of measures and activities based on set business objectives from the Work Programme of HEP d.d. and the Work Programme of HEP DSO for the period 2012-2016 was conducted. Fundamental business objectives are expressed through the quality of electricity supply, increased energy efficiency in electricity distribution and use, development of the distribution network into the distribution system with advanced solutions considering the inevitable establishment of distributed generation and its consolidation with the network, organizational and business harmonization with the new legal framework, service provision and network customer relation improvement, HR management and knowledge transfer.

The business operations of HEP DSO in 2014 were characterised by the following: the upgrade of accounting unbundling of distribution, supply and auxiliary activity, the development of the 10-year development plan, increased efficiency of receivables collection, intensified electricity market related activities and the enhancement of environmental protection and work safety.

Investment and development programmes are planned and carried out for the purpose of achieving a balanced and efficient development and the construction of distribution network.

In view of the constantly changing business environment and work technologies, we keep investing into the development of new knowledge and skills of our employees through professional educations, specialisations and training.

The main business objective is to establish the business excellence of the new distribution system operator pursuant to the company's Work Programme and valid regulations.

In conclusion, the year 2014 was one of the most successful business years during which key business objectives were fulfilled.

Director

Željko Šimek

NUMBER OF TRANSFORMER STATIONS BY VOLTAGE LEVEL

TS 35(30)/10(20) kV	TS 20/0.4 kV	TS 10/0.4 kV
321	4,822	20,388

LINE LENGTHS BY VOLTAGE LEVEL AND LINE TYPE

110 kV lines (km)			35.30 kV lines (km)			20 kV lines (km)		
OHL	Cable	Undersea	OHL	Cable	Undersea	OHL	Cable	Undersea
5.5	4.8	0	3,154.5	1,375.7	138.1	3,434.9	3,587.6	2.6
Lines 10 kV (km)			Network 0.4 kV (km)			Household connections (km)		
OHL	Cable	Undersea	OHL-bare	OHL-insulated	Cable	OHL-bare	OHL-insulated	Cable
17,373.3	11,297.4	235.6	17,406.5	28,662.1	16,122.5	3,459.8	18,123.7	11,399.1

NUMBER OF CUSTOMERS/METERING POINTS BY CONSUMPTION CATEGORY (VOLTAGE LEVEL)

Description	Number of metering points
High voltage 110 kV	4
Total medium voltage	2,127
Low voltage – commercial (excl. public lighting)	190,204
Low voltage – commercial (public lighting)	23,934
Low voltage – residential	2,157,442
Total	2,373,711

ELECTRICITY SALES BY CUSTOMER CATEGORY IN 2014 (KWh)

Description	Total-Croatia
Commercial - high voltage (HV)	123,736,869
Commercial – medium voltage (MV)	3,530,604,841
TOTAL Commercial HV and MV	3,654,341,710
Commercial – low voltage (LV)	4,067,253,211
Commercial – low voltage (LV) – public lighting	428,832,559
Residential – low voltage (LV)*	6,032,926,244
TOTAL LOW VOLTAGE	10,529,012,014
Public service of supply	6,540,305,271
Market suppliers customers	7,643,048,453
Total sales on distribution network	14,183,353,724
Sale to customers without a supplier within guaranteed supply (HOPS network)	1,578,368

FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the Owner of HEP - Operator distribucijskog sustava d.o.o.:

1. We have audited the accompanying annual financial statements of the company HEP - Operator distribucijskog sustava d.o.o., Zagreb, Ulica grada Vukovara 37, (hereinafter "the Company") for the year ended 31 December 2014, which comprise the Balance Sheet/Statement of Financial Position as of that date; the Statement of Income/Statement of Comprehensive Income; the Statement of Changes in Equity; the Cash Flows Statement for the year then ended; and the accompanying Notes to the Financial Statements which concisely set out the principal accounting policies and other disclosures.

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT

2. The Company's Management is responsible for the preparation and fair presentation of the enclosed Financial Statements according to the International Financial Reporting Standards in effect in the European Union and for internal controls that Management identifies are relevant to prepare the financial statements free from any significant misstatements whether due to fraud or error.

RESPONSIBILITY OF AUDITOR

3. Our responsibility is to express an opinion on the enclosed financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the said circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

4. In our opinion, the enclosed financial statements present fairly, in all material respects, the financial position of the company HEP - Operator distribucijskog sustava d.o.o. at 31 December 2014, the results of its operations and its cash flows for 2014 in accordance with the Accounting Act and International Financial Reporting Standards applicable in the Republic of Croatia.

EMPHASIS OF MATTER

5. As described in the Note 1, to the enclosed unconsolidated financial statements, HEP d.d. has leased property, plant and equipment to its subsidiaries under finance lease agreements. The leases bear interest to the extent that the HEP d.d. has acquired external financing to construct the underlying assets. These liabilities are stated at their nominal value because of the specifics of the HEP Group.

OTHER LEGAL AND REGULATORY REQUIREMENTS

6. The Management Board is responsible to prepare the annual Financial Statements of the Company for the year ended 31 December 2014 in the prescribed format on the basis of the Regulation on the Structure and Content of the Annual Financial Statements (National gazette No 38/08,

12/09, 130/10) ("Standard Annual financial statements"). The financial information set out in standard Company's Annual Financial Statements are identical to the information stated in the Company's Annual Financial Statements shown on pages 4 to 60 which are the subject of our opinion as set out in section Opinion, above.

COMPLIANCE WITH THE ANNUAL REPORT

7. The Management Board of the Company is responsible for compiling the Annual report of the Company. In accordance with article 17 of the Accounting Law. We are required to express our opinion on the compliance of the annual financial reports and the Annual report. In our opinion, on the basis of our audit of the Company and comparison with the Company's Annual Report for the year ended 31 December 2014, the financial information stated in the Annual report, approved by the Company's Management on 17 April 2015, are in accordance with the financial information stated in the Company's Annual Financial Reports shown on pages 4 to 60 which are the subject of our opinion as set out in the section Opinion, above.

In Zagreb, 24 April 2015

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

Zdenko Balen, Member of the Board
Darko Karić, Certified Auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić, Member of the Board
Dubravka Tršinar, Certified Auditor

HEP - Operator distribucijskog sustava d.o.o. Statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK thousand	u tisućama kuna
Electricity distribution fee income – related companies	1,716,595	3,506,891
Electricity distribution fee income – universal supply	3,069,351	545,536
Income from the sale of electricity – grid charges	1,523,742	
Income from sale of services	342,024	333,528
Other income – related parties	18,707	123,275
Other operating income	377,584	611,850
Total operating income	7,048,003	5,121,080
Purchase of electricity from HEP d.d.	(2,697,549)	(499,946)
Purchase of electricity from HROTE	(215,346)	(158,219)
Cost of losses on the grid	(533,989)	(672,349)
Service expenses	(207,952)	(203,881)
Staff expenses	(1,028,063)	(1,049,834)
Depreciation and amortization	(818,649)	(806,499)
Administrative expenses – related companies	(146,771)	(179,180)
Other operating expenses	(559,051)	(798,536)
Total operating expenses	(6,207,370)	(4,368,444)
Profit from operations	840,633	752,636
Financial income	14,826	1,220
Financial expenses	(73,513)	(84,876)
Net financial loss	(58,687)	(83,656)
Profit before tax	781,946	668,980
Income tax expense	(161,885)	(79,920)
Profit for the current year	620,061	589,060

HEP - Operator distribucijskog sustava d.o.o.
Statement of comprehensive income
For the year ended 31 December 2014 (continued)

	2014	2013
	HRK thousand	HRK thousand
Profit before tax	620,061	589,060
Other comprehensive income for the current year	-	-
Total comprehensive income for the current year	620,061	589,060

Signed on behalf of the Company on 24 April 2015 by:

Željko Šimek
Director

HEP- Operator distribucijskog sustava d.o.o. Balance sheet/Statement of financial position

AT 31 DECEMBER 2014

ASSETS	31 December 2014	31 December 2013
	HRK thousand	HRK thousand
Property, plant and equipment	12,060,480	12,083,748
Capital work in progress	907,441	713,648
Intangible assets	24,969	21,040
Investment properties	59,203	59,137
Receivables from sale of flats	14,848	16,748
Prepayments for tangible assets	571	1,898
Deferred tax assets	69,549	48,368
Financial assets	16,393	15,940
Total non-current assets	13,153,454	12,960,527
Inventories	238,394	268,676
Trade receivables	724,402	875,587
Receivables from related companies	2,182,514	1,981,365
Current portion of long-term receivables	3,301	3,632
Other current assets	63,097	74,336
Cash and cash equivalents	129,040	73,625
Total current assets	3,340,748	3,277,221
TOTAL ASSETS	16,494,202	16,237,748

HEP- Operator distribucijskog sustava d.o.o.
Balance sheet/Statement of financial position
at 31 december 2014 (continued)

EQUITY AND LIABILITIES	31 December 2014	31 December 2013
	HRK thousand	HRK thousand
Share capital	699,456	425,456
Capital reserves	15,940	15,940
Retained earnings	622,968	590,682
Total equity	1,338,364	1,032,078
Long-term liabilities to related companies	7,667,726	7,602,054
Other non-current liabilities	3,522,161	3,704,868
Long-term provisions	274,787	226,292
Total non-current liabilities	11,464,674	11,533,214
Trade payables	387,654	299,557
Liabilities to related companies	1,933,241	2,231,303
Current portion of long-term liabilities	597,127	592,361
to related company	773,142	549,235
Other current liabilities	3,691,164	3,672,456
TOTAL CAPITAL AND LIABILITIES	16,494,202	16,237,748

Signed on behalf of the Company on 24 April 2015 by:

Željko Šimek
 Director

HEP Toplinarstvo d.o.o.

HEP-Toplinarstvo (District Heating) met its fundamental tasks in 2014 by ensuring a continuous, reliable and quality supply of heat energy to all its end customers.

The 2014 business operations were primarily marked by the intensive process of harmonization with the provisions of the Heat Energy Act and its accompanying by-laws, most of which entered into force in early September 2014. Under the new Heat Energy Market Act, significant and fundamental changes were introduced into the operation of all energy entities providing heat energy production, distribution and supply in Croatia, leaving very short adjustment periods. These changes aim at the establishment of the heat energy market and the encouragement of competitiveness, innovation and entrepreneurship in the management and maintenance of heat substations and boiler rooms as well as the collection of heat energy receivables.

