OT-Optima Telekom d.d.

and subsidiaries, Zagreb

Consolidated Financial Statements

as of 31 December 2011

together with Independent Auditor's Report

Content

Responsibility for the financial statements

Pursuant to the Croatian Accounting Law, the Management Board is responsible for ensuring that the consolidated financial statements are prepared for each financial year in accordance with International Financial Reporting Standards ("the IFRS") as published by the International Accounting Standards Board ("IASB") which give a true and fair view of the state of affairs and results of the company OT-Optima Telekom d.d. and its subsidiaries (the "Group").

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

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

- suitable accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- the applicable accounting standards are followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- the consolidated financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Group will continue in business

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

Signed on behalf of the Management Board:

Matija Martić	Goran Jovičić	Jadranka Suručić
President of the Management Board	Member of the Management Board	Member of the Management Board

OT-Optima Telekom d.d.
Bani 75a, Buzin
10010 Zagreb

Republic of Croatia
Zagreb, 27 March 2012

Deloitte

Deloitte d.o.o.
ZagrebTower
Radnička cesta 80
10 000 Zagreb
Hrvatska
OIB: 11686457780

Tel: +385 (0) 1 2351 900
Fax: +385 (0) 1 2351 999
www.deloitte.com/hr

Independent Auditor's Report

To the owners of OT-Optima Telekom d.d.

We have audited the accompanying consolidated financial statements of OT-Optima Telekom d.d. and its subsidiaries (the "Group"), set up on pages 4 to 63 which comprise the consolidated statement of financial position as of 31 December 2011 and the consolidated statement of comprehensive income, consolidated statement of changes in shareholders' equity and consolidated statement of 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 consolidated 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 consolidated 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 consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance 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 the internal controls relevant to the 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 Group's internal controls. 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.

Independent Auditor's Report (continued)

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2011 and the results of its operations and its cash flow for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of matter

The accompanying financial statements have been prepared assuming that the Group will continue as a going concern We draw attention to Note 1 to the consolidated financial statements concerning the consideration given by the Board to the preparation of the consolidated financial statements on the going concern basis in the context of continuing cash flow constraints and future debt repayment schedules.

As discussed in Note 1 the Group incurred a net loss of HRK 67,649 thousand for the year ended 31 December 2011, as of that date, the Company current liabilities exceeded the current assets for the amount of HRK 401,493 thousand.

The Group's ability to cover all of its liabilities will be dependent upon the extent to which the Group's businesses are able to generate cash flows from current operations and collect outstanding receivables in the coming months, and the extent to which it is able to refinance any outstanding debt. As discussed in Note 1, based on the consideration by the Board of all the matters referred to above and given the permanent growth of its market, customer base and development of own infrastructure within the Group, the Board has concluded that the Group will be able to service its liabilities as they fall due and, consequently, considers that the preparation of the consolidated financial statements on the going concern basis is appropriate. If the Group should fail to accomplish the plans, the ability of the Company to continue as a going concern may become doubtful. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Our opinion is not modified in respect of this matter.

Deloitte d.o.o., Zagreb

Branislav Vrtačnik, Certified Auditor and Member of the Board

Zagreb, 27 March 2012

Consolidated statement of comprehensive income

For the year ended 31 December 2011

(All amounts are expressed in thousands of kunas)

	Notes	2011	2010
Sales	4	481,007	448,946
Other operating income	5	5,701	3,999
		486,708	**452,945**
Interconnection fee expenses		(163,820)	(149,757)
Rent of telecommunication equipment		(44,369)	(42,514)
Customer connection related expenses		(15,210)	(13,879)
Staff costs	6	(53,085)	(51,419)
Depreciation and amortization	7	(56,316)	(52,259)
Value adjustments of current and non-current assets		(10,165)	(16,028)
Provisions for jubilee awards and retirement benefits		(681)	(1,710)
Loss from sale of subsidiary		-	(98)
Net loss from sale of assets and equipment		(61)	(58)
Other operating expenses	8	(124,586)	(124,202)
		(468,293)	**(451,924)**
Financial income	9	7,475	6,647
Financial expenses	10	(92,510)	(70,286)
		(85,035)	**(63,639)**
LOSS BEFORE TAX		**(66,620)**	**(62,618)**
Income tax profit charge	11	(849)	(227)
LOSS FOR THE YEAR		**(67,469)**	**(62,845)**
Other comprehensive income/(loss)		5	(55)
TOTAL COMPREHENSIVE LOSS FOR THE YEAR		**(67,464)**	**(62,900)**
Loss per share (HRK)	21	(23,92)	(22.28)
Attributable to:			
Equity holders of the parent		(67,464)	(62,900)
Non-controlling interests		-	-

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

Signed on behalf of the Group on 27 March 2012:

Matija Martić	Goran Jovičić	Jadranka Suručić
President of the Management Board	Member of the Management Board	Member of the Management Board

Consolidated statement of financial position

As of 31 December 2011

(All amounts are expressed in thousands of kunas)

	Notes	2011	2010
ASSETS			
Non-current assets			
Intangible assets	12	25,143	32,417
Property, plant and equipment	13	374,372	388,943
Other non-current assets	14	47,967	43,719
Deferred tax assets	11	-	-
Total non-current assets		**447,482**	**465,079**
Current assets			
Inventories	15	2,239	3,679
Trade receivables	16	82,171	77,236
Receivables from the state and other institutions	17	328	388
Given loans and deposits	18	661	559
Prepayments for services and inventory		868	1,497
Other receivables		449	118
Prepaid expenses and accrued income	19	61,349	54,942
Cash and cash equivalents	20	1,395	1,216
Total current assets		**149,460**	**139,635**
TOTAL ASSETS		**596,942**	**604,714**

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

Signed on behalf of the Group on 27 March 2012:

Matija Martić	Goran Jovičić	Jadranka Suručić
President of the Management Board	Member of the Management Board	Member of the Management Board

OT-Optima Telekom d.d.
ZAGREB

Consolidated statement of financial position (continued)

