

Croatian Telecom Inc.

Financial statements

31 December 2013

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Supervisory Board

The members of the Supervisory Board who served during 2013 and subsequently are as follows:

Mark Klein	Chairman	Member from 25 April 2012 Chairman from 10 September 2012
Ivica Mišetić, Ph. D.	Deputy chairman	Member from 21 April 2008 Deputy chairman from 8 May 2008
Oliver Morbach	Member	Until 17 June 2013
Dr. Ralph Rentschler	Member	From 15 December 2003
Dr. Oliver Knipping	Member	From 25 April 2012
Dr. Kathryn Walt Hall	Member	From 21 April 2008
Mark Nierwetberg M. A.	Member	From 17 June 2013
Ilias Drakopoulos, Ph. D.	Member	From 17 June 2013
Juko Cikojević	Member, workers' representative	From 1 January 2011
Damir Grbavac	Member	From 25 April 2012

Management Board

The members of the Management Board who served during 2013 and subsequently are as follows:

Ivica Mudrinić	President	Until 31 December 2013
Davor Tomašković	President	From 1 January 2014
Dino Ivan Dogan, Ph. D.	Member	From 1 April 2011
Božidar Poldrugáč	Member	From 15 March 2007
Irena Jolić Šimović	Member	From 1 August 2006
Norbert Hentges	Member	From 1 September 2012
Nataša Rapaić	Member	From 1 February 2013
Jens Hartmann	Member	From 17 June 2013

Responsibility for the financial statements

Pursuant to the Croatian Accounting Act in force, the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union ("EU") give a true and fair view of the financial position and results of Croatian Telecom Inc. (the "Company") for that period.

The Management Board has a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Management Board continues to adopt the going concern basis in preparing the financial statements.

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

- suitable accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- applicable accounting standards are followed; and
- the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

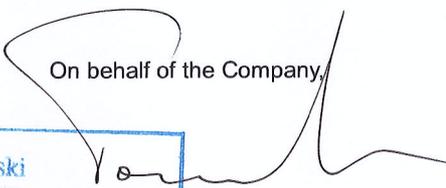
The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and must also ensure that the financial statements comply with the Croatian Accounting Act in force. The Management Board is also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The accompanying financial statements were approved for issuance by the Management Board on 11 February 2014.

Croatian Telecom Inc.
Savska cesta 32
10000 Zagreb
Republic of Croatia

11 February 2014

On behalf of the Company,



Mr. Davor Tomašković
President of the Management Board (CEO)



Independent auditor's report

To the shareholders and Board of directors of Croatian Telecom Inc.

We have audited the accompanying financial statements of Croatian Telecom Inc. (the 'Company') which comprise the statement of financial position as at 31 December 2013 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted in the European Union, and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these 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 whether 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 judgement, 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 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

In our opinion, the financial statements present fairly, in all material respects, the financial position of Croatian Telecom Inc. as at 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted in the European Union.

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Commercial Court in Zagreb, no. Tt-99/7257-2, Reg. No.: 080238978; Company ID No.: 81744835353; Founding capital: HRK 1,810,000.00, paid in full; Management Board: Hrvoje Zgombic, President; J. M. Gasparac, Member; S. Dusic, Member; T. Macasovic, Member; Giro-Account: Raiffeisenbank Austria d.d., Petrinjska 59, Zagreb, IBAN: HR8124840081105514875.

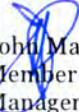


Emphasis of matter

Without qualifying our opinion, we draw attention to Notes 11 and 27 b) to the financial statements, which describe the uncertainty related to the ownership of distributive telecommunications infrastructure (DTI) of which the net book value recognised as assets by the Company as at 31 December 2013 is HRK 838 million. Efforts are being undertaken by the Company to obtain certain legal documents and registrations necessary to fully evidence the Company's ownership of these assets. The Company is defending a lawsuit claiming ownership of DTI in the city of Zagreb together with a demand for payment of HRK 390 million plus interest in respect of the Company's use of these assets in prior years. The Company has not recognised any adjustments to its assets and liabilities in respect of these matters due to the uncertainty as to their outcome and their impact on the financial statements.


PricewaterhouseCoopers d.o.o.
Zagreb, 12 February 2014


pwc
PricewaterhouseCoopers d.o.o.³
za reviziju i konzalting
Zagreb, Ulica kneza Lj. Posavskog 2


John Mathias Gasparac
Member of the
Management Board


Hrvoje Zgombić
President of the
Management Board


Tamara Mačašović
Certified Auditor

Statement of comprehensive income
For the year ended 31 December 2013

	Notes	2013 HRK millions	2012 HRK millions Restated
Revenue	3	6,418	6,984
Other operating income		116	141
Merchandise, material and energy expenses		(712)	(619)
Service expenses	4	(806)	(955)
Employee benefits expenses	6	(993)	(1,092)
Work performed by the Company and capitalised		97	82
Depreciation, amortization and impairment of non-current assets	5	(1,313)	(1,278)
Other expenses	7	(1,197)	(1,237)
Operating profit	3	1,610	2,026
Finance income		51	79
Finance costs		(61)	(58)
Finance (costs)/income – net		(10)	21
Share from investment in joint venture	13	21	25
Profit before income tax		1,621	2,072
Income tax expense	8	(189)	(392)
Profit for the year		1,432	1,680
Other comprehensive income/(loss) for the year			
Items that will not be reclassified to comprehensive income			
Remeasurement of post employment benefit obligations		25	(3)
Equity-settled share based payments		0	0
		25	(3)
Items that may be subsequently reclassified to comprehensive income			
Change in value of available-for-sale financial assets		(0)	2
		(0)	2
Other comprehensive income/(loss) for the year, net of tax		25	(1)
Total comprehensive income for the year, net of tax		1,457	1,679

Statement of comprehensive income (continued)

For the year ended 31 December 2013

	Notes	2013 HRK millions	2012 HRK millions Restated
Profit attributable to:			
Owners of the Company		<u>1,432</u>	<u>1,680</u>
		<u>1,432</u>	<u>1,680</u>
Total comprehensive income arisen from continuing operations attributable to:			
Equity holders of the Company		<u>1,457</u>	<u>1,679</u>
		<u>1,457</u>	<u>1,679</u>
Earnings per share			
Basic and diluted, from continuing operations attributable to equity holders of the Company during the year	9	<u>HRK 17.48</u>	<u>HRK 20.52</u>

The accompanying accounting policies and notes are an integral part of these financial statements.

Statement of financial position
As at 31 December 2013

	Notes	31 December 2013 HRK millions	31 December 2012 HRK millions
ASSETS			
Non-current assets			
Intangible assets	10	1,145	928
Property, plant and equipment	11	5,428	5,603
Investments in subsidiaries	12	530	522
Investments accounted for using the cost method	13	337	337
Available-for-sale financial assets	14	196	499
Loans given to subsidiary		133	101
Trade and other receivables	17	125	20
Deferred income tax assets	8	58	63
Total non-current assets		7,952	8,073
Current assets			
Inventories	16	89	133
Trade and other receivables	17	1,089	1,071
Receivables from subsidiaries		25	30
Prepayments		126	131
Income tax prepayments		206	4
Available-for-sale financial assets	14	382	75
Loans to banks	15	317	239
Time deposits	18 b)	635	261
Cash and cash equivalents	18 a)	1,963	3,104
Total current assets		4,832	5,048
TOTAL ASSETS		12,784	13,121

Statement of financial position (continued)
As at 31 December 2013

	Notes	31 December 2013 HRK millions	31 December 2012 HRK millions
EQUITY AND LIABILITIES			
Issued capital and reserves			
Issued share capital	23	8,189	8,189
Legal reserves	24	409	409
Fair value reserves		(1)	(1)
Retained earnings	25	2,224	2,432
Total issued capital and reserves		10,821	11,029
Non-current liabilities			
Provisions for other liabilities and charges	22	62	87
Employee benefit obligations	21	70	139
Deferred income	20	4	2
Other liabilities	19	130	47
Deferred income tax liability	8	2	-
Total non-current liabilities		268	275
Current liabilities			
Trade payables and other liabilities	19	1,476	1,395
Provisions for other liabilities and charges	22	47	223
Payables to subsidiaries		59	81
Deferred income	20	113	118
Total current liabilities		1,695	1,817
Total liabilities		1,963	2,092
TOTAL EQUITY AND LIABILITIES		12,784	13,121

The accompanying accounting policies and notes are an integral part of these financial statements.

Signed on behalf of the Company on 11 February 2014:

Mr. Davor Tomašković
President of the Management Board (CEO)



Mr. Jens Hartmann
Member of the Management Board of HT d.d. and Chief Operating Officer Business

Statement of cash flows
For the year ended 31 December 2013

	Notes	2013 HRK millions	2012 HRK millions
Operating activities			
Profit before income tax		1,621	2,072
Depreciation, amortization and impairment of non-current assets	5	1,313	1,278
Interest income		(31)	(60)
Gain on disposal of assets		(54)	(58)
Share of profit in joint venture	13	(21)	(25)
Decrease in inventories		44	21
(Increase)/Decrease in receivables and prepayments		(126)	62
Increase in payables and accruals		110	139
Decrease in employee benefit obligations	21	(52)	(19)
Decrease in provisions		(146)	(49)
Other non-cash items		(3)	(11)
Cash generated from operations		2,655	3,350
Income tax paid		(387)	(425)
Net cash flows from operating activities		2,268	2,925
Investing activities			
Purchase of non-current assets	3, 10, 11	(1,359)	(1,126)
Proceeds from sale of non-current assets		69	63
Purchase of available-for-sale financial assets		(690)	(1,480)
Proceeds from sale of available-for-sale financial assets		313	1,033
Purchase of reverse REPO arrangements	15	(463)	(634)
Proceeds from reverse REPO arrangements	15	385	395
Interest received		24	48
Loans given to subsidiary		(24)	-
Acquisition of subsidiary	12	(8)	-
Dividend received	13	21	25
Net cash flows used in investing activities		(1,732)	(1,676)
Financing activities			
Dividends paid	25	(1,679)	(1,813)
Net cash flows used in financing activities		(1,679)	(1,813)
Net decrease in cash and cash equivalents		(1,143)	(564)
Exchange gains on cash and cash equivalents		2	3
Cash and cash equivalents as at 1 January		3,104	3,665
Cash and cash equivalents as at 31 December	18 a)	1,963	3,104

The accompanying accounting policies and notes are an integral part of these financial statements.

Statement of changes in equity
For the year ended 31 December 2013

	Issued share capital HRK millions (Note 23)	Legal reserves HRK millions (Note 24)	Fair value reserves HRK millions	Retained earnings HRK millions (Note 25)	Total HRK millions
Balance as at 1 January 2012	8,189	409	(3)	2,568	11,163
Profit for the year	-	-	-	1,680	1,680
Other comprehensive loss for the year	-	-	2	(3)	(1)
Total comprehensive income for the year	-	-	2	1,677	1,679
Dividends paid to equity holders of the Company	-	-	-	(1,813)	(1,813)
Balance as at 31 December 2012	8,189	409	(1)	2,432	11,029
Effect of changes in accounting policies (Note 2.2.)	-	-	-	14	14
Profit for the year	-	-	-	1,432	1,432
Other comprehensive income for the year	-	-	(0)	25	25
Total comprehensive income for the year	-	-	(0)	1,457	1,457
Dividends paid to equity holders of the Company	-	-	-	(1,679)	(1,679)
Balance as at 31 December 2013	8,189	409	(1)	2,224	10,821

The accompanying accounting policies and notes are an integral part of these financial statements.

Notes to the financial statements

For the year ended 31 December 2013

1 Corporate information

Croatian Telecom Inc. ("HT" or the "Company") is a joint stock company whose majority shareholder is T-Mobile Global Holding Nr. 2 GmbH. Pursuant to the Share transfer agreement concluded in 2013, Deutsche Telekom AG ("DT AG") has transferred a total of 41,763,153 shares of the Company, representing 51% of the issued share capital of the Company and the same number of votes at the General Assembly of the Company, to T-Mobile Global Holding Nr. 2 GmbH, a company 100% owned by DT AG. The said transfer of shares was executed as a part of the internal restructuring performed within DT AG and as a result thereof DT AG's influence in the Company remains unchanged. DT AG is ultimate controlling parent.