HEP-Toplinarstvo met all its legally prescribed operating conditions for performing heat energy production, distribution and supply in Zagreb, Osijek, Sisak, Velika Gorica, Samobor and Zaprešić. It also registered as a heat energy buyer. As such, HEP District Heating became a market participant despite this market still not being fully operational in the true sense of the Heat Energy Market Act.

As a registered heat energy buyer, in July 2014 HEP District Heating sent to addresses of authorized representatives of residential co-owners supplied by heat energy the offer for conducting the activity of the heat energy buyer containing the full service, long standing experience and knowledge in heating facility management and maintenance, a high level of service provision, technical and human readiness, capacities for investing into new technologies and system development as well as the non-stop on-call office for reporting technical failures.

The operation of HEP District Heating in 2014 was also marked by the adoption of the Ordinance on the Amendments of the Heat Energy Market Act, in effect as of 23 August 2014, under which HEP District Heating as the heat energy supplier must assume the obligation of a heat energy buyer for all end customers who have still not entered into the contract with their selected heat energy buyers.

For the purpose of harmonizing its operations with the Heat Energy Market Act, single tariff items for heat energy in effect until 31 August 2014 were separated into new elements in line with the mandatory separation of heat business activities into heat energy production, distribution and supply as well as the new activity of the heat energy buyer.

Since early September 2014, single tariff items for capacity and energy were separated into tariff items for heat energy production (energy and capacity), tariff items for heat energy distribution (energy and capacity), the fee for heat energy supply and the fee for the business activity of the heat energy buyer. In line with the above said, HEP District Heating adjusted its billing and cost allocation for heat energy supply and introduced new elements into heat energy bills.

The operation of HEP District Heating is focused on always being available to its end customers and facilitating the implementation of their obligations under the Heat Energy Market Act. The cooperation and the two-way communication gave concrete results i.e. end customers have recognized the quality and values of HEP District Heating resulting in the conclusion of heat energy contracts during last year with about 70 percent of end customers in Zagreb, Osijek, Sisak, Velika Gorica, Samobor and Zaprešić.

HEP District Heating sees the opportunity for increasing its income from future business activities in the provision of additional services and the offer of new products as well as in the connection of new end customers onto district heating systems. Quality service, multi-year experience and employee knowledge as well as its adjustment to wishes and needs of end customers represent a solid foundation for building the Company's business policy and future development plans.

Robert Krklec

Director

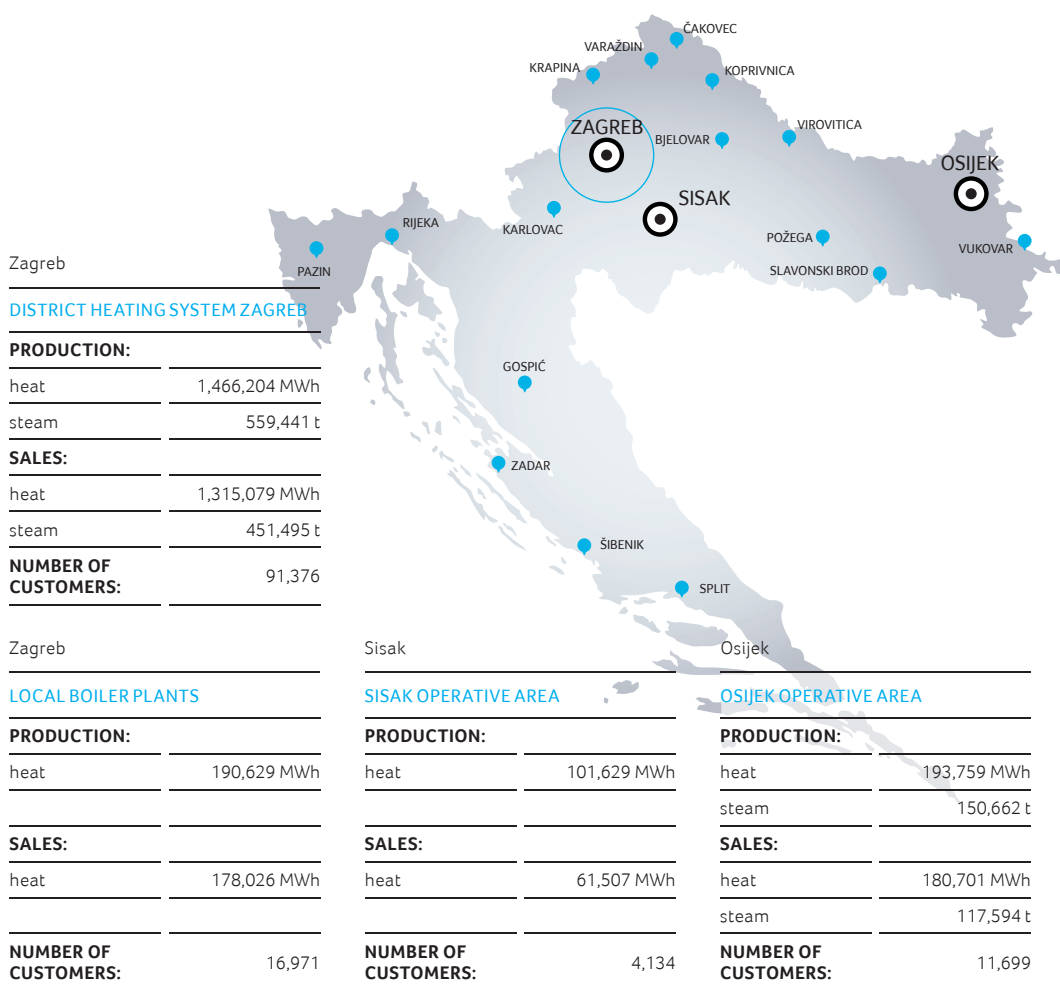
HEP DISTRICT HEATING IN 2014

During 2014, the number of end heat energy customers rose by 0.3 percent to a total number of 124,564 until end 2014, of which 118,427 (95.1%) are households and 6,137 (4.9%) corporate entities.

In heat consumption (district heat and process steam), households account for 59.1 percent (46.8% in income) and corporate entities for 40.9 percent (54.2% in income). The ratio of supplied heat energy (hot water) to process steam (in MWh) was 78.3%:21.7%.

In consumption of district heat, the share of Zagreb (including Samobor, Velika Gorica and Zaprešić) was 85.6 percent, Osijek 10.8 percent, and Sisak 3.5 percent. The consumption of process steam was 484,326 tonnes (Zagreb 74.8%, Osijek 21.2%, Sisak 4%).

In 2014, heat energy sales decreased by 15.8 percent compared to the year before. Taking each of the two main products of HEP District Heating separately, heat and process steam sales decreased by 16.1% and 14.9%, respectively.



FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the owner of the company HEP Toplinarstvo d.o.o.

1. We have audited the accompanying annual financial statements of the company HEP Toplinarstvo d.o.o., Zagreb, Mišvečka 15a, (hereinafter "the Company") for the year ended 31 December 2014, which comprise the Balance Sheet / Statement of Financial Position as of that date; Statement of Comprehensive Income; the Statement of Changes in Equity; the Cash Flow Statement for the year then ended; and the accompanying Notes to the Financial Statements which concisely set out the principal accounting policies and other explanations.

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT FOR FINANCIAL STATEMENTS

2. The Company's Management is responsible for the preparation and fair presentation of the enclosed Financial Statements according to the Interofficial Financial Reporting Standards in effect in the European Union and for internal controls that Management identifies are relevant to prepare the financial statements free from any significant misstatements whether due to fraud or error.

RESPONSIBILITY OF THE AUDITOR

3. Our responsibility is to express an opinion on the enclosed Financial Statements based on the audit performed. We conducted our audit in accordance with Interofficial Standards of Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatements. An audit includes performing of procedures to obtain audit evidence supporting the amounts and disclosures in the Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements in the Financial Statements, whether due to fraud or error. In making these risk assessments, the auditor considers internal controls relevant to the Company's preparation and fair presentation of the Financial Statements in order to conduct audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Company's Management, as well as evaluating the overall presentation of the Financial Statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

4. In our opinion, the enclosed financial statements, in all materially significant aspects, give a true and fair view of the financial position of the Company HEP Toplinarstvo d.o.o. as at 31 December 2014 and of the financial performance and cash flows of the Company for 2014 in accordance with the Croatian Accounting Act and Interofficial Financial Reporting Standards that are effective in the European Union.

EMPHASIS OF MATTER

5. We draw attention to the fact that the Company at 31 December 2014 has stated a loss above the level of capital in the amount of HRK 139,902 thousand and that short-term liabilities exceed short-term assets in the amount of HRK 164,553 thousand. According to the Law on Financial Operations and Pre-bankruptcy Proceedings, the Company does not meet the required criteria of capital adequacy. The Company's continued operations under the going concern principal depends on the Company's ability to secure sufficient resources to settle obligations in a timely manner, to secure adequate sources on financing and to commence doing business at a profit. In order to achieve this as described in Note 1 to the Financial Statements, a member of the Company has obliged

to offer financial support to the HEP Company and the Company's Management has made an effort to improve current operations and the Company's financial position.

6. As described in the Note 1, to the enclosed financial statements, HEP d.d. has leased property, plant and equipment to its subsidiaries under finance lease agreements. The leases bear interest to the extent that the HEP d.d. has acquired external financing to construct the underlying assets. These liabilities are stated at their nominal value because of the specifics of the HEP Group.

OPINION ON THE ADJUSTMENT TO OTHER LEGAL AND REGULATORY REQUIREMENTS

7. The Company's Management is responsible for the preparation of the Company's annual financial statements for the year ended 31 December 2014 in the prescribed format on the basis of the Regulation on the Structure and Content of the Annual Financial Statements (Official gazette No 38/08, 12/09, 130/10) ("Standard Annual financial statements"). The financial information set out in standard Company's Annual Financial Statements are identical to the information stated in the Company's Annual Financial Statements shown on pages 5 to 56 which are the subject of our opinion as set out in section Opinion, above.