As of 31 December 2011

(All amounts are expressed in thousands of kunas)

	Notes	2011	2010
EQUITY AND LIABILITIES			
Equity			
Subscribed capital	21	28,201	28,201
Capital gain	21	194,354	194,354
Accumulated loss		(709,234)	(641,770)
		(486,679)	**(419,215)**
Non-controlling interests		-	-
Total equity		**(486,679)**	**(419,215)**
Long term borrowings	22	530,140	522,732
Provision for jubilee awards and retirement benefits		2,548	2,119
Total long term liabilities		**532,688**	**524,851**
Short term borrowings	22	120,064	66,352
Issued bonds	23	267,953	266,491
Trade payables	24	97,928	136,498
Accrued expenses and deferred income	26	46,627	19,554
Other current liabilities	25	18,361	9,254
Provision for tax expenses		-	929
Total short term liabilities		**550,933**	**499,078**
TOTAL EQUITY AND LIABILITIES		**596,942**	**604,714**

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

Signed on behalf of the Group on 27 March 2012:

Matija Martić	Goran Jovičić	Jadranka Suručić
President of the Management Board	Member of the Management Board	Member of the Management Board

OT-Optima Telekom d.d. ZAGREB

Consolidated statement of changes in shareholders' equity

For the year ended 31 December 2011

(All amounts are expressed in thousands of kunas)

	Subscribed capital	Capital gain	Accumulated loss	Total
Balance as of 31 December 2010	**28,201**	**194,354**	**(578,870)**	**(356,315)**
Loss for the year	-	-	(62,845)	(62,845)
Reversal of deferred tax	-	-	(55)	(55)
Total comprehensive loss for the year	-	-	(62,900)	(62,900)
Balance as of 31 December 2011	**28,201**	**194,354**	**(641,770)**	**(419,215)**
Loss for the year	-	-	(67,469)	(67,469)
Foreign exchange differences	-	-	5	5
Total comprehensive loss for the year	-	-	(67,464)	(67,464)
Balance as of 31 December 2011	**28,201**	**194,354**	**(709,234)**	**(486,679)**

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

Signed on behalf of the Group on 27 March 2012:

Matija Martić
President of the Management Board

Goran Jovičić
Member of the Management Board

Jadranka Suručić
Member of the Management Board

ZAGREB

Consolidated statement of cash flows

For the year ended 31 December 2011

(All amounts are expressed in thousands of kunas)

	Notes	2011	2010
Operating activities			
Total comprehensive loss for the year		(67,464)	(62,845)
Adjustments for:			
Income tax		-	227
Depreciation and amortisation		56,316	52,259
Increase in provisions for jubilee awards and retirement benefits		429	1,709
Provisions for tax		(929)	-
Other non cash adjustments- minority interest		-	(83)
Loss from sale of property, plant and equipment		61	58
Impairment of loans and deposits		-	16
Deferred tax assets		-	55
Impairment of trade receivables		4,948	14,594
Interest expense		78,535	66,641
Non cash movement on issued bonds		1,462	1,461
Operating loss before working capital changes		*73,358*	*74,092*
Decrease in inventories		1,440	4,970
Increase in trade receivables		(9,883)	(16,019)
Decrease in receivables from the state and other institutions		60	1,899
Increase in other receivables		(331)	(1,070)
Decrease/(increase) in prepaid expenses and accrued income		(5,778)	1,200
(Decrease)/increase in trade payables		(38,570)	14,688
Increase /(decrease) in accrued expenses and deferred income		27,073	(2,220)
Increase /(decrease) in other short-term liabilities		9,107	(3,300)
Net cash generated from in operating activities		**56,476**	**74,240**
Cash flows from investing activities			
Purchases of tangible and intangible assets		(34,911)	(29,228)
Sale of property		379	631
Net cash used in investing activities		**(34,532)**	**(28,597)**

Consolidated statement of cash flows (continued)

For the year ended 31 December 2011

(All amounts are expressed in thousands of kunas)

	Notes	2011	2010
Cash flows from financing activities			
Increase/(decrease) in loans and non current receivables		(4,350)	1,346
Decrease in borrowings		(17,415)	(50,275)
Net cash used in financing activities		**(21,765)**	**(48,929)**
Net increase/ (decrease) in cash and cash equivalents		**179**	**(3,286)**
Cash and cash equivalents at 1 January		1,216	4,502
Cash and cash equivalents at 31 December	20	**1,395**	**1,216**

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

Signed on behalf of the Group on 27 March 2012:

Matija Martić	Goran Jovičić	Jadranka Surućić
President of the Management Board	Member of the Management Board	Member of the Management Board

OT-Optima Telekom d.d.
ZAGREB

(All amounts are expressed in thousands of kunas)

1. GENERAL

History and incorporation

The company, OT-Optima Telekom d.o.o. (the "Company"), was founded in 1994 under the name Syskey d.o.o. and on 22 April 2004 changed its name to OT-Optima Telekom d.o.o. as well as its principal business activity to telecommunication service provider. The Company changes its legal status from limited liability company to shareholding company during July 2007. Croatian Telecommunication Agency Council gave the right on 19 November 2004 to the Company to provide telecommunication services for period of 30 years.

Principal activities

Principal business activity of the Company is providing telecommunication services to private and business users in the Croatian market. The Company launched its telecommunication services in May 2005. OT-Optima Telekom's initial focus was the corporate segment, however, shortly after the launch, it also began to target the residential market with good value voice packages. For business users, The Company provides direct access and internet services as well as voice service via its own network and/or carried preselected services. In addition, the Company's flagship corporate services are its IP Centrex solution, which is a first in the Croatian market, and its IP VPN services. The Company's existing facilities also allow it to provide co-location and hosting.

The Company set up as sole owner Optima Telekom d.o.o., Koper, Slovenia in 2007.

On 16 August 2011 the Company established, as the sole owner, Optima Telekom d.o.o., a real estate management and consultancy company which did not operate during the reporting period and is still dormant.

