

**Ericsson Nikola Tesla d.d. Zagreb**

**Annual financial report**

**31 December 2009**

This version of the accompanying documents is a translation from the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

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## Company profile

### **History and incorporation**

Ericsson Nikola Tesla d.d. Zagreb (the Company) is a Croatian company with sixty years of continuous operations. It has always been a leading specialized supplier and exporter of telecommunications equipment, software solutions and services in Central and Eastern Europe.

The Company was founded as a result of the privatisation of the enterprise Nikola Tesla - Poduzeće za proizvodnju telekomunikacijskih sistema i uređaja, po.

According to the ownership structure as at 31 December 2009, Telefonaktiebolaget LM Ericsson (Ericsson) holds 49.07% of the shares. The Croatian Privatisation Fund owns 0.89% of the Company's shares, treasury shares amount to 1.09% and other shareholders own the remaining 48.95% of the Company's shares.

### **Principal activities**

The principal activities of the Company are the following: research and development of telecommunications software and services, design and integration of total communications solutions for operators and enterprises as well as testing, sales and maintenance of communications solutions and systems in the Republic of Croatia, selected customers in Central and Eastern Europe, the Middle East and Africa as well as companies within the Ericsson Group.

Ericsson Nikola Tesla d.d. Zagreb is a joint stock company incorporated in Croatia. The headquarters of the Company are in Zagreb, Krapinska 45.

## Company profile (continued)

### **Supervisory Board, Management Board and executive management**

#### *The Supervisory Board*

The Supervisory Board members during 2009 and up to the release of these statements were:

Roland Nordgren	Appointed on 27 May 2008	Chairperson
Ignac Lovrek	Reappointed on 31 May 2007	Member; Vice-Chairperson
Carita Jönsson	Reappointed on 27 May 2008	Member
Zvonimir Jelić	Reappointed on 5 June 2006	Member and employees' representative
Darko Marinac	Resigned as member on 20 November 2009	

#### *The Management Board*

The Management Board has one member:

Gordana Kovačević	Appointed on 1 January 2005	President
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## Company profile (continued)

### *Executive management*

As at 31 December 2009, the Company's executive management comprised:

#### ETK Core MT:

Gordana Kovačević	Company President
Andrew Skelton	Company CFO
Hrvoje Benčić	Director, Operators Segment
Josip Jakovac	Director, Sales and Marketing for CIS
Lars Olander	Director, Research and Development Center
Milan Živković	Director, Strategy and Business Development

#### ETK Extended MT:

##### Core MT members

Alen Ludaš	Head of MCA Mobilkom Austria Group
Boris Drilo	Director, ICT for Government/Enterprise Segment
Branko Dronjić	Director, Business Ericsson Test Environment
Damir Bušić	Unit Manager, Multimedia
Dragan Fratrić	Acting Unit Manager, General Services
Goran Ožbolt	Director, Sales and Marketing for Tele2 and Alternative Operators
Ivan Barać	Director, Sales and Marketing for T-HT
Jagoda Barać	Director, Sales and Marketing for Neighboring countries
Marijana Đuzel	Director, HR and Organization (including Legal Affairs)
Mathias Danielsson	Director, Global Service Delivery Center
Milan Popović	Director, Project Management
Miroslav Kantolić	Director, Sales and Marketing for VIPnet and Si.mobil
Snježana Bahtijari	Director, Communication
Snježana Ivezić-Torbarina	Director, Sales and Marketing for Enterprise
Tihomir Šicel	Sales Advisor

## Responsibilities of the Management and Supervisory Boards for the preparation and approval of the annual financial statements

The Management Board is required to prepare financial statements for each financial year which give a true and fair view of the financial position of the Company and of the results of its operations and cash flows, in accordance with applicable accounting standards, and is responsible for maintaining proper accounting records to enable the preparation of such financial statements at any time. It has a general responsibility for taking such steps as are reasonably available to it to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; make judgements and estimates that are reasonable and prudent; and prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the business situation of the Company together with the annual financial statements, following which the Supervisory Board is required to approve the annual financial statements which will be presented to the General Assembly of Shareholders.

The financial statements set out on pages 6 to 69 were authorised by the Management Board on 23 February 2010 for issue to the Supervisory Board and are signed below.



Gordana Kovačević  
Director  
Ericsson Nikola Tesla d.d. Zagreb  
Krapinska 45  
10000 Zagreb  
Croatia

**Independent auditors' report**

**To the shareholders of Ericsson Nikola Tesla d.d., Zagreb**

We have audited the accompanying financial statements of Ericsson Nikola Tesla d.d (the 'Company') which comprise the statement of financial position as of 31 December 2009 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 notes.

**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. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

**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 judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the 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 accompanying financial statements present fairly, in all material respects, the financial position of the Company as of 31 December 2009, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

*PricewaterhouseCoopers d.o.o.*

PricewaterhouseCoopers d.o.o.  
Zagreb, 23 February 2010

Ericsson Nikola Tesla d.d. Zagreb  
Statement of comprehensive income  
for the year ended 31 December 2009

	<i>Notes</i>	<b>2009</b>	<b>2008</b>
		<b>HRK '000</b>	<b>HRK '000</b>
Sales revenue	3	1,400,011	1,800,059
Cost of sales		(1,213,945)	(1,499,146)
<b>Gross profit</b>		186,066	300,913
Other income	5	17,325	20,110
Distribution expenses		(72,894)	(85,027)
Administrative expenses		(37,024)	(44,825)
Other expenses	6	(27,793)	(28,303)
<b>Operating profit</b>		65,680	162,868
Finance income	8	61,894	63,389
Finance expense	8	(757)	(14,287)
Finance income - net		61,137	49,102
<b>Profit before tax</b>		126,817	211,970
Income tax	9	1,630	(7,602)
<b>Profit for the year</b>		<u>128,447</u>	<u>204,368</u>
Other comprehensive income		-	-
Total comprehensive income for the year		<u>128,447</u>	<u>204,368</u>
Earnings per share (HRK)	10	<u>98.09</u>	<u>155.50</u>

The notes set out on pages 12 to 69 form an integral part of these financial statements.



Ericsson Nikola Tesla d.d. Zagreb

Statement of financial position

as at 31 December 2009

	<i>Notes</i>	<b>2009</b> <b>HRK '000</b>	<b>2008</b> <b>HRK '000</b>
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	11	146,351	163,289
Intangible assets	12	4,425	6,265
Loans and receivables	13	278,897	349,911
Equity securities		45	45
Deferred tax assets	14	12,295	13,008
<b>Total non-current assets</b>		<u>442,013</u>	<u>532,518</u>
<b>Current assets</b>			
Inventories	15	24,059	53,110
Trade receivables	16	451,247	486,732
Receivables from related parties	28(c)	58,905	59,111
Income tax receivable		9,452	-
Other receivables	17	29,588	20,524
Financial assets at fair value through profit or loss	18	120,873	49,331
Prepayments and accrued income		1,371	1,290
Cash and cash equivalents	19	414,935	318,303
<b>Total current assets</b>		<u>1,110,430</u>	<u>988,401</u>
<b>TOTAL ASSETS</b>		<u>1,552,443</u>	<u>1,520,919</u>

The notes set out on pages 12 to 69 form an integral part of these financial statements.

Ericsson Nikola Tesla d.d. Zagreb  
Statement of financial position (continued)  
as at 31 December 2009

	<i>Notes</i>	<b>2009</b>	<b>2008</b>
		<b>HRK '000</b>	<b>HRK '000</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>			
Share capital	<i>20(a)</i>	133,165	133,165
Treasury shares	<i>20(b)</i>	(34,173)	(46,389)
Legal reserves	<i>20(c)</i>	20,110	20,110
Retained earnings		1,081,121	1,059,241
<b>Total equity</b>		<u>1,200,223</u>	<u>1,166,127</u>
<b>Non-current liabilities</b>			
Interest-bearing borrowings	<i>23</i>	4,965	6,425
Employee benefits	<i>24</i>	5,126	5,009
<b>Total non-current liabilities</b>		<u>10,091</u>	<u>11,434</u>
<b>Current liabilities</b>			
Payables to related parties	<i>28(c)</i>	67,839	74,281
Interest-bearing borrowings	<i>23</i>	1,655	2,408
Trade and other payables	<i>25</i>	101,605	102,020
Income tax payable		-	2,811
Financial liabilities at fair value through profit or loss	<i>18</i>	-	6,360
Provisions	<i>26</i>	23,730	12,477
Accrued charges and deferred revenue	<i>27</i>	147,300	143,001
<b>Total current liabilities</b>		<u>342,129</u>	<u>343,358</u>
<b>Total liabilities</b>		<u>352,220</u>	<u>354,792</u>
<b>TOTAL EQUITY AND LIABILITIES</b>		<u>1,552,443</u>	<u>1,520,919</u>

The notes set out on pages 12 to 69 form an integral part of these financial statements.

Ericsson Nikola Tesla d.d. Zagreb

Statement of cash flows

for the year ended 31 December 2009

	<i>Notes</i>	<b>2009</b>	<b>2008</b>
		<b>HRK '000</b>	<b>HRK '000</b>
<b>Cash flows from operating activities</b>			
<i>Profit before tax</i>		<u>126,817</u>	<u>211,970</u>
Adjustments for:			
Depreciation and amortisation	11,12	64,787	73,283
Impairment losses and reversals		21,901	28,303
Net creation/(reversal) of provisions	26	16,176	(375)
Net gain on sale of property, plant and equipment	5	(65)	(117)
Net (gain)/loss on re-measurement of financial assets	8	(429)	14,084
Amortisation of discount	8	(15,985)	(13,261)
Interest income	8	(39,538)	(48,711)
Interest expense	8	757	203
Foreign exchange gains		(5,942)	(1,417)
Equity-settled transactions		<u>11,129</u>	<u>6,656</u>
		179,608	270,618
Decrease in loans and receivables		78,336	19,055
Decrease in inventories		28,800	2,022
Decrease in receivables		20,976	120,016
Decrease in payables		<u>(10,653)</u>	<u>(83,929)</u>
<i>Cash generated from operations</i>		<u>297,067</u>	<u>327,782</u>
Interest paid		(757)	(203)
Income taxes (paid)/refunded		<u>(12,262)</u>	<u>14,852</u>
<b><i>Net cash from operating activities</i></b>		<b><u>284,048</u></b>	<b><u>342,431</u></b>
<b>Cash flows from investing activities</b>			
Interest received		37,922	48,655
Proceeds from sale of property, plant and equipment		151	291
Purchases of property, plant and equipment, and intangible assets	11,12	(46,095)	(63,901)
Increase in non-current deposits		522	478
(Purchase of)/proceeds from disposal of financial assets		<u>(77,473)</u>	<u>686</u>
<b><i>Net cash used in investing activities</i></b>		<b><u>(84,973)</u></b>	<b><u>(13,791)</u></b>

The notes set out on pages 12 to 69 form an integral part of these financial statements.

Ericsson Nikola Tesla d.d. Zagreb  
Statement of cash flows (continued)  
for the year ended 31 December 2009

	<i>Notes</i>	<b>2009</b>	<b>2008</b>
		<b>HRK '000</b>	<b>HRK '000</b>
<b>Cash flows from financing activities</b>			
Proceeds from borrowings		-	8,085
Repayment of interest-bearing borrowings		(2,213)	(655)
Purchase of treasury shares	20(b)	(11,380)	(3,895)
Dividends paid	21	(91,758)	(355,305)
<b>Net cash used in financing activities</b>		<b>(105,351)</b>	<b>(351,770)</b>
Effects of exchange rate changes on cash and cash equivalents		2,908	3,157
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>96,632</b>	<b>(19,973)</b>
Cash and cash equivalents at the beginning of the year	19	318,303	338,276
<b>Cash and cash equivalents at the end of the year</b>	<b>19</b>	<b>414,935</b>	<b>318,303</b>

The notes set out on pages 12 to 69 form an integral part of these financial statements.