OPINION ON COMPLIANCE TO THE ANNUAL REPORT

8. The Company's Management is responsible for the preparation of the Company's Annual statement . As a result of the provisions of article 17 of the Accounting Act, we are obliged to express an opinion on adjustment of the Company's Annual statement with the Company's Annual Financial Statements. In our opinion and on the basis of the performed audit of the Company's Annual Financial Statements and a comparison with the company's Annual Statement for the year which ended 31 December 2014, the financial information set out in the Company's Annual Statement and approved for issuance by the Company's Management on 17 April 2015, are in accordance with the financial information set out in the company's Annual Financial Statements shown on pages 5 to 56 which were the subject of our opinion, as set out in section Opinion.

In Zagreb, 24 April 2015

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

Zdenko Balen,
Member of the Management Board

Darko Karić, Certified Auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić,
Member of the Management Board

Dubravka Tršinar, Certified Auditor

HEP Toplinarstvo d.o.o.

Statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK thousand	HRK thousand
Income from thermal energy sale to the buyers outside the HEP Group	671,946	763,461
Income from sale of electric energy to eligible customers	11,485	11,134
Income from thermal energy and other income – related companies	4,481	4,899
Restaurant income	415	585
Other operating income	57,986	55,209
	746,313	835,288
Energy, material and spare parts expenses	(629,946)	(773,884)
Service expenses	(22,331)	(22,131)
Staff expenses	(51,372)	(49,946)
Depreciation and depreciation	(57,478)	(59,933)
Expense in respect of electricity generation and other expenses – related companies	(21,282)	(25,743)
Other operating expenses	(98,972)	(70,266)
	(881,381)	(1,001,903)
Loss from operations	(135,068)	(166,615)
Financial revenues	41	43
Financial expenses	(14,884)	(18,400)
Net financial loss	(14,843)	(18,357)
Loss before tax	(149,911)	(184,972)
Income tax	-	-
Loss for the current year	(149,911)	(184,972)

HEP Toplinarstvo d.o.o.,
Statement of comprehensive income
For the year ended 31 December 2014 (continued)

	2014	2013
	HRK thousand	HRK thousand
Loss for the current year	(149,911)	(184,972)
Other comprehensive income for the current year	-	-
Total comprehensive loss for the current year	(149,911)	(184,972)

Signed on behalf of the Company on 24 April 2015 by:

Robert Krklec

Director

HEP Toplinarstvo d.o.o.

Balance sheet / Statement of financial position

AT 31 DECEMBER 2014

ASSETS	31 December 2014	31 December 2013
	HRK thousand	HRK thousand
Property, plant and equipment	881,002	903,655
Assets under construction	83,932	69,988
Intangible assets	1,071	927
Receivables from the sale of flats	469	527
Advances for property, plant and equipment	308	528
Investment property	260	300
Total non-current assets	967,042	975,925
Inventories	37,833	26,670
Trade receivables	163,326	191,727
Receivables from related companies	49,212	2,308
Other receivables	5,577	22,761
Current portion of long-term receivables	123	159
Cash and cash equivalents	10,289	9,824
Total current assets	266,360	253,449
TOTAL ASSETS	1,233,402	1,229,374

Signed on behalf of the Company on 24 April 2015 by:

Robert Krklec

Director

HEP Toplinarstvo d.o.o.,
Balance sheet/Statement of financial position
At 31 December 2014 (continued)

	31 December 2014	31 December 2013
	HRK thousand	HRK thousand
Share capital	1,801,230	20
Reserves	20	20
Accumulated losses	(1,941,152)	(1,791,241)
Total equity	(139,902)	(1,791,201)
Long-term liabilities to related companies	815,413	848,531
Other long-term liabilities	325	379
Long-term provisions	6,490	9,846
Deferred income	120,163	128,370
Total non-current liabilities	942,391	987,126
Trade payables	38,674	30,664
Liabilities to related companies	305,560	1,941,951
Current portion of long-term debt to related companies	49,164	51,535
Other short-term liabilities	37,515	9,299
Total current liabilities	430,913	2,033,449
TOTAL EQUITY AND LIABILITIES	1,233,402	1,229,374

Signed on behalf of the Company on 24 April 2015 by:

Robert Krklec
 Director

HEP Plin d.o.o.

HEP-Plin (HEP Gas) carries out two energy-related businesses of the gas sector: gas distribution and gas supply to customers. Gas distribution is carried out according to regulated principles of public service provision. Gas supply is carried out pursuant to regulated principles of public service provision to tariff customers (households) and to other customers according to market principles - by individually negotiated mutual rights and obligations.

Gas distribution tasks were successfully carried out in 2013 having met expectations set by us, most of our customers and our concessionaires – regional and local self-governments. The distribution network was maintained in a working and functional order. Technical services conducted repairs on gas acceptance points in the shortest time possible. There was no major delays in gas supply due to gas network breakdowns. Special attention was continuously paid to environmental protection by preventing gas leakages into the atmosphere. The construction of the gas network in line with the concession agreements continued in 2014. The portion of works will be conducted in 2015. Unfortunately, the connection of new customers onto the built network was not carried out according to expectations due to the economic and social crisis resulting in lower profitability of investments made into the construction of the gas network. All necessary modifications and reconstructions were carried out on the existing network.

The Croatian accession to EU on 1 July 2013 launched a more intensive harmonization of HEP Gas operations with new gas sector regulations, which were additionally and fully harmonized with EU guidelines, especially in gas regulation performed according to principles of public service provision. In line with the above, in late 2013, HERA adopted several very important implementing regulations: Gas Distribution System Grid Code, General Terms of Gas Supply, Methodology for setting tariff item amounts for gas distribution, Methodology for setting tariff item amounts for the public service of gas supply and for the guaranteed service and Methodology for setting the non-standard service prices. These regulations have brought about the changes and the operating harmonization in terms of end customer relations.

Until full gas market opening for household customers, a transitional period until 31 March 2017 was set. The market has been opened for other customers for a number of years although HEP Gas started facing a more serious market competition in 2014.

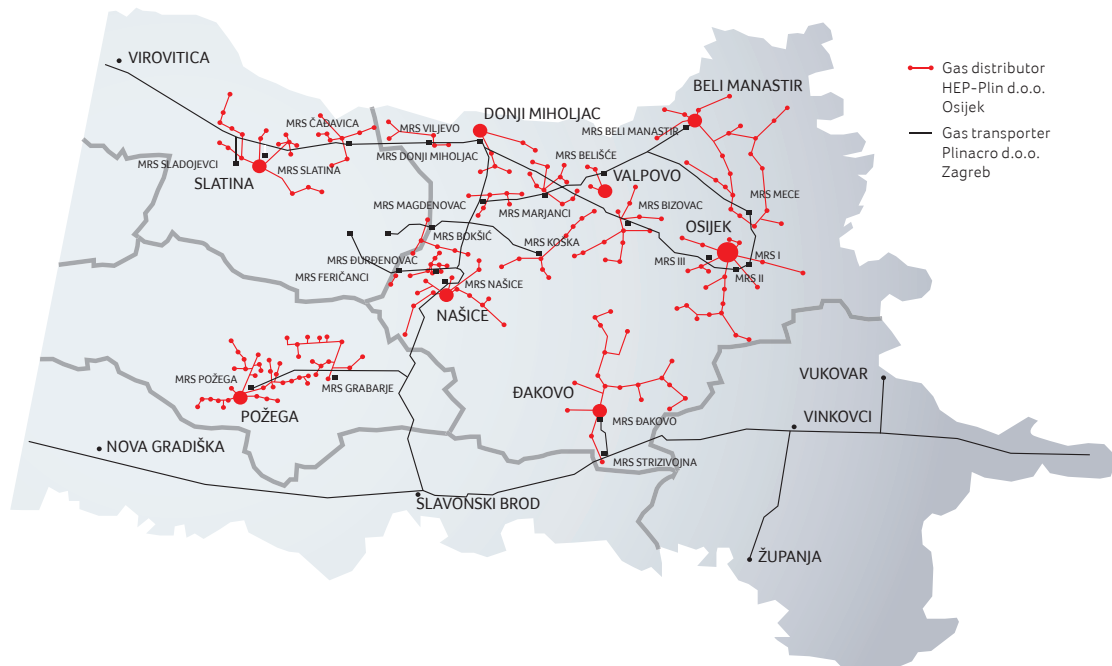
In terms of distribution activities, there is no competition as long as the existing concession agreements are valid and the activity is performed according to contracted terms. If HEP Gas loses the right to distribute gas in some areas, the distribution network owned by HEP Gas will be leased or sold to the new concessionaire, thus compensating for current investments. The monopoly of distribution is restricted by the state under prescribed rights and obligations on part of the distributor as a provider of the public service of gas distribution as well as by regulating and controlling it through HERA, which sets the grid code for gas distribution and regulates the price of its public service.

The business of customer gas supply faces much bigger competition. HEP Gas carries out the supply of households under the public service of supply as an incumbent supplier, while the supply of business customers is faced with a stronger competition than during the year before. There are 55 companies in Croatia with the licence for gas supply. As the gas supply market has still not been fully regulated, some suppliers can offer unreal gas supply prices due to mutual subsidies of gas business.

Upon full gas market opening and the end of price regulation for all eligible customers, we expect permanent and uncertain market competition. On the other hand, gas market opening represents an opportunity for HEP Gas to expand its operations to some other areas either by obtaining concession rights or taking over some smaller neighbouring or even farther energy entities without a solid perspective of independent survival.