The registered office address of the Company is Savska cesta 32, Zagreb, Croatia.

The total number of employees of the Company as at 31 December 2013 was 5,232 (31 December 2012: 5,441).

The principal activities of the Company are described in Note 3.

The financial statements for the financial year ended 31 December 2013 were authorized for issue in accordance with a resolution of the Management Board on 11 February 2014. These financial statements are subject to approval of the Supervisory Board as required by the Croatian Company Act.

2.1. Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the EU. The financial statements also comply with the Croatian Accounting Act on financial statements, which refers to the IFRS as endorsed by the EU.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets (Note 14), as disclosed in the accounting policies hereafter.

The Company's financial statements are presented in Croatian Kuna ("HRK") which is the Company's functional currency. All amounts disclosed in the financial statements are presented in millions of HRK if not otherwise stated.

The Company has also prepared consolidated financial statements in accordance with IFRS for the Company and its subsidiaries (the "Group"), which were approved by the Management Board on 11 February 2014. In the consolidated financial statements, subsidiary undertakings (Note 12) have been fully consolidated. Users of these separate financial statements should read them together with the Group's consolidated financial statements as at and for the year ended 31 December 2013 in order to obtain full information on the financial position, results of operations and changes in the financial position of the Group as a whole.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.2. Changes in accounting policies and disclosures

The accounting policies adopted are consistent with those of the previous financial year unless otherwise stated and disclosed.

The Company has adopted the following new and amended IFRS and IFRIC interpretations during the year which were endorsed by the EU. When the adoption of the standard or interpretation is deemed to have an impact on the financial statements or performance of the Company, its impact is described below.

Amendment to IAS 1 Financial Statement Presentation Regarding Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012)

The main change resulting from these amendments is a requirement for entities to group items presented in other comprehensive income ("OCI") on the basis of whether they are potentially reclassifiable to comprehensive income subsequently (reclassification adjustments). The amendments do not address which items are presented in OCI. The amendment affects presentation only and therefore did not have an impact on the Company's financial position or performance.

IAS 19 Employee Benefits (revised 2011) and Amendment to IAS 19 (effective for annual periods beginning on or after 1 January 2013)

These amendments eliminate the corridor approach and calculate finance costs on a net funding basis. *IAS 19 Employee benefits* was revised in June 2011. The revised employee benefit standard introduces changes to the recognition, measurement, presentation and disclosure of post-employment benefits. The standard also requires net interest expense/income to be calculated as the product of the net defined benefit liability/asset and the discount rate as determined at the beginning of the year. The effect of this is to remove the previous concept of recognising an expected return on plan assets. The primary effect of revised IAS 19 relates to the recognition of past service cost. Under IAS 19 (revised 2011), past service cost have to be recognized immediately in the statement of comprehensive income. Prior to the amendments, past service costs had to be amortized in the statement of comprehensive income on a straight-line basis over the vesting periods.

The change in accounting policy has been accounted for from the period beginning on 1 January 2013 and the effects are shown as follows:

- Statement of financial position

<i>Position</i>	Impact of change HRK millions
Employee benefit obligations	(17)
Deferred income tax liability	3
Retained earnings	14

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.2. Changes in accounting policies and disclosures (continued)

Amendment to IFRS 1 First Time Adoption on Government Loans (effective for annual periods beginning on or after 1 January 2013)

This amendment addresses how a first-time adopter would account for a government loan with a below-market rate of interest when transitioning to IFRS. It also adds an exception to the retrospective application of IFRS, which provides the same relief to first-time adopters granted to existing preparers of IFRS financial statements when the requirement was incorporated into IAS 20 in 2008. This amendment is not relevant to the Company's operations because the Company is not first-time adopter neither the user of government loans.

Amendment to IFRS 7 Financial Instruments: Disclosures on Asset and Liability Offsetting (effective for annual periods beginning on or after 1 January 2013)

This amendment includes new disclosures to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP. The amendment had an impact on disclosure only, but not on measurement and recognition of the financial instruments in the Company's financial position or performance.

The following financial assets and financial liability are subject to offsetting:

	Trade receivables		Trade payables	
	31 December 2013	31 December 2012	31 December 2013	31 December 2012
	HRK millions	HRK millions	HRK millions	HRK millions
Gross recognised amounts	131	217	368	612
Offsetting amount	(90)	(175)	(90)	(175)
	<u>41</u>	<u>42</u>	<u>278</u>	<u>437</u>

IFRS 13 Fair Value Measurement (effective for annual periods beginning on or after 1 January 2013)

IFRS 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements, which are largely aligned between IFRS and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP. IFRS 13 did not have an impact on Company's financial statements.

IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine (effective for annual periods beginning on or after 1 January 2013)

This interpretation sets out the accounting for overburden waste removal (stripping) costs in the production phase of a mine. The interpretation may require mining entities reporting under IFRS to write off existing stripping assets to opening retained earnings if the assets cannot be attributed to an identifiable component of an ore body. This interpretation is not relevant to the Company's operations.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.2. Changes in accounting policies and disclosures (continued)

Annual improvements 2011 (effective for annual periods beginning on or after 1 January 2013)

These annual improvements, address six issues in the 2009-2011 reporting cycle. It includes changes to:

IFRS 1 First time adoption

IAS 1 Financial statement presentation

IAS 16 Property plant and equipment

IAS 32 Financial instruments; Presentation

IAS 34 Interim financial reporting

These improvements did not have an impact on Company's financial statements.

Standards and interpretations issued but not yet effective:

IFRS 10 Consolidated Financial Statements (effective for annual periods beginning on or after 1 January 2014)

The objective of IFRS 10 is to establish principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entity (an entity that controls one or more other entities) to present consolidated financial statements. It defines the principle of control, and establishes control as the basis for consolidation. It sets out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee. It also sets out the accounting requirements for the preparation of consolidated financial statements. The Company is currently assessing the impact that IFRS 10 will have on the financial statements but does not expect any impact on them. The Company plans to adopt this new standard on its effective date.

IFRS 11 Joint Arrangements (effective for annual periods beginning on or after 1 January 2014)

IFRS 11 is a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement rather than its legal form. There are two types of joint arrangement: joint operations and joint ventures. Joint operations arise where a joint operator has rights to the assets and obligations relating to the arrangement and therefore accounts for its interest in assets, liabilities, revenue and expenses. Joint ventures arise where the joint operator has rights to the net assets of the arrangement and therefore equity accounts for its interest. Proportional consolidation of joint ventures is no longer allowed. The Company is currently assessing the impact that IFRS 11 will have on the financial statements but does not expect any impact on them. The Company plans to adopt this new standard on its effective date.

IFRS 12 Disclosures of Interests in Other Entities (effective for annual periods beginning on or after 1 January 2014)

IFRS 12 includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The Company is currently assessing the impact of IFRS 12 on financial statements. The Company plans to adopt this new standard on its effective date.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.2. Changes in accounting policies and disclosures (continued)

Standards and interpretations issued but not yet effective (continued):

IAS 27 (revised 2011) Separate Financial Statements (effective for annual periods beginning on or after 1 January 2014)

IAS 27 (revised 2011) includes the provisions on separate financial statements that are left after the control provisions of IAS 27 have been included in the new IFRS 10. The Company is currently assessing the impact that IAS 27 will have on the financial statements but does not expect any impact on them. The Company plans to adopt this new standard on its effective date.

IAS 28 (revised 2011) Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2014)

IAS 28 (revised 2011) includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11. The Company is currently assessing the impact that IAS 28 will have on the financial statements but does not expect any impact on them. The Company plans to adopt this new standard on its effective date.

Amendment to IFRSs 10, 11 and 12 on Transition Guidance (effective for annual periods beginning on or after 1 January 2014)

These amendments provide additional transition relief to IFRSs 10, 11 and 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. For disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied. The Company is currently assessing the impact of the amendments on its financial statements but does not expect any impact on them. The Company plans to adopt this amendment on its effective date.

Amendments to IFRS 10, IFRS 12 and IAS 27 – on Consolidation for Investment Entities (issued on 31 October 2012 and effective for annual periods beginning 1 January 2014)

These amendments mean that many funds and similar entities will be exempt from consolidating most of their subsidiaries. Instead, they will measure them at fair value through comprehensive income. The amendments give an exception to entities that meet an 'investment entity' definition and which display particular characteristics. Changes have also been made IFRS 12 to introduce disclosures that an investment entity needs to make. The Company is currently assessing the impact of the amendments on its financial statements but does not expect any impact on them. The Company plans to adopt this amendment on its effective date.

Amendments to IAS 32 Financial Instruments: Presentation on Asset and Liability Offsetting (issued in December 2012 and effective for annual periods beginning on or after 1 January 2014)

These amendments are to the application guidance in *IAS 32 Financial instruments: Presentation*, and clarify some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position. The Company is currently assessing the impact of the amendments that could have an impact on presentation in Company's financial statements. The Company plans to adopt this new amendment on its effective date.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.2. Changes in accounting policies and disclosures (continued)

Standards and interpretations issued but not yet effective (continued):

Amendment to IAS 36 Impairment of Assets on Recoverable Amount Disclosures (issued on 29 May 2013 and effective for annual periods beginning 1 January 2014)

This amendment addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The amendment could have an impact on disclosure only, but not on measurement and recognition of the assets in the Company's financial position or performance. The Company plans to adopt this amendment on its effective date.

Amendment to IAS 39 Financial Instruments: Recognition and Measurement 'Novation of Derivatives' (issued on 27 June 2013 and effective for annual periods beginning 1 January 2014)

This amendment provides relief from discontinuing hedge accounting when novation of a hedging instrument to a central counter party meets specified criteria. The amendment is not relevant for the Company's operations because derivatives are not used. The Company plans to adopt this amendment on its effective date.

IFRS 9 Financial Instruments (effective for annual periods beginning on or after 1 January 2015)

IFRS 9 is the first standard issued as part of a wider project to replace *IAS 39 Financial Instruments: Recognition and Measurement*. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. The Company does not expect IFRS 9 to have an impact on the financial statements. The Company plans to adopt this new standard on the effective date as of and when endorsed by the EU.

IFRIC 21 Levies (issued on 20 May 2013 and effective for annual periods beginning on or after 1 January 2014)

This is an interpretation of *IAS 37 Provisions, contingent liabilities and contingent assets*. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. The Company does not expect IFRIC 21 to have an impact on the financial statements. The Company plans to adopt this new interpretation on the effective date as of and when endorsed by the EU.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.3. Significant accounting judgments, estimates and assumptions

The preparation of the Company's financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, during the reporting period or at the reporting date respectively. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods. The key assumptions concerning the future and other key sources of estimation uncertainty at the statement of financial position date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Provisions and contingencies

The Company is exposed to a number of legal cases and regulatory proceedings and ownership dispute over distributive telecommunication infrastructure that may result in significant outflow of economic resources or derecognition of related assets. The Company uses internal and external legal experts to assess the outcome of each case and makes judgments if and what amount needs to be provided for in the financial statements as more explained in Notes 22 and 27. Changes in these judgments could have a significant impact on the financial statements of the Company.

Impairment of non-financial assets

The determination of impairment of assets involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of services, current replacement costs, prices paid in comparable transactions and other changes in circumstances that indicate an impairment exists. The recoverable amount and the fair values are typically determined using the discounted cash flow method which incorporates reasonable market participant assumptions. The identification of impairment indicators, as well as the estimation of future cash flows and the determination of fair values for assets (or groups of assets) require management to make significant judgments concerning the identification and validation of impairment indicators, expected cash flows, applicable discount rates, useful lives and residual values. Specifically, the estimation of cash flows underlying the fair values of the business considers the continued investment in network infrastructure required to generate future revenue growth through the offering of new data products and services, for which only limited historical information on customer demand is available. If the demand for those products and services does not materialize as expected, this would result in less revenue, less cash flow and potential impairment to write down these investments to their fair values, which could adversely affect future operating results.