Ericsson Nikola Tesla d.d. Zagreb

Statement of changes in equity  
for the year ended 31 December 2009

	Share capital HRK '000	Treasury shares HRK '000	Legal reserves HRK '000	Retained earnings HRK '000	Total HRK '000
<b>As at 1 January 2008</b>	133,165	(45,165)	20,110	1,207,524	1,315,634
<b>Changes in equity for 2008</b>					
Total comprehensive income	-	-	-	204,368	204,368
Dividend distribution for 2007, Note 21	-	-	-	(355,305)	(355,305)
Repurchase of treasury shares, Note 20 (b)	-	(3,895)	-	-	(3,895)
Share-based payments, Note 24 (b)	-	2,671	-	(2,671)	-
Equity-settled transactions, Note 24 (b)	-	-	-	6,656	6,656
Deferred tax related to equity increase, Note 9	-	-	-	(1,331)	(1,331)
<b>As at 31 December 2008</b>	<u>133,165</u>	<u>(46,389)</u>	<u>20,110</u>	<u>1,059,241</u>	<u>1,166,127</u>
<b>As at 1 January 2009</b>	133,165	(46,389)	20,110	1,059,241	1,166,127
<b>Changes in equity for 2009</b>					
Total comprehensive income	-	-	-	128,447	128,447
Dividend distribution for 2008, Note 21	-	-	-	(91,758)	(91,758)
Repurchase of treasury shares, Note 20 (b)	-	(11,380)	-	-	(11,380)
Share-based payments, Note 24 (b)	-	23,596	-	(23,596)	-
Equity-settled transactions, Note 24 (b)	-	-	-	11,129	11,129
Deferred tax related to equity increase, Note 9	-	-	-	(2,342)	(2,342)
<b>As at 31 December 2009</b>	<u>133,165</u>	<u>(34,173)</u>	<u>20,110</u>	<u>1,081,121</u>	<u>1,200,223</u>

The notes set out on pages 12 to 69 form an integral part of these financial statements.

# Notes to the financial statements

## 1 Significant accounting policies

### ***Reporting entity***

Ericsson Nikola Tesla d.d. Zagreb (the Company) is a joint stock company incorporated and domiciled in Croatia. The address of its registered office is Krapinska 45, 10000 Zagreb, the Republic of Croatia. The Company's shares are listed on the Public Joint Stock Company listing on the Zagreb Stock Exchange. These financial statements were authorised for issue by the Management Board on 23 February 2010 for approval by the Supervisory Board. A summary of the Company's principal accounting policies is set out below.

### ***Statement of compliance***

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). These financial statements also comply with the Croatian Accounting Act in effect on the date of issue of these financial statements. These financial statements are a translation of the official statutory IFRS financial statements.

### ***Basis of preparation***

The financial statements are prepared on the historical cost basis, with the exception of financial instruments which are carried at fair value. These comprise derivative financial instruments and financial assets and liabilities at fair values through profit or loss. The accounting policies have been consistently applied to all periods presented in these financial statements and are consistent with those used in the previous year.

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of revision and future periods if the revision affects both current and future periods. Judgements made by management in the application of IFRSs that have significant effect on the financial statements and estimates are discussed in Note 2.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures

##### *(a) New and amended standards adopted by the Company*

The Company has adopted the following new and amended IFRSs as of 1 January 2009:

IFRS 7, 'Financial instruments – Disclosures' (Amendment) – effective 1 January 2009. The amendment requires enhanced disclosures about fair value measurement and liquidity risk. In particular, the amendment requires disclosure of fair value measurements by level of fair value hierarchy. As the change in accounting policy only results in additional disclosures, there is no impact on earnings per share.

Revised IAS 1, 'Presentation of Financial Statements' (effective for annual periods beginning on or after 1 January 2009). The revised Standard requires information in financial statements to be aggregated on the basis of shared characteristics and introduces a statement of comprehensive income. Items of income and expense and components of other comprehensive income may be presented either in a single statement of comprehensive income (effectively combining the income statement and all non-owner changes in equity in a single statement), or in two separate statements (a separate income statement followed by a statement of comprehensive income). As the change in accounting policy only impacts presentation aspects, there is no impact on earnings per share.

IFRS 2 (Amendment), 'Share-based Payment' (effective from 1 January 2009). The amendments to the Standard clarify the definition of vesting conditions and introduce the concept of non-vesting conditions. Non-vesting conditions are to be reflected in grant-date fair value and failure to meet non-vesting conditions will generally result in treatment as a cancellation. The amendment does not have a material impact on Company's financial statements.

IFRS 8, 'Operating segments' (effective from 1 January 2009). IFRS 8 replaces IAS 14, 'Segment reporting'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes. In addition, the segments are reported in a manner that is more consistent with the internal reporting provided to the chief operating decision-maker.

Revised IAS 23, 'Borrowing costs' (effective from 1 January 2009). The revised Standard removes the option to expense borrowing costs and requires the capitalization of borrowing costs that relate to qualifying assets (those that take a substantial period of time to get ready for use or sale). The Company has fully adopted the revised IAS 23 which had no impact on the financial statements.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures (continued)

##### *(a) New and amended standards adopted by the Company (continued)*

IAS 27 (Amendment), 'Consolidated and separate financial statements' (effective from 1 January 2009). The amendment is part of the IASB's annual improvements project published in May 2008. Where an investment in a subsidiary that is accounted for under IAS 39, 'Financial instruments: recognition and measurement' is classified as held for sale under IFRS 5, 'Non-current assets held for sale and discontinued operations', IAS 39 would continue to be applied. The amendment will not have an impact on the Company's operations.

IAS 32 (Amendment), 'Financial Instruments: Presentation of Financial Statements' (effective for annual periods beginning on or after 1 January 2009). The amendments introduce an exemption to the principle otherwise applied in IAS 32 for the classification of instruments as equity; the amendments allow certain puttable instruments issued by an entity that would normally be classified as liabilities to be classified as equity if, and only if, they meet certain conditions. The amendments are not relevant to the Company's financial statements as no puttable instruments have been issued in the past.

IFRIC 13, 'Customer loyalty programmes' (effective from 1 July 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. IFRIC 13 is not relevant because the Company does not operate any customer loyalty programmes.

IAS 36 (Amendment), 'Impairment of assets' (effective from 1 January 2009). Where fair value less costs to sell is calculated on the basis of discounted cash flows, disclosures equivalent to those for value-in-use calculation should be made. The Company will apply the IAS 36 (Amendment) and provide the required disclosure where applicable for impairment tests from 1 January 2009.

IAS 16 (Amendment), 'Property, plant and equipment' (and consequential amendment to IAS 7, 'Statement of cash flows') (effective from 1 January 2009). Entities whose ordinary activities comprise renting and subsequently selling assets present proceeds from the sale of those assets as revenue and should transfer the carrying amount of the asset to inventories when the asset becomes held for sale. A consequential amendment to IAS 7 states that cash flows arising from purchase, rental and sale of those assets are classified as cash flows from operating activities. The amendment will not have an impact on the Company's operations because the Company's do not involve in these activities.



## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures (continued)

*(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company*

Certain new standards (IFRS), amendments and interpretations (IFRIC) to existing standards have been published. The Company has not early adopted them, but they are mandatory for the Company's accounting periods beginning on 1 January 2009 or later periods. They are as follows:

IFRIC 17, 'Distributions of Non-cash Assets to Owners (effective prospectively for annual periods beginning on or after 1 July 2009). The Interpretation applies to non-reciprocal distributions of non-cash assets to owners acting in their capacity as owners. In accordance with the Interpretation a liability to pay a dividend shall be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity and shall be measured at the fair value of the assets to be distributed. The carrying amount of the dividend payable shall be remeasured at each reporting date, with any changes in the carrying amount recognised in equity as adjustments to the amount of the distribution. When the dividend payable is settled the difference, if any, between the carrying amount of the assets distributed and the carrying amount of the dividend payable shall be recognised in profit or loss. IFRIC 17 is not expected to have any impact on the financial statements.

IFRIC 18, 'Transfers of Assets from Customers' (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. IFRIC 18 is not expected to have any impact on the Company's financial statements.

IFRIC 19, 'Extinguishing Financial Liabilities with Equity Instruments' (effective for annual periods beginning on or after 1 July 2010). This IFRIC clarifies the accounting when an entity settles its debt by issuing its own equity instruments. A gain or loss is recognised in profit or loss based on the fair value of the equity instruments compared to the carrying amount of the debt. The Company is currently assessing the impact of the interpretation on its financial statements.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures (continued)

*(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company (continued)*

Revised IFRS 3, 'Business Combinations' (effective for annual periods beginning on or after 1 July 2009). The scope of the revised Standard has been amended and the definition of a business has been expanded. The revised Standard also includes a number of other potentially significant changes including:

- All items of consideration transferred by the acquirer are recognised and measured at fair value as of the acquisition date, including contingent consideration.
- Subsequent change in contingent consideration will be recognized in profit or loss.
- Transaction costs, other than share and debt issuance costs, will be expensed as incurred.
- The acquirer can elect to measure any non-controlling interest at fair value at the acquisition date (full goodwill), or at its proportionate interest in the fair value of the identifiable assets and liabilities of the acquiree, on a transaction-by-transaction basis.

Revised IFRS 3 will not have any impact on the financial statements.

IFRS 5 (Amendment), 'Measurement of non-current assets (or disposal groups) classified as held-for-sale'. The amendment is part of the IASB's annual improvements project published in April 2009. The amendment provides clarification that IFRS 5 specifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations. It also clarifies that the general requirement of IAS 1 still apply, particularly paragraph 15 (to achieve a fair presentation) and paragraph 125 (sources of estimation uncertainty) of IAS 1. The Company will apply IFRS 5 (amendment) from 1 January 2010. It is not expected to have a material impact on the Company's financial statements.

IAS 1 (Amendment), 'Presentation of financial statements'. The amendment is part of the IASB's annual improvements project published in April 2009. The amendment provides clarification that the potential settlement of a liability by the issue of equity is not relevant to its classification as current or non current. By amending the definition of current liability, the amendment permits a liability to be classified as non-current (provided that the entity has an unconditional right to defer settlement by transfer of cash or other assets for at least 12 months after the accounting period) notwithstanding the fact that the entity could be required by the counterparty to settle in shares at any time. The Company will apply IAS 1 (amendment) from 1 January 2010. It is not expected to have a material impact on the Company's financial statements.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures (continued)

*(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company (continued)*

IFRS 9, 'Financial Instruments Part 1: Classification and Measurement'. IFRS 9 was issued in November 2009 and replaces those parts of IAS 39 relating to the classification and measurement of financial assets. Key features are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and (ii) the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.

While adoption of IFRS 9 is mandatory from 1 January 2013, earlier adoption is permitted.

The Company is considering the implications of the standard, the impact on the Company and the timing of its adoption by the Company.

Revised IAS 27, 'Consolidated and Separate Financial Statements' (effective for annual periods beginning on or after 1 July 2009). In the revised Standard the term minority interest has been replaced by non-controlling interest, and is defined as "the equity in a subsidiary not attributable, directly or indirectly, to a parent". The revised Standard also amends the accounting for non-controlling interest, the loss of control of a subsidiary, and the allocation of profit or loss and other comprehensive income between the controlling and non-controlling interest. Revised IAS 27 is not expected to have any impact on the financial statements.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### Changes in accounting policies and disclosures (continued)

*(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company (continued)*

IAS 38 (Amendment), 'Intangible Assets'. The amendment is part of the IASB's annual improvements project published in April 2009 and the Company will apply IAS 38 (amendment) from the date IFRS 3 (revised) is adopted. The amendment clarifies guidance in measuring the fair value of an intangible asset acquired in a business combination and it permits the grouping of intangible assets as a single asset if each asset has similar useful economic lives. The amendment will not result in a material impact on the Company's financial statements.

IAS 39 (Amendment), 'Financial Instruments: Recognition and Measurement' (effective for annual periods beginning on or after 1 July 2009). The amended Standard clarifies the application of existing principles that determine whether specific risks or portions of cash flows are eligible for designation in a hedging relationship. In designating a hedging relationship the risks or portions must be separately identifiable and reliably measurable; however inflation cannot be designated, except in limited circumstances. The amendments are not relevant to the Company's operations as the Company does not apply hedge accounting.

#### **Functional and presentational currency**

The Company's financial statements have been prepared in Croatian kuna (HRK), which is the currency of the primary economic environment in which the entity operates (the functional currency) and the presentation currency, and are rounded to the nearest thousand. The closing exchange rate as at 31 December 2009 was HRK 5.08930 per USD 1 (2008: HRK 5.15555) and HRK 7.30620 per EUR 1 (2008: HRK 7.32447).

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Property, plant and equipment***

Items of property, plant and equipment are shown at cost or deemed cost, less accumulated depreciation and impairment losses.