Group structure as of 31 December 2011 is as follows:

Parent company

OT-Optima Telekom d.d.

Subsidiaries	Percentage of ownership
Optima Direct d.o.o., Croatia	100%
Optima Telekom d.o.o., Slovenia	100%
OPTIMA TELEKOM za upravljanje nekretninama i savjetovanje d.o.o.	100%

The transactions inside the Group have been done under arm's length principle.

(All amounts are expressed in thousands of kunas)

1. GENERAL (continued)

Staff

As of 31 December 2011, the Group had 387 employees (2010: 376 employees).

Governance and management

In 2011 members of the Management Board of the Parent Company were as follows:

Matija Martić	President
Goran Jovičić	Member
Jadranka Surućić	Member

In 2011 members of the Supervisory Board of the Parent Company were as follows:

Nada Martić	President
Marijan Hanžeković	Member *(from 6 June 2011, Deputy of the President until 6 June 2011)*
Ivan Martić	Deputy of the President (*from 6 June 2011, Deputy of the President until 6 June 2011)*
Zrinka Vuković Berić	Member *(from 6 June 2011)*
Duško Grabovac	Member *(until 6 June 2011)*

Going concern assumption

During the year ended 31 December 2011 the Group incurred a net loss of HRK 67,469 thousand (2010: HRK 62,845 thousand) and, as of that date, the Group's equity is negative in amount of HRK 486,679 thousand (2010: HRK 419,215 thousand). Furthermore, ratios set forth in Note 28 show high indebtedness of the Group. These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. The Group is planning to incur positive EBIT is planned to be achieved in year 2012. Based on the previous period the Group management believes that the plans to achieve positive EBIT in 2012 are realistic.

The Group has reprogrammed its loan facilities with Zagrebačka banka d.d. in 2011 as disclosed in note 22. This has improved the current liquidity position of the Group and increases the Group's ability to cover its liabilities in the following year. The Group ability to cover all of its liabilities will be dependent upon the extent to which the Group's businesses are able to generate cash flows from current operations and collect outstanding receivables in the coming months, and the extent to which it is able to refinance any outstanding debt.

Having considered all these factors and given the continuous market growth, the growth of the customer base and the development of the Group's own infrastructure, the Board has concluded that the Group will be able to meet its debts as they fall due and that it is therefore appropriate to prepare these financial statements on the going concern basis.

2. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs")

Standards and Interpretations effective in the current period

The following amendments to the existing standards issued by the International Accounting Standards Board and interpretations issued by the International Financial Reporting Interpretations Committee are effective for the current period:

- **Amendments to IFRS 1** ***First-time Adoption of IFRS***- Limited Exemption from Comparative IFRS 7 *Disclosures* for First-time Adopters (effective for annual periods beginning on or after 1 July 2010),

- **Amendments to IAS 24** ***Related-party Disclosures*** – Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after 1 January 2011),

- **Amendments to IAS 32** ***Financial Instruments: Disclosure*** **- Accounting for rights issues** (effective for annual periods beginning on or after 1 February 2010),

- **Amendments to various standards and interpretations "Improvements to IFRSs (2010)"** resulting from the Annual Qualitative Improvement of IFRSs, published on 6 May 2010 (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34, IFRIC 13) primarily with a view to removing inconsistencies and clarifying wording (to be applied for annual periods beginning on or after 1 July 2010 or on or after 1 January 2011, depending on the standard/interpretation),

- **Amendments to IFRIC 14 IAS 19 —** ***The Limit on a defined benefit Asset, Minimum Funding Requirements and their Interaction*** - Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after 1 January 2011),

- **IFRIC 19** ***Extinguishing Financial Liabilities with Equity Instruments*** (effective for annual periods beginning on or after 1 July 2010)

The adoption of the amended and revised Standards and Interpretations has not lead to any changes in the Company's accounting policies.

2. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs") (CONTINUED)

Standards and Interpretations in issue not yet adopted

At the date of authorization of these financial statements the following Standards, revisions and Interpretations were in issue but not yet effective:

- **IFRS 9 *Financial Instruments*** (effective for annual periods beginning on or after 1 January 2013),
- **IFRS 10 *Consolidated Financial Statements*** (effective for annual periods beginning on or after 1 January 2013),
- **IFRS 11 *Joint Arrangements*** (effective for annual periods beginning on or after 1 January 2013),
- **IFRS 12 *Disclosures of Involvement with Other Entities*** (effective for annual periods beginning on or after 1 January 2013),
- **IFRS 13 *Fair Value Measurement*** (effective for annual periods beginning on or after 1 January 2013),
- **IAS 27 (revised in 2011) *Separate Financial Statements*** (effective for annual periods beginning on or after 1 January 2013),
- **IAS 28 (Revised in 2011) *Investments in Associates and Joint Ventures*** (effective for annual periods beginning on or after 1 January 2013),
- **Amendments to IFRS 1 *First-time Adoption of IFRS*** - Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (effective for annual periods beginning on or after 1 July 2011),
- **Amendments to IFRS 7 *Financial Instruments: Disclosures*** - Transfers of Financial Assets (effective for annual periods beginning on or after 1 July 2011),
- **Amendments to IAS 1 *Presentation of Financial Statements*** - Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012),

2. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs") (CONTINUED)

Standards and Interpretations in issue not yet adopted (continued)

- **Amendments to IAS 12 *Income Taxes*** - Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after 1 January 2011),

- **Amendments to IAS 19 *Employee Benefits*** - Improvements to the Accounting for Post-employment Benefits (effective for annual periods beginning on or after 1 January 2013),

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

The Management of the Company elected not to adopt those Standards, revisions and Interpretations in advance of their effective dates and anticipates that they will have a certain impact on the financial statements in the period of their adoption in the part that relates specifically for groups and changes in the presentation of items of other comprehensive income. Before the effective dates, the Management will take certain steps to assess the impact of their adoption in connection with all the Standards.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (the "IFRS").