Damir Pečušak
Director

HEP-PLIN D.O.O. IN 2014



NUMBER OF CUSTOMERS

Supply area	No. of metering points	Customer category	No. of metering points
Osijek-Baranja County	62,560	TM1-TM4 Residential	69,255
Požega-Slavonija County	8,145	TM1-TM8 Commercial (under 1 m ³)	5,351
Virovitica-Podravina County	3,828	TM9-TM12 Commercial (over 1 m ³)	5
Other counties	78		
Total	74,611	Total	73,932

TM – tariff model

GAS NETWORK

	2013	2014	2014/2013 (%)
Gas lines – owned by HEP d.d. (km)	2,060	2,119	2.9
Gas lines – owned by other parties (km)	492	492	0.0
Gas lines – total	2,552	2,611	2.3
Reducing stations – DRS (number)	52	52	0.0
Odorizers (number)	25	25	0.0

ENERGY BALANCE (103 M3)

	2013	2014	2014/2013 (%)
Procurement (103 m ³)	130,593	119,372	-8.6
Sales (103 m ³)	124,834	114,945	-7.9

GAS SALE STRUCTURE (103 M3)

Customer categories	2013	2014	2014/2013 (%)
TM1-TM4 Residential	74,797	61,844	-17.3
TM1-TM8 Commercial (under 1 m ³)	32,887	39,957	21.5
TM9-TM12 Commercial (over 1 m ³)	17,150	13,144	-23.4
Total	124,834	114,945	-7.9

FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the Owner of HEP Plin d.o.o.:

1. We have audited the accompanying annual financial statements of the company HEP Plin d.o.o., Osijek, Cara Hadrijana 7, (hereinafter "the Company") for the year ended 31 December 2014, which comprise of the Balance sheet / Statement of Financial Position on 31 December 2014; the Statement of Comprehensive Income; the Statement of Changes in Equity; the Cash Flows Statement for the year then ended; and the accompanying Notes to the Financial Statements which concisely set out the principal accounting policies and other disclosures .

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT

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

RESPONSIBILITY OF AUDITOR

3. Our responsibility is to express an opinion on the enclosed Financial Statements based on the audit performed. The audit was performed in accordance with the International Auditing Standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatements. An audit includes performing of procedures to obtain audit evidence supporting the amounts and disclosures in the Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements in the Financial Statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the Financial Statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Company's management, as well as evaluating the overall presentation of the Financial Statements. We believe that auditing proof and evidence collected by us are sufficient and suitable as the basis for our opinion.

OPINION

4. In our opinion, the enclosed financial statements present fairly, in all material respects, the financial position of the Company at 31 December 2014, the financial success and its cash flows for 2014 in accordance with the Accounting Act and International Financial Reporting Standards applicable in the European Union.

EMPHASIS OF MATTER

5. We draw attention to the fact that the Company in the Balance sheet / Statement of financial position at 31 December 2014 has the stated loss over the level of capital in the amount of HRK 5,940 thousand and that the short term liabilities exceed short term assets for the amount of HRK 8,677 thousand. According to Law on financial operations and the pre-bankruptcy agreement, the Company does not fulfill the prescribed conditions for adequacy of capital. The continuation of operations of the Company under the going concern assumption depends on ability of the Company to assure sufficient money assets how to be able to settle the liabilities in time, assure adequate sources of financing. How to attain this, as is described in Note 1 to the

financial statements, a Company's member, HEP d.d. has engaged itself to offer the financial support to Company and the Company's Management makes efforts to improve current operations and the financial position of the Company.

6. As described in the note 1 to the enclosed financial statements, the HEP d.d. has under finance lease agreements leased property, plant and equipment to its subsidiaries. The leases bear interest to the extent that the HEP d.d. has acquired external financing to construct the underlying assets. These liabilities are stated at nominal value because of the specifics of the HEP Group.

OPINION ON THE ADJUSTMENT TO OTHER LEGAL AND REGULATORY REQUIREMENTS

7. The Company's Management is responsible for the preparation of the annual financial statements of the Company for the year ended 31 December 2014 in prescribed form on the basis of the Regulation on the structure and content of annual financial statements (Official gazette No 38/08,12/09,130/10) and in accordance with the other provisions which regulate the operations of the Company ("Standard Annual Financial Statements").The financial information set out in the standard annual financial statements of the Company are in accordance with the information stated in the annual financial statements of the Company shown on pages 4 to 50 which are the subject of our opinion, as set out in the section Opinion.

OPINION ON ADJUSTMENT TO ANNUAL STATEMENT

8. The Company's Management is responsible for the preparation of the Annual statement of the Company. As a result of the provisions of article 17 of the Accountancy Act, we are obliged to express an opinion on adjustment of the Annual statement of the Company with the annual financial statements of the Company. In our opinion, on the basis of the performed audit of the annual financial statements of the Company and the comparison with the Annual statement of the Company for the year which ended 31 December 2014, the financial information set out in the Annual statement of the Company, approved for their issuance by the Company's Management on 10 April 2015, are in accordance with the financial information set out in the annual financial statements of the Company shown on pages 4 to 50 which were the object of our opinion, as set out in section Opinion.

In Zagreb, 24 April 2015

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

Zdenko Balen
member of the Management

Darko Karić, certified auditor

Audit d.o.o.
Baštijanov 52a
10000 Zagreb

Marijana Pranjić,
member of the Management

Dubravka Tršinar, certified auditor

HEP Plin d.o.o., Statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK thousand	HRK thousand
Gas sales	371,490	406,167
Service revenues	1,988	2,522
Income from related companies	2,298	2,445
Other operating income	27,153	27,441
Total operating income	402,929	438,575
Cost of gas purchase and material used	(322,214)	(363,440)
Service expenses	(5,262)	(3,823)
Staff expenses	(20,169)	(18,502)
Depreciation and amortization	(9,342)	(12,152)
Expenses with related parties	(4,486)	(4,601)
Other operating expenses	(34,926)	(38,859)
Total operating expenses	(396,399)	(441,377)
Profit/(Loss) from operations	6,530	(2,802)
Financial income	2,025	379
Financial expenses	(2,048)	(992)
Net financial loss	(23)	(613)
Profit/(Loss) from operations before tax	6,507	(3,415)
Income tax	(2,744)	1,095
Profit/(Loss) for the year	3,763	(2,320)

HEP Plin d.o.o.,
Statement of comprehensive income
For the year ended 31 December 2014 (continued)

	2014	2013
	HRK thousand	HRK thousand
Profit/(Loss) for the year	3,763	(2,320)
Other comprehensive income for the year	-	-
Total comprehensive / (loss) for the year	3,763	(2,320)

Signed on behalf of the Company on 24 April 2015 by:

Damir Pećušak
Director

HEP Plin d.o.o.,

Balance sheet/Statement of financial position

AT 31 DECEMBER 2014

ASSETS	31 December 2014	31 December 2013
	HRK thousand	HRK thousand
Property, plant and equipment	213,652	205,018
Investment in progress and prepayments	4,092	3,964
Intangible assets	219	210
Prepayments for non-current assets	92	297
Deferred tax assets	556	1,848
Total non-current assets	218,611	211,337
Inventories	1,498	1,305
Trade receivables	114,311	104,927
Receivables from related companies	6,893	494
Other current assets	1,129	6,126
Cash and cash equivalents	53,653	23,643
Total current assets	177,484	136,495
Total assets	396,095	347,832

**HEP Plin,
Balance sheet/Statement of financial position
At 31 December 2014 (continued)**

SHAREHOLDERS' EQUITY AND LIABILITIES	Notes	31 December 2014	31 December 2013
		HRK thousand	HRK thousand
Share capital		20	20
Accumulated losses		(5,960)	(9,328)
Total equity	18	(5,940)	(9,308)
Long-term liabilities to related companies	19,24	130,956	114,776
Deferred income	21	82,140	85,593
Other non-current liabilities	20	2,778	3,474
Total non-current liabilities		215,874	203,843
Trade payables	22	5,523	58,582
Liabilities to related companies	24	160,796	81,827
Current portion of long-term liabilities to related companies	19, 24	5,864	7,502
Other current liabilities	23	13,978	5,386
Total current liabilities		186,161	153,297
TOTAL CAPITAL AND LIABILITIES		396,095	347,832

Signed on behalf of the Company on 24 April 2015 by:

Damir Pečušak
Director

HEP Opskrba d.o.o.

HEP Opskrba (HEP Supply) has been operating on the open electricity market for six years. Regardless of its increasing competition, it is still the utmost market leader. Apart from being the first choice of large consumers and businesses, we have experienced a significant success in the acquisition of new household customers.

In 2014, HEP Supply faced the ongoing unfavourable economic trends. Due to special efforts by all our employees, we have remained the first choice of the biggest customers in Croatia, 200 of which account for more than 20 percent of total consumption, which has additionally confirmed our competitiveness in view of large customers who are also the most sensitive in terms of price and security of supply. Our market position is proven daily by competitive prices, clear and transparent supply conditions and service quality. We have achieved a superior result in public procurement procedures among 19 alternative suppliers, by winning more than 76 percent of the total value of published tenders in 2014.

Our business operations strive at meeting ever increasing demands of our customers and the market. Although placing an emphasis on new solutions and innovative products, we also pay special attention to service quality and customer relation. More than 96 percent of customer queries are resolved upon the first call, the number of complaints has been reduced to 0.7 percent, we have engaged five certified mediators for dispute resolution. We built our business relationship on the two-way communication with our customers by responding to their needs with concrete solutions. One such product Let's team up has become very popular with our business customers.

The innovativeness of our ZelEn product was recognized in 2014 by over 30 companies, which follow market trends and stress their socially responsible operations. Funds collected through the sale of ZelEn are dedicated solely to investments into energy efficiency and RES projects integrated in the buildings which will achieve measurable effects of greenhouse gas emission reduction. On the basis of the tender, the first donation was awarded to the Children's Home Ivana Brlić Mažuranić from Lovran for their energy efficiency project. As part of the ZelEn promotion, the campaign called 'A Hundred Green Trees' was launched to plan the environment around HEP hydropower plants.

As part of the ELEN development project, the electric vehicle charging system was set up and eight parking spaces equipped in the garage of HEP's new office building. Five AC/DC fast charging stations were set up in the city of Koprivnica. The project was also promoted at conferences and introduced to interested partners for the building of public charging stations. The cooperation agreement was concluded with over 30 cities and institutions. Charging stations are expected to be set up in the first half 2015. A more than a year from its launch, the Hepi product for households is still positioned as the most innovative service package on the market, confirmed by more than 21,000 households which entered into the agreement with HEP Supply. The competitive price and added benefits including the Hepi Club – loyalty programme, the possibility of self-metering, the 'pay as much as you consume' option, the 24 hour invoice access, on-line agreement conclusion and payment make this product especially attractive for customers.

The traditional annual Meetings with HEP Supply Customers were organized this year in Split, Rijeka, Osijek and Zagreb gathering more than 700 key customers.

Our last year engagement and our socially responsible operations was recognized by awards: Greenovation 2014 for ZelEn as the best Croatian green economy programme in total and the Croatian Energy Award for the significant contribution in the field of the national energy system and industry development as well as the contribution in the establishment of the sustainable and successful business model by introducing nation-wide unique products and services.