The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the financial plan covering a mid-term period. The cash flows beyond the planning period are extrapolated using appropriate growth rates given in Note 10. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash inflows and the growth rate used for extrapolation purposes. Further details including carrying values and effects on the result of the period are given in Notes 10 and 11.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.3. Significant accounting judgments, estimates and assumptions (continued)

Useful lives of assets

The determination of the useful lives of assets is based on historical experience with similar assets as well as any anticipated technological development and changes in broad economic or industry factors. The appropriateness of the estimated useful lives is reviewed annually, or whenever there is an indication of significant changes in the underlying assumptions. We believe that this is a critical accounting estimate since it involves assumptions about technological development in an innovative industry and is heavily dependent on the investment plans of the Company. Further, due to the significant weight of depreciable assets in Company's total assets, the impact of significant changes in these assumptions could be material to financial position and results of operations of the Company.

The following table demonstrates the sensitivity to a reasonably possible change in useful life on amortization and depreciation, with all other variables held constant, on the Company's profit post tax:

	Increase/ decrease in %	Effect on profit post tax HRK millions
Year ended 31 December 2013	+10	86
	-10	(81)
Year ended 31 December 2012	+10	88
	-10	(80)

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies

a) *Operating profit*

Operating profit is defined as the result before income taxes and finance items. Finance items comprise interest revenue on cash balances in the bank, deposits, treasury bills, interest bearing available for sale financial assets, dividend income from associate, subsidiaries and joint venture, interest expense on borrowings, gains and losses on the sale of available-for-sale financial assets and foreign exchange gains and losses on all monetary assets and liabilities denominated in foreign currency.

b) *Investments in subsidiaries*

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights are currently exercisable or convertible are considered when assessing whether the Company controls another entity. Investments in subsidiaries are measured at cost less any impairment in value.

c) *Investment in associate*

In the Company's financial statements, investment in associated company (generally a shareholding of between 20% and 50% of voting rights) where significant influence is exercised by the Company is measured at cost less any impairment in value. An assessment of investment in associate is performed when there is an indication that the asset has been impaired or that the impairment losses recognized in previous years no longer exist.

d) *Investment in joint venture*

The Company has an interest in a joint venture which is a jointly controlled entity, whereby the venturers have a contractual arrangement that establishes joint control over the economic activities of the entity. This investment is measured at cost less any impairment in value. An assessment of investment in joint venture is performed when there is an indication that the asset has been impaired or that the impairment losses recognized in previous years no longer exist.

e) *Intangible assets*

Intangible assets are measured initially at cost. Intangible assets are recognized in the event that the future economic benefits that are attributable to the assets will flow to the Company, and that the cost of the asset can be measured reliably. After initial recognition, intangible assets are measured at cost less accumulated amortization and any accumulated impairment losses. Intangible assets are amortised on a straight-line basis over the best estimate of their useful life. There are no intangible assets that are assessed to have an indefinite useful life. The amortization method is reviewed annually at each financial year-end.

Amortization of the telecommunication licence has started when licence is acquired, the amortization period is the term of the licence.

The Company recognizes costs of content as an intangible asset at the inception of related contract. The Company determined that the following conditions have to be met for capitalization of content provider contracts: contract duration must be longer than one year, cost must be determined or determinable, contracted rights must be continuous and costs under the contract are unavoidable. Assets recognized under these contracts will be amortized over the contract period.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

e) *Intangible assets (continued)*

Useful lives of intangible assets are as follows:

Licences and rights

Radio frequency spectrum in 2100 MHz frequency band	20 years
Radio frequency spectrum in 900/1800 MHz frequency bands	15 years
Radio frequency spectrum in 800 MHz frequency band	11 – 12 years
Right of servitude for Distributive Telecommunication Infrastructure (DTI)	30 years
Software, content and other assets	2 – 5 years

Assets under construction are not amortised.

f) *Property, plant and equipment*

An item of property, plant and equipment that qualifies for recognition as an asset is measured at its cost. The cost of an item of property, plant and equipment comprises its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

In addition to directly attributable costs, the costs of internally constructed assets include proportionate indirect material and labour costs, as well as administrative expenses relating to production or the provision of services.

After recognition as an asset, an item of property, plant and equipment is measured at cost less accumulated depreciation and any accumulated impairment losses.

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately.

Depreciation is computed on a straight-line basis.

Useful lives of newly acquired assets are as follows:

Buildings	10 – 50 years
Telecom plant and machinery	
Cables	8 – 18 years
Cable ducts and tubes	30 years
Other	2 – 15 years
Tools, vehicles, IT, office and other equipment	4 – 15 years
Customer premises equipment (CPE)	7 years

Land and assets under construction are not depreciated.

The useful life, depreciation method and residual values are reviewed at each financial year-end, and if expectations differ from previous estimates, the change(s) are accounted for as a change in an accounting estimate.

Construction-in-progress represents plant and properties under construction and is stated at cost.

Depreciation of an asset begins when it is available for use.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

g) *Impairment of assets*

Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment is reviewed for possible reversal of the impairment at each reporting date.

Impairment of trade receivables

A provision for impairment of trade and other receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the underlying arrangement. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments as well as historical collections are considered indicators that the trade receivable is impaired. Value adjustment is done for outstanding domestic receivables older than 120 days, and for outstanding foreign receivables that are due more than 150 days. Value adjustment for receivables from subsidiaries, domestic telecommunication operators, receivables for the international settlement and key customers under extraordinary collection method and from companies with whom prebankruptcy procedures has been made value adjustment is done according to the collection estimate. Short-term receivables are written-off in the case when the debtor is liquidated or ceased its business activities; when the legal case is lost by the final court decision or in the case of lapse of receivables.

Impairment of available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the statement of comprehensive income, is transferred from equity to the statement of comprehensive income. Reversals in respect of equity instruments classified as available-for-sale are not recognized in the statement of comprehensive income. Reversals of impairment losses on debt instruments are reversed through the statement of comprehensive income if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in the statement of comprehensive income.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

h) Inventories

Inventories are valued at the lower of cost and net realisable value, after provision for obsolete items. Net realisable value is the selling price in the ordinary course of business, less the costs necessary to make the sale. Cost is determined on the basis of weighted average cost.

Phone sets are often sold for less than cost in connection with promotions to obtain new and/or retain existing subscribers with minimum commitment periods. Such loss on the sale of equipment is only recorded when the sale occurs if the normal resale value is higher than the cost of the phone set. If the normal resale value is lower than costs, the difference is recognized as an inventory impairment immediately.

i) Receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less, they are classified as current assets. If not, the receivables are presented as non-current assets. Receivables are stated at the fair value of the consideration given and are carried at amortised cost, after provision for impairment.

j) Foreign currencies

Transactions denominated in foreign currencies are translated into local currency at the middle exchange rates of the Croatian National Bank prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into local currency at the middle exchange rates of the Croatian National Bank prevailing at the statement of financial position date. Any gain or loss arising from a change in exchange rates subsequent to the date of the transaction is included in the statement of comprehensive income within financial income or financial expense, respectively.

k) Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statement of comprehensive income on a straight-line basis over the period of the lease.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

l) Taxation

The income tax charge is based on profit for the year and includes deferred taxes. Deferred taxes are calculated using the liability method.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes at the reporting date.

Deferred tax is determined using income tax rates that have been enacted or substantially enacted by the financial statement date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would arise from the manner in which the enterprise expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit (or reversing deferred tax liabilities) will be available against which the temporary differences can be utilized.

Deferred tax assets and liabilities are not discounted and are classified as non-current assets and liabilities in the statement of financial position. Deferred tax assets are recognized when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised.

Current tax and deferred tax are charged or credited in other comprehensive income if the tax relates to items that are credited or charged, in the same or a different period in other comprehensive income.

m) Employee benefit obligations

The Company provides other long-term employee benefits (Note 21). These benefits include retirement and jubilee (length of service) payments. The defined benefit obligation is calculated annually by independent actuary using a projected unit credit method. The projected unit credit method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation.

Past service costs are recognized in statement of comprehensive income immediately in the period in which they occur. Gains or losses on the curtailment or settlement of benefit plans are recognized when the curtailment or settlement occurs. The benefit obligation is measured at the present value of estimated future cash flows using a discount rate that is similar to the interest rate on government bonds where the currency and terms of the government bonds are consistent with the currency and estimated terms of the benefit obligation. Gains and losses resulting from changes in actuarial assumptions are recognized in other comprehensive income in the period in which they occur.

The Company provides death in service short term benefits which are recognized as an expense of the period in which it incurred.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

n) Revenue recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and sales taxes or duty. The Company assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent. The Company has concluded that it is acting as a principal in all of its revenue arrangements with the exception of the provision of its telecommunications infrastructure to third parties that offer value added services to its customer. In these cases, the Company is acting as an agent.

Revenue from fixed telephony includes revenue from activation fees, monthly fees, calls placed by fixed line subscribers and revenue from additional services in fixed telephony. Revenue from activation fees is recognized on a straight-line basis throughout future periods depending on estimated life of a customer's connection. Estimated life is 6 years in 2013 (2012: 3 years).

Revenue from wholesale services includes interconnection services for domestic and international carriers, and revenue from usage of network by other operators.

Revenues from the provision of its network to the provider of value added services are reported on a net basis. Revenues are exclusively the amount of the commission received.

Third parties using the Company's telecommunications network include roaming customers of other service providers and other telecommunications providers which terminate or transit calls on the Company's network. These wholesale (incoming) traffic revenues included in voice and non-voice (data and internet) revenues are recognized in the period of related usage. A proportion of the revenue received is often paid to other operators (interconnect) for the use of their networks, where applicable. The revenues and costs of these transit calls are stated gross in the financial statements as the Company is the principal supplier of these services using its own network freely defining the pricing of the services, and recognized in the period of related usage.

Revenue from mobile telephony includes revenue from monthly fee and call charges for "post-paid" mobile customers, call charges for "pre-paid" mobile customers, call charges for customers of international mobile operators when roaming on the Company's mobile network, sale of mobile handsets, domestic interconnection revenues related to mobile network, revenues for short and multimedia messages and data traffic revenues.

Revenue from unused tariff packages and prepaid vouchers is recognized when they are realised. Before their realisation, they are recorded as deferred revenues.

The Company offers certain multiple-element arrangements (bundled product offers) arrangements. For multiple-element arrangements, revenue recognition for each of the units of accounting (elements) identified must be determined separately. Total arrangement consideration relating to the bundled contract is allocated among the different elements based on their relative fair values (i.e., a ratio of the fair value of each element to the aggregated fair value of the bundled deliverables is generated). The relative fair value of an individual element is limited by the proportion of the total arrangement consideration to be provided by the customer, the payment of which does not depend on the delivery of additional elements. If the fair value of the delivered elements cannot be determined reliably but the fair value of the undelivered elements can be determined reliably, the total arrangement consideration provided by the customer is allocated by determining the fair value of the delivered elements as the difference between the total arrangement consideration and the fair value of the undelivered elements.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

n) Revenue recognition (continued)

Revenue from internet and data services includes revenue from leased lines, frame relay, ATM, Ethernet services, ADSL subscription and traffic, fixed line access, VPN online, internet traffic to T-Com call number, Multimedia services, IP phone (access and traffic) and IPTV. Service revenues are recognized when the services are provided in accordance with contractual terms and conditions.

Revenue from ICT includes revenue from restructuring business processes services, application management services, technology infrastructure and system maintenance and the design and development of complex IT systems to a client's specifications (design and build) and WEB hosting.

Revenues from application management services, technology infrastructure and system maintenance are recognised on a straight-line basis over the term of the contract. Revenues from time and material contracts are recognised based on contracted prices and direct cost incurred. Revenue from product maintenance contracts are recognized on a straight-line basis over the delivery period.

Revenues and expenses from fixed-price design and build contracts where the outcome can be estimated reliably are recognised under percentage-of completion (POC) method. Estimates are revised and can result in decrease or an increase of estimated revenues and expenses and are included in statement of comprehensive income in the year in which circumstances that give rise to the revision become known to management.

Revenues from one-time-charge licensed software are recognized at the inception of licence term all revenue recognition criteria have been met. Revenues from monthly licence charges are recognised on a subscription basis over the period that the client is entitled to use the licence. Revenues for maintenance, unspecified upgrades and technical support are recognised over the period such items are delivered.