Basis of presentation

The consolidated financial statements of the Group include the financial statements of the company OT-Optima Telekom d.d., Zagreb and its subsidiaries, listed in Note 1 (the "Group").

The financial statements have been prepared on the historical cost basis, except for the valuation of certain non-current assets and financial instruments.

Reporting currency

The financial statements of the Group have been prepared in Croatian Kuna (HRK). At 31 December 2011, the effective exchange rate for EUR 1 and USD 1 was HRK 7.53 and HRK 5.81 respectively (31 December 2010: HRK 7.38 and HRK 5.57, respectively).

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and the entities controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition or up to the effective date of disposal, as appropriate.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of consolidation (continued)

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

All intra-Group transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets (excluding goodwill) of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination.

Losses applicable to the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Investments in associates

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results, assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting, except when the investment is classified as held for sale, in which case it is accounted for in accordance with IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations". Under the equity method, investments in associates are carried in the consolidated statement of financial position at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's and net investment in the associate) are not recognised, unless the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

Where a Group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets

Intangible assets includes right to provide telecommunication services, license and concession for operate different types on the telecommunication services and are carried at cost less accumulated amortisation and any accumulated impairment loss. The useful life of the right, concession and licenses to operate telecommunication services are determined based on the underlying agreements and are amortized on a straight line basis over the period from the moment when it has been approved by regulatory body until the end of the initial right, concession or license term. No renewal periods are considered in the determination of useful life.

The right to provide telecommunication services is given for period of 30 years, while licenses and concession are approved for period of 4 years.

Other intangible assets refer to software license and it is carried at cost less accumulated amortisation and any accumulated impairment loss. The useful life of software is 5 years.

Property, plant and equipment

Property, plant and equipment are shown at historical cost or valuation less accumulated depreciation and any accumulated impairment loss, except for land, which is stated at cost.

Property, plant and equipment in use are depreciated on a straight-line basis using the following rates:

	2011	**2010**
Buildings	40 years	40 years
Vehicles	5 years	5 years
Plant and equipment	5 to 20 years	5 to 20 years
Office equipment	4 years	4 years

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment (continued)

The initial cost of property, plant and equipment comprises its purchase price, including import duties and non-refundable purchase taxes and any directly attributable costs of bringing an asset to its working condition and location for its intended use.

Expenditures incurred after property, plant and equipment have been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to income in the period in which the costs are incurred.

In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment beyond its originally assessed standard performance, the expenditures are capitalised as an additional cost of property, plant and equipment.

The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

Impairment of PP&E and intangible assets

Items of PP&E and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognised immediately in profit or loss.

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

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

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of PP&E and intangible assets (continued)

The net selling price is the amount obtainable from the sale of an asset in an arm's length transaction less the cost of disposal, while value in use is the present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

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

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

Cash and cash equivalents

Cash and cash equivalents comprise cash with bank and on hand. Cash equivalents comprise demand deposits and term deposits with maturities of up to three months.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Finance and operating leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly as an expense, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below). Contingent rentals are recognised as expenses in the periods in which they are incurred.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Inventories

Inventories comprise mainly spare parts for telecommunication equipment, other spare parts office supplies and are stated at the lower of cost and net realisable value. Management provides an allowance for inventories based on a review of the overall ageing of all inventories and a specific review of significant individual amounts included in inventories.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Trade and other receivables

Trade and other receivables are recognised initially at fair value less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables.

Foreign currencies

The financial statements of the Group are presented in the currency of the primary economic environment in which the entity operates (its functional currency). Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

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

Retirement benefits and jubilee awards

The Group provides employees with jubilee and one off retirement awards. The obligation and costs of these benefits are determined using a projected unit credit method. The projected unit credit method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The pension obligation is measured at the present value of estimated future cash flows using an average discount rate on long-term government bonds, where the currency and terms of the government bonds are consistent with the currency and estimated terms of the benefit obligation.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax

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

Current tax

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

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and when the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period

Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items credited or debited directly to other comprehensive income, in which case the tax is also recognised directly in other comprehensive income.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable (i.e. more likely than not) that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate. Where the effect of discounting is material, the amount of the provision is the present value of the expenditures expected to be required to settle the obligation, determined using the estimated risk free interest rate as the discount rate. Where discounting is used, the reversal of such discounting in each year is recognized as a financial expense and the carrying amount of the provision increases in each year to reflect the passage of time.

Provisions for restructuring costs are recognized when the Group has a detailed formal plan for the restructuring that has been communicated to parties concerned.

Financial assets

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

Financial assets are classified into as 'financial assets at fair value through profit or loss' (FTPL), 'investments held to maturity' (HTM), 'available-for-sale financial assets' (AFS) and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest basis for debt instruments other than those financial assets designated as at FVTPL.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Financial assets at fair value through profit or loss (FVTPL)

A financial asset is classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in statement of comprehensive income. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset. Fair value is determined in the manner described in Note 28.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity. Subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method less any impairment.

Available-for-sale financial assets (AFS)

AFS financial assets are non-derivatives that are either designated as AFS or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

Dividends on AFS equity instruments are recognised in statement of comprehensive income when the Group's right to receive the dividends is established.

The fair value of AFS monetary financial assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate prevailing at the end of the reporting period. The foreign exchange gains and losses that are recognised in profit or loss are determined based on the amortised cost of the monetary asset. Other foreign exchange gains and losses are recognised in other comprehensive income.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment.

Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For AFS equity investments, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as a default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation; or
- the disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 60 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Impairment of financial assets (continued)

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

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognised in other comprehensive income are reclassified to profit or loss in the period.

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

In respect of AFS equity securities, impairment losses previously recognised in profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognised in other comprehensive income and accumulated under the heading of investments revaluation reserve. In respect of AFS debt securities, impairment losses are subsequently reversed through profit or loss if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities and equity instruments

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of direct issue costs.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies.