Entrepreneurial approach, learning organization, operational excellence, efficiency, customer focus, business excellence and effectiveness are key long term objectives which will serve as the basis for HEP Supply transformation in order to respond to increasing market requirements.

We promote and live the 'Energy among Us' as a team!

Director

Tina Jakaša

NUMBER OF METERING POINTS

Customer category	2013	2014	14/13 (%)
High voltage	47	46	-2.1
Medium voltage	1,365	1,193	-12.6
Low voltage - commercial	79,614	91,300	14.7
Low voltage - public lighting	10,175	12,146	19.4
Low voltage - residential	17	20,655	
Total low voltage	89,806	124,101	38.2
Total	91,218	125,340	37.4

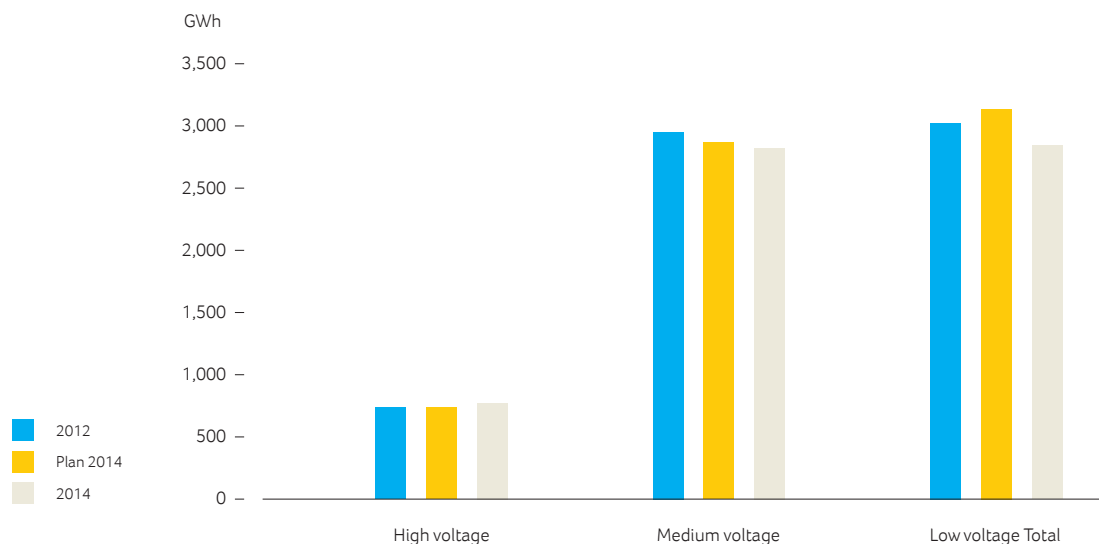
NUMBER OF CUSTOMERS

Customer category	2013	2014	14/13 (%)
Number of customers	34,630	64,949	87.6
Number of metering points per customer	2.6	1.9	-26.9
	MWh/customer	211	99
Electricity sale per customer	HRK/customer	83,526	36,859
			-53.1

ELECTRICITY SALE IN GWH PER CONSUMPTION CATEGORIES (VOLTAGE LEVELS)

Customer category	2013	2014	14/13 (%)
High voltage	776	861	11.0
Medium voltage	3,080	2,782	-9.7
Low voltage - commercial	2,830	2,548	-10.0
Low voltage - public lighting	203	188	-7.7
Low voltage - residential	0.7	54.4	7307.9
Total low voltage	3,034	2,790	-8.0
Total eligible customers in Croatia	6,889	6,434	-6.6
Foreign eligible customers	434	0	-
Total eligible customers	7,323	6,434	-12.2

ELECTRICITY SALE PER VOLTAGE LEVELS



FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the owner of the company HEP Opskrba d.o.o., Zagreb:

1. We have audited the accompanying annual financial statements of the company HEP Opskrba d.o.o., Zagreb (hereinafter "the Company") for the year ended 31 December 2014, which comprise of the Balance Sheet/Statement of Financial Position as of that date; Statement of Comprehensive Income; the Statement of Changes in Equity; the Cash Flows Statement for the year then ended; and the accompanying Notes to the Financial Statements which concisely set out the principal accounting policies and other explanations.

RESPONSIBILITY OF THE COMPANY'S MANAGEMENT FOR FINANCIAL STATEMENTS

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

RESPONSIBILITY OF THE AUDITOR

3. Our responsibility is to express an opinion on the enclosed Financial Statements based on the audit performed. We conducted our audit in accordance with International Standards of Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatements. An audit includes performing of procedures to obtain audit evidence supporting the amounts and disclosures in the Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements in the Financial Statements, whether due to fraud or error. In making these risk assessments, the auditor considers internal controls relevant to the Company's preparation and fair presentation of the Financial Statements in order to conduct audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Company's Management, as well as evaluating the overall presentation of the Financial Statements. We believe that auditing proof and evidence collected by us are sufficient and suitable as the basis for expressing our opinion.

OPINION

4. In our opinion, the enclosed financial statements present fairly, in all significant terms of reference, truthfully and fairly present the financial position of the company HEP Opskrba d.o.o. at 31 December 2014, and its financial performance and the cash flows of the Company for 2014 in accordance with the Accounting Act and International Financial Reporting Standards effective in the European Union.

OPINION ON THE ADJUSTMENT TO OTHER LEGAL AND REGULATORY REQUIREMENTS

5. The Company's Management is responsible for the preparation of the annual financial statements of the Company for the year ended 31 December 2014 in prescribed form on the basis of the Regulation on the structure and content of annual financial statements (Official gazette No 38/08,12/09,130/10) and in accordance with the other provisions which regulate the operations of the Company ("Standard Annual Financial Statements").The financial information set out in the standard annual financial statements of the Company are in accordance with the information stated in the annual financial statements of the Company shown on pages 4 to 44 which are the subject of our opinion, as set out in the section Opinion, above.

Opinion on adjustment to Annual statement

6. The Company's Management is responsible for the preparation of the Annual statement of the Company. As a result of the provisions of article 17 of the Accountancy Act, we are obliged to express an opinion on adjustment of the Annual statement of the Company with the annual financial statements of the Company. In our opinion, on the basis of the performed audit of the annual financial statements of the Company and the comparison with the Annual statement of the Company for the year which ended 31 December 2014, the financial information set out in the Annual statement of the Company, approved for their issuance by the Company's Management on 24 April 2015, are in accordance with the financial information set out in the annual financial statements of the Company shown on pages 4 to 44 which were the object of our opinion, as set out in section Opinion.

In Zagreb, 24 April 2015

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

Zdenko Balen,
member of the Management

Darko Karić, certified auditor

Audit d.o.o.
Baštijanova 52a
10000 Zagreb

Marijana Pranjić,
member of the Management

Dubravka Tršinar, certified auditor

HEP Opskrba d.o.o.,

Statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2014

	2014	2013
	HRK thousand	HRK thousand
Income from related companies	268,345	213,910
Other operating income	23,617	12,821
	291,962	226,731
Purchase of el. energy out of renewable sources' system	(211,504)	(143,893)
Material and spare parts expenses	(539)	(577)
Service expenses	(3,532)	(2,906)
Staff expenses	(12,350)	(10,917)
Depreciation and amortization	(338)	(387)
Costs based on energy balance	(19,719)	(43,236)
Administrative expenses – related companies	(8,230)	(2,835)
Other operating expenses	(34,158)	(21,029)
	(290,370)	(225,780)
Profit from operations	1,592	951
Financial revenues	386	475
Financial expenses	(16)	(236)
Net financial gains	370	239
Profit before tax	1,962	1,190
Income tax	(440)	(266)
Profit for the year	1,522	924

HEP Opskrba d.o.o.,
Statement of comprehensive income
For the year ended 31 December 2014 (continued)

	2014	2013
	HRK thousand	HRK thousand
Profit for the current year	1,522	924
Other comprehensive income for the current year	-	-
Total comprehensive income for the current year	1,522	924

Signed on behalf of the Company on 24 April 2015 by:

Tina Jakaša

Director

HEP Opskrba d.o.o.,

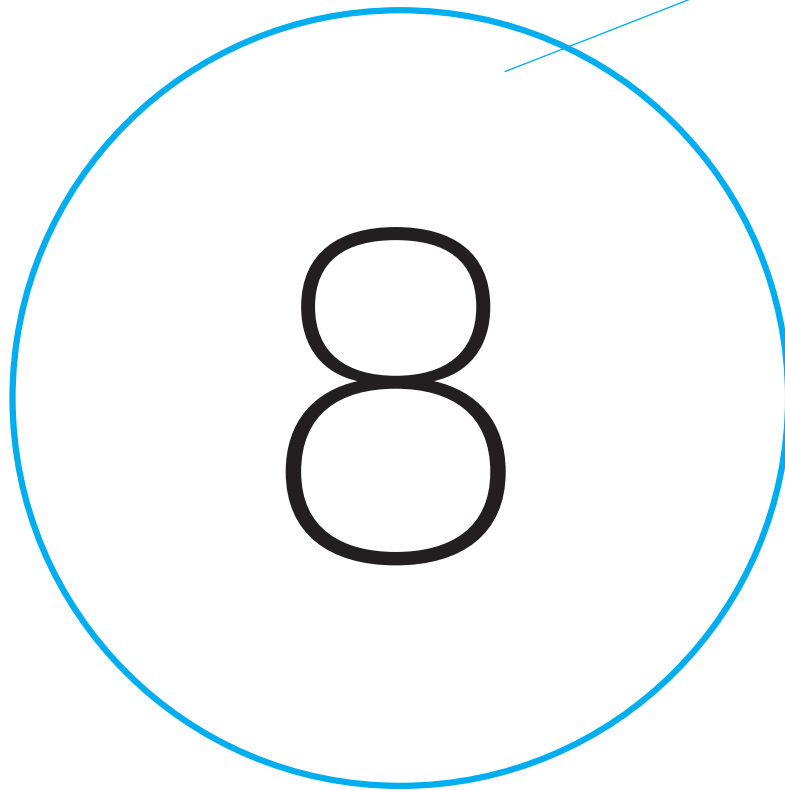
Balance Sheet/Statement of financial position

AT 31 DECEMBER 2014

ASSETS	Notes	31 December 2014	31 December 2013
		HRK thousand	HRK thousand
Intangible assets	8	213	240
Prepayments for tangible assets		3	-
Property, plant and equipment	8	1,049	1,659
Long-term loan receivables	9	129	129
Deferred tax assets	7	123	200
Total non-current assets		1,517	2,228
Trade receivables	10	427,948	456,678
Receivables from related companies	16	45,313	45,182
Inventory of real estate's acquired by pre-bankruptcy settlement		132	4,904
Other short-term asset	11	17,950	20,960
Cash and cash equivalents		15,315	11,664
Total current assets		506,658	539,388
TOTAL ASSETS		508,175	541,616
EQUITY AND LIABILITIES			
Share capital		20	20
Retained earnings		1,522	924
Total equity	12	1,542	944
Long-term liabilities to related companies	16	1,583	890
Other long-term liabilities	13	612	1,002
Total non-current liabilities		2,195	1,892
Trade payables	14	42,646	17,144
Liabilities to related companies	16	434,072	485,763
Other current liabilities	15	27,720	35,873
Total current liabilities		504,438	538,780
TOTAL EQUITY AND LIABILITIES		508,175	541,616

Signed on behalf of the Company on 24 April 2015 by:
Tina Jakaša, Director

REPORTS BY OTHER
HEP GROUP COMPANIES



HEP Trgovina d.o.o.