Revenues and expenses associated with the sale of telecommunications equipment and accessories are recognized when the products are delivered, provided that there are no unfulfilled obligations that affect the customer's final acceptance of the arrangement.

Revenue from dividends is recognized when the Company's right to receive the payment is established.

Interest revenue is recognized as interest accrues (using the effective interest rate that is the rate that exactly discounts receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

The Company maintains a loyalty point's programme, T-Club. In accordance with IFRIC 13, customer loyalty credits are accounted for as a separate component of the sales transaction in which they are granted. A portion of the fair value of the consideration received is allocated to the award credits and deferred. This is then recognized as revenue over the period that the award credits are redeemed.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

o) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, demand deposits and short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and which are subject to an insignificant risk of change in value.

p) Borrowings

Borrowing costs, which include interest and other costs incurred in connection with the borrowing of funds, including exchange differences arising from foreign currency borrowings, are expensed in the period in which they are incurred, except those which directly attributable to the acquisition, construction or production of qualifying assets and are capitalised. Borrowings are initially recognized in the amount of the proceeds received net of transaction costs.

q) Financial assets

All investments, other than loans and receivables originated by the Company, are classified as available-for-sale.

Available-for-sale financial assets are classified as current assets if management intends to realise them within 12 months after the statement of financial position date. All purchases and sales of investments are recognized on the settlement date.

Financial assets are initially measured at cost, which is the fair value of the consideration given for them, including transaction costs.

Available-for-sale financial assets and trading financial assets are subsequently carried at fair value without any deduction for transaction costs by reference to their quoted market price at the statement of financial position date. Gains or losses on measurement to the fair value of available-for-sale financial assets are recognized in other comprehensive income, until the investment is sold or otherwise disposed of, or until it is determined to be impaired, at which time the cumulative gain or loss previously recognized in other comprehensive income is included in the net profit or loss for the period.

Financial instruments are generally recognized as soon as the Company becomes a party to the contractual regulations of the financial instrument. However, in the case of regular way purchase or sale (purchase or sale of a financial asset under a contract whose terms require delivery of the asset within the timeframe established generally by regulation or convention in the marketplace concerned), the settlement date is relevant for the initial recognition and derecognition. A financial asset is derecognized when the cash is collected or the rights to receive cash from the assets have expired. A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

Securities purchased under agreements to resell ("reverse REPOs") are recorded as loans to banks and cash equivalents, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

r) *Provisions*

A provision is recognized when, and only when, the Company has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at each statement of financial position date and adjusted to reflect the current best estimate.

Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditures expected to be required to settle the obligation. When discounting is used, the increase in provision reflecting the passage of time is recognized as interest expense.

Provisions for termination benefits are recognized when the Company is demonstrably committed to a termination of employment contracts, that is when the Company has a detailed formal plan for the termination which is without realistic possibility of withdrawal. Provisions for termination benefits are computed based on amounts paid or expected to be paid in redundancy programs.

s) *Contingencies*

A contingent asset is not recognized in the financial statements but is disclosed when an inflow of economic benefits is probable.

Contingent liabilities are not recognized in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

t) *Share-based payments*

The cost of cash-settled and equity-settled transactions is measured initially at fair value at the grant date using a binomial model, further details of which are given in Note 32. This fair value is expensed over the period until the vesting date with recognition of a corresponding liability. The liability is remeasured to fair value at each statement of financial position date up to and including the settlement date with changes in fair value recognized in the statement of comprehensive income.

u) *Events after reporting period*

Post-year-end events that provide additional information about the Company's position at the statement of financial position date (adjusting events) are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes when material.

v) *Trade payables*

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.

w) *Dividend distribution*

Dividend distribution to the Company's shareholders is recognized as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

Notes to the financial statements (continued)

For the year ended 31 December 2013

2.4. Summary of accounting policies (continued)

x) *Earnings per share*

Earnings per share are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year excluding ordinary shares purchased by the Company and held as treasury shares.

y) *Reclassifications*

In 2013, the Company has changed the presentation of certain ancillary income within statement of comprehensive income. In order to reconcile the presentation of comparable period data with data presented in 2013, following positions in the financial statements for the year ended 31 December 2012 were reclassified:

- Statement of comprehensive income

<i>Position</i>	2012 As reported HRK millions	Impact on change HRK millions	2012 Restated HRK millions
Revenue	6,886	98	6,984
Other operating income	239	(98)	141

The Company believes that presentation of all ancillary income in connection with the delivery of goods and rendering of services in the course of an entity's ordinary activities should be presented as revenue (e.g. dunning fees, contractual penalties, fees charged for the (temporary) disconnection or reconnection of services, reimbursements of costs from third parties and default interest). In other words: if income from the agreed consideration of a rendered service is treated as revenue, the same holds true for all other amounts charged to the customer in conjunction with this service. Such ancillary income primarily results from customers' defaults. Such accounting treatment is in alignment with the now predominant accounting practice in telecommunication industry followed by DT AG and consequently the Company believes the new way of presentation is more appropriate. The Company believes that third statement of financial position is not necessary to be presented because there is no any impact on the financial position of previous periods.

Notes to the financial statements (continued)

For the year ended 31 December 2013

3 Segment information

Business reporting format is determined to be Residential, Business and Network and Support Function segments as the Company's risks and rates of return are affected predominantly by differences in the market and customers. The segments are organised and managed separately according to the nature of the customers and markets that the services rendered, with each segment representing a strategic business unit that offers different products and services.

The Residential Segment includes marketing, sales and customer services, focused on providing mobile, fixed line telecommunications and TV distribution services to residential customers.

The Business Segment includes marketing, sales and customer services, focused on providing mobile and fixed line telecommunications and systems integration services to corporate customers, small- and medium-sized businesses and the public sector. The Business Segment is also responsible for the wholesale business in both fixed and mobile services.

The Network and Support Functions performs cross-segment management and support functions, and includes the Technology, Procurement, Accounting, Treasury, Legal and other central functions. The Network and Support Functions is included in segment information as a voluntary disclosure since it does not meet the criteria for an operating segment.

The Management Board, as the chief operating decision maker, monitors the operating results of business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on contribution margin II or segment results (as calculated in the table below).

The Company's geographical disclosures are based on the geographical location of its customers.

Management of the Company does not monitor assets and liabilities by segments and therefore this information has not been disclosed.

Notes to the financial statements (continued)
For the year ended 31 December 2013

3 Segment information (continued)

Residential and Business segments

The following tables present revenue and direct cost information regarding the Company's segments:

Year ended 31 December 2012	Residential HRK millions	Business HRK millions	Network & Support functions HRK millions	Total HRK millions
Segment revenue (restated) (Note 2.4. y))	3,997	2,987	-	6,984
<i>Service revenues</i>	3,788	2,772	-	6,560
<i>Terminal equipment</i>	134	49	-	183
<i>Other (restated)</i>	75	166	-	241
Usage related direct costs	(305)	(409)	-	(714)
Income and losses on accounts receivable	(6)	(57)	-	(63)
Contribution margin I (restated)	3,686	2,521	-	6,207
Non-usage related direct costs	(508)	(190)	-	(698)
Segment result (restated)	3,178	2,331	-	5,509
Other income (restated) (Note 2.4. y))	-	-	141	141
Other operating expenses	(374)	(232)	(1,740)	(2,346)
Depreciation, amortization and impairment of non-current assets	-	-	(1,278)	(1,278)
Operating profit (restated)	2,804	2,099	(2,877)	2,026
Capital expenditures	368	133	625	1,126
Year ended 31 December 2013				
Segment revenue	3,801	2,617	-	6,418
<i>Service revenues</i>	3,586	2,417	-	6,003
<i>Terminal equipment</i>	157	55	-	212
<i>Other</i>	58	145	-	203
Usage related direct costs	(300)	(298)	-	(598)
Income and losses on accounts receivable	7	(46)	-	(39)
Contribution margin I	3,508	2,273	-	5,781
Non-usage related direct costs	(471)	(281)	-	(752)
Segment result	3,037	1,992	-	5,029
Other income	-	-	116	116
Other operating expenses	(377)	(273)	(1,572)	(2,222)
Depreciation, amortization and impairment of non-current assets	-	-	(1,313)	(1,313)
Operating profit	2,660	1,719	(2,769)	1,610
Capital expenditures	596	237	526	1,359

Notes to the financial statements (continued)
For the year ended 31 December 2013

3 Segment information (continued)

Revenue by geographical area

	2013 HRK millions	2012 HRK millions Restated
Republic of Croatia	6,049	6,472
Rest of the World	369	512
	<u>6,418</u>	<u>6,984</u>

All of Company's assets are located in Croatia.

None of the Company's external customers represent a significant source of revenue.

4 Service expenses

	2013 HRK millions	2012 HRK millions
Domestic interconnection	345	381
International interconnection	253	334
Other services	208	240
	<u>806</u>	<u>955</u>

5 Depreciation, amortization and impairment of non-current assets

	2013 HRK millions	2012 HRK millions
Depreciation	871	884
Amortization	390	336
	<u>1,261</u>	<u>1,220</u>
Impairment loss	52	58
	<u>1,313</u>	<u>1,278</u>

Notes 10 and 11 disclose further details on amortization and depreciation expense and impairment loss.

Notes to the financial statements (continued)
For the year ended 31 December 2013

6 Employee benefits expenses

	2013	2012
	HRK millions	HRK millions
Gross salaries	759	758
Taxes, contribution and other payroll costs	184	207
Redundancy expenses (Note 22)	66	144
Long-term employee benefits (Note 21)	(16)	(17)
	<u>993</u>	<u>1,092</u>

7 Other expenses

	2013	2012
	HRK millions	HRK millions
Maintenance services	286	273
Rent (Note 26)	175	175
Licence cost	170	160
Advertising	96	108
Selling commission	94	111
Contract workers	51	29
Postal expenses	47	66
Non-income taxes and contribution	41	45
Provision of trade receivables	38	63
Call centre and customer care support	34	43
Education and consulting	19	17
Write down of inventories	17	21
Daily allowances and other costs of business trips	16	16
Insurance	13	13
Loss on disposal of fixed assets	0	1
Other operating charges	100	96
	<u>1,197</u>	<u>1,237</u>

Notes to the financial statements (continued)
For the year ended 31 December 2013

8 Income tax expense

a) *Tax on profit*

	2013	2012
	HRK millions	HRK millions
Current tax expense	191	403
Deferred tax income	(2)	(11)
	<u>189</u>	<u>392</u>

b) *Reconciliation of the taxation charge to the income tax rate*

	2013	2012
	HRK millions	HRK millions
Profit before taxes	<u>1,621</u>	<u>2,072</u>
Income tax at 20% (domestic rate)	324	414
Tax effect of:		
Reinvested profit not subject to tax	(139)	-
Income not subject to tax	(8)	(15)
Tax adjustment related to previous years	8	(11)
Expenses not deductible for tax purposes	2	2
Other	<u>2</u>	<u>2</u>
	<u>189</u>	<u>392</u>
Effective tax rate	<u>11.66%</u>	<u>18.92%</u>

The Company utilized tax relief for 2013 based on reinvested profit, and consequently issued share capital will be increased by HRK 694 million in accordance with Management Board Decision.

Notes to the financial statements (continued)
For the year ended 31 December 2013

8 Income tax expense (continued)

Components and movements of deferred tax assets and liabilities are as follows:

Deferred tax assets and liabilities recognized in:	31 December 2013	Charged/ (credited) in 2013	Effect of changes in accounting policies	31 December 2012	Charged/ (credited) in 2012	31 December 2011
	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions
<i>Statement of comprehensive income</i>						
Non-tax deductible value adjustments	22	(1)	-	23	1	22
Property, plant and equipment write down	17	1	-	16	7	9
Accrued interest on legal cases	4	(3)	-	7	1	6
Other	15	2	-	13	2	11
	<u>58</u>	<u>(1)</u>	<u>-</u>	<u>59</u>	<u>11</u>	<u>48</u>
<i>Statement of other comprehensive income</i>						
Actuarial gains and losses	-	(4)	-	4	0	4
Deferred tax asset	<u>58</u>	<u>(5)</u>	<u>-</u>	<u>63</u>	<u>11</u>	<u>52</u>
<i>Statement of comprehensive income</i>						
Past service costs	-	(3)	3	-	-	-
	<u>-</u>	<u>(3)</u>	<u>3</u>	<u>-</u>	<u>-</u>	<u>-</u>
<i>Statement of other comprehensive income</i>						
Actuarial gains and losses	2	2	-	-	-	-
Deferred tax liability	<u>2</u>	<u>(1)</u>	<u>3</u>	<u>-</u>	<u>-</u>	<u>-</u>

Notes to the financial statements (continued)

For the year ended 31 December 2013

8 Income tax expense (continued)

A deferred tax asset has been recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets have not been discounted.