Financial liabilities

Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

Financial liabilities at fair value through profit or loss (FVTPL)

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities and equity instruments (continued)

Financial liabilities at fair value through profit or loss (FVTPL) (continued)

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in statement of comprehensive income. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

Other financial liabilities

Other financial liabilities, including borrowings and bonds, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

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

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Contingent liabilities

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

Revenue recognition

Revenue is recognised when it is probable that economic benefits associated with the transaction will flow to the Group and the amount of revenue can be measured reliably. Revenues for all services are recognised net of VAT and discounts when the services are provided.

Revenue from fixed telephony includes revenue from activation, monthly fee, calls placed by fixed line subscribers and revenue from additional services in fixed telephony.

Revenue from carrier services includes interconnection services for domestic and international carriers.
Revenue from internet and date services included revenue from Internet subscription, ADSL traffic and fixed line access.

Rental income and income from sale of goods relate to the rental and sale of telecommunications equipment required to provide telecommunication services.

Interest income is accrued on a time basis, by reference to the actual yield on the underlying asset.

Interconnection fee expenses

Interconnection fee expenses for using telecommunication infrastructure of other telecommunication providers are recognized in the period they relate to.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Segment reporting

International Financial Reporting Standards define an operating segment as a component of an entity:

a) that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity),
b) whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and
c) for which discrete financial information is available.

The Group has only one segment and is not able to differ property, plant and equipment to the services it provides. The same equipment is used for transfer of voice and data. Management assesses the performance on the level of entire Group. The Group operates on Croatian market which is by the Management is considered as one reporting segment.

Subsequent events

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Critical judgments in applying accounting policies

In the application of the Group's accounting policies, which are described in Note 3, the directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Useful lives of property, plant and equipment

The Group reviews the estimated useful lives of property, plant and equipment at the end of each annual reporting period.

Availability of taxable profits against which the deferred tax assets could be recognised

A deferred tax asset is recognized only to the extent that it is probable that the related tax benefit will be realized. In determining the amount of deferred taxes that can be recognised significant judgments are required, which are based on the probable quantification of time and level of future taxable profits, together with the future tax planning strategy.

Estimates used in determining the jubilee awards retirement bonuses

The Group reviews key variables in determining the value of provisions for jubilee awards and retirement benefits on the annual basis including the adequacy of the discount rate used in determining the present value of estimated future cash flows and also assessing the adequacy of the fluctuation rates used in calculating provisions.

Consequences of certain legal actions

The Company is involved in legal actions which have arisen from the regular course of its operations. Based on the estimates of the probable outcome of legal actions the provisions are assessed and recognised on a consistent basis.

(All amounts are expressed in thousands of kunas)

4. SALES

	2011	2010
Carried pre select services revenue	264,123	275,271
Interconnection revenue	101,642	77,818
Internet services	68,691	57,600
Data services	21,769	20,400
Multimedia services	10,689	3,964
Revenues from commercial representation	5,124	5,754
Rent and sale of equipment	2,513	1,685
Sales of goods and services	-	760
Other sales revenue	6,456	5,694
	481,007	**448,946**

5. OTHER OPERATING INCOME

	2011	2010
Income from collection of receivables previously provided for	3,764	2,950
Income from benefits in kind	426	421
Revenues from penalties collected	-	77
Other income	1,511	551
	5,701	**3,999**

(All amounts are expressed in thousands of kunas)

6. STAFF COSTS

	2011	2010
Net salaries	28,397	27,608
Taxes and contributions	22,257	21,787
Reimbursement of costs to employees	2,431	2,024
	53,085	**51,419**
Number of staff as of 31 December	387	376

Costs reimbursed to employees comprise daily allowances, overnight accommodation and transport related to business travels, commutation allowance, and reimbursement of costs for the use of personal cars for business purposes and similar.

Other employee benefits comprise benefits payable under the Collective Agreements, such as vacation bonus, jubilee awards, Christmas bonus, various supports, and similar.

7. DEPRECIATION AND AMORTISATION

	2011	2010
Depreciation	45,880	42,175
Amortisation	10,436	10,084
	56,316	**52,259**

(All amounts are expressed in thousands of kunas)

8. OTHER OPERATING EXPENSES

	2011	2010
Cost of connection pairs	59,511	62,332
Maintenance expenses	14,770	16,064
Utilities	9,706	8,547
Marketing expenses	7,182	2,725
Invoicing expenses	7,011	8,073
Cost of goods and services sold	4,940	6,224
Residential sales services	4,501	4,244
Cost of services	-	3,769
Bank and financial institutions charges	3,434	3,666
Cost of material	2,463	1,850
Cost of intellectual services	2,170	1,756
Insurance premium	1,677	1,835
Representation	1,114	993
Taxes and contributions irrespective of the result	1,101	1,406
Sponsorships	297	84
Subsequently operating costs	-	130
Other expenses	4,709	504
	124,586	**124,202**

9. FINANCIAL INCOME

	2011	2010
Income from interest and fees	6,176	5,951
Foreign exchange gains	1,299	696
	7,475	**6,647**

(All amounts are expressed in thousands of kunas)

10. FINANCIAL EXPENSES

	2011	2010
Interest expense and fees	80,052	66,641
Foreign exchange losses	12,458	3,645
	92,510	**70,286**

Interest expenses refer to the interest expense from borrowings and issued bonds and to penalty interest expense from transactions with suppliers.
Foreign exchange losses increased as a result of the depreciation of the Croatian kuna against the euro during the reporting period and foreign-currency pegged long-term debt.

11. INCOME TAX EXPENSE

The Group is subject to income tax, according to the laws and regulations of the Republic of Croatia and Republic of Slovenia. The tax base is determined as the difference between income and expenses for the period, increased by tax non-deductible expenses. The income tax rate is 20% (21% in Republic of Slovenia). The Company Optima Telekom d.d. had no income tax liability for year 2011 because it incurred losses from operations. Subsidiaries Optima Direct d.o.o., Buje and OT-Optima Telekom d.o.o., Koper had income tax liability based on realized profit in 2011.