The Company recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Company and the cost of the item can be measured reliably. All other expenditure on repairs and maintenance is expensed as incurred. Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Land and assets under construction or development are not depreciated. Depreciation on other assets is provided on a straight-line basis to allocate their cost over the estimated economic useful life of the assets. The estimated useful lives are as follows:

	Useful lives	
	2009	2008
Buildings	5 – 30 years	5 – 30 years
Plant and equipment	2 – 10 years	2 – 10 years
Other	5 – 7 years	5 – 7 years

The depreciation method, useful lives and residual values are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount, and are included in the statement of comprehensive income.

#### ***Intangible assets***

Intangible assets are stated on initial recognition at cost and subsequently at cost less accumulated amortisation and impairment losses.

Amortisation is provided on a straight-line basis over the estimated useful lives of intangible assets. Intangible assets include acquired computer software, and are amortised on a straight-line basis over their useful life of 2-4 years (2008: 2-4 years). Cost associated with maintaining computer software is recognised as an expense as incurred.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

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

Assets that have an indefinite useful life are not amortized but tested annually for impairment. Property, plant and equipment, intangible assets, financial instruments and receivables are reviewed for impairment at each balance sheet date or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its estimated recoverable amount, an impairment loss is recognised in the statement of comprehensive income for items of property, plant and equipment, intangible assets, financial instruments and receivables carried at cost.

The recoverable amount of property, plant and equipment and intangible assets is the higher of an asset's fair value less costs to sell or 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). In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date. Impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

The recoverable amount of held-to-maturity investments and receivables carried at amortised cost is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset.

Short-term receivables are not discounted. The recoverable amount of other assets is the higher of the asset's net selling price and its value in use.

An impairment loss in respect of held-to-maturity investments and receivables is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

#### ***Financial instruments***

The Company classifies its financial instruments in the following categories: financial assets and financial liabilities at fair value through profit or loss, loans and receivables, available-for-sale financial assets or held-to-maturity investments. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition and re-evaluates this at every reporting date.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Financial instruments (continued)***

Financial instruments at fair value through profit or loss category have two sub-categories: “financial instruments held for trading”, and those designated by management at fair value through profit or loss at inception. Financial instruments acquired principally for the purpose of generating a short-term profit are classified as held for trading and included in current assets. These include derivative financial instruments, which do not qualify for hedge accounting. Financial instruments at fair value through profit or loss include debt and equity securities and investments in investment funds.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Company intends to sell immediately or in the near term, which are designated at fair value through profit or loss or as available for sale. These include non-current receivables and deposits with financial institutions.

Financial instruments with fixed or determinable payments and fixed maturity that the Company has positive intent and ability to hold to maturity are classified as held-to-maturity investments. All other financial instruments are classified as available for sale. Financial instruments at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets are recognised on the trade date, which is the date that the Company commits to purchase or sell the instrument. Loans and receivables and other financial liabilities are recognised on the day they are transferred to the Company.

Financial assets are initially measured at the fair value of the consideration given for them, including transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets and financial liabilities at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the statement of comprehensive income. All financial assets and financial liabilities at fair value through profit or loss and available-for-sale financial assets are subsequently carried at fair value without any deduction for transaction costs that the Company may incur on sale or other disposal. Available-for-sale financial assets for which fair value cannot be reliably measured are stated at cost, including transaction costs, less impairment losses. Held-to-maturity investments and loans and receivables are carried at amortised cost less impairment losses. Amortised cost is calculated using the effective interest rate method. Premiums and discounts on held-to-maturity investments and available-for-sale financial assets, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument. Other financial liabilities are initially recognised at fair value and subsequently carried at amortised cost.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Financial instruments (continued)***

The fair value of financial instruments at fair value through profit or loss or available for sale is based on their quoted market price at the balance sheet date, without any deduction for transaction costs. The fair value of derivatives that are not exchange-traded is estimated at the amount that the Company would receive or pay to terminate the contract at the balance sheet date. Realised and unrealised gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are recognised in the statement of comprehensive income in the period in which they arise.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available for sale are analysed between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security. The translation differences are recognised in profit or loss, and other changes in carrying amount are recognised in equity. Changes in the fair value of other monetary securities classified as available for sale and non-monetary securities classified as available for sale are recognised in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as 'realised gains and losses from available-for-sale securities'.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the statement of comprehensive income. Dividends on available-for-sale equity instruments are recognised in the statement of comprehensive income when the Company's right to receive payments is established.

A financial asset is derecognised when the Company loses the contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when it is extinguished. Financial instruments at fair value through profit or loss, available-for-sale financial assets and held-to-maturity investments are derecognised and corresponding receivables from the buyer for the payment are recognised as of the date the Company commits to sell the assets. The Company uses the specific identification method to determine the gain or loss on derecognition. Loans and receivables are derecognised on the day they are transferred by the Company. Other financial liabilities are derecognised when the Company's contractual obligations are discharged, cancelled or expire.

The Company uses derivative financial instruments to hedge economically its exposure to foreign exchange risk arising from operational activities. Hedge accounting has not been applied and those derivative instruments are accounted for as financial instruments held for trading. Derivative instruments are measured initially at fair value and the related transaction costs are recognised in the statement of comprehensive income and subsequent to initial recognition, are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss. The fair value of a forward exchange contract is its quoted price at the balance sheet date, being the present value of the quoted forward price.



## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Trade and other receivables***

Receivables are initially recognised at the fair value of consideration given and are carried at amortised cost, using the effective interest rate. Receivables are written down to their estimated realisable value through an impairment allowance.

Service contract work-in-progress is stated at cost plus profit recognised to date less a provision for foreseeable losses and less progress billings on long-term contracts. Cost includes all expenditure related directly to specific projects and an allocation of fixed and variable overheads incurred in the Company's contract activities based on budgeted capacity.

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

Cash comprises cash held at banks and on hand. Cash equivalents include demand deposits and time deposits with maturities up to three months.

#### ***Trade and other payables***

Trade and other payables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate.

#### ***Inventories***

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of other inventories is based on the First In First Out (FIFO) principle and includes expenditures incurred in acquiring the inventories and bringing them to their location and condition. In case of manufactured inventories the cost includes materials, labour and related overhead, and expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. Slow-moving and obsolete inventories have been written down to their estimated realisable value.

#### ***Share capital and reserves***

Share capital is stated in HRK at nominal value. The amount of consideration paid on repurchase of share capital, including directly attributable costs, is recognised as a charge in equity. Repurchased shares are classified as treasury shares and presented as a deduction from total equity.

Where the Company purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Share capital and reserves (continued)***

The result for the year is transferred to retained earnings. Dividends are recognised as a liability in the period in which they are declared. Dividends are paid out of the retained earnings.

#### ***Income tax***

The income tax charge is based on taxable profit for the year and comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred taxes are calculated by using the balance sheet liability method. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the balance sheet. Deferred tax assets are recognised when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised. At each balance sheet date, the Company reassesses unrecognised deferred tax assets and the carrying amount of deferred tax assets.

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. Deferred tax assets and liabilities are measured by using the tax rates expected to apply to taxable profit in the years in which those temporary differences are expected to be recovered or settled based on tax rates enacted or substantially enacted at the balance sheet date.

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

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Foreign currencies***

Transactions denominated in foreign currencies are translated into HRK at the rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currency at the balance sheet date have been translated to HRK at the foreign exchange rate ruling at that date. Foreign exchange differences arising from translation are included in the statement of comprehensive income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to HRK at foreign exchange rates ruling at the dates the values were determined. Non-monetary assets and items that are measured in terms of "historical cost of a foreign currency" are not retranslated.

#### ***Recognition of revenues***

Sales revenue represents the value of goods and services supplied to customers during the period, excluding value added taxes, trade discounts and rebates. Revenue is recognized with reference to all significant contractual terms when the product or service has been delivered, when the revenue amount is fixed or determinable, and when collection is reasonably assured. Specific contractual performance and acceptance criteria may impact the timing and amounts of revenue recognized.

The Company uses 3 main contract types with end customers as follows:

- Delivery-type contracts: Contracts for delivery of a product or a combination of products to form a whole or a part of a network as well as delivery of stand-alone products. Medium-size and large delivery type contracts generally include multiple elements. Such elements are normally standardized types of equipment or software as well as services such as network rollout.

Revenue is recognized when risks and rewards have been transferred to the customer, normally stipulated in the contractual terms of trade. For delivery-type contracts that have multiple elements, revenue is allocated to each element based on relative fair values.

- Construction-type contracts: Contracts where the Company supplies to a customer, a complete network, which to a large extent is based upon new technology or includes major components which are specifically designed for the customer.

Revenues from construction-type contracts are recognized according to the stage of completion, using either the milestone output method or cost incurred method. Long-term construction contracts are assessed on a contract by contract basis and reflected in the statement of comprehensive income by recording revenue and related costs in line with contract activity.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Recognition of revenues (continued)***

- Service contracts: Contracts for various services such as: training, consulting, engineering, installation, and multi-year managed services.

Revenue is generally recognized when the services have been provided. Revenue for fixed price services contracts covering longer periods is recognized pro rata over the contract period.

The majority of the Company's products and services are sold under delivery-type contracts including multiple elements, such as base stations, base station controllers, mobile switching centers, routers, microwave transmission links, various software products and related installation and integration services. Such contract elements generally have individual item prices in agreed price lists per customer.

The profitability of individual contracts is periodically assessed, and provisions for any estimated losses are made immediately when losses are probable.

#### ***Employee benefits***

##### *a) Long-term service benefits*

The Company provides employees with jubilee and one-off retirement awards. The obligation and costs of these benefits are determined by using the Projected Unit Credit Method. The Projected Unit Credit Method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The obligation is measured at the present value of estimated future cash flows using a discount rate that is similar to the interest rate on government bonds where the currency and terms of the government bonds are consistent with the currency and estimated terms of the benefit obligation.

##### *b) Share-based payments*

The Company operates an equity-settled, share-based compensation plan allowing the Company's employees to receive shares. The fair value of the employee services received in exchange for the grant of the Company's shares is recognised as an expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the shares. The total amount to be expensed over the vesting period is determined by reference to the fair value of the shares granted. At each balance sheet date, the Company revises its estimates of the number of shares that are expected to become granted. It recognises the impact of the revision of original estimates, if any, in the statement of comprehensive income, with a corresponding adjustment to equity. When distributed upon vesting date, treasury shares are credited at average purchase cost and recorded against retained earnings.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### ***Provisions***

A provision is recognised when the Company has a present obligation (legal or constructive) as a result of a past event and it is probable (i.e. more likely than not) 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 balance sheet date and adjusted to reflect the current best estimate. The most significant provisions in the financial statements are provisions for warranty claims, penalty claims and litigation. If the effect is material and if the obligation is expected to be settled in a period of over 12 months, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. A provision for warranties is recognised when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities.

#### ***Net financial income***

Net financial income comprises interest receivable on non-current loans, interest receivable on funds invested, foreign exchange gains and losses and gains and losses on financial assets at fair value through profit and loss and any cost related to borrowings. Interest income is recognised in the statement of comprehensive income as it accrues, using the effective interest method.

#### ***Segment reporting***

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Management Board that makes strategic decisions.

#### ***Borrowings***

Borrowings are initially recognized at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method.

## Notes to the financial statements (continued)

### 1 Significant accounting policies (continued)

#### **Leases**

Leases on terms in which the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that type of asset, although the depreciation period must not exceed the lease term.

Other leases are operating leases, and the leased assets under such contracts are not recognized on the balance sheet. Costs under operating leases are recognized in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

#### **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)

### **2 Critical accounting estimates and judgements**

Accounting estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions 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.

#### *(a) Impairment losses on loans and receivables*

The Company reviews its loan portfolios to assess impairment on a monthly basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Company makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and receivables before the decrease can be identified with an individual loan or receivable in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with parameters relevant to assets in the group.

#### *(b) Financial crisis impact*

The ongoing global liquidity crisis which commenced in the middle of 2007 has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector, and, at times, higher interbank lending rates and very high volatility in stock markets. The uncertainties in the global financial markets have also led to bank failures and bank rescues in the United States of America, Western Europe, Russia and elsewhere. Indeed the full extent of the impact of the ongoing financial crisis is proving to be impossible to anticipate or completely guard against.

The customers of the Company may also be affected by the lower liquidity situation which could in turn impact their ability to repay their outstanding debts. Deteriorating operating conditions for borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has reflected revised estimates of expected future cash flows in their impairment assessments.