HEP-Trgovina d.o.o. (HEP Trade) has operated as a company within HEP Group since 2007. During 2014, the company fulfilled all its business tasks by optimizing the operation of HEP Group power plants in combination with the purchase and sale of electricity in the electricity market. In discharging its day-to-day work, the company needed to adjust to the changing conditions in the electricity market, electricity consumption volatility, changeable hydrology and sporadic unavailability of generating plants.

HEP Trade is in charge of entering into the contracts for gas purchase and sale, transport system capacity lease, organizing and managing the gas balance responsible group, CO₂ emission and green certificate trading on foreign markets.

During 2014, HEP Trade continued its activities relating to the operation of foreign companies in the neighbouring countries focusing on increasing profits by achieving lower prices in electricity buying and selling. The Croatian accession to EU provided HEP d.d. with the possibility of its direct access to liquid West European electricity, gas, coal and CO₂ emission market. All wholesale electricity sale and purchase transactions in the EU were transferred from HEP Trade foreign daughter companies onto HEP d.d., primarily to achieve better operational liquidity and reduce operating costs. Therefore, the recorded trading volume of HEP Trade daughter companies in 2014 was 1,474 GWh, which is 40 percent less compared to the achieved trading volume in 2013. The market access in non-EU countries (Serbia, B&H, Kosovo) is still maintained through HEP Trade daughter companies.

HEP Trade purchases gas in the name and for the account of HEP d.d. for supplying thermal power plants and cogeneration plants of HEP Generation as well as HEP Gas business customers. In March 2014, HEP d.d. entered into the register of balance responsible parties on the gas market while HEP Trade entered the same register in May 2014. This entry into the register of balance responsible parties secured the gas transport system capacity lease as well as gas trade on the virtual trading point. A total of 4,027 GWh of gas was purchased for 2014, which is 8.4 percent less than planned due to above average temperatures during the heating season resulting in decreased gas consumption by a portion of customers (HEP Gas) and the lower need for heat energy generation (HEP Generation).

Apart from the bilateral purchase of CO₂ emissions, as of April 2014 HEP Trade participates in the name and for the account of HEP d.d. in primary auctions for the procurement of CO₂ emissions organized by the EEX exchange. During 2014, a total of 5,881,000 tonnes of CO₂ emissions was purchased, covering all HEP Group needs for CO₂ emissions in electricity and heat energy production in 2014 and 2015.

Total electricity consumption in Croatia was 16,922 GWh, which is 2.2% less than in 2013, and 2.1 less compared to the consumption planned in the energy balance. The share of HEP tariff and eligible customers in the consumption structure is 96 percent. The consumption of HEP Group customers accounted for 14,932 GWh, of which 1,960 GWh was allocated to the consumption of customers outside HEP Group. In late 2014, the market share of suppliers other than HEP Group was 15.3 percent.

Due to extremely favourable hydrology, hydro generation recorded in 2014 was record high of 8,356 GWh (68 percent more than planned) and 47 GWh more than the current all-time maximum in 2010. Hydro power plants had thus covered 56 percent of total HEP customer consumption. Recorded energy value of water flows amounted to 8,700 GWh, which is 75 percent more than planned.

Thermal generation was 37 percent lower than planned due to the generation cost optimization. The record-low fuel oil consumption of 29,595 tonnes was recorded, which is by 52.5 percent less than planned, while the gas consumption amounted to 367.4 m³, 33 percent less than planned. In light of the above mentioned energy circumstances, the electricity import amounted to 1,853 GWh i.e. 33% less than planned, while the export volume was 12 times higher than planned (primarily due to exceptionally favourable hydrology. During 2014, the trading volume recorded was 3,953 GWh, which is 35.1 percent more than planned.

Director

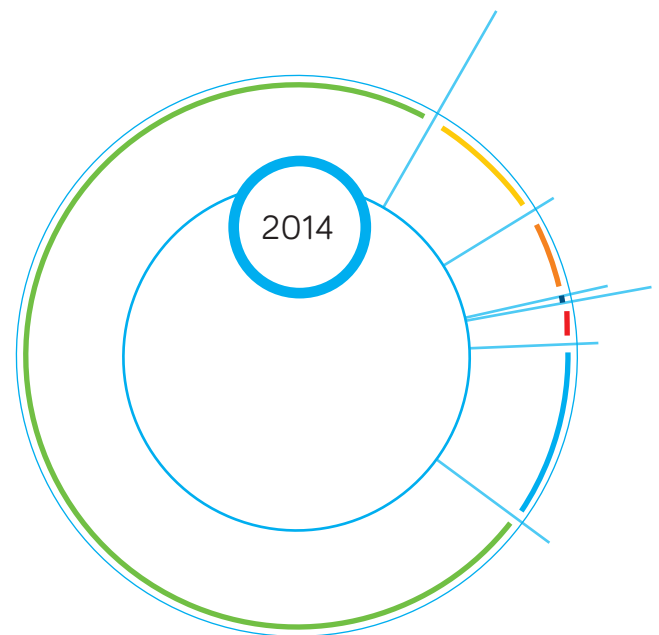
Ante Ćurić

ACHIEVED IN 2014 – ENERGY DATA

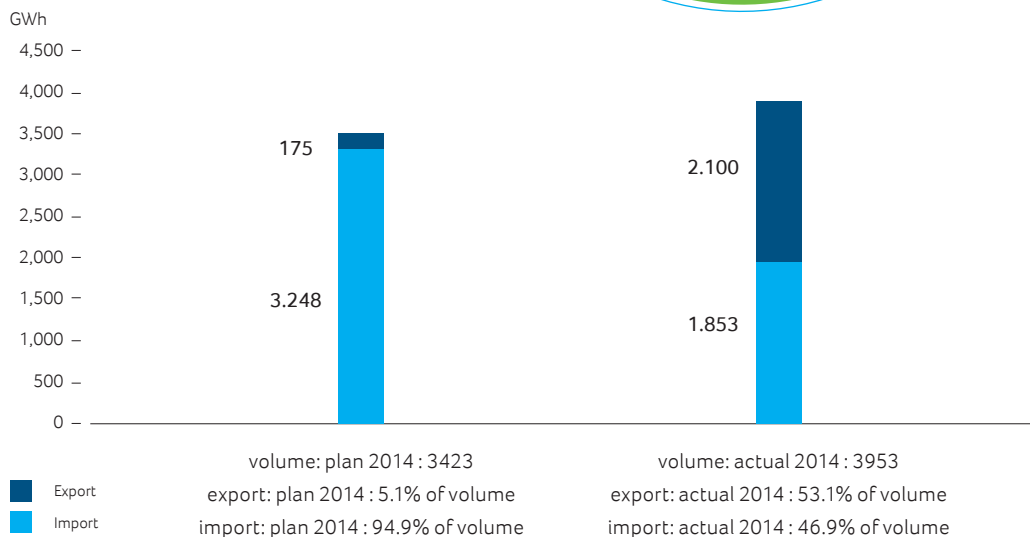
	GWh				
	2013	2014	2014/2013 (%)	2014 (plan)	2013/2013 (%) (plan)
Electricity consumption Croatia	17,296	16,922	-2.2	17,280	-2.1
Electricity consumption HEP	16,618	14,962	-10.0	15,930	-6.1
Hydro generation	8,054	8,356	3.7	4,978	67.9
Thermal generation	2,629	1,450	-44.8	2,286	-36.6
NPP Krško	2,518	3,030	20.3	2,950	2.7
TPP Plomin B	1,448	1,441	-0.5	1,500	-3.9
Import	3,649	1,853	-49.2	3,248	-42.9
Export	-2,347	-2,100	-10.5	-175	1100.0
Producers outside HEP Group	18	19	5.6	27	-29.6
Eligible producers	649	913	40.7	1,116	-18.2
Total available electricity HEP	649	1,960	189.1	1,350	45.2
Total available electricity Croatia	16,618	14,962	-10.0	15,930	-6.1
Total available electricity in Croatia	17,296	16,922	-2.2	17,280	-2.1

STRUCTURE OF ELECTRICITY CONSUMPTION IN 2013 (GWH; %)

HEP customers	12972	77%
Customers outside HEP	1960	12%
Transmission losses	506	3%
Pumping energy	168	1%
Distribution losses	1257	7%
Other consumption	59	0%



HEP D.D. TRADING VOLUME



HEP Opskrba plinom d.o.o.

HEP - Opskrba plinom d.o.o. (HEP Gas Supply) is a new HEP Group company established on 5 May 2014 for the performance of business activities connected with the provision of gas supply. The Company operates in business activities of trade mediation on domestic and foreign markets, contracting the procurement and sale of fuel (natural gas) for the needs of public service users, companies within HEP Group and other end customers. The Company optimizes the gas portfolio of the balance responsible group under the organization and management of HEP d.d. for the needs of suppliers under public service obligation.