Income tax comprises of:

	2011	2010
Current income tax in Croatia	738	142
Current income tax in Slovenia	111	85
Income tax (recognized in statement of comprehensive income)	**849**	**227**

Relation between accounting profit and losses available for carry forward is shown as follows:

	2011	2010
Accounting loss before tax	**(66,620)**	**(62,618)**
Tax calculated at weighted average tax rates applicable for profits in the respective countries	(13,324)	(12,524)
Effect of permanent tax differences	466	411
Effect of tax losses available for carry forward	13,707	12,340
Income tax (recognized in statement of comprehensive income)	**849**	**227**

(All amounts are expressed in thousands of kunas)

11. INCOME TAX EXPENSE (continued)

Tax losses for the year 2011 are carried forward as a tax deductible item as follows:

Year of tax loss	Amount	Year of expiry
2007	126,455	2012
2009	100,916	2013
2010	110,799	2014
2011	64,157	2015
2012	67,737	2016
	470,064	

As of yearend the Group did not recognize deferred tax assets in the amount HRK 94,013 thousand arising from tax losses carried forward because the availability of future taxable profit against which the unused tax losses can be utilized is not certain.

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

(All amounts are expressed in thousands of kunas)

12. INTANGIBLE ASSETS

	Concessions and rights	Software	Intangible assets under construction	Total intangible assets
COST				
At 31 December 2009	**8,188**	**76,541**	-	**84,729**
Additions	-	924	-	924
At 31 December 2010	**8,188**	**77,465**	-	**85,653**
Additions	-	-	2,855	2,855
Transfer	-	2,855	(2,855)	-
Disposals	-	(9)	-	(9)
At 31 December 2011	**8,188**	**80,311**	-	**88,499**
ACCUMULATED AMORTISATION				
At 31 December 2009	**1,113**	**42,039**	-	**43,152**
Charge for the year	273	9,811	-	10,084
At 31 December 2010	**1,386**	**51,850**	-	**53,236**
Charge for the year	272	9.852	-	10.124
Disposals	-	(4)	-	(4)
At 31 December 2011	**1.658**	**61.698**	-	**63.356**
NET BOOK VALUE				
At 31 December 2011	**6,530**	**18,613**	-	**25,143**
At 31 December 2010	**6,802**	**25,615**	-	**32,417**

The intangible assets of the Group include the right to operate telecommunication services (concession and rights) with the carrying value HRK 6,530 thousand as of 31 December 2011 (2010: HRK 6,802 thousand). The right has been approved to the Company by the Croatian agency for Telecommunication on 19 November 2004.

As of 31 December 2011 cost value of intangible assets with restricted ownership as a result of collateralization amounts to HRK 74,538 thousand (2010: HRK 65,845 thousand).

(All amounts are expressed in thousands of kunas)

13. PROPERTY, PLANT AND EQUIPMENT

	Land	Buildings	Plant and equipment	Vehicles	Work of Arts	Assets in progress	Leasehold improvements	Total
COST								
At 31 December 2009	**23**	**25,524**	**443,194**	**90**	**46**	**55,032**	**3,768**	**527,677**
Additions	-	-	5,582	253	-	22,469	-	28,304
Transfer from assets in progress	-	-	35,597	-	-	(35,597)	-	-
Disposals	-	-	(535)	(217)	-	-	-	(752)
At 31 December 2010	**23**	**25,524**	**483,838**	**126**	**46**	**41,904**	**3,768**	**555,229**
Additions	-	369	1,545	-	-	29,863	273	32,056
Transfer from assets in progress	-	-	66,544	-	-	(66,544)	-	-
Disposals	-	-	(1,637)	-	-	-	-	(1,638)
Na dan 31. prosinca 2011.	**23**	**25,893**	**550,290**	**126**	**46**	**5,229**	**4,041**	**585,647**
ACCUMULATED DEPRECIATION								
At 31 December 2009	**-**	**3,711**	**117,904**	**55**	**-**	**-**	**2,504**	**124,174**
Charge for the year	-	646	40,805	18	-	-	706	42,175
Disposals	-	-	(63)	-	-	-	-	(63)
At 31 December 2010	**-**	**4,357**	**158,646**	**73**	**-**	**-**	**3,210**	**166,286**
Charge for the year	-	651	45,206	23	-	-	312	46,192
Disposals	-	-	(1,203)	-	-	-	-	(1,203)
Na dan 31. prosinca 2011.	**-**	**5,008**	**202,649**	**96**	**-**	**-**	**3,522**	**211,275**
NET BOOK VALUE								
At 31 December 2011	**23**	**20,884**	**347,641**	**30**	**46**	**5,229**	**519**	**374,372**
At 31 December 2010	**23**	**21,167**	**325,192**	**53**	**46**	**41,904**	**558**	**388,943**

(All amounts are expressed in thousands of kunas)

13. PROPERTY, PLANT AND EQUIPMENT (continued)

As of 31 December 2011, cost value of property, plant and equipment with restricted ownership as a result of collateralization amounts to HRK 461,869 thousand (2010: HRK 408,737 thousand).

14. OTHER NON CURRENT ASSETS

	2011	2010
Loan to the majority company owner	12,913	12,180
Loan to third party companies	34,989	31,548
Long term deposit	3,524	3,420
	51,426	**47,148**
Impairment of loans and deposits	(3,459)	(3,429)
	47,967	**43,719**

On 31 March 2006 Optima Direct d.o.o. approved a loan to Mr. Matija Martić, majority owner of the Company, in the amount of HRK 6,000 thousand. Purpose of the loan was refinancing of borrowings and advances to resolve housing and other requirements. The annual interest rate is 6% and maturity of the loan is 31 March 2021. Loan collateral are 6 blank debit notes and 6 bills of exchange.