## Notes to the financial statements (continued)

### 2 Critical accounting estimates and judgements (continued)

#### *(b) Financial crisis impact (continued)*

Management is unable to reliably estimate the effects on the Company's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and growth of the Company's business in the current circumstances.

#### *Judgements*

The Company has entered into several service contracts combining features and elements of other contracts for which Management has had to use judgement to determine appropriate accounting treatment.

Certain service contracts under which the Company also provides financing to the contracts are separated into sales revenue and financial income. The financial income is recognised using the effective interest over the life of the contract.

### 3 Sales revenue

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Sales revenue from sales of products	619,138	969,326
Sales revenue from sales of services	780,873	830,733
	<u>1,400,011</u>	<u>1,800,059</u>



## Notes to the financial statements (continued)

### 4 Segment reporting

The Company has determined the operating segments based on the reports reviewed by the Management Board that are used to make strategic decisions. The Management Board assesses the performance of the operating segments based on a measure of adjusted Operating profit. The measurement basis excludes the effects of gains/losses on disposal of intangibles, property, plant and equipment and administration expenses.

When determining the operating segments, the Company has looked at which market and to what type of customers the Company's products are aimed, and through what distribution channels they are sold, as well as to commonality regarding technology, research and development. Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

The Company is organised into business units and has three primary reportable operating segments as follows:

- i) Networks, that includes products for mobile and fixed broadband access, core networks, transmission and next-generation IP networks. Related network rollout services are also included. In addition, power modules and cables operations are included within Networks.
- ii) Professional services, that includes all service operations, excluding Network rollout reported under Networks. Services related to system integration of IP and core networks are classified as Professional services.
- iii) Multimedia, that includes multimedia systems, enterprise solutions and mobile platforms.

Segments are managed in Europe, the Middle East and Africa. Revenues determined based on the geographic location of customers are disclosed in this note. All the Company's assets are located in Croatia.

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Sales revenue in Croatia	481,693	556,447
Sales revenue in Russia, Belarus, Kazakhstan, Georgia, Kyrgyzstan, Moldova	215,237	388,044
Sales revenue to the European Union	423,155	419,689
Sales revenue in Bosnia and Herzegovina, Montenegro, Macedonia and Kosovo	265,048	417,030
Other export sales revenue	14,878	18,849
	<u>1,400,011</u>	<u>1,800,059</u>

## Notes to the financial statements (continued)

### 4 Segment reporting (continued)

	Networks		Professional services		Multimedia		Total	
	2009	2008	2009	2008	2009	2008	2009	2008
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
<b>Segment sales revenue</b>	922,523	1,247,703	416,321	436,204	61,167	116,152	1,400,011	1,800,059
<b>Segment other income</b>	11,373	13,858	5,133	4,845	754	1,290	17,260	19,993
<b>Segment results from operating activities</b>	48,476	92,120	64,316	113,829	(10,153)	1,626	102,639	207,575
Unallocated other income							65	117
Unallocated expenses*							(37,024)	(44,825)
<b>Operating profit</b>							65,680	162,867
<b>Segment finance income</b>	18,998	22,468	5,832	12,421	9,101	4,153	33,931	39,042
<b>Segment results</b>	67,474	114,588	70,148	126,250	(1,052)	5,779		
Unallocated finance income							27,963	24,348
Finance expense							(757)	(14,287)
Profit before tax							126,817	211,970
Income tax expense							1,630	(7,602)
<b>Profit for the year</b>							<b>128,447</b>	<b>204,368</b>
<b>Segment assets</b>	586,015	721,142	264,460	252,115	38,855	67,133	889,330	1,040,390
<b>Segment liabilities</b>	125,320	115,114	56,555	40,244	8,309	10,716	190,184	166,074
<b>Other segment information:</b>								
Additions to property, plant and equipment	29,250	40,936	13,200	14,312	1,940	3,811	44,390	59,059
Acquisitions of intangible assets	1,123	3,356	507	1,173	75	313	1,705	4,842
Depreciation and amortisation	8,028	41,580	3,623	14,537	532	3,871		

\*Including audit fee expenses of HRK 415 thousand (2008: HRK 455 thousand)

## Notes to the financial statements (continued)

### 4 Segment reporting (continued)

Reportable segments' assets are reconciled to total assets as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Segment assets	889,330	1,040,390
<b>Unallocated:</b>		
Cash and cash equivalents	414,935	318,303
Financial assets at fair value through profit and loss	120,873	49,331
Property, plant and equipment	29,031	31,485
Deferred tax assets	12,295	13,008
Loans and receivables	45,523	46,543
Other receivables	29,588	20,524
Income tax receivable	9,452	-
Prepayments and accrued income	1,371	1,290
Equity securities	45	45
Total assets per the statement of financial position	<u>1,552,443</u>	<u>1,520,919</u>

Reportable segments' liabilities are reconciled to total liabilities as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Segment liabilities	190,184	166,074
<b>Unallocated:</b>		
Interest-bearing borrowings	6,620	8,833
Accrued charges and deferred revenue	147,300	143,001
Income tax payable	-	2,811
Trade and other payables	2,990	22,704
Financial assets at fair value through profit and loss	-	6,360
Employee benefits	5,126	5,009
Total liabilities per the statement of financial position	<u>352,220</u>	<u>354,792</u>

## Notes to the financial statements (continued)

### 5 Other income

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Commission income	777	1,601
Reversal of unused provisions (Note 26)	-	375
Rental income	16,159	17,280
Net gain on disposal of property, plant and equipment	65	117
Other income	324	737
	<u>17,325</u>	<u>20,110</u>

### 6 Other expenses

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Increase in provisions (Note 26)	5,892	-
Impairment loss on loans and receivables (Note 16)	21,650	27,926
Obsolescence allowance on inventories	251	377
	<u>27,793</u>	<u>28,303</u>

## Notes to the financial statements (continued)

### 7 Personnel expenses

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Net salaries	209,381	199,753
Taxes and contributions	195,307	195,712
Other payroll-related costs	25,527	16,260
Equity-settled transactions (Note 24 b)	11,712	6,656
	<u>441,927</u>	<u>418,381</u>

Personnel expenses include HRK 70,326 thousand (2008: HRK 64,648 thousand) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross II). In addition, Personnel expenses include HRK 10,284 thousand (2008: Nil) in respect of voluntary redundancy compensation as described in Note 26, Provisions.

At the year-end, the Company employed the following personnel:

	<b>2009</b>	<b>2008</b>
Operations	542	526
Global Service Delivery Center	258	235
Business Ericsson Test Environment	48	43
Research and Development Center	589	590
Sales	55	69
Support functions	160	159
Employees on long-term assignment abroad	9	9
	<u>1,661</u>	<u>1,631</u>

## Notes to the financial statements (continued)

### 8 Finance income and expense

#### *Finance income*

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Interest income (Note 8 a)	39,538	48,711
Net gains from re-measurement of financial assets at fair value through profit or loss (Note 8 c)	429	-
Amortization of discount (Note 8 b)	15,985	13,261
Net foreign exchange gain	5,942	1,417
	<u>61,894</u>	<u>63,389</u>

#### *Finance expense*

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Interest expense	757	203
Net losses on re-measurement of financial assets at fair value through profit or loss (Note 8 c)	-	14,084
	<u>757</u>	<u>14,287</u>

#### 8 (a)

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Interest income		
- on loans to customers	17,316	24,153
- on debt securities	2,720	2,723
- on term deposits	18,079	19,380
- on other receivables	1,423	2,455
	<u>39,538</u>	<u>48,711</u>

#### 8 (b)

The Company released HRK 15,985 thousand (2008: HRK 13,261 thousand) into finance income due to amortisation of discount according to the net present value method of impairment.

## Notes to the financial statements (continued)

### 8 Finance income and expense (continued)

8 (c)

	<b>2009</b>	<b>2008</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Net gains/(losses) from re-measurement of financial assets at fair value through profit or loss		
- Derivative financial instruments	1,588	(12,063)
- Equity securities	(385)	(1,994)
- Investment in investment funds	86	66
- Debt securities	(860)	(93)
	<u>429</u>	<u>(14,084)</u>

### 9 Income tax expense

Income tax has been calculated on the taxable income at statutory tax rate of 20% (2008: 20%).

Income tax expense recognised in the statement of comprehensive income comprises:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Current income tax expense	-	(12,218)
Deferred tax income relating to the origination and reversal of temporary differences	1,630	4,616
Total income tax expense in the statement of comprehensive income	<u>1,630</u>	<u>(7,602)</u>

Deferred tax recognised directly to equity:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Relating to equity-settled transactions	<u>(2,342)</u>	<u>(1,331)</u>

## Notes to the financial statements (continued)

### 9 Income tax expense (continued)

The reconciliation between tax expense and accounting profit is shown as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Profit before tax	126,817	211,970
Income tax at 20% (2008: 20%)	25,363	42,394
Non-deductible expenses	3,338	1,476
Tax exempt revenues	300	606
Tax incentives	(30,631)	(36,874)
Total tax expense	<u>(1,630)</u>	<u>7,602</u>
Effective tax rate	<u>(1.3%)</u>	<u>3.6%</u>

Tax incentives include additional tax allowances for certain expenditure totalling HRK 30.3 million (2008: HRK 36.3 million) which meets research and development incentives definitions under Croatian tax legislation.

In accordance with local regulations, the Tax Authority may at any time inspect the Company's books and records within 3 years following the end of the year in which the tax liability is reported and may impose additional tax assessments and penalties. The Company's management is not aware of any circumstances, which may give rise to a potential material liability in this respect.

### 10 Earnings per share

	<b>2009</b>	<b>2008</b>
Profit for the year (HRK '000)	128,447	204,368
Weighted Average Number of Shares Outstanding at the year-end	<u>1,309,435</u>	<u>1,314,238</u>
Earnings per share (HRK)	<u>98.09</u>	<u>155.50</u>

Basic and fully diluted earnings per share are the same, since the Company does not have any dilutive potential ordinary shares.



## Notes to the financial statements (continued)

### 11 Property, plant and equipment

2009	Land and buildings HRK '000	Plant and equipment HRK '000	Other HRK '000	Total HRK '000
<b>As at 1 January 2008</b>				
Cost or valuation	154,650	357,936	328	512,914
Accumulated depreciation	(88,782)	(249,271)	(173)	(338,226)
Net book amount	<u>65,868</u>	<u>108,665</u>	<u>155</u>	<u>174,688</u>
<b>Year ended 31 December 2008</b>				
Opening net book amount	65,868	108,665	155	174,688
Additions	805	58,254	-	59,059
Disposals	-	(173)	-	(173)
Depreciation charge	(3,694)	(66,583)	(8)	(70,285)
<b>Closing net book amount</b>	<b><u>62,979</u></b>	<b><u>100,163</u></b>	<b><u>147</u></b>	<b><u>163,289</u></b>
<b>As at 31 December 2008</b>				
Cost or valuation	155,455	397,620	328	553,403
Accumulated depreciation	(92,476)	(297,457)	(181)	(390,114)
Net book amount	<u>62,979</u>	<u>100,163</u>	<u>147</u>	<u>163,289</u>
<b>Year ended 31 December 2009</b>				
Opening net book amount	62,979	100,163	147	163,289
Additions	-	44,390	-	44,390
Disposals	-	(86)	-	(86)
Depreciation charge	(3,589)	(57,645)	(8)	(61,242)
<b>Closing net book amount</b>	<b><u>59,390</u></b>	<b><u>86,822</u></b>	<b><u>139</u></b>	<b><u>146,351</u></b>
<b>As at 31 December 2009</b>				
Cost or valuation	155,455	312,094	328	467,877
Accumulated depreciation	(96,065)	(225,272)	(189)	(321,526)
<b>Net book amount</b>	<b><u>59,390</u></b>	<b><u>86,822</u></b>	<b><u>139</u></b>	<b><u>146,351</u></b>

Included in cost is HRK 198 million (2008: HRK 256.1 million) of fully depreciated property, plant and equipment that are still used by the Company.

As at 31 December 2009, the Company had contracts totalling HRK 1,552 thousand (2008: HRK 7,852 thousand) related to future equipment purchases.

## Notes to the financial statements (continued)

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

The Company acts as a lessor under operating leases, mainly land and buildings. Property leased to others with a carrying value of HRK 23,901 thousand (2008: HRK 26,207 thousand) is included within land and buildings. These assets are depreciated at the same depreciation rates as other buildings. HRK 18,655 thousand (2008: 20,119 thousand) of leased assets is leased for a non-cancellable period of five years which commenced in 2005. Subsequent renewals are negotiated with the lessee. No contingent rents are charged. Portions of the property which is held for rental could not be sold separately or leased out separately under finance lease. Consequently, the IAS 40 criteria for separate investment property recognition are not met.