The deferred tax asset of the Company arises on the property, plant and equipment impairment as a result of the fact that HRK 395 million of the impairment reported in 2001 was not tax deductible in that year. Of this amount, HRK 369 million became tax deductible in the period from 2002 to 2013, and the remaining HRK 26 million will be tax deductible in future periods.

There are no formal procedures in the Republic of Croatia to agree the final level of tax charge upon submission of the declaration for corporate tax and VAT. However, such tax settlements may be subject to review by the relevant tax authorities during the limitation period of three years. The limitation period of three years starts with the year that follows the year of submission of tax declarations, i.e. 2014 for the 2012 tax liability. The counting of three years starts again with any action of tax authorities with the purpose to collect tax, interest or fines until the absolute statute of limitation of 6 years expires.

9 Earnings per share

Basic earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the Company by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are equal to basic earnings per share since there are no dilutive potential ordinary shares or share options.

The following reflects the income and share data used in the basic and diluted earnings per share computations:

	2013	2012
Profit for the year attributable to ordinary equity holders of the Company in HRK millions	1,432	1,680
Weighted average number of ordinary shares for basic earnings per share	81,885,322	81,887,256
	<u>HRK 17.48</u>	<u>HRK 20.52</u>

Notes to the financial statements (continued)

For the year ended 31 December 2013

10 Intangible assets

	Licences	Software	Other assets	Assets under construction	Total
	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions
As at 1 January 2012					
Cost	281	2,628	257	35	3,201
Accumulated amortization	(151)	(2,051)	(130)	(8)	(2,340)
Net book value	130	577	127	27	861
Year ended 31 December 2012					
Opening net book value	130	577	127	27	861
Additions	150	179	32	48	409
Transfers	-	38	3	(41)	-
Amortization charge	(12)	(256)	(68)	-	(336)
Impairment loss	-	(6)	-	-	(6)
Net book value	268	532	94	34	928
As at 31 December 2012					
Cost	432	2,727	254	34	3,447
Accumulated amortization	(164)	(2,195)	(160)	-	(2,519)
Net book value	268	532	94	34	928
Year ended 31 December 2013					
Opening net book value	268	532	94	34	928
Additions	149	212	170	87	618
Transfers	-	51	13	(64)	-
Amortization charge	(24)	(254)	(112)	-	(390)
Impairment loss	-	(5)	(6)	-	(11)
Net book value	393	536	159	57	1,145
As at 31 December 2013					
Cost	581	2,826	437	57	3,901
Accumulated amortization	(188)	(2,290)	(278)	-	(2,756)
Net book value	393	536	159	57	1,145

Notes to the financial statements (continued)

For the year ended 31 December 2013

10 Intangible assets (continued)

The intangible assets of the Company as at 31 December 2013 include four licences for use of the radio frequency spectrum (Notes 2.4. e) and 31 b)).

Assets under construction primarily relate to software and the various licences for the use of software.

Additions of intangible assets

Major additions in the reporting period relate to applicative, system and network technology software and user licences in the amount of HRK 202 million, capitalised costs of content in the amount of HRK 170 million and new licence for use of the radio frequency spectrum in 800 MHz frequency band (digital dividend) in the amount of HRK 149 million. Out of the total, HRK 43 million relates to capitalization of discounted amount of annual fees payments until expiration of the licence. This licence is amortized over a period of 11 years (starting from December 2013) according to licence conditions granted.

Impairment loss

During 2013, the Company recognized impairment loss of intangible assets of HRK 11 million (2012: HRK 6 million).

Notes to the financial statements (continued)
For the year ended 31 December 2013

11 Property, plant and equipment

	Land and buildings	Telecom plant and machinery	Tools, vehicles, IT and office equipment	Assets under construction and other assets	Total
	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions
As at 1 January 2012					
Cost	2,151	11,254	1,092	239	14,736
Accumulated depreciation	(1,030)	(7,019)	(824)	(23)	(8,896)
Net book value	1,121	4,235	268	216	5,840
Year ended 31 December 2012					
Opening net book value	1,121	4,235	268	216	5,840
Additions	29	286	31	371	717
Transfers	7	70	13	(90)	-
Disposals	(16)	-	(1)	(1)	(18)
Depreciation charge	(104)	(687)	(93)	-	(884)
Impairment loss	-	(49)	-	(3)	(52)
Net book value	1,037	3,855	218	493	5,603
As at 31 December 2012					
Cost	2,159	11,214	1,101	496	14,970
Accumulated depreciation	(1,122)	(7,359)	(883)	(3)	(9,367)
Net book value	1,037	3,855	218	493	5,603
Year ended 31 December 2013					
Opening net book value	1,037	3,855	218	493	5,603
Additions	88	308	34	311	741
Transfers	82	258	38	(378)	-
Disposals	(2)	-	(2)	-	(4)
Depreciation charge	(94)	(690)	(87)	-	(871)
Impairment loss	(17)	(20)	-	(4)	(41)
Net book value	1,094	3,711	201	422	5,428
As at 31 December 2013					
Cost	2,309	11,382	965	426	15,082
Accumulated depreciation	(1,215)	(7,671)	(764)	(4)	(9,654)
Net book value	1,094	3,711	201	422	5,428

Notes to the financial statements (continued)

For the year ended 31 December 2013

11 Property, plant and equipment (continued)

Included within assets under construction of the Company are major spare parts of HRK 17 million (31 December 2012: HRK 19 million), net of an impairment provision of HRK 2 million (31 December 2012: HRK 1 million).

Beginning in 2001, the Company has performed additional procedures which have provided support for the existence of legal title to land and buildings transferred from HPT s.p.o. under the Separation Act of 10 July 1998. The Company is still in the process of formally registering this legal title.

The Company does not have any material property, plant and equipment held for disposal, nor does it have any material idle property, plant and equipment.

Impairment loss

In 2013, the Company recognized an impairment loss of property, plant and equipment of HRK 41 million (2012: HRK 52 million) mostly due to transfer to the newer technology. The recoverable amount of that equipment is its estimated fair value less costs to sell, which is based on the best information available to reflect the amount that the Company could obtain, at the statement of financial position date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal.

Disposal of property, plant and equipment

The disposal of the property, plant and equipment primarily relates to the disposal of telecom machinery, old tools, IT, office equipment and vehicles in the gross amount of HRK 622 million (2012: HRK 420 million).

Ownership over ducts

Although assets (including the ducts as a part of the infrastructure) were transferred from the legal predecessor of the Company, HPT Public Company, by virtue of the "Law on Separation of Croatian Post and Telecommunication" and contributed by the Republic of Croatia to the share capital at the foundation of the Company on 1 January 1999, according to other Croatian legislation, part of the Company's infrastructure that is considered as a real estate, which is also known as Distributive Telecommunication Infrastructure (DTI, TI or ducts), does not have all the necessary documents (building, use permits etc.) and the major portion of these assets are not registered in the land registry, which may be relevant to the issue of proving the ownership towards third parties. Intrusions in HT's ducts by other competitors and some requirements of ownership over these assets by the local authorities (the City of Zagreb and City of Split present the majority of problems), may have a material effect on the financial statements in the case that HT will not be able to prove its ownership rights for some ducts.

The Company formed the Registration And Contractual Relation Management Department that is responsible to assure that all network technology related assets are properly legalised, documented and that this documentation is available to all relevant departments and authorities. The overall process is slow and complex since the registration depends not only on HT but also on local and state authorities. Since the year 2006, the actions of HT have been concentrated on the conclusion of "right of servitude" contracts with local municipalities and "right of use" contracts with Croatian and County Roads.

Notes to the financial statements (continued)

For the year ended 31 December 2013

11 Property, plant and equipment (continued)

Ownership over ducts (continued)

In connection with the offer for sale of ordinary shares held by the Government of Republic of Croatia in 2007, the Government of Republic of Croatia, the Company and DT AG have entered into a Memorandum of Understanding on how the various issues relating to the Initial Public Offering, including DTI infrastructure should be resolved. Inter alia, this provides the underlying principles under which right of way charges and shared usage issues will be based.

The Government of Republic of Croatia has committed, within the limits of its authority, to use its reasonable efforts to provide for the appropriate legislation and regulations under the Croatian legal system as soon as practicably possible.

In accordance with Ordinance on Manner and Conditions for Access and Joint Use of Electronic Communications Infrastructure and Related Equipment (Official Gazette No. 154/08 effective as at 6 January 2009) and Ordinance on Certificate and Fees for the Right of Way (Official Gazette No. 31/09 effective as of 19 March 2009 and Official Gazette No. 152/11 effective as of 4 January 2012), the Croatian Post and Electronic Communications Agency ("HAKOM") issues certificates for the rights of way to HT. HAKOM granted HT certificates for the right of way for approximately 50% of ducts in the City of Zagreb, based on which HT pays certain fee. The Company believes that the issued certificates for the rights of way might help HT in the lawsuit filed by Zagreb Holding Ltd. branch Zagreb Digital City ("ZHSDG") (Note 27 b). Due to existing of those certificates, ZHSDG corrected their lawsuit in its statement submitted to the Court and admitted ownership rights to HT for DTI where the certificates were obtained.

The legalization process is to be speed up due to Law on Electronic Communications which obliges local municipality and other owners of the land where the electronic communication infrastructure were constructed to tolerate "right of way" which HT owns based on the Law, except if owner of the land and HT do not agree any other right.

The Company assessed and declared the existence of the risks thereon, including obtaining legal opinions with respect to certain of the issues involved. However, due to the fact that these issues are very complex, so far the Company has not yet been able to determine possible outcome and whether it will result in any impairment of the DTI assets concerned due to any inability to prove title, or as a result of the additional right of way charges that may be imposed, which could have a retrospective effect. Therefore, no adjustments were made to these financial statements in respect of this matter.

The net book value of all the Company's ducts as at 31 December 2013 is HRK 838 million (31 December 2012: HRK 855 million).

Notes to the financial statements (continued)
For the year ended 31 December 2013

12 Investments in subsidiaries

The net book value of investments in subsidiaries comprises:

	31 December 2013	31 December 2012
	HRK millions	HRK millions
Iskon Internet d.d.	330	330
Combis d.o.o.	189	189
E-tours d.o.o.	8	-
KDS d.o.o.	3	3
	<u>530</u>	<u>522</u>

The Company has the following subsidiaries in the Republic of Croatia:

<i>Company</i>	<i>Country of Business</i>	<i>Principal Activities</i>	<i>Ownership interest</i>
Iskon Internet d.d.	Republic of Croatia	Provision of internet and data services	100%
Combis d.o.o.	Republic of Croatia	Provision of IT services	100%
E-tours d.o.o.	Republic of Croatia	Provision of travel agency services	100%
KDS d.o.o.	Republic of Croatia	Provision of cable TV services	100%

E-tours d.o.o. was the company 100% owned by Iskon Internet d.d. until 27 September 2013.

Notes to the financial statements (continued)
For the year ended 31 December 2013

13 Investments accounted for using the cost method

The net book value of investments accounted for using the cost method comprises:

	31 December 2013 HRK millions	31 December 2012 HRK millions
<i>Joint venture:</i>		
HT d.d. Mostar	335	335
	<u>335</u>	<u>335</u>
<i>Associate:</i>		
HP d.o.o. Mostar	2	2
	<u>2</u>	<u>2</u>
	337	337
	<u>337</u>	<u>337</u>

a) Investment in joint venture:

The Company has an ownership interest of 39.1% in its joint venture HT d.d. Mostar which is incorporated in the Republic of Bosnia and Herzegovina. The principal activity of this company is provision of telecommunication services.