On 27 February 2014, the Croatian Government adopted the Decision on appointing the supplier on the gas wholesale market (Official Gazette 29/14), under which HEP d.d. was appointed the supplier of the gas wholesale market for the period between 1 April 2014 until 31 March 2017. During said period, the supplier of the gas wholesale market has been allocated 70 percent of the overall available number of standard storage capacity packages. The wholesale market supplier shall procure gas from the natural gas producer in Croatia under regulated terms and sell it to suppliers under the public service of supply ensuring safe and reliable gas supply.

Under the Mutual Relations Agreement concluded with HEP d.d., HEP Gas Supply conducts the business of the supplier of the gas wholesale market in the name and for the account of HEP d.d. During 2014, the procedure of contracting the fuel (gas) procurement was conducted, Contractual Terms for Gas Sale to the Supplier under Public Service Obligation published and contracts with suppliers under the public service obligation concluded. Annual, monthly and daily transport system capacities were reserved under the planned consumption of the balance responsible group on the information platform of the transport system operator. Annual standard storage capacity packages of the gas storage system operator were also reserved. By diversifying input gas volumes i.e. by combining the use of storage capacity and input gas volumes on the virtual trading point, the required storage occupancy as of 31 December 2014 was met in line with the instruction of the Ministry of Economy. This ensured sufficient gas capacities from the storage system for providing safe and reliable gas supply to protected customers in line with the findings of the stress test under the Ordinance (EU) 994/2010. By conducting daily gas transport system and balance responsible group balancing as well as by conducting trade transactions on the virtual trading point, all Company's obligations and duties as the appointed seller of annual balancing energy were met. All operating challenges were successfully responded through daily portfolio monitoring and the communication with partners for the purpose of optimizing the balance responsible group management and ensuring the timely and quality submission of information.

According to transporter system operator data, total gas volume supplied to customers in the Republic of Croatia in 2014 was 22,381 GWh, which is a 13.5 percent decrease compared to 2013. The share of HEP d.d. as the supplier on the gas wholesale market was 14 percent i.e. 3,021 GWh of gas supplied in the period from 1 April until 31 December 2014. During 2014, HEP Gas Supply recorded total income of HRK 800,880,532 in the name and for the account of HEP d.d.; receivables of HRK 990,469,753 and the 100% collection.

For the purpose of improving and monitoring market trends, HEP Gas Supply employees participated in conferences in Croatia and abroad. The workshop for the suppliers under the public service was also organized which focused on presenting all relevant gas related information for 2014/2015. To be able

to successfully respond to market challenges, it has been planned to employ more professionals during 2015 and to equip the Company with the new business-information system which will provide the quality monitoring support of the Company's current and future business activities.

The openness of the European energy market and the experience of near markets encourage the need to create new energy products even faster for increasing the competitiveness of HEP Group companies and facilitate their strengthening and energy market positioning in both Croatia and in the surrounding countries. The increasing openness of the energy market as well as the time-limited role of the gas wholesale market supplier in Croatia for the suppliers under the public service obligation requires the definition of strategic objectives of gas business development within HEP Group until 31 March 2017. It is our goal to ensure all preconditions and prepare the Company for its active inclusion into the Croatian gas market following its full liberalisation by taking over those customers who use the public service of supply, by retaining the existing customers i.e. gas suppliers who currently conduct the public service of supply and by acquiring business customers.

HEP Gas Supply is prepared to become a part of the service definition process and the offer of a new energy product to end customers together with other companies of HEP Group. This would increase efficiency and optimize the cost of operational control, monitoring and management stemming from contractual obligations with other gas market stakeholders as well as optimize and reduce gas procurement cost for the need of HEP Group.

In conclusion, HEP Gas Supply in the cooperation with all the departments of HEP d.d. and other HEP Group companies successfully responded to all business challenges in 2014 by monitoring legislation changes and executing all legally prescribed obligations in the name and for the account of HEP d.d. set under regulations, general acts and decisions adopted by the Croatian Government.

Director

Marko Blažević

HEP ESCO d.o.o.

HEP ESCO was founded for developing, executing and funding energy efficiency projects according to the ESCO model (Energy Service Company), under which all project investments are returned through energy savings after the investment has been completed.

During eleven years of its operation and more than 60 successfully conducted projects in building design and construction, industry, public lighting and energy supply systems, HEP ESCO has become recognizable as a company for developing, managing and funding energy efficiency and RES projects in public and private sectors.

In 2014, HEP ESCO continued preparing numerous market-based projects. As industry being the key segment of ESCO project development, the following projects were either completed or commenced:

- the construction of nine photovoltaic power plants on building roofs owned by HEP d.d.;
- the implementation of energy efficiency measures in the lighting system of ELKA plant, Phase 2;
- the implementation of energy efficiency measures in PPK plants;
- the construction of the cogeneration facility and the biomass dryer at the Tršće site (1 MWe) of Orkan Energija;
- energy efficient upgrade of the outdoor, indoor and temporary lighting in Viktor Lenac Shipyard;
- the energy efficiency project by implementing the heat energy recovery measure from compressors K3 and K4 inside the F facility and compressors K5 and K6 in the D facility of Elektrokontakt.

Apart from conducting its ESCO projects, HEP ESCO expanded its energy services to a number of consulting services offered to its clients. During 2014, HEP ESCO offered building certification services, energy audits of buildings, development of detailed investment studies, introduction of energy management, energy consumption optimization as well as system management and introduction of energy and water consumption remote readings

HEP ESCO and its potential clients prepared a number of consulting services, most of which for facility certification.

During 2014, HEP ESCO continued to develop new products and services. The ESCO Monitor® is a computerised business system for systematic energy management providing the monitoring of building's energy features and systems, public lighting installations, industrial plants and RES systems. It was envisaged as a computerised support to ESCO projects implementation as well as to the introduction of new services such as the energy consumption optimization within the systematic energy management service. The ESCO Monitor will ensure not only the above mentioned energy effect based contracts but also the introduction of new HEP ESCO services through energy consumption optimization agreements. ESCO Monitor® Panel is an addition to the core product, primarily intended for communication with employees.

During spring and autumn of 2014, HEP ESCO Training Center conducted two specialized courses in energy efficiency and RES - Certified Expert for the use of the RETScreen® software and Certified Expert for savings measuring and verification. It also launched the education for Energy Management under ISO 50001 in the cooperation with the Croatian Metrology Society. During 2014, HEP ESCO agreed with Pliva the education programme called Green Office.

In the cooperation with HEP Supply, HEP ESCO launched the implementation of the energy efficiency project in the Children's Home Ivana Brlić Mažuranić from Lovran – Rijeka Branch Office, funded by ZelEn project funds dedicated for energy efficiency and RES projects.

ESCO service as well as products and services of HEP Group as a whole have been continuously promoted through the offer of new energy services in direct contact with potential clients and market partners.

In 2014, HEP ESCO continued its partnership activities on three EU funded projects. All three projects build on HEP ESCO experience and knowledge required for their execution as well as EU financial strategic determinants and objectives.

Director

Vlasta Zanki

HEP Obnovljivi izvori energije d.o.o.

HEP-Obnovljivi izvori energije d.o.o. (Renewable Energy Sources) is a company specialized in the organization and operational management of construction, management, operation and maintenance of RES facilities for electricity and heat energy generation for the purpose of achieving sustainable development and meeting HEP Group's environmental protection objectives. The organization and business management of RES project research, development and preparation is carried out within the company as well. HEP RES participates in the energy market as an investor into RES run plants and as such equally competes with other market investors. The majority of HEP RES activities in 2014 was connected with the preparation and organization of the potential cooperation with partners on the joint development of several wind farm projects by means of joint ventures. One form of such cooperation was the acquisition of business shares in the companies which were lead partners in projects of various development degree, from those with only the construction permit and the concluded electricity purchase agreement with HROTE to those which have been operational. A short-term interest of HEP in this segment is focused on the acquisition of wind farm projects undergoing the process of construction development or with already built capacities. Continuing with the activities commenced in 2013 with a certain number of expressed interests for the cooperation on the windfarm projects in various development degrees and under the earlier announced HEP's public invitation to interested potential partners, the development of strategic and operational documents had commenced followed by comprehensive activities necessary for the preparation of potential acquisitions (due diligence preparation and execution, transaction structuring and negotiations with potential partners).

In the second half 2014, the pre-project documentation and feasibility studies for several solar power plants on HEP's roof surfaces was completed. Business decisions regarding the construction of photovoltaic power plants will be adopted depending on the Croatian policy in the RES sector.

During 2014, the company continued its activities on the development of own wind farm projects, particularly the measuring campaign by using three 100 m high metering poles for measuring wind characteristics funded by the KfW loan.

During 2014, technical solutions for installing small hydro units in several existing water-based facilities were completed i.e. the reconstruction of several abandoned small hydropower plants as well as the underlying documentation for incorporating the project into physical plans.

In the field of environmental protection, HEP RES's plan for the implementation of renewable energy sources was incorporated in the HEP Group's Plan for reducing CO₂ emissions.

The work on the development of new competencies and raising awareness of the role of renewable energy sources within and outside HEP Group continued, in professional communities and among general public.

Taking the above into consideration, it can be asserted that the successful delivery of the objectives continued in accordance with the company's mission and vision as well as further development of quality projects and the participation in EU projects which have opened the possibilities for further advances and the expansion and for better positioning of HEP RES on the RES market.

Director

Hubert Bašić

Program Sava d.o.o.

Pursuant to the Decision adopted by the Croatian Government, the Programme of development, re-regulation and use of the Sava River and its river banks from the border with Slovenia to the city of Sisak continued aimed at the stabilization of subterranean water levels, enhancement of flood protection systems and the multi-purpose use of the river. Apart from financial contributions from HEP and Hrvatske vode to the Programme development, last year it was joined by the Environmental Protection Fund, the Agency for Inland Waterways, the Sisak-Moslavina County, the Zagreb County and the City of Zagreb. The international consultancy consortium of MottMacdonald–WYG–Atkins, which was entrusted with the development of feasibility study and the strategic environmental impact assessment study funded by EU, last year successfully prepared three comparable system alternatives. The following was prepared and analysed: Option 0 (minimum interventions without energy use of the river), Option 1 (the water wave flows through Zagreb) and Option 2 (the water wave flows next to Zagreb through the flood relief channel). By using the multicriteria analysis method, 20 experts and representatives of non-government organizations from the Professional Council set the metrics and evaluated the above options. As the highest number of grades was awarded to Option 2 developed in 2013, its comprehensive feasibility study continued to be developed. The participation of academic community in the selection of the most appropriate option is in line with the sustainable development principles, especially transparency of all programme solutions.