On 27 February 2007, before changing incorporation (change of its legal status to share capital company) the Company has approved a loan to Mr. Matija Martić in the total amount of HRK 3,200 thousand. The interest rate of the loan is variable and is periodically adjusted with average interest rate on loans received from banks (Zagrebačka banka d.d. and Hypo Alpe-Adria-Bank d.d.). The annual interest rate is 8.5%. The loan matures on 27 February 2022. The loan collateral are blank promissory notes. Purpose of the loan is purchase of business share in the company OT-Optima Telekom d.d.

The Company has approved two short term loans to Optima OSN Inženjering d.o.o., Rijeka in the amounts of HRK 28,535 thousand and HRK 2,994 thousand respectively with the interest rate of 11.5% per annum. The loans were approved for the purpose of development of IP Centrex service which is planned to be used by the Company. The collaterals of loans are two debentures in the amount of the loan approved increased for the interests, fees and expenses as well as e two blank promissory notes. During 2010 the Management of the Company has agreed annexes to the loans agreements for the extension of the maturity date to 30 April 2013 and 13 August 2012 respectively. The Management Board believes that the receivables to Optima OSN inženjering d.o.o., Rijeka is fully recoverable.

(All amounts are expressed in thousands of kunas)

15. INVENTORIES

	2011	2010
Telecommunication merchandise	2,239	3,679
	2,239	**3,679**

16. TRADE RECEIVABLES

	2011	2010
Domestic trade receivables	99,922	92,658
Foreign trade receivables	12,487	9,135
Interest receivables	78	811
Allowance for bad debt	(30,316)	(25,368)
	82,171	**77,236**

	2011	2010
Trade receivables	112,409	101,793
Provision for bad debt	(30,316)	(25,368)
Net trade receivables	**82,093**	**76,425**

The net trade receivables do not include interest receivables for which maturity is expected within agreed terms.

(All amounts are expressed in thousands of kunas)

16. TRADE RECEIVABLES (continued)

Movement of provision for doubtful trade receivables:

	2011	2010
01 January	25,368	8,039
Bad debt write-off	(1,182)	2,883
Collected during the period	(3,002)	(2,091)
Additionally provided	9,132	16,537
Closing balance	**30,316**	**25,368**

Ageing of trade receivables for the Company:

	2011	2010
Undue	62,937	55,734
up to 120 days	18,243	28,016
120 - 360 days	7,445	5,753
over 360 days	23,784	12,290
Total	**112,409**	**101,793**

17. RECEIVABLES FROM THE STATE AND OTHER INSTITUTIONS

	2011	2010
Other receivables from state and other institutions	328	388
	328	**388**

(All amounts are expressed in thousands of kunas)

18. GIVEN LOANS AND DEPOSITS

	2011	2010
Deposits	661	559
	661	**559**

Current financial assets in 2010 consist only of deposits. The carrying amounts of cash items do not differ significantly from their market value.

19. PREPAID EXPENSES AND ACCRUED INCOME

	2011	2010
Deferred customer related expenses	41,286	48,420
Prepaid expenses for goods not received	18,896	4,884
Deferred loans origination fees	1,167	1,638
	61,349	**54,942**

Movement in prepaid expenses and accrued income:

	2011	2010
1 January	54,942	56,142
Increase in prepaid expenses and accrued income	49,115	37,617
Expensed during the year	(42,708)	(38,817)
Closing balance	**61,349**	**54,942**

(All amounts are expressed in thousands of kunas).

20. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash in hand, current account balances and other balances with banks.

	2011	2010
Bank balances	967	1,126
Foreign account balance	413	7
Cash in hand	15	83
	1,395	**1,216**
Deposits with maturity up to 3 months	-	-
Cash and cash equivalents	**1,395**	**1,216**

21. SUBSCRIBED CAPITAL

Majority owner of Company Matija Martić paid in additional capital of HRK 20 million at 24 August 2007. Subscribed capital of the Company has been increased from HRK 201 thousand to HRK 20,201 thousand. The Company has also changed its legal status and became shareholding company. Total number of ordinary shares was 2,020,070 with nominal value of HRK 10. Sole owner of the company remained Matija Martić.

The Company increased its subscribed capital through the initial public offer in November 2007. The Company issued additional 800,000 shares with nominal value of HRK 10. This increased number of shares to 2,820,070. The Company also achieved capital gain of HRK 194,354 thousand as difference between nominal amount and issued price. The shares started to trade on 7 January 2008 on Zagreb stock exchange. The owners of the previously issued bonds had a first right of buy on initial public offer.

Earnings per shares were as follows:

	2011	2010
Loss for the year	(67,469)	(62,845)
Number of shares	2,820,070	2,820,070
Loss per share	**(23.92)**	**(22.28)**

(All amounts are expressed in thousands of kunas)

21. SUBSCRIBED CAPITAL (continued)

Shareholders structure as of 31 December was as follows:

Shareholders	2011	%	2010	%
MARTIĆ MATIJA	18,596	65.94	18,596	65.94
	18,596	**65.94**	**18,596**	**65.94**
ZAGREBAČKA BANKA D.D./ZBIRNI SKRBNIČKI RAČUN ZA UNICREDIT BANK AUSTRIA AG	1,605	5.69	-	-
ZAGREBAČKA BANKA D.D./ZBIRNI SKRBNIČKI RAČUN ZAGREBAČKA BANKA D.D./DF	1,385	4.91	45	0.16
RAIFFEISENBANK AUSTRIA D.D./R5	1,345	4.77	1,345	4.77
RAIFFEISENBANK AUSTRIA D.D./RBA	979	3.47	979	3.47
SOCIETE GENERALE-SPLITSKA BANKA D.D./ AZ OBVEZNI MIROVINSKI FOND (1/1)	766	2.72	766	2.72
ZAGREBAČKA BANKA D.D. (1/1)	428	1.52	1,716	6.09
ŽUVANIĆ ROLAND (1/1)	303	1.07	303	1.07
JOVIČIĆ GORAN (1/1)	202	0.72	202	0.72
HRVATSKA POŠTANSKA BANKA D.D./ZBIRNI RAČUN ZA KLIJENTE BANKE	144	0.51	144	0.51
SOCIETE GENERALE-SPLITSKA BANKA D.D./ AZ PROFIT DOBROVOLJNI MIROVINSKI FOND (1/1)	127	0.45	229	0.81
INTERKAPITAL D.D. (1/1)	108	0.38	166	0.59
ČORAK LJERKA (1/1)	100	0.35	100	0.35
RAIFFEISENBANK AUSTRIA D.D. (1/1)	91	0.32	365	1.29
INTERKAPITAL VRIJEDNOSNI PAPIRI D.O.O./ZBIRNI SKRBNIČKI RAČUN ZA DP	85	0.30	-	-
ČERNOŠEK KRUNOSLAV (1/1)	74	0.26	65	0.23
VARVODIĆ ANTE (1/1)	60	0.21	46	0.16
RAIFFEISENBANK AUSTRIA D.D./ZBIRNI SKRBNIČKI RAČUN ZA DF	57	0.20	57	0.20
KMETOVIĆ IVO (1/1)	43	0.15	43	0.15
OREŠKOVIĆ STJEPAN (1/1)	38	0.13	38	0.13
HUGHES KATICA (1/1)	38	0.13	-	-
PBZ D.D./I - ZBIRNI SKRBNIČKI RAČUN	34	0.12	-	-