All decisions made by the Management Board and all decisions made by the Supervisory Board have to be approved by both of the majority shareholders. Therefore, the investment is classified as a jointly controlled entity. The rest of the company is mainly owned by Federation of Bosnia and Herzegovina (50.10%).

In 2013, HT received a dividend of HRK 21 million from HT d.d. Mostar (2012: HRK 25 million).

b) Investment in associate:

The Company has an ownership interest of 30.29% in its associate HP d.o.o. Mostar which is incorporated in the Republic of Bosnia and Herzegovina. The principal activity of the associate is provision of postal services.

Notes to the financial statements (continued)
For the year ended 31 December 2013

14 Available-for-sale financial assets

Available-for-sale financial assets, at fair value, include the following:

<i>Issuer</i>	<i>Currency</i>	<i>Maturity</i>	31 December 2013 HRK millions	31 December 2012 HRK millions
<i>Domestic bond:</i>				
Government Republic of Croatia	HRK	8 February 2017	35	35
<i>Foreign bonds:</i>				
Government of France	EUR	25 September 2014	153	153
Government of Germany	EUR	12 September 2014	153	151
Government of Germany	EUR	13 July 2014	76	75
Government of Netherland	EUR	15 April 2015	77	77
Government of Netherland	EUR	15 April 2016	76	-
Government of France	EUR	12 January 2013	-	75
Other			8	8
			578	574
Non-current			196	499
Current			382	75
			578	574

Interest rate on domestic bond is 4.75%. Interest rates on foreign bonds are up to 0.75%.

The estimated fair value of investments in bonds at 31 December 2013 is determined by reference to their market value offered on the secondary capital market, which is an active market, at the statement of financial position date and belong to the first financial instruments hierarchy category. There were no changes among financial instruments hierarchy categories in 2013.

Notes to the financial statements (continued)
For the year ended 31 December 2013

15 Loans to banks

<i>Issuer</i>	<i>Currency</i>	<i>Maturity</i>	31 December 2013 HRK millions	31 December 2012 HRK millions
<i>Reverse REPO agreements (Note 29 g) :</i>				
Erste Steiermärkische Bank d.d.	HRK	5 February 2014	149	-
Erste Steiermärkische Bank d.d.	HRK	22 January 2014	95	-
Raiffeisen Bank Austria d.d.	HRK	28 January 2014	73	-
Erste Steiermärkische Bank d.d.	HRK	23 January 2013	-	86
Erste Steiermärkische Bank d.d.	HRK	27 February 2013	-	79
Privredna banka Zagreb d.d.	HRK	29 March 2013	-	74
			317	239

Interest rates at 31 December 2013 on reverse REPO agreements range up to 1.50%.

16 Inventories

	31 December 2013 HRK millions	31 December 2012 HRK millions
Inventories and spare parts	53	78
Merchandise	36	55
	89	133

Notes to the financial statements (continued)
For the year ended 31 December 2013

17 Trade and other receivables

	31 December 2013 HRK millions	31 December 2012 HRK millions
Trade receivables	106	-
Other receivables	19	20
Non-current	<u>125</u>	<u>20</u>
Trade receivables	1,053	1,005
Other receivables	36	66
Current	<u>1,089</u>	<u>1,071</u>
	<u>1,214</u>	<u>1,091</u>

During 2013, the Company entered into several prebankruptcy settlements with its debtors which stipulates that part of reported current trade receivables is converted to non-current receivables (HRK 53 million) with maturities up to 5 years and part of receivables will be subsequently converted to shares in some of entities (HRK 53 million) when procedures of court registration are finalized.

The aging analysis of trade receivables is as follows:

	Total HRK millions	Neither past due nor impaired HRK millions	Past due but not impaired				
			< 30 days HRK millions	31-60 days HRK millions	61-90 days HRK millions	91-120 days HRK millions	>120 days HRK millions
31 December 2013	1,053	757	153	40	29	23	51
31 December 2012	1,005	731	148	69	29	26	2

As at 31 December 2013, trade receivables with a nominal value of HRK 1,083 million (31 December 2012: HRK 1,076 million) were deemed impaired and fully provided for.

Movements in the provision for impairment of receivables were as follows:

	2013 HRK millions	2012 HRK millions
As at 1 January	1,076	1,043
Charge for the year	126	145
Unused amounts reversed	(87)	(82)
Receivables written-off	<u>(32)</u>	<u>(30)</u>
As at 31 December	<u>1,083</u>	<u>1,076</u>

Notes to the financial statements (continued)
For the year ended 31 December 2013

18 Cash and cash equivalents and time deposits

a) *Cash and cash equivalents*

Cash and cash equivalents comprise the following amounts:

	31 December 2013 HRK millions	31 December 2012 HRK millions
Cash on hand and balances with banks	1,198	714
Time deposits with maturity less than 3 months	765	1,842
Reverse REPO agreements affairs with maturity less than 3 months	-	548
	<u>1,963</u>	<u>3,104</u>

b) *Time deposits with maturities more than 3 months*

	31 December 2013 HRK millions	31 December 2012 HRK millions
Foreign bank	634	259
Domestic banks	1	2
	<u>635</u>	<u>261</u>

c) *Currency breakdown of cash and cash equivalents and time deposits:*

	31 December 2013 HRK millions	31 December 2012 HRK millions
HRK	1,852	2,635
EUR	667	712
USD	79	18
	<u>2,598</u>	<u>3,365</u>

Notes to the financial statements (continued)
For the year ended 31 December 2013

19 Trade payables and other liabilities

	31 December 2013 HRK millions	31 December 2012 HRK millions
Content contracts	78	28
Licence for radio frequency spectrum	34	-
Other	18	19
	<hr/>	<hr/>
Non-current	130	47
	<hr/>	<hr/>
Trade payables	1,302	1,268
VAT and other taxes payable	95	44
Payroll and payroll taxes	63	65
Other	16	18
	<hr/>	<hr/>
Current	1,476	1,395
	<hr/>	<hr/>
	1,606	1,442
	<hr/>	<hr/>

20 Deferred income

	31 December 2013 HRK millions	31 December 2012 HRK millions
Connection fee	4	2
	<hr/>	<hr/>
Non-current	4	2
	<hr/>	<hr/>
Prepaid vouchers	68	74
Customer loyalty programme	27	34
Connection fee	1	2
Other	17	8
	<hr/>	<hr/>
Current	113	118
	<hr/>	<hr/>
	117	120
	<hr/>	<hr/>

Notes to the financial statements (continued)

For the year ended 31 December 2013

21 Employee benefit obligations

Long-term employee benefits include retirement and jubilee (length of service) payments. One off retirement benefits are dependent on employees fulfilling the required conditions to enter retirement and are determined in the amount of six average monthly salaries paid to employees in the preceding month. Jubilee benefits are paid in the fixed amount depending on the number of years of service in the Company.

Long-term employee benefits are determined using the projected unit credit method. Gains and losses resulting from changes in actuarial assumptions are recognized as other comprehensive income in the period in which they occur.

Long-term employee benefits include a compensation for the employees detailed described in Note 32.

The movement in the liability recognized in the statement of financial position was as follows:

	2013 HRK millions	2012 HRK millions
As at 1 January	139	158
Effect of change in accounting policy (Note 2.2.)	(17)	-
LTIP – Variable II (Notes 6 and 32)	2	1
Service costs (Note 6)	10	10
Interest costs	7	8
Past service cost (Note 6)	(1)	-
Amortization losses/(gains) (Note 6)	(27)	(1)
Benefit paid	(11)	(13)
Curtailments (Note 6)	-	(27)
Actuarial losses/(gains)	(32)	3
As at 31 December	70	139
Retirement	14	60
Jubilee	52	77
LTIP – Variable II	4	2
	70	139

The principal actuarial assumptions used to determine retirement benefit obligations as at 31 December were as follows:

	2013 in %	2012 in %
Discount rate (annually)	6.5	6.5
Wage and salary increases (annually)	2.0	2.0

Notes to the financial statements (continued)
For the year ended 31 December 2013

22 Provisions for other liabilities and charges

	Legal claims	Asset retirement obligation	Redundancy	Variable salary	Unused vacation	Total
	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions	HRK millions
As at 1 January 2013	66	21	146	64	13	310
Additions	12	1	66	37	10	126
Utilisation	(15)	(1)	(212)	(64)	(13)	(305)
Reversals	(24)	-	-	-	-	(24)
Interest costs	-	2	-	-	-	2
As at 31 December 2013	39	23	-	37	10	109
Non-current	39	23	-	-	-	62
Current	-	-	-	37	10	47
	39	23	-	37	10	109

Notes to the financial statements (continued)

For the year ended 31 December 2013

22 Provisions for other liabilities and charges (continued)

a) *Legal claims*

As at 31 December 2013, the Company has provided estimated amounts for several legal actions and claims that management has assessed as probable to result in outflow of resources of the Company.

b) *Asset retirement obligation*

Asset retirement obligation primarily exists in the case of telecommunications structures constructed on third parties' properties. The Company carries out a revision of the necessary provisions every year.

c) *Redundancy*

Redundancy expenses and provisions include the amount of gross severance payments and other related costs for employees whose employment contracts are terminated during 2013 due to business reasons.

23 Issued share capital

Authorised, issued, fully paid and registered share capital:

	31 December 2013 HRK millions	31 December 2012 HRK millions
81,888,535 ordinary shares of HRK 100 each	<u>8,189</u>	<u>8,189</u>

The number of shares in issue remained unchanged between 1 January 1999 and 31 December 2013.

In 2013, the Company acquired 2,000 of its own shares and are held as 'treasury shares' (2012: 1,931). The Company holds total 3,931 of its own shares as at 31 December 2013.

24 Legal reserves

Legal reserves represent reserves prescribed by the Company Act in the amount of 5% of the net profit for the year, until these reserves amount to 5% of the issued capital. Legal reserves that do not exceed the above amount can only be used to cover current year or prior year losses. If the legal reserves exceed 5% of the issued capital they can also be used to increase the issued capital of the Company. These reserves are not distributable.

25 Retained earnings

In 2013, the Company paid a dividend of HRK 20.51 per share (2012: HRK 22.14) for a total of HRK 1,679 million (2012: HRK 1,813 million).

Notes to the financial statements (continued)
For the year ended 31 December 2013

26 Commitments

a) Operating lease commitments

The Company has operating lease commitments in respect of buildings, land, equipment and cars.

Operating lease charges:

	2013 HRK millions	2012 HRK millions
Current year expense (Note 7)	<u>175</u>	<u>175</u>

Future minimum lease payments under non-cancellable operating leases were as follows:

	31 December 2013 HRK millions	31 December 2012 HRK millions
Within one year	168	174
Between 1 and 5 years	542	573
Greater than 5 years	<u>404</u>	<u>428</u>
	<u>1,114</u>	<u>1,175</u>

The contracts relate primarily to property leases and car leases.

b) Capital commitments

The Company was committed under contractual agreements to capital expenditure as follows:

	31 December 2013 HRK millions	31 December 2012 HRK millions
Intangible assets	92	63
Property, plant and equipment	<u>610</u>	<u>869</u>
	<u>702</u>	<u>932</u>

Notes to the financial statements (continued)

For the year ended 31 December 2013

27 Contingencies

At the time of preparation of these financial statements, there are a number of claims outstanding against the Company. In the opinion of the management, the settlement of these cases will not have a material adverse effect on the financial position of the Company, except for certain claims for which a provision was established (Note 22).

a) Competition / Regulatory matters

The Company vigorously defends all of its competition/regulatory situations, including those disclosed below. There is no history of significant settlements in Croatia under either the Competition Law or imposed by Misdemeanour Courts. Due to the lack of relevant practice and due to the fact that the proceedings are still in progress, the Company is not able to determine the possible outcome of these cases. However management believes that any settlement will be significantly less than the maximum penalties outlined below.