Future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods are:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Less than one year	6,064	5,870
Between one and five years	-	2,935
	<u>6,064</u>	<u>8,805</u>

## Notes to the financial statements (continued)

### 12 Intangible assets

The movement on intangible assets in the year ended 31 December 2009 may be analysed as follows:

<b>2009</b>	<b>Application software HRK '000</b>
<b>As at 1 January 2008</b>	
Cost or valuation	13,782
Accumulated depreciation	(9,361)
Net book amount	<u>4,421</u>
<b>Year ended 31 December 2008</b>	
Opening net book amount	4,421
Additions	4,842
Depreciation charge	(2,998)
<b>Closing net book amount</b>	<b><u>6,265</u></b>
<b>As at 31 December 2008</b>	
Cost or valuation	16,620
Accumulated depreciation	(10,355)
Net book amount	<u>6,265</u>
<b>Year ended 31 December 2009</b>	
Opening net book amount	6,265
Additions	1,705
Depreciation charge	(3,545)
<b>Closing net book amount</b>	<b><u>4,425</u></b>
<b>As at 31 December 2009</b>	
Cost or valuation	16,264
Accumulated depreciation	(11,839)
<b>Net book amount</b>	<b><u>4,425</u></b>

Included in the cost amount is HRK 6.4 million (2008: HRK 5.1 million) of fully amortised intangible assets that are still used by the Company.

## Notes to the financial statements (continued)

### 13 Loans and receivables

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Deposits with financial institutions, denominated in foreign currency	6,878	7,400
Non-current receivables from foreign customers, denominated in foreign currency	260,469	320,094
Non-current receivables from domestic customers, denominated in HRK	12,445	26,022
Receivables for sold apartments		
- denominated in foreign currency	5,498	5,512
- denominated in HRK	1,415	1,989
Housing loans to employees, denominated in HRK	7	207
Total loans and receivables	286,712	361,224
Impairment allowance on loans and receivables (Note 16)	(7,815)	(11,313)
	<u>278,897</u>	<u>349,911</u>

Deposits with financial institutions are placed as guarantee deposits for housing loans provided to the Company's employees, earning interest at variable rates ranging from 1.07% to 1.10% per annum (2008: 1.07% to 1.10% per annum), and with a remaining maturity of over three years.

Receivables from customers are partially secured with bank guarantees and letters of credit. The current portion of the non-current receivables is classified under current assets.

### Non-current portion of foreign and domestic loans and receivables

Due	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
2010	-	92,564
2011	74,978	60,124
2012	42,247	38,345
2013	36,656	35,754
2014	34,009	34,095
2015-2020	85,024	85,234
	<u>272,914</u>	<u>346,116</u>

Receivables for sold apartments are shown net of amounts due to the Croatian state. Housing loans to employees are linked to the counter value of euro, repayments are made by deduction from monthly salary and the loans are secured with charges on the house or apartment. Receivables for sold apartments and housing loans provided to a limited number of employees bear fixed interest rates of up to 5% per annum. A discount in the amount of HRK 3,120 thousand (2008: HRK 3,496 thousand) is recognised in respect of these loans and amortised to the statement of comprehensive income, using the effective interest rate method at a rate of 7% per annum.

## Notes to the financial statements (continued)

### 14 Deferred tax assets

#### *Recognised deferred tax assets and liabilities*

Movements in temporary differences and components of deferred tax assets and liabilities are as follows:

	2009		Credited / (charged) to statement of comprehensive income	Credited / (charged) to equity	2008	
	Assets	Liabilities			Assets	Liabilities
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Receivables	5,995	-	(1,483)	-	7,478	-
Inventories	2,251	-	(25)	-	2,277	-
Employee benefits	819	-	34	-	785	-
Non-current receivables for sold apartments	624	-	(75)	-	699	-
Negative fair value of financial instruments	447	-	(1,154)	-	1,601	-
Accrued charges	2,159	-	1,991	-	168	-
Increase in equity related to equity-settled transactions	10,119	(10,119)	2,342	(2,342)	7,777	(7,777)
	<u>22,414</u>	<u>(10,119)</u>	<u>1,630</u>	<u>(2,342)</u>	<u>20,785</u>	<u>(7,777)</u>
Set-off of tax	<u>(10,119)</u>	<u>10,119</u>	<u>-</u>	<u>-</u>	<u>(7,777)</u>	<u>7,777</u>
Deferred tax assets	<u>12,295</u>	<u>-</u>	<u>1,630</u>	<u>(2,342)</u>	<u>13,008</u>	<u>-</u>

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. The Company did not recognise deferred income tax assets of HRK 15,760 thousand (2008: nil) in respect of tax losses amounting to HRK 78,799 thousand (2008: nil) that can be carried forward against future taxable income. Tax losses carried forward amounting to HRK 78,799 thousand (2008: nil) expire in 2014.

## Notes to the financial statements (continued)

### 14 Deferred tax assets (continued)

*Recognised deferred tax assets and liabilities (continued)*

Movements in temporary differences and components of deferred tax assets and liabilities are as follows:

	2008		Credited / (charged) to statement of comprehensive income	Credited / (charged) to equity	2007	
	Assets HRK '000	Liabilities HRK '000			Assets HRK '000	Liabilities HRK '000
Receivables	7,478	-	2,929	-	4,549	-
Inventories	2,277	-	(183)	-	2,460	-
Employee benefits	785	-	28	-	757	-
Non-current receivables for sold apartments	699	-	(82)	-	781	-
Negative fair value of financial instruments	1,601	-	1,289	-	312	-
Accrued charges	168	-	(696)	-	864	-
Increase in equity related to equity-settled transactions	7,777	(7,777)	1,331	(1,331)	6,446	(6,446)
	20,785	(7,777)	4,616	(1,331)	16,169	(6,446)
Set-off of tax	(7,777)	7,777	-	-	(6,446)	6,446
Deferred tax assets	13,008	-	4,616	(1,331)	9,723	-

### 15 Inventories

	2009 HRK '000	2008 HRK '000
Raw materials	7,363	9,021
Work-in-progress and semi-finished goods	17,657	44,816
Total inventories	25,020	53,837
Obsolescence allowance	(961)	(727)
	24,059	53,110

## Notes to the financial statements (continued)

### 16 Trade receivables

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Foreign trade receivables	193,517	83,170
Current portion of non-current foreign receivables	152,938	286,366
Total current foreign receivables	<u>346,455</u>	<u>369,536</u>
Domestic trade receivables	110,974	132,259
Current portion of non-current domestic receivables	19,273	15,102
Total current domestic receivables	<u>130,247</u>	<u>147,361</u>
Impairment allowance on receivables	<u>(25,455)</u>	<u>(30,165)</u>
	<u>451,247</u>	<u>486,732</u>

Included in trade receivables is HRK 15,725 thousand (2008: HRK 2,700 thousand) of contract work in progress.

Movements in impairment allowance on loans and receivables were as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
As at 1 January (Notes 13,16)	41,478	27,201
Provision for receivables impaired during the year	22,612	29,042
Receivables written off during the year as uncollectible	(13,873)	(388)
Unused amounts reversed	(962)	(1,116)
Amortisation of discount (Note 8)	(15,985)	(13,261)
As at 31 December (Notes 13,16)	<u>33,270</u>	<u>41,478</u>

Of the total HRK 33 million of impairment allowances as at 31 December 2009, HRK 30 million relates to Customer loans and receivables.

### 17 Other receivables

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Net receivables for prepaid VAT	9,456	6,209
Receivables for withholding tax	11,267	10,001
Receivables from employees	1,039	541
Accrued interest receivable	3,364	1,748
Other receivables	4,462	2,025
	<u>29,588</u>	<u>20,524</u>

## Notes to the financial statements (continued)

### 18 Financial assets and liabilities at fair value through profit or loss

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
<i>Financial assets at fair value through profit or loss, trading assets</i>		
- Positive fair value of derivative financial instruments	-	4,198
<i>Financial assets at fair value through profit or loss</i>		
- Debt securities, Ministry of Finance	43,284	44,145
- Equity securities	603	988
- Investment in open-ended investment funds	76,986	-
	<u>120,873</u>	<u>49,331</u>
<i>Financial liabilities at fair value through profit or loss</i>		
- Negative fair value of derivative financial instruments	-	6,360
	<u>-</u>	<u>6,360</u>

### 19 Cash and cash equivalents

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Cash and demand deposits	44,851	14,728
Term deposits originated by the Company, with original maturity up to 3 months	370,084	303,575
	<u>414,935</u>	<u>318,303</u>



## Notes to the financial statements (continued)

### 20 Equity

#### (a) Share capital

As at 31 December 2009, the share capital of the Company is represented by 1,331,650 (2008: 1,331,650) of authorised, issued and fully paid ordinary shares, with a total registered value of HRK 133,165 thousand (2008: HRK 133,165 thousand). The nominal value of one share is HRK 100 (2008: HRK 100). The holders of the ordinary shares are entitled to receive dividends as declared at the General Assembly and are entitled to one vote per share at the General Assembly.

The Company's shareholders as at 31 December 2009 are:

	<b>2009</b>	<b>2009</b>	<b>2008</b>	<b>2008</b>
	<b>Number of shares</b>	<b>% held</b>	<b>Number of shares</b>	<b>% held</b>
Telefonaktiebolaget LM Ericsson	653,473	49.07	653,473	49.07
Small shareholders	651,830	48.95	652,741	49.02
Croatian Privatisation Fund	11,879	0.89	11,848	0.89
Treasury shares	14,468	1.09	13,588	1.02
	<u>1,331,650</u>	<u>100.00</u>	<u>1,331,650</u>	<u>100.00</u>

#### (b) Treasury shares

During 2007, the Company acquired 15,000 of its own shares. The amount paid was HRK 52,456 thousand out of 2006 net income as decided by the General Assembly held on 31 May 2007. During 2008, the Company acquired additional 3,000 of its own shares. The amount paid was HRK 3,895 thousand out of 2006 net income, as decided by the General Assembly held on 31 May 2007. During 2009, the Company acquired additional 8,893 of its own shares. The amount paid was HRK 11,380 thousand out of 2008 net income as decided by the General Assembly held on 27 May 2008. These shares are held as "treasury shares" and will be granted to key management and other employees as a part of the share-based program established during 2004, as described in Note 24 (b).

Movements in treasury shares are as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
At 1 January (Note 20 (a))	13,588	16,535
Purchases during the year	8,893	3,000
Distributed during the year	<u>(8,013)</u>	<u>(5,947)</u>
At 31 December (Note 20 (a))	<u>14,468</u>	<u>13,588</u>

#### (c) Legal reserves

A legal reserve in the amount of 5% of total share capital was formed during previous periods by appropriation of 5% of net profit per annum up to a cap of 5% of share capital. The legal reserve may be used to cover losses if the losses are not covered by current net profit or if other reserves are not available. The Company recorded the required level of legal reserves in the year 2000 and no further allocation to legal reserves is required.

## Notes to the financial statements (continued)

### 21 Proposed dividends

Dividends payable are not accounted for until they have been ratified at the General Assembly of shareholders. On 26 May 2009, the General Assembly approved a regular dividend in respect of 2008 of HRK 20.00 per share, and additional extraordinary dividend of HRK 50.00 per share, totalling HRK 91.8 million. At a meeting held on 23 February 2010, the Management Board proposed a regular dividend in respect of 2009 in the amount of HRK 20 per share, and a additional extraordinary dividend of HRK 100 per share. The dividend will be paid from the remaining part of retained earnings realized in 2008 as well as from a part of profit for 2009, after approval by the General Assembly, which will be held on 20 May 2010.

Cash dividends authorised and paid for previous years were as follows:

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
HRK 70.00 per share for 2008	91,758	-
HRK 270.00 per share for 2007	-	355,305

### 22 Capital management

The Company's objectives when managing capital are:

- To safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- To provide adequate requirements for capital resources, as far as possible, by the retention of profit; and
- To maintain the balance sheet with a large component of cash and short-term assets, as well as equity and other investments.

The Company is generating sufficient cash from operations to fund liabilities as they become due, finance customers and budgeted investments, and pay dividends.