Under the decision of the Ministry of Economy, the development of the strategic environmental impact assessment study started by defining its content. Similar to the multi-criteria analysis, the invitation to comment was sent to civil society organizations engaged in environmental protection issues so as to include their opinion from the very start of the development of said document and ensure its sustainability. During 2014, the Programme sustainability was assessed under the Hydropower Sustainability Assessment Protocol Methodology. It has thus become the first project in the world to be assessed during such an early development stage. The Methodology was jointly developed by organizations such as Transparency International, WWF, Nature Conservancy and financial institutions including the World Bank and the CITY Group. The methodology aims at identifying sustainable projects with a decreased investment risk. The assessment was conducted by International Hydropower Association professionals from Great Britain, Germany, Sweden and China. The Programme met basic sustainability criteria in all nine assessed categories.

In view of all which has been done to date, the Croatian Government listed the first system facility, Podsused Hydropower Plant, among Croatian projects bidding to be included in the EU Investment Plan. This facility has become a part of this 300 million euro worth European plan.

The delivery of the HPP Podsused project will be launched in the forthcoming period. Its construction start is expected in 2017, while the completion of the strategic EIAS and the entire Programme feasibility study is expected until end October 2015.

Director

Dubravko Ponoš

HEP Telekomunikacije d.o.o.

HEP-Telekomunikacije d.o.o. (Telecommunications) was established on 31 October 2013 under the Articles of Association of the limited liability company signed between the founder and members of Hrvatska elektroprivreda d.d., HEP Distribution System Operator d.o.o. and the Croatian Transmission System Operator d.o.o. During 2014, employees of the IT and Telecommunications Department of HEP d.d., mainly employed on telecommunication activities, were transferred into HEP Telecommunications d.o.o. and continued to conduct their business activities. On 7 October 2014, the Management Board of HEP d.d. adopted the Decision on the division i.e. the transmission of competence of business activities conducted by the IT and Telecommunications Department of HEP d.d. onto HEP Telecommunications d.o.o.

HEP-Telecommunications provide the support to the operation of HEP Group as a whole. In the area of telecommunication technology, HEP Telecommunications control the telecommunication infrastructure and the telecommunication system of the Company and HEP Group as a whole. The telecommunication infrastructure includes all passive telecommunication equipment and systems (optic infrastructure, antenna towers etc.), while the telecommunication system includes all active network equipment, accompanying systems and equipment. HEP Telecommunications have the sole jurisdiction over the following tasks: defining general telecommunication rules, standards and procedures in the development and use of telecommunication infrastructure and system of the Company and HEP Group as a whole; planning, designing, development, construction and maintenance of telecommunication infrastructure and system of the Company and HEP Group as a whole.

During 2015, the replacement of the 10-thread OPGW and the underground optic cable is planned primarily along HEP's main fiber-optic infrastructure. The list of routes has been prepared and the execution priorities defined. The upgrade of the LAN/WAN network is planned for 2015 in the part regarding the installation of the active and passive network equipment in the facilities with new optical network (OPGW and PSK), the installation of the equipment for resolving site redundancies (own infrastructure or leased lines on the telecommunication market), and the upgrade of the LAN network on sites (structured cabling, upgraded switch for LAN connection, wireless network).

Apart from the upgrade of the access part of the network, the upgrade of the LAN/WAN network also includes the IP network framework i.e. routers located in Zagreb, Split, Rijeka and Osijek datacentres and the setting up of 1G and 10 G connections in the framework via DWDM, EWDM and CWDM technologies.

The existing DWDM transmission system of HEP will be upgraded with new user cards and interfaces according to DWDM system users.

The upgrade of the SDH transmission system includes the replacement of the outdated SDH equipment, the upgrade of the existing system according to SDH system user requirements, and the connection of facilities containing new optical connections (OPGW and PSK) with the SDH system (equipment installation). In light of the above, the strategic focus needs to be set so as to continue with the maintenance and the use of the SDH system as long as there is the need expressed by HEP Group members.

In 2015, we plan to establish a centralized and single ITSM service management of the SLA according to standards and certifications. The Company wishes to improve the telecommunication infrastructure management, to control and upgrade operating activities, improve business results, achieve a measurable return of investment, and measure the TCO (Total Cost of Operation). The above can be achieved by introducing the IT Service Management based on ITIL best practices (IT Infrastructure Library). The main objective is to significantly increase user efficiency and satisfaction by reducing costs.

Director

Željko Rakanović

HEP Odmor i rekreacija d.o.o.

HEP – Odmor i rekreacija d.o.o. (HEP Leisure and Recreation) was established to provide vacation and recreation services to HEP Group employees

The Company intends to conduct its operations in a market-wise sustainable manner by using property in an optimal manner focusing on better utilization of its portfolio market potential and increased organizational and management efficiency. Keeping tourism subsidies for HEP Group employees also represents one of our clear objectives along with a potential expansion onto the commercial market.

In 2014, there were vacation houses available to HEP Group employees on 15 locations along the Adriatic Coast. These units are used only by HEP Group employees based on the results of the competition for the use of vacation houses. External guests can use the vacation house located at Biograd 2 hostel and Karlobag sites. The competition for the use of vacation houses is valid for the period from June 20 to September 8 each year and the employees use the units in ten-day shifts (eight shifts).

The intention of the Company is to extend the season to at least 120 days and in certain vacation houses to a year-round operation. During 2014, there were 29,766 overnight stays.

In 2014, the Company set the task of completing facility reconstruction projects resulting in more facilities with defined categorization and increased income from its core activity.

In 2014, regular maintenance funds were used according to the adopted plan aimed at the improvement of accommodation capacities under the management of HEP Leisure and Recreation. 91.4 percent of investments were carried out. The process of equipping two-, three, or four- star standard facilities (construction and adaptation in Karlobag, Jadrija, Biograd 1, Preko 1 vacation facilities) commenced, while the reconstruction of Pakoštane and Rovanjaska facilities was finished.

An important part of the activities conducted included the issuance of facility categorization decisions, the resolution of property legal issues, entry into land registry, facility legalization and the issuance of operational permits.

Director

Karolina Juzbašić

*As of April 2015, the company changed its name to HEP-Asset Management d.o.o. Stanko Kežman was appointed the new company director.

Ustanova HEP

Nastavno-obrazovni centar

HEP – Nastavno obrazovni centar (HEP Education and Training Center) in Velika is primarily intended for education and professional improvement of HEP Group employees in live work technology. It is also intended for the education and professional development of HEP Group employees in other technologies according to HEP Group's requirements. Having been approved and registered as an institution, the Center has also been granted public access.

The verification of training and professional improvement programmes met all legal preconditions for acquiring new qualifications and knowledge. Education, provided for employees of other companies, represents a significant source of income for HEP NOC. The Centre has expanded its activity to include periodical testing of personal protective equipment and insulation tools in the control-testing laboratory accredited by the Croatian Accreditation Agency.

Under the Secondary Education Act and the Center's Articles of Association, the Steering Committee adopted the Annual Plan and Programme of HEP NOC Operations – adult education during the school year 2013/2014. The form and content of said plan and programme has been harmonized with positive experiences from similar institutions based on objectives and requirements of HEP Group. The plan was based on own experience gathered during previous years of autonomous operations. HEP NOC offers a total of 16 verified education programmes.

The Control-Testing Laboratory of HEP NOC expanded the scope of its work in periodic testings (controls) of insulation tools and equipment used in HEP DSO (Elektra Sisak is the new service user) to users outside HEP Group.

It has been concluded that all our plans have been delivered as planned. A significant source of income during the circumstances of lower engagement of our capacities by HEP companies came from the export of LV live work technology to Slovenia and the education of private company employees. Therefore, one of the characteristics of the last business year was the focus of HEP NOC activities on the companies nearby and setting objectives for furthering successful cooperation with companies from the Republic of Slovenia, especially Krško Nuclear Power Plant, Power Plants on the River Sava and Elektro Maribor, Elektro Gorenjska and Elektro Ljubljana.

In terms of educational and accommodation occupancy, during the eight year of its autonomous operation, HEP NOC achieved solid occupancy in all the months except a part of July and August, when collective vacations are used. A total of 5,012 people stayed the night in 2014, mainly in the full-board arrangement. Almost 1520 people participated in education programmes, seminars, work groups and conferences.

In 2014, the control-testing laboratory received, reviewed and tested 992 units of specialized insulation tools and personal protective gear. In terms of tool testing, HEP NOC established a successful cooperation with 18 customers. Even higher capacity occupancy is expected in future under the cooperation with several new customers on work safety improvement by testing tools in the control-testing laboratory of HEP NOC. During 2014, the andragogue schooling attendance continued as well as the participation in the professional gatherings of EDZ, CROLAB etc. The most significant professional event in 2014 was the ICOLIM Conference in Hungary during which the members of the European Live Work Association adopted the Guidelines for Further Development.

Head

Zdenko Miletić

Notes

TIMEFRAME OF THE REPORT

This Annual Report gives an overview of the business year 2014 – from January 1 to December 31, 2014. Data on the events important for HEP Group operations occurring after December 31 are also given, but no later than June 30, 2015

FINANCIAL REPORTS OF HEP GROUP COMPANIES

In the financial reports of the companies in the Chapter 'Reports by HEP Group Companies with Financial Statements', the authorized auditor provides references to the notes which are an integral part of the financial statements. In this Annual Report, due to its scope, accompanying notes are not provided. The full statements with notes are available at HQ of the companies concerned.

CROATIAN TRANSMISSION SYSTEM OPERATOR DATA PRESENTATION

The Croatian Transmission System Operator Ltd. (HOPS), unbundled from HEP Group in 2013 under the Electricity Market Act and according to the independent transmission operator (ITO) model, has been presented in this Annual Report only under Business Operations in 2014 and in the Consolidated Financial Statements for HEP Group together with the Report from Independent Auditor. In line with the independent status of HOPS, data regarding its business operations have not been displayed in any other chapters of the 2014 Annual Report.

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