Access to 064/069 numbers case

Pursuant to Metronet notification from 2010, HAKOM initiated supervision and in April 2010 issued a decision that HT shouldn't have conditioned network access with the changed numbering of VAS services with the contract annex, but should have provided the service directly instead. Pursuant to this decision, HT, in June 2012, received a Misdemeanour Indictment based on HAKOM's decision from 2010 proposing 1% fine on the T-Com business annual gross revenue from the year 2008. On the basis of the results for 2008, 1% of the gross revenue would amount to HRK 48 million. HT submitted written defence and proposed suspension of the procedure until the Constitutional Court of RoC decides on HT's Request on conformity assessment of the Law on electronic communications. The last oral hearing was held in April 2013. The Court concluded the trial and HT is waiting now for a Court to render a judgement.

Competition Agency proceedings regarding retransmission of football games

Competition Authority initiated, ex officio, by its decision dated 3 January 2013, formal proceedings against HT relating to abuse of dominant position determining retail market of retransmission of pay TV channels as relevant market due to the fact that ArenaSport channels and premium sport content (such as Croatian national league – MAXtv Prva liga, UEFA Champions League and UEFA Europe League) are available only through MAXtv service.

In June 2013, HT received a Statement of Objections in which it is stated that Competition Agency concluded that, so far, determined facts would imply that HT abused its dominant position on the retail market of the retransmission of pay TV channels by restricting the market to the detriment of consumers, which would amount to the breach of Article 13 item 2 of the Competition Act. HT submitted in writing all objections to the Statement.

The pecuniary fine is limited to up to 10% of yearly turnover of the Company in the last year for which financial reports have been concluded. Also, according to the Agency's practice, the fine is usually connected with the turnover acquired from the services provided on the relevant market. In this case, it would be the turnover realized from provision of a pay-tv service (MAXtv). On the basis of the results for 2012, 10% of the gross revenue of MAXtv services would amount to HRK 68 million.

Notes to the financial statements (continued)

For the year ended 31 December 2013

27 Contingencies (continued)

b) Ownership claim of Distributive Telecommunication Infrastructure (DTI) by the City of Zagreb

With respect to the ducts issue mentioned under Property, plant and equipment (Note 11), on 16 September 2008, the Company received a lawsuit filed by the Zagreb Holding Ltd. branch Zagreb Digital City ("ZHZDG") against the Company. ZHZDG is claiming the ownership of the City of Zagreb over DTI on the area of the City of Zagreb and demanding a payment in the range up to 390 million plus interest.

The suit is based on the legal acts adopted by the Administration and Assembly of the City of Zagreb in the years 2006 and 2007 by which management of DTI has been declared as communal activity executed by the City of Zagreb.

On 10 December 2012, the Company received the partial interlocutory judgement and partial judgement by which it is determined that HT is obliged to pay to ZHZDG the fee for usage of the DTI system, and that until the legal validity of this partial interlocutory judgment, litigation will be stopped regarding the amount of the claim. Furthermore, the claim in the part concerning the establishment of the ownership of the City of Zagreb over DTI and other communal infrastructure for laying telecommunication installations on the area of the City of Zagreb for the purpose of communication-information systems and services is rejected. Decision on the litigation costs is left for the later judgment. On 21 December 2012, the Company submitted the appeal against this judgment, which is still pending.

Since the plaintiff was rejected with the main part of his claim, and since the interlocutory partial judgement defines that the amount of the claim shall be discussed only after legal validity of the judgement, management concluded that no provision is required to be recognised in the financial statements for this case.

Notes to the financial statements (continued)

For the year ended 31 December 2013

28 Balances and transactions with related parties

The transactions disclosed below primarily relate to transactions with the companies owned by DT AG. The Company enters into transactions in the normal course of business on an arm's length basis. These transactions included the sending and receiving of international traffic to/from these companies during 2013 and 2012. Further, DT AG provided technical assistance to the Company of HRK 19 million (2012: HRK 13 million).

The main transactions with related parties during 2013 and 2012 were as follows:

	Revenue		Expenses	
	2013	2012	2013	2012
<i>Related party:</i>	HRK millions	HRK millions	HRK millions	HRK millions
<i>Immediate parent</i>				
Deutsche Telekom AG, Germany	30	30	70	59
<i>Joint venture</i>				
HT d.d. Mostar, Bosnia and Herzegovina	23	32	42	53
<i>Subsidiaries of immediate parent</i>				
Telekom Deutschland GmbH, Germany	9	19	4	8
T-Mobile Austria GmbH, Austria	3	5	1	3
T-Systems International GmbH, Germany	3	3	9	6
Others	19	22	11	8
	87	111	137	137

The statement of financial position includes the following balances resulting from transactions with related parties:

	Receivables		Payables	
	31 December	31 December	31 December	31 December
<i>Related party:</i>	2013	2012	2013	2012
	HRK millions	HRK millions	HRK millions	HRK millions
<i>Immediate parent</i>				
Deutsche Telekom AG, Germany	3	4	149	48
<i>Joint venture</i>				
HT d.d. Mostar, Bosnia and Herzegovina	-	-	9	3
<i>Subsidiaries of immediate parent</i>				
Telekom Deutschland GmbH, Germany	-	-	45	80
T-Mobile Austria GmbH, Austria	-	-	4	18
T-Mobile Czech a.s., Czech Republic	-	-	6	16
T-Systems International GmbH, Germany	-	-	6	2
Others	6	3	22	68
	9	7	241	235

Notes to the financial statements (continued)
For the year ended 31 December 2013

28 Balances and transactions with related parties (continued)

The Company had the following balances on transactions with its subsidiaries excluding loans in the amount of HRK 133 million (31 December 2012: HRK 101 million):

<i>Subsidiaries:</i>	Revenue HRK millions	Expenses HRK millions	Receivables HRK millions	Payables HRK millions
2013 / 31 December 2013	109	122	25	59
2012 / 31 December 2012	<u>90</u>	<u>122</u>	<u>30</u>	<u>81</u>

The Company was committed under contractual agreements to capital expenditure with its subsidiaries as follows:

	31 December 2013 HRK millions	31 December 2012 HRK millions
Intangible assets	50	20
Property, plant and equipment	<u>30</u>	<u>37</u>
	<u>80</u>	<u>57</u>

Compensation of the Supervisory Board

The chairman of the Supervisory Board receives remuneration in the amount of 1.5 of the average net salary of the employees of the Company paid in the preceding month. To the deputy chairman, the amount of 1.25 of the average net salary of the employees of the Company paid in the preceding month is paid, while any other member receives the amount of one average net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time the Chairman of the Audit Committee of the Supervisory Board, in the amount of 1.5 of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time a Member of the Audit Committee of the Supervisory Board, in the amount of 1.25 of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time a Member of the Compensation and Nomination Committee of the Supervisory Board, in the amount of 1.25 of the average monthly net salary of the employees of the Company paid in the preceding month. DT AG representatives do not receive any remuneration for the membership in the Supervisory Board due to a respective policy of DT AG.

Notes to the financial statements (continued)
For the year ended 31 December 2013

28 Balances and transactions with related parties (continued)

Compensation of the Supervisory Board (continued)

In July 2013, the Supervisory Board established the Sustainability Committee. The Committee consists of three members, two external experts and one member of the Supervisory Board. Members of the Sustainability Committee who are not at the same time members of the Supervisory Board are entitled to monthly remuneration in the amount of 0.25 of the average net salary of employees of the Company paid in the preceding month. At this time, only one member receives remuneration, which is not being paid directly to him but in line with his instruction, remuneration is paid out to the benefit of the Fund for award of scholarships to Croatian Homeland War veterans and their children.

In 2013, the Company paid a total amount of HRK 0.7 million (2012: HRK 0.7 million) to the members of its Supervisory Board. No loans were granted to the members of the Supervisory Board.

Compensation to key management personnel

In 2013, the total compensation paid to key management personnel of the Company amounted to HRK 33 million (2012: HRK 33 million). Key management personnel include members of the Management Boards and the operating directors of the Company.

Compensation paid to key management personnel includes:

	2013	2012
	HRK millions	HRK millions
Short-term benefits	33	30
Share-based payments	-	3
	<u>33</u>	<u>33</u>

Notes to the financial statements (continued)

For the year ended 31 December 2013

29 Financial risk management objectives and policies

The Company is exposed to international service-based markets. As a result, the Company can be affected by changes in foreign exchange rates. The Company also extends credit terms to its customers and is exposed to a risk of default. The significant risks, together with the methods used to manage these risks, are described below. The Company does not use derivative instruments either to manage risk or for speculative purposes.

a) Credit risk

The Company has no significant concentration of credit risk with any single counter party or group of counterparties with similar characteristics. The Company procedures are in force to ensure on a permanent basis that sales are made to customers with an appropriate credit history and do not exceed an acceptable credit exposure limit.

The Company does not guarantee obligations of other parties. The Company has issued guarantees for obligations of its subsidiary in total amount of EUR 7.8 million (currency clause).

The Company considers that its maximum exposure is reflected by the amount of debtors (Note 17) net of provisions for impairment recognized at the statement of financial position date.

Additionally, the Company is exposed to risk through cash deposits in the banks. As at 31 December 2013, the Company had business transactions with nine banks (2012: nine banks). The Company held cash and deposits in six banks almost exclusively. For five domestic banks with foreign ownership, the Company received guarantees for deposits given from parent banks which have a minimum rating of BBB+ or guarantees in form of low-risk government securities. The management of this risk is focused on dealing with the most reputable banks in foreign and domestic ownership at the domestic and foreign markets and on contacts with the banks on a daily basis.

The credit quality of financial assets that are neither past due nor impaired can be assessed by historical information about counterparty default rates:

	31 December 2013	31 December 2012
	HRK millions	HRK millions
Trade receivables for rendered telecom services to domestic customers	736	705
Trade receivables for rendered telecom services to foreign customers	21	26
	<u>757</u>	<u>731</u>

Notes to the financial statements (continued)
For the year ended 31 December 2013

29 Financial risk management objectives and policies (continued)

b) Liquidity risk

The Company policy is to maintain sufficient cash and cash equivalents or to have available funding through an adequate amount of committed credit facilities to meet its commitments for the foreseeable future.

Any excess cash is invested mostly in available-for-sale financial assets.

all amounts in HRK millions	Trade and other payables			Other non-current liabilities			Total
	Less than 3 months	3 to 12 months	Total	1 to 3 years	3 to 5 years	> 5 years	
Year ended 31 December 2013	1,385	91	1,476	91	22	17	130
Year ended 31 December 2012	1,345	50	1,395	29	6	12	47

c) Interest rate risk

The Company's exposure to the risk of changes in market interest rates relates primarily to the Company's available-for-sale financial assets, cash, cash equivalents and time deposits.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Company's profit post tax (through the impact on floating rate investments).

	Increase/ decrease in basis points	Effect on profit post tax HRK millions
Year ended 31 December 2013		
HRK	+100	9
	-100	(9)
EUR	+100	9
	-100	(9)
Year ended 31 December 2012		
HRK	+100	13
	-100	(13)
EUR	+100	9
	-100	(9)

Notes to the financial statements (continued)

For the year ended 31 December 2013

29 Financial risk management objectives and policies (continued)

d) Foreign currency risk

The Company's functional currency is the Croatian Kuna. Certain assets and liabilities are denominated in foreign currencies which are translated at the valid middle exchange rate of the Croatian National Bank at each statement of financial position date. The resulting differences are charged or credited to the statement of comprehensive income but do not affect short-term cash flows.

A significant amount of deposits in the banks, available-for-sale financial assets and cash equivalents are made in foreign currency, primarily in Euro. The purpose of these deposits is to hedge foreign currency denominated liabilities and liabilities indexed to foreign currencies from changes in the exchange rate. The following table demonstrates the sensitivity to a reasonably possible change in the Euro exchange rate, with all other variables held constant, of the Company's profit post tax due to changes in the fair value of monetary assets and liabilities.

	Increase/ decrease in EUR rate	Effect on profit post tax HRK millions
Year ended 31 December 2013	+3%	26
	-3%	(26)
Year ended 31 December 2012	+3%	27
	-3%	(27)

e) Fair value estimation

The fair value of securities included in available-for-sale financial assets is estimated by reference to their quoted market price at the statement of financial position date. The Company's principal financial instruments not carried at fair value are trade receivables, other receivables, non-current receivables, trade and other payables. The historical cost carrying amounts of receivables and payables, including provisions, which are all subject to normal trade credit terms, approximate their fair values.

f) Capital management

The primary objective of the Company's capital management is to ensure that it supports its business and maximise shareholder value. The capital structure of the Company consists of equity attributable to shareholders, comprising issued capital, reserves and retained earnings and totals HRK 10,821 million as at 31 December 2013 (31 December 2012: HRK 11,029 million).