The Company monitors capital using the statutory minimum capital requirement. Shareholders' equity is disclosed in Note 20 to the financial statements.

## Notes to the financial statements (continued)

### 23 Interest-bearing borrowings

During 2008, the Company borrowed the amount of HRK 8,085 thousand from HBOR and delivered information and communication equipment to a customer. The Ministry of Health and Social Welfare ("the Ministry") took over the obligations towards the Company on behalf of the customer and, based on the cession agreement between the Company, the customer and the Ministry, the Ministry is obliged to perform the repayment of the due amounts in favour of the customer directly to HBOR. The Company's liability to HBOR decreases as the Ministry repays. The HBOR loan was granted over a 5-year period. The current portion of the loan amounts to HRK 1,655 thousand, while the remaining amount is repayable in semi-annual instalments until 2013, bearing an interest rate of six-month EURIBOR plus a margin of 2% per annum. There is no security or pledges in relation to these borrowings. In 2008, the amount of HRK 748 thousand bore a fixed interest rate of 7.9%.

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Non-current portion of loans	4,965	6,425
Current portion of loans	1,655	2,408
	<u>6,620</u>	<u>8,833</u>

### 24 Employee benefits

#### *(a) Long-term service benefits*

The Company does not operate any pension schemes or other retirement benefit schemes for the benefit of any of its employees or management. In respect of all of the Company's personnel such social payments as required by the authorities are paid. These contributions form the basis of social benefits payable out of the Croatian Pension Insurance Institute to the Croatian employees upon their retirement. Additionally, during 2001 the Company signed an Annex to the Union Agreement based on which employees are entitled to a benefit upon early retirement.

However, the Company pays a one-time benefit amounting to HRK 8,000 for each employee who retires. Additionally, the Company pays jubilee awards in respect of each 5 years of service, of an employee, starting from the 10<sup>th</sup> year and ending in the 40<sup>th</sup> year. The principal actuarial assumptions used to determine retirement and jubilee obligations as at 31 December 2009 were a 6% discount rate (2008: 6%) and a 3,01% (2008: 3.06%) rate of average employment turnover.

## Notes to the financial statements (continued)

### 24 Employee benefits (continued)

#### (a) Long-term service benefits (continued)

Movements in long-term service benefits were as follows:

	<b>2009</b>	<b>2009</b>	<b>2009</b>	<b>2008</b>	<b>2008</b>	<b>2008</b>
	<b>Jubilee awards</b>	<b>Retirement</b>	<b>Total</b>	<b>Jubilee awards</b>	<b>Retirement</b>	<b>Total</b>
	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>
As at 1 January	3,927	1,082	5,009	3,786	936	4,722
Obligation created during the year	657	336	993	469	202	671
Obligation fulfilled during the year	(406)	(48)	(454)	(328)	(32)	(360)
Obligation reversed during the year	(83)	(339)	(422)	-	(24)	(24)
As at 31 December	<u>4,095</u>	<u>1,031</u>	<u>5,126</u>	<u>3,927</u>	<u>1,082</u>	<u>5,009</u>

#### (b) Share-based payments

During 2004, the Company established its Loyalty program, a share-based scheme under which management and other employees are entitled to receive the Company's shares conditional on the employee completing certain years of service (the vesting period) from the grant date.

In addition, the Company also grants treasury shares to senior management and other employees as a bonus arrangement under its Award program.

The treasury shares are distributed to eligible employees upon ratification at the General Assembly.

## Notes to the financial statements (continued)

### 24 Employee benefits (continued)

#### (b) Share-based payments (continued)

The terms and conditions of the grants are as follows:

<b>Employees entitled/grant date</b>	<b>Number of granted shares</b>	<b>Vesting conditions</b>
<i>Loyalty program</i>		
Share grant to key management during 2004	690	Three to five years of service
Share grant to other employees during 2004	8,355	Three to five years of service
Share grant to key management during 2005	-	Three to five years of service
Share grant to other employees during 2005	(125)	Three to five years of service
Share grant to key management during 2006	-	Three to five years of service
Share grant to other employees during 2006	4,575	Three to five years of service
Share grant to key management during 2007	-	Three to five years of service
Share grant to other employees during 2007	(145)	Three to five years of service
Share grant to key management during 2008	450	Three to five years of service
Share grant to other employees during 2008	2,285	Three to five years of service
Share grant to key management during 2009	460	Three to five years of service
Share grant to other employees during 2009	3,505	Three to five years of service
	<u>20,050</u>	
<i>Award program</i>		
Share grant to key management during 2004	1,640	Upon granting
Share grant to other employees during 2004	730	Upon granting
Share grant to key management during 2005	-	Upon granting
Share grant to other employees during 2005	-	Upon granting
Share grant to key management during 2006	1,200	Upon granting
Share grant to other employees during 2006	-	Upon granting
Share grant to key management during 2007	3,162	Upon granting
Share grant to other employees during 2007	2,577	Upon granting
Share grant to key management during 2008	1,287	Upon granting
Share grant to other employees during 2008	2,430	Upon granting
Share grant to key management during 2009	51	Upon granting
Share grant to other employees during 2009	2,886	Upon granting
	<u>15,963</u>	

## Notes to the financial statements (continued)

### 24 Employee benefits (continued)

#### (b) Share-based payments (continued)

The fair value of service received in return for shares granted is measured by reference to the observable market price of shares at the grant date.

	Number of granted shares	Weighted average fair value per share
Shares granted in 2004	11,415	HRK 656.68
Shares granted in 2005	(125)	HRK 735.99
Shares granted in 2006	5,775	HRK 2,330.18
Shares granted in 2007	5,594	HRK 3,387.12
Shares granted in 2008	6,452	HRK 1,380.27
Shares granted in 2009	6,902	HRK 1,696.91

During 2009, the Company recognised HRK 11,712 thousand (2008: HRK 6,656 thousand) of expenses in respect of share-based payments, which are included in personnel expenses as disclosed in Note 7. During 2009, there was no decision on new Loyalty programs, only the share distribution according to existing Loyalty programs was executed. The Award program for 2009 included the length of service with the Company component and was completely granted and mainly distributed during 2009. As for 2008, out of 2,900 shares approved for distribution under the Award program during 2007, an amount of 1,600 shares totalling HRK 5,472 thousand, as disclosed in Note 28 (b), was not granted. An amount of 1,917 shares under the Award program was distributed during 2008 while 1,800 shares were distributed during 2009. Of the 6,902 shares granted in 2009, 1,194 shares will be distributed in the following financial year.

Shares granted under the Loyalty program vested during 2009. The total weighted average cost of shares granted during 2009 under the Award and Loyalty programs amounted to HRK 23,596 thousand (2008: HRK 2,671 thousand).

Movements in shares under the Award and Loyalty programs are as follows:

	2009 HRK '000	2008 HRK '000
As at 1 January	13,580	8,145
Granted	2,937	14,577
Exercised	(5,708)	(7,542)
Expired	-	(1,600)
As at 31 December	<u>10,809</u>	<u>13,580</u>

## Notes to the financial statements (continued)

### 25 Trade and other payables

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Trade payables	43,410	36,391
Liabilities to employees	42,215	51,954
Other current liabilities	15,980	13,675
	<u>101,605</u>	<u>102,020</u>

### 26 Provisions

Movements in provisions were as follows:

	<b>2009</b>	<b>2009</b>	<b>2009</b>	<b>2009</b>	<b>2008</b>	<b>2008</b>	<b>2008</b>
	<b>Warranty</b>	<b>Penalty</b>	<b>Voluntary</b>	<b>Total</b>	<b>Warranty</b>	<b>Penalty</b>	<b>Total</b>
	<b>reserve</b>	<b>reserve</b>	<b>redundancy</b>	<b>HRK</b>	<b>reserve</b>	<b>reserve</b>	<b>HRK</b>
	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>'000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>
As at 1 January	11,634	843	-	12,477	14,806	1,856	16,662
Provision created during the year	3,179	5,789	10,284	19,252	4,673	1,105	5,778
Provision reversed during the year	(2,355)	(721)	-	(3,076)	(4,297)	(1,856)	(6,153)
Provision used during the year	(2,456)	(2,467)	-	(4,923)	(3,548)	(262)	(3,810)
As at 31 December	<u>10,002</u>	<u>3,444</u>	<u>10,284</u>	<u>23,730</u>	<u>11,634</u>	<u>843</u>	<u>12,477</u>

The warranty reserve is established to cover the expected warranty claims on products sold during the year. The penalty reserve is created to cover the expected claims from customers in respect of delays in deliveries of products and services having occurred during the year. Reversal of warranty reserves relates to expired warranties and reversal of penalty reserve relates to waived or expired obligations.

An agreement was reached in 2009 with the local union representatives, which specifies the number of staff involved and the early retirement compensation package offered by the Company, as well as amounts payable to those having accepted the package, before the financial year-end. The estimated staff restructuring costs to be incurred are HRK 10.2 million as at 31 December 2009, and are included in the Note 7, Personnel expenses.

## Notes to the financial statements (continued)

### 27 Accrued charges and deferred revenue

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Advances from domestic customers	315	2,160
Advances from foreign customers	16,280	15,551
Deferred revenue	50,722	31,551
Accrued charges for unused holidays	10,548	10,906
Accrued charges for legal claims	898	801
Accrued charges in respect of service contracts	54,067	70,126
Other accrued charges	14,470	11,906
	<u>147,300</u>	<u>143,001</u>

Deferred revenue represents amounts due to customers under contracts for work not performed.

Accrued charges in respect of service contracts mainly represent costs incurred for which no invoice has been received at the balance sheet date.



## Notes to the financial statements (continued)

### 28 Balances and transactions with related parties

For the purposes of these financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

The Company is a related party to the Ericsson Group via the 49.07% (2008: 49.07%) shareholding by Telefonaktiebolaget LM Ericsson, which is also the ultimate parent of the Ericsson Group.

The Company has a related-party relationship with Telefonaktiebolaget LM Ericsson, Ericsson Group subsidiaries and associates, the Supervisory Board, the Management Board and other executive management.

#### (a) Key transactions with the related parties

Major transactions with the Ericsson Group companies may be summarised as follows:

	Telefonaktiebolaget LM Ericsson		Other Ericsson Group consolidated companies		Total	
	2009 HRK '000	2008 HRK '000	2009 HRK '000	2008 HRK '000	2009 HRK '000	2008 HRK '000
<b>Sales of goods and services</b>						
Sales revenue	-	-	435,610	453,187	435,610	453,187
Commission income	-	-	777	1,601	777	1,601
Total sales	-	-	436,387	454,788	436,387	454,788
<b>Purchases of goods and services</b>						
Licences	4,781	6,770	35,666	35,955	40,447	42,725
Technical cooperation fee	-	-	14,153	5,022	14,153	5,022
Cost of sales	416	-	477,261	766,377	477,677	766,377
Total purchases	5,197	6,770	527,080	807,354	532,277	814,124

The sales of goods and services transactions have been directly negotiated between the involved parties and agreed on an individual basis. The Company pays licence fees on sales of wireline products, sales of services, corporate trade mark licences and technical cooperation fees. The licence fee is paid as a percentage of sales of wireline products and solutions, and sales of services, per product sold. The transactions between related parties are carried out on an arm's length basis.

## Notes to the financial statements (continued)

### 28 Balances and transactions with related parties (continued)

#### *(b) Key management compensation*

The Company's key management include the executive management listed on page 3, comprising the Management Board member and directors of the main organisational units.

	<b>2009</b>	<b>2008</b>
	<b>HRK '000</b>	<b>HRK '000</b>
Salaries and other short-term employee benefits	16,364	24,122
Other long-term benefits	4	-
Share-based payments	830	4,365
Reversal of share-based payments reserve from prior year (Note 24 b)	-	(5,472)
	<u>17,198</u>	<u>23,015</u>

The members of the executive management and the Supervisory Board held 5,158 ordinary shares at the year-end (2008: 4,981 shares).

Included in the loans and receivables are HRK 14 thousand (2008: HRK 77 thousand) in respect of loans and advances granted to key management. During 2009, the Company collected HRK 2 thousand (2008: HRK 6 thousand) of interest from these loans.

In addition, the Company paid remuneration totalling HRK 319 thousand (2008: HRK 314 thousand) to the Supervisory Board.