The Company manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes during the years ended 31 December 2013 and 31 December 2012 (Notes 23 and 25).

Notes to the financial statements (continued)
For the year ended 31 December 2013

29 Financial risk management objectives and policies (continued)

g) Accepted collaterals

Accepted collaterals for reverse REPO affairs include:

	31 December 2013 HRK millions	31 December 2012 HRK millions
<i>Foreign bonds:</i>		
Government of Germany	251	-
Government of Austria	-	581
Government of France	-	75
<i>Foreign treasury bills:</i>		
Government of France	76	-
Government of Germany	-	150
	<u>327</u>	<u>806</u>

All above stated values are fair market values. None of accepted collaterals is currently sold nor repledged. There are no specific terms and conditions related to the use of collaterals.

30 Financial instruments

Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments:

	Carrying amount		Fair value	
	31 December 2013 HRK millions	31 December 2012 HRK millions	31 December 2013 HRK millions	31 December 2012 HRK millions
<i>Financial assets:</i>				
Cash and cash equivalents	1,963	3,104	1,963	3,104
Time deposits	635	261	635	261
Available-for-sale assets, non-current	196	499	196	499
Available-for-sale assets, current	382	75	382	75
Loans to banks	317	239	317	239
Loans given to subsidiary	133	101	133	101
<i>Financial liabilities:</i>				
Interest-bearing loans	12	13	12	13

Market values have been used to determine the fair value of listed available-for-sale financial assets. The fair value of loans has been calculated by discounting the expected future cash flows at prevailing interest rates.

Notes to the financial statements (continued)

For the year ended 31 December 2013

31 Authorization for Services and Applicable Fees

The Company is party to the following Authorization for Services, none of which are within the scope of IFRIC 12:

a) Service authorization for the performance of electronic communications services in a fixed and mobile network

On 1 July 2008, a new Law on Electronic Communications entered into force and introduced general authorization for all electronic communications services and networks. In the meantime, three Amendments to the Law on Electronic Communications entered into force and were published in the Official Gazette No. 90/11, 133/12 and 80/13. Pursuant to Article 32 of the Law on Electronic Communications, the Company is entitled to provide the following electronic communication services based on the general authorisation which was last updated on 15 November 2010:

- publicly available telephone service in the fixed electronic communications network,
- publicly available telephone service in the mobile electronic communications network,
- lease of electronic communication network and/or lines,
- transmission of image, voice and sound through electronic communication networks (which excludes services of radio diffusion),
- value added services,
- internet access services,
- voice over internet protocol services,
- granting access and shared use of electronic communications infrastructure and associated facilities,
- satellite services,
- providing of information about the numbers of all subscribers of publicly available telephony services in the Republic of Croatia,
- issuing of comprehensive publicly available directory of all subscribers of publicly available telephone services in the Republic of Croatia, and
- other services.

In accordance with HAKOM's decision of 28 November 2005, the Company was designated as the Universal services provider for a period of five years i.e. till 29 November 2010. Due to expiration of the 5-year period, on 27 October 2010, HAKOM adopted a new decision thereby designating the Company as the operator of the following universal services in the territory of the Republic of Croatia for the next 5-year period starting from 29 November 2010:

- access to the public telephone network and publicly available telephone services at a fixed location, allowing end-users to make and receive local, national and international telephone calls, facsimile communications and data communications, at data rates that are sufficient to permit functional internet access, taking into account prevailing technologies used by the majority of subscribers and technological feasibility,
- access for end-users, including users of public pay telephones, to a telephone directory enquiry service,
- setting up of public pay telephones on public places accessible at any time, in accordance with the reasonable needs of end-users in terms of the geographical coverage, the quality of services, the number of public pay telephones and the accessibility of such telephones for disabled persons,
- special measures for disabled persons, including access to emergency services, telephone directory enquiry services and directories, equivalent to that enjoyed by other end-users, and
- special pricing systems adjusted to the needs of the socially disadvantaged groups of end-users.

Notes to the financial statements (continued)

For the year ended 31 December 2013

31 Authorization for Services and Applicable Fees (continued)

a) *Service authorization for the performance of electronic communications services in a fixed and mobile network (continued)*

Following the later decision of HAKOM, the Company is no longer designated as universal service operator for service access for end-users to at least one comprehensive directory of all subscribers of publicly available telephone services, however, shall continue to provide the service on commercial basis.

b) *Authorization for usage of radio frequency spectrum*

HAKOM issued to the Company the following licenses for use of the radio frequency spectrum for public mobile electronic communications networks:

- licence for the use of radio frequency spectrum in 900 MHz and 1800 MHz frequency bands with the validity from 1 December 2011 until 18 October 2024,
- licence for the use of radio frequency spectrum in 2100 MHz frequency band with the validity from 1 January 2010 until 18 October 2024,
- licence for the use of radio frequency spectrum in 800 MHz frequency band with the validity from 29 October 2012 until 18 October 2024, and
- licence for the use of radio frequency spectrum in 800 MHz frequency band with the validity from 6 November 2013 until 18 October 2024.

HAKOM also issued to the Company licences for the use of radio frequency spectrum for satellite services (DTH services) with the validity from 12 August 2010 until 11 August 2015.

c) *Fees for providing electronic communications services*

Pursuant to the Law on Electronic Communications, the Company is obliged to pay the fees for the use of addresses and numbers, radio frequency spectrum and for the performance of other tasks of HAKOM pursuant to the ordinances of HAKOM and Ministry of the maritime affairs, transport and infrastructure. The said regulations prescribe the calculation and the amount of fees. These fees are paid for the current year or one year in advance (in case of fees for usage of radio frequency spectrum).

In 2013, the Company paid the following fees:

- the fees for the use of addresses, numbers and radio frequency spectrum pursuant to the ordinance passed by the Ministry of the maritime affairs, transport and infrastructure (in favour of State budget, Official Gazette No. 154/08, 28/09, 97/10 and 92/12) and
- the fees for use of addresses, numbers and radio frequency spectrum and for the performance of other tasks of HAKOM. Pursuant to the ordinance passed by HAKOM (in favour of HAKOM's budget, Official Gazette No. 138/12).

Notes to the financial statements (continued)

For the year ended 31 December 2013

31 Authorization for Services and Applicable Fees (continued)

d) *Audiovisual and electronic media services*

Pursuant amendment of the Law on audiovisual activities, which entered into the force in July 2011, the Company is obliged to pay the fee in the amount of 2% of the total annual gross income generated from the performing of audiovisual activities on demand for the purpose of the implementation of the National Programme.

Also, the Company (as the operator of public communication network) is obliged to pay a fee in the amount of 0.8% of the total annual gross income generated in previous calendar year by performing transmission and/or retransmission of audiovisual programmes and their parts through public communication network, including internet and cable distribution for the purpose of the implementation of the National Programme.

Pursuant to the Law on Electronic Media, which entered into force on 29 December 2009, the Company is obliged to pay upon the request the fee of 0.5% of the annual gross revenues realized from the provision of audiovisual media services and the electronic publication services.

e) *Electronic communications infrastructure and associated facilities*

The Company, as the infrastructure operator, is obligated to pay fees for the right of way in accordance with the Law on Electronic Communications. The fees for the right of way are defined by the Ordinance on Certificate and Fees for the Right of Way (Official Gazette No. 152/11) that was adopted by HAKOM in December 2011 and became effective as of 4 January 2012. The fee is calculated according to the area of land used for the installation of electronic communications infrastructure and associated facilities.

Notes to the financial statements (continued)

For the year ended 31 December 2013

32 Share-based and non share-based payment transactions

Various mid-term (Transitional HT MTIP 2011) and long-term incentive plans (LTIPs – HT Variable II 2011, HT Variable II 2012 and HT Variable II 2013) exist at Company level to ensure competitive total compensation for members of the Management Board, senior executives and other beneficiaries. The plans promote the medium and long-term value enhancement of the Company, thus aligning the interests of management and shareholders.

Transitional HT MTIP 2011 is set up as a cash-based plan linked to achievement of two equally weighted, share-based performance parameters, related to the value of HT share – one absolute and one relative. The first target is based on the performance of the share price by a certain percentage and the second is related to the share price development compared to the composite return index. If both performance targets are achieved, then the total amount earmarked as an award to the beneficiaries by the respective employers is paid out; if one performance target is achieved, 50% of the amount is paid out, and if neither performance target is achieved, no payment is made. MTIP targets cannot be changed during the MTIP duration. Duration of the plan is three years effective from 1 January 2011 to 31 December 2013.

Upon expiry of the term of the plan, the Supervisory Board shall determine whether each of the targets has been achieved. Based on the findings of the Supervisory Board, the Management Board shall determine and announce the level of target achievement.

The incentives themselves consist of 20% or 30% of the participants' individual annual salary as contracted on the beginning of the plan, depending on the management level of the participant and according to the Supervisory Board decision. Participant's individual annual salary is defined as the annual amount of total fixed salary and the amount of variable salary in case of a 100% target achievement.

In 2013, there was no reward payment to participants of HT MTIP 2010, which ended on 31 December 2012. Based on decision of the Supervisory Board it was established that none of HT MTIP 2010 target out of two has been achieved.

Compensation model for International Business Leaders (BLT's) was introduced in 2011. It consists of Variable I (Matching Shares Plan - MSP) and Variable II.

LTIPs – HT Variable II 2011, HT Variable II 2012 and HT Variable II 2013 are cash-based plans with four equally weighted performance parameters that cannot be changed during plan duration. Two targets are financial KPIs, adjusted Earnings Per Share (EPS) and adjusted operating Return On Capital Employed (ROCE), third and fourth targets are customer and employee satisfaction. Duration of the plan is four years effective from 1 January every year.

The Variable II amount awarded to International Business Leaders (BLT's) is fixed sum specified in the individual employment contract, while to other participants rewarded amount is 30% or 20% of the participants' individual annual salary as contracted on the beginning of the plan, depending on management level of the participant and according to the Supervisory Board decision. Participants' individual annual salary is defined as the annual total fixed salary and the annual variable salary in case of a 100% target achievement.

In contrast to the former MTIP structure, Variable II offers the option of exceeding the amounts earmarked for award, limited to 150% of the award volume per parameter. The parameters are independent of each other hence, each parameter is assessed separately. Both potential excesses and shortfalls in relation to targets are accounted for on a graded basis per target parameter (departure from the principle of "all or nothing").

Notes to the financial statements (continued)

For the year ended 31 December 2013

32 Share-based and non share-based payment transactions (continued)

The MSP is program under which the participant can receive HT shares on expiry of a four-year period. The participant is obliged to invest an amount from 10% to a maximum 33.33% of the paid out gross annual variable salary to HT shares. The participant is granted one additional HT share for each share, under condition that he/she held them continuously for a period of at least four years from the date of purchase (vesting period). Employee services are recognized as expenses on a pro rata basis over the vesting period. The Company is measuring value of employee services, indirectly, by reference to the fair value of the equity instruments granted. The fair value of the equity instruments granted is measured at grant date by using observable market price.

All gains and expenses resulting from changes of the related provisions for all MTIP and LTIP plans recognized for employee services received during the year are shown in the following table:

	2013 HRK millions	2012 HRK millions
Expenses for providing for payments	(2)	(1)
Gains arising from cancellation of provision	-	3
	<u>(2)</u>	<u>2</u>

33 Auditor's fees

The auditors of the Company's financial statements have rendered services of HRK 4.3 million in 2013 (2012: HRK 4.3 million). Services rendered in 2013 and 2012 mainly relate to audits and reviews of the financial statements, audit of financial statements prepared for regulatory purposes and upgrade of Cost and Profitability Calculation tool.

34 Events after reporting period

No events or transactions have occurred since 31 December 2013 or are pending that would have a material effect on the financial statements at that date or for the period then ended, or that are of such significance in relation to the Company's affairs to require disclosure in the financial statements.