## Notes to the financial statements (continued)

### 28 Balances and transactions with related parties (continued)

#### (c) Year-end balances arising from sales and purchases of goods and services

Year-end balances arising from key transactions with Ericsson Group companies may be summarised as follows:

	Receivable		Payable	
	2009	2008	2009	2008
	HRK '000	HRK '000	HRK '000	HRK '000
<b>Main shareholder</b>				
Telefonaktiebolaget LM Ericsson (LME)	-	-	(1,718)	477
<b>Ericsson Group consolidated companies</b>				
Ericsson AB (EAC)	-	-	-	5,531
Ericsson AB (EAB)	42,809	45,439	63,816	63,487
Ericsson Telecomunicazioni S.P.A. (TEI)	-	68	46	-
Ericsson Corporatia AO (ECR)	2,617	4,895	-	-
LM Ericsson Limited (LMI)	176	-	614	425
Ericsson SP. Z.O.O. (EPO)	42	157	-	-
Ericsson Network Technologies AB (ECA)	-	-	1,920	510
Ericsson Austria A.G. (SEA)	55	5	-	-
Ericsson SPOL.S.R.O. (ECZ)	76	4	-	-
Ericsson Egypt Ltd. (EEL)	489	401	-	-
Ericsson Telecomm. Equipment S.A. (ETG)	214	124	-	-
Ericsson Hungary Ltd. (ETH)	11	468	-	41
Ericsson Ltd. (ETL)	445	303	11	74
Ericsson Telecommunicatia B.V. (ETM)	2,793	487	1,676	2,415
OY LM Ericsson AB (LMF)	-	18	107	-
Ericsson Slovakia SPOL.S.R.O. (SBB)	25	150	-	-
Ericsson d.o.o. (EBA)	20	88	715	172
Ericsson GMBH Group (EDD)	300	-	89	405
Ericsson De Panama S.A. (EDP)	-	14	-	-
Ericsson Espana S.A. (EEM)	18	101	57	-
Ericsson Maroc SARL (EMO)	124	1,120	-	-
Ericsson Telekomunications Bulgaria EOOD (ETB)	114	75	-	-
Ericsson d.o.o. (EVN)	-	2	-	104
Ericsson International Services B.V. Group (ISN)	-	-	44	-
LM Ericsson Ltd. (Nigeria) Group (LMN)	406	90	-	-
Nippon Ericsson K.K. Group (NRJ)	217	-	-	-
Ericsson (China) Communications (CBC)	346	-	-	-
Ericsson TEMS AB Group (TMS)	-	-	-	96
Marconi Sud S.P.A. (MSI)	-	-	-	26
Ericsson Australia PTY LTD. (EPA)	-	-	137	82
Ericsson (Malaysia) SDN, BHD (ECM)	395	-	-	-

Notes to the financial statements (continued)

28 Balances and transactions with related parties (continued)

(c) Year-end balances arising from sales and purchases of goods and services (continued)

	Receivable		Payable	
	2009	2008	2009	2008
	HRK '000	HRK '000	HRK '000	HRK '000
<b>Ericsson Group consolidated companies (continued)</b>				
Kuwait Ericsson Telephone Equipment and Services (KET)	-	-	-	-
Telefonaktiebolaget LM Ericsson, Abu Dabi Branch (TKU)	-	376	-	-
Telefonaktiebolaget LM Ericsson, Tech. Office Oman (TKA)	63	-	-	-
Ericsson AB, Saudi Arabia Branch (BSA)	266	965	-	-
Ericsson AB Sudan Co. Limited (BSD)	77	-	-	-
Ericsson India Private Ltd. (EIL)	7	-	45	-
Ericsson AB(Tunisian Branch) (BTN)	406	-	-	-
Ericsson Algerie S.A.R.L. (EAL)	-	15	-	-
Ericsson NV/SA - Belux (EBR)	-	-	186	-
Ericsson Servicos De Telecomunicacoes LTDA (EBS)	-	154	-	-
Ericsson Telecomunicacoes LDA (SEP)	259	107	-	-
Ericsson Regional Office (RJO)	-	286	-	-
P.T. Ericsson Indonesia (EID)	-	46	-	-
Ericsson Telecommunications Romania S.R.L. (ETR)	198	85	-	-
Ericsson South Africa Ltd. (ESA)	1,167	592	-	-
Ericsson d.o.o. za telekomunikacije (EYU)	-	231	-	-
Ericsson AB Bahrain Branch (BBH)	-	117	-	-
Ericsson Sub-Saharan Africa L.T.D. (ASL)	4	63	-	-
Ericsson AB Jordan (BJO)	-	171	-	-
TOO Ericsson Kazahstan (EKZ)	-	-	-	217
Kuwait Ericsson Telephone Equipment and Services (KET)	-	-	-	211
Ericsson Canada Inc. (EMC)	686	-	-	8
Ericsson Television Limited (TTE)	-	-	94	-
Ericsson de Honduras S.A. (HND)	34	-	-	-
Ericsson France S.A.S. (ESF)	525	-	-	-
Ericsson Iran (IRN)	166	-	-	-
Ericsson Kenya Limited (EKL)	69	-	-	-
Ericsson Korea LTD. (EKK)	50	-	-	-
Ericsson Lebanon Communications (ELC)	40	-	-	-
Ericsson Limited (EHK)	268	-	-	-
Ericsson Radio Systems Ghana (BGH)	594	-	-	-
Ericsson Telekomunikasyon A.S. Istanbul (ENK)	88	-	-	-
Ericsson Vietnam Comp. Limited (ETV)	34	-	-	-
Telefonaktiebolaget LM Ericsson (TKU)	91	-	-	-
Other	2,121	1,894	-	-
	<u>58,905</u>	<u>59,111</u>	<u>67,839</u>	<u>74,281</u>

## Notes to the financial statements (continued)

### **29 Financial risk management**

The Company's activities expose it to a variety of financial risks: market risk (including currency risk, interest rate risk, and price risk), credit risk and liquidity risk. Exposure to currency, interest rate and credit risk arises in the normal course of the Company's business. Risk management is carried out by a treasury department and its principal role is to actively manage investment of excess liquidity as well as financial assets and liabilities, and to manage and control financial risk exposures. The Company also has a customer finance function with the main objective to find suitable third-party financing solutions for customers and to minimize recourse to the Company. Risk management policies that relate to financial instruments can be summarised as follows:

#### ***(a) Currency risk***

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Company is exposed to US dollars and to euro, as a substantial proportion of receivables and foreign revenues are denominated in these currencies. Risk management relies on attempts to match, as much as possible, revenues in each currency with the same currency expenditure. Additionally, the Company enters into foreign currency forward contracts to hedge economically its exposure to currency risk arising on operating cash flows. All derivative contracts have maturities of less than one year after the balance sheet date.

As at 31 December 2009, if the euro had weakened/strengthened by 0.43% (2008: 0.68%) against HRK, with all other variables held constant, and if the US dollar had weakened/strengthened by 2.54% (2008: 8%), with all other variables held constant, the net result after tax for the reporting period would have been HRK 3,997 thousand (2008: HRK 18,108 thousand) higher/lower for the Company, mainly as a result of foreign exchange gains/losses on translation of significant cash and cash equivalents denominated in euro, customer financing at variable rate denominated in euro and foreign receivables denominated in euro.

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (a) Currency risk (continued)

The tables below present the currency analysis and resulting gap.

#### 2009

	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	256,171	12,341	-	268,512	10,385	278,897
Trade and other receivables	373,750	27,307	344	401,401	147,791	549,192
Financial assets at fair value through profit or loss	-	-	-	-	120,873	120,873
Cash and cash equivalents	368,980	4,060	98	373,138	41,797	414,935
	<b>998,901</b>	<b>43,708</b>	<b>442</b>	<b>1,043,051</b>	<b>320,846</b>	<b>1,363,897</b>
Interest-bearing borrowings*	7,505	-	-	7,505	-	7,505
Trade and other payables	83,245	7,300	298	90,843	78,601	169,444
	<b>90,750</b>	<b>7,300</b>	<b>298</b>	<b>98,348</b>	<b>78,601</b>	<b>176,949</b>
Currency gap	<b>908,151</b>	<b>36,408</b>	<b>144</b>	<b>944,703</b>	<b>242,245</b>	<b>1,186,948</b>

\* include interest payable of HRK 885 thousand

#### 2008

	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	314,648	13,453	-	328,101	21,810	349,911
Trade and other receivables	199,275	215,498	60	414,833	151,534	566,367
Financial assets at fair value through profit or loss	-	4,198	-	4,198	45,133	49,331
Cash and cash equivalents	263,077	11,775	26	274,878	43,425	318,303
	<b>777,000</b>	<b>244,924</b>	<b>86</b>	<b>1,022,010</b>	<b>261,902</b>	<b>1,283,912</b>
Interest-bearing borrowings*	10,550	-	-	10,550	-	10,550
Trade and other payables	57,067	28,154	466	85,687	90,614	176,301
Financial liabilities at fair value through profit or loss	-	6,360	-	6,360	-	6,360
	<b>67,617</b>	<b>34,514</b>	<b>466</b>	<b>102,597</b>	<b>90,614</b>	<b>193,211</b>
Currency gap	<b>709,383</b>	<b>210,410</b>	<b>(380)</b>	<b>919,413</b>	<b>171,288</b>	<b>1,090,701</b>

\* include interest payable of HRK 1,717 thousand

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### *(b) Interest rate risk*

Interest rate price risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. As the Company maintains its liquid funds mainly on short-term notice, the risk is limited to investments in the Ministry of Finance bonds, as well as non-current deposits in financial institutions (Notes 13, 18).

At 31 December 2009, if the effective EUR interest rate on borrowings had increased/decreased by 1.2% (2008: 0.6%) on an annual level, the net result after tax for the reporting period would have varied by HRK 1,711 thousand (2008: HRK 1,657 thousand) reflecting different levels of interest income from financial assets classified as fair value through profit and loss, customer financing contracts and higher/lower interest expense on interest bearing borrowings.

The following table present the average interest rates.

	<b>2009</b>	<b>2008</b>
	<b>Average</b>	<b>Average</b>
	<b>interest rates</b>	<b>interest rates</b>
	<b>%</b>	<b>%</b>
Loans and receivables	4.54	6.37
Trade and other receivables	1.22	4.78
Financial assets at fair value through profit or loss	1.97	5.38
Cash and cash equivalents	2.94	5.03
Interest-bearing borrowings	3.46	7.15

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (b) Interest rate risk (continued)

The tables below present the interest rate repricing analysis and resulting gap.

#### 2009

	Non interest bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	(3,355)	-	-	-	222,313	59,939	278,897	51,806
Trade and other receivables	391,825	38,689	18,509	100,169	-	-	549,192	84,918
Financial assets at fair value through profit or loss	603	-	107,019	-	13,251	-	120,873	43,284
Cash and cash equivalents	-	221,554	193,381	-	-	-	414,935	414,935
	<b>389,073</b>	<b>260,243</b>	<b>318,909</b>	<b>100,169</b>	<b>235,564</b>	<b>59,939</b>	<b>1,363,897</b>	<b>594,943</b>
Interest-bearing borrowings*	-	-	-	2,024	5,481	-	7,505	-
Trade and other payables	169,444	-	-	-	-	-	169,444	-
	<b>169,444</b>	<b>-</b>	<b>-</b>	<b>2,024</b>	<b>5,481</b>	<b>-</b>	<b>176,949</b>	<b>-</b>
Interest rate gap	<b>219,629</b>	<b>260,243</b>	<b>318,909</b>	<b>98,145</b>	<b>230,083</b>	<b>59,939</b>	<b>1,186,948</b>	<b>594,943</b>

\* include interest payable of HRK 885 thousand

#### 2008

	Non interest bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	26	1,130	256,197	83,610	8,948	349,911	83,783
Trade and other receivables	287,758	31,372	42,560	204,677	-	-	566,367	269,695
Financial assets at fair value through profit or loss	5,186	-	-	44,145	-	-	49,331	44,145
Cash and cash equivalents	-	318,303	-	-	-	-	318,303	318,303
	<b>292,944</b>	<b>349,701</b>	<b>43,690</b>	<b>505,019</b>	<b>83,610</b>	<b>8,948</b>	<b>1,283,912</b>	<b>715,926</b>
Interest-bearing borrowings*	-	385	-	2,687	7,478	-	10,550	774
Trade and other payables	176,301	-	-	-	-	-	176,301	-
Financial liabilities at fair value through profit or loss	6,360	-	-	-	-	-	6,360	-
	<b>182,661</b>	<b>385</b>	<b>-</b>	<b>2,687</b>	<b>7,478</b>	<b>-</b>	<b>193,211</b>	<b>774</b>
Interest rate gap	<b>110,283</b>	<b>349,316</b>	<b>43,690</b>	<b>502,332</b>	<b>76,132</b>	<b>8,948</b>	<b>1,090,701</b>	<b>715,152</b>

\* include interest payable of HRK 1,717 thousand



## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (c) Price risk

The Company is exposed to equity securities price risk arising from investments that the Company holds in equity and debt securities. These are all classified as financial assets at fair value through profit or loss and are all actively traded on the Zagreb Stock Exchange. Movements of CROBEX and CROBIS indices may therefore have an impact on operating results.

The table below shows the impact of increases/decreases of the index on the Company's net profit, based on the assumption that the CROBEX index had increased/decreased by 39% (2008: 25%) and the CROBIS index had increased/decreased by 5% (2008: 5%). The effect on profit after tax is as follows:

Index	Impact on post-tax profit	
	2009	2008
	HRK '000	HRK '000
CROBEX	188	188
CROBIS	1,633	1,633

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### **(d) Credit risk**

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Significant risk is associated with the high level of customer finance receivables. The Company finances its customers to a significant extent, which exposes it to a significant risk. New customers are only accepted on satisfactory completion of a detailed credit check of the customer and a review of the related country risk. Outstanding credit arrangements are monitored frequently. Impairment losses are calculated using the net present value method. Additionally, there is credit concentration risk as the Company has a significant portion of receivables from some customers. As at 31 December 2009, the five largest customers represent 49% of total net trade receivables (2008: 65%). The Company considers that its maximum exposure to credit risk is reflected in the amount of trade receivables (Notes 13 and 16) and other receivables (Note 17), net of impairment loss for doubtful receivables. Ageing analysis of these receivables is within the maturity analysis table shown further in this note.

Letters of credit are used as a method for securing payments from customers operating in certain markets, in particular in markets with unstable political and/or economic environments. By having banks confirming the letters of credit, the political and commercial credit risk exposures are mitigated.

Prior to the approval of new facilities reported as customer finance, an internal credit risk assessment is conducted in order to assess the credit rating (for political and commercial risk) of each transaction. A reassessment of the credit rating for each customer finance facility is made on a regular basis.

Provisions related to customer finance risk exposures are only made when they are reliably measurable and where events occur after the financing arrangement has become effective, which are expected to have a significant adverse impact on the borrower's ability and/or willingness to service the outstanding debt. These events can be political (normally outside the control of the borrower) or commercial, e.g. the borrower's deteriorating creditworthiness.

Security arrangements for customer finance facilities normally include pledges of equipment and pledges of certain of the borrower's assets. If available, third-party risk coverage may also be arranged. "Third-party risk coverage" means that a financial payment guarantee covering the credit risk has been issued by a bank, an export credit agency or other financial institution. It may also be a credit risk transfer under a so called "sub participation arrangement" with a bank, whereby the credit risk and the funding is taken care of by the bank for the part covered by the bank. A credit risk cover from a third party may also be issued by an insurance company.

As at 31 December 2009, total outstanding exposure related to customer finance was HRK 445 million (2008: HRK 648 million).

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (d) Credit risk (continued)

The following tables provide an ageing detail of current and overdue amounts in respect of all customer loans and receivables as at Dec 31, 2009.

2009	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	77,696	120,821	147,755	108,836	151,816	606,924
Domestic receivables	8,280	95,808	26,158	12,445	-	142,691
Receivables from related parties	9,106	49,799	-	-	-	58,905
<b>Total</b>	<b>95,082</b>	<b>266,428</b>	<b>173,913</b>	<b>121,281</b>	<b>151,816</b>	<b>808,520</b>

2009	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	42,817	33,360	1,404	115	77,696
Domestic receivables	4,406	2,956	918	-	8,280
Receivables from related parties	6,194	2,850	62	-	9,106
<b>Total</b>	<b>53,417</b>	<b>39,166</b>	<b>2,384</b>	<b>115</b>	<b>95,082</b>

2009	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	77,696	114,048	143,583	108,836	151,816	595,979
Domestic receivables	8,280	23,548	11,314	12,445	-	55,587
Receivables from related parties	9,106	44,871	-	-	-	53,977
<b>Total</b>	<b>95,082</b>	<b>182,467</b>	<b>154,897</b>	<b>121,281</b>	<b>151,816</b>	<b>705,543</b>

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (d) Credit risk (continued)

2009	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	34,362	20,770	1,398	115	56,645
Domestic receivables	756	579	39	-	1,374
Receivables from related parties	6,194	2,850	62	-	9,106
<b>Total</b>	<b>41,312</b>	<b>24,199</b>	<b>1,499</b>	<b>115</b>	<b>67,125</b>

As at 31 December 2009, total balances outstanding in respect of customer loans and receivables was HRK 808 million (Table 1), of which HRK 535 million is due for payment within 1 year. As at 31 December 2009, amounts totalling HRK 95 million were overdue (Table 2), of which HRK 92 million is less than 1 year overdue.

As at 31 December 2009, total balances outstanding in respect of customers for which any portion of their account was overdue at 31 December 2009 was HRK 705 million (Table 3). Of this total, HRK 432 million is already due or due for payment within the next year.

In the current economic climate, there is increased risk and uncertainty with regards the ultimate collectability of some of these balances. At 31 December 2009, impairment allowances totalling HRK 30 million were provided in respect of total customer loans and receivables. Amounts totalling HRK 67 million (Table 4) are past due but not impaired at 31 December 2009.

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (e) Liquidity risk

Liquidity risk, also referred to as funding risk, is the risk that an enterprise will encounter difficulty in raising funds to meet commitments associated with financial instruments. As the Company has no commitments in financial instruments, the risk lies only in its daily operations. The Company has a strong focus on its cash flow with daily updates on actual development and monthly updated forecasts. The Company's maturity profile demonstrates the strong liquidity position of the Company and therefore the risk is considered low. The table below presents the maturity analysis and resulting gap.

<b>2009</b>	<b>Up to 1 month</b>	<b>1 - 3 months</b>	<b>3 - 12 months</b>	<b>1 - 5 years</b>	<b>Over 5 years</b>	<b>Total</b>
	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>
Loans and receivables	-	-	-	218,958	59,939	278,897
Trade and other receivables	291,984	146,661	110,547	-	-	549,192
Financial assets at fair value through profit or loss	-	-	120,873	-	-	120,873
Cash and cash equivalents	61,351	353,584	-	-	-	414,935
	<b>353,335</b>	<b>500,245</b>	<b>231,420</b>	<b>218,958</b>	<b>59,939</b>	<b>1,363,897</b>
Interest-bearing borrowings*	-	-	2,024	5,481	-	7,505
Trade and other payables	133,444	36,000	-	-	-	169,444
	<b>133,444</b>	<b>36,000</b>	<b>2,024</b>	<b>5,481</b>	<b>-</b>	<b>176,949</b>
Maturity gap	<b>219,891</b>	<b>464,245</b>	<b>229,396</b>	<b>213,477</b>	<b>59,939</b>	<b>1,186,948</b>

\* include interest payable of HRK 885 thousand

<b>2008</b>	<b>Up to 1 month</b>	<b>1 - 3 months</b>	<b>3 - 12 months</b>	<b>1 - 5 years</b>	<b>Over 5 years</b>	<b>Total</b>
	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>	<b>HRK '000</b>
Loans and receivables	26	1,130	4,598	260,247	83,910	349,911
Trade and other receivables	222,702	130,002	213,663	-	-	566,367
Financial assets at fair value through profit or loss	-	-	5,186	40,318	3,827	49,331
Cash and cash equivalents	318,303	-	-	-	-	318,303
	<b>541,031</b>	<b>131,132</b>	<b>223,447</b>	<b>300,565</b>	<b>87,737</b>	<b>1,283,912</b>
Interest-bearing borrowings*	385	-	2,687	7,478	-	10,550
Trade and other payables	162,296	14,005	-	-	-	176,301
Financial liabilities at fair value through profit or loss	4,013	2,194	153	-	-	6,360
	<b>166,694</b>	<b>16,199</b>	<b>2,840</b>	<b>7,478</b>	<b>-</b>	<b>193,211</b>
Maturity gap	<b>374,337</b>	<b>114,933</b>	<b>220,607</b>	<b>293,087</b>	<b>87,737</b>	<b>1,090,701</b>

\* include interest payable of HRK 1,717 thousand

## Notes to the financial statements (continued)

### 29 Financial risk management (continued)

#### (f) Fair value estimation

The fair value of financial assets at fair value through profit or loss is estimated by reference to their quoted market price at the balance sheet date. The Company's principal financial instruments not carried at fair value are cash and cash equivalents, trade receivables, other receivables, non-current loans and receivables, trade and other payables and interest-bearing borrowings. The fair values of financial instruments together with carrying amounts shown in the balance sheet are as follows:

	Carrying amount 2009 HRK '000	Fair value 2009 HRK '000	Unrecognised gain/(loss) 2009 HRK '000	Carrying amount 2008 HRK '000	Fair value 2008 HRK '000	Unrecognised gain/(loss) 2008 HRK '000
Loans and receivables	278,897	275,736	(3,161)	349,911	348,799	(1,112)
Trade and other receivables	574,647	575,377	730	566,367	566,367	-
Financial assets at fair value through profit or loss	120,873	120,873	-	49,331	49,331	-
Cash and cash equivalents	414,935	414,935	-	318,303	318,303	-
Interest-bearing borrowings	(6,620)	(6,614)	(6)	(8,833)	(8,230)	603
Trade and other payables	(169,444)	(169,444)	-	(176,301)	(176,301)	-
Financial liabilities at fair value through profit or loss				(6,360)	(6,360)	-
	<u>1,213,288</u>	<u>1,210,863</u>	<u>(2,437)</u>	<u>1,092,418</u>	<u>1,091,909</u>	<u>(509)</u>

The fair value of loans and receivables and the fair value of interest-bearing borrowings are calculated based on the Management's best estimate of discounted expected future principal and interest cash flows, using the market-related rate for a similar instrument at the balance sheet date as a discount rate. Fair values and carrying amounts are not significantly different as the (significant) part of loans and non-current receivables were granted at a combination of fixed and variable market rates. Current financial assets, including derivatives are stated at fair value that is based on quoted prices at the balance sheet date without any deduction for transaction costs.

The carrying amount of cash and cash equivalents and of bank deposits deemed to reflect the fair value due to the short-term maturity of these financial instruments. Similarly, the amortised cost carrying amounts of trade receivables and payables with remaining life of less than one year which are all subject to normal trade credit terms deemed to reflect the fair values, except for current portion of non-current receivables that are subject to the contracted interest rate. The following interest rates were used for determining fair values, which are based on available market rates for similar financial instruments:

	2009	2008
Loans and receivables	6.60%	8.00%
Interest-bearing borrowings	6.60%	10.75%

## Notes to the financial statements (continued)

### 30 Derivative instruments

Since 2003, the Company entered into foreign currency forward agreements to hedge economically its operating cash flows denominated in foreign currency, predominately USD and EUR. As these hedges do not qualify for hedge accounting, these are accounted for as trading instruments, with all gains and losses on fair value being recognised in the statement of comprehensive income.

The contractual notional amount of these derivatives (over the counter) at the year-end amounted to nil (2008: HRK 166 million). Their fair values at 31 December 2008 amounted to HRK 4,198 thousand (assets) and HRK 6,360 thousand (liability). These derivatives had remaining periods to maturity of less than one year.

The majority of the Company's purchases and sales contracts are denominated in foreign currency. The embedded derivative component of these contracts is not measured and presented separately as derivatives given that EUR and USD are functional currencies to the counterparties of these contracts and/or EUR and USD are commonly used currencies for the Company's main markets or lines of business.

### 31 Contingent liabilities

In December 1999 the Company received notification of a lawsuit brought against it by a number of small shareholders. According to this lawsuit, the Zagreb Commercial Court was required to declare certain decisions of the General Assembly, held on 18 June 1998, null and void. The Company has submitted its response to the Court. In January 2004 the Zagreb Commercial Court published the first instance judgement in which the plaintiffs' requests have been refused. On 2 March 2004 the plaintiffs appealed and the Appeal Court (Croatian High Commercial Court) has still not made a decision on the appeal. The Company's Management Board is of the opinion that no material liabilities for the Company will result from this lawsuit. No developments have occurred since 2005.