(All amounts are expressed in thousands of kunas)

21. SUBSCRIBED CAPITAL (continued)

Shareholders structure as of 31 December was as follows (continued):

Shareholders (continued)	2011	%	2010	%
KANTOCI IVANIŠEVIĆ KRISTINA (1/1)	32	0.11	-	-
CELIŽIĆ MARIO (1/1)	30	0.11	-	-
	8,072	28.63	6,608	23.43
Small shareholders	1,533	5.43	2,997	10.63
	28,201	100.00	28,201	100.00

(All amounts are expressed in thousands of kunas)

22. LONG TERM AND SHORT TERM BORROWINGS

	2011	2010
Borrowings	644,372	588,102
Interest	5,832	982
Total borrowings	**650,204**	**589,084**
Short term portion of borrowings	**(120,064)**	**(66,352)**
Long term portion of borrowings	**530,140**	**522,732**

As of 31 December 2011, cost value of property, plant and equipment with restricted ownership as a result of collateralization amounts to HRK 461,869 thousand (2010: HRK 408,737 thousand).

(All amounts are expressed in thousands of kunas)

22. LONG TERM AND SHORT TERM BORROWINGS (continued)

Bank	Original currency	Loan amount in currency	Maturity date	2011	2010
Loans					
Hypo banka	EUR	6,750	1.9.2013	30,567	45,092
Zagrebačka banka	EUR	42,860	15.1.2014	322,754	316,528
Zagrebačka banka	EUR	20,325	15.1.2014	153,056	150,104
BKS banka	EUR	5,000	31.12.2013	22,715	22,279
Optima OSN Inženjering	HRK	3,400	31.5.2012	340	1,020
OTP banka	EUR	756	1.11.2013	3,849	5,579
Kreditna banka Zagreb	HRK	1,800	5.5.2012	1,800	-
Centar banka	HRK	4,500	15.9.2012	4,542	-
OTP banka	HRK	200	11.11.2012	90	-
Leasings					
Hypo leasing Kroatien	EUR	115	1.7.2015	381	462
Raiffeisen leasing	EUR	2,536	22.1.2011	-	502
Raiffeisen leasing	EUR	528	1.10.2012	1,611	3,348
Hypo leasing Kroatien	EUR	780	1.6.2023	3,961	4,101
IT Tel	EUR	1,513	19.2.2015	6,244	7,950
IT Tel	EUR	1,298	1.2.2015	5,223	6,693

(All amounts are expressed in thousands of kunas)

22. LONG TERM AND SHORT TERM BORROWINGS (continued)

	Original currency	Loan amount in currency	Maturity date	2011	2010
Leasings (continued)					
Computech	HRK	2,808	31.12.2011	-	117
HUAWEI	EUR	3,908	30.5.2011	-	15,633
Euroleasing	EUR	6	30.9.2011	-	41
Storm	HRK	327	-	33	327
Storm	HRK	8,326	29.2.2012	2,974	8,326
Huawei	EUR	2,770	1.8.2013	17,849	-
SG Leasing	EUR	168	11.12.2014	1,276	-
Erste factoring	HRK	58,428	31.5.2012	58,428	-
IBM	USD	778	1.3.2013	2,476	-
Kapsh Tis	HRK	3,229	15.11.2012	2,583	-
Computech	EUR	200	15.3.2012	1,620	-
				644,372	**588,102**

The weighted average interest rate on long-term and short-term borrowings was 7.50%

(All amounts are expressed in thousands of kunas)

22. LONG TERM AND SHORT TERM BORROWINGS (continued)

	2011	2010
EUR	571,106	578,312
HRK	70,790	9,790
USD	2,476	-
Long term borrowings	**644,372**	**588,102**

During 2010 total amount of short-term and long-term borrowings towards Zagrebačka banka d.d., Zagreb and Hypo Alpe-Adria-Bank d.d., Zagreb have been reprogrammed in long-term borrowings.

On 31 December 2010, Zagrebačka banka d.d., Zagreb, approved to the Company a long-term loan with the principal amount of EUR 42,860 thousand. The interest is accrued quarterly at the rate of 3-month EURIBOR, plus a margin of 4.80 pp annually. The purpose of the loan facility is to settle the liabilities for fees on the guarantees issued as well as on the basis of guarantees and/or accrued interest on the following long-term and short-term loans: Agreement No. 3203453577 concluded on 29 August 2008; Agreement No. 3206986895 concluded on 14 February 2007; Agreement No. 3206986931 concluded on 10 July 2007; Agreement No. 3206986942, concluded on 3 September 2007; Agreement No. 3214906421, concluded on 2 December 2009; Agreement No. 3218711059, concluded on 28 January 2010. The ultimate repayment date is 15 January 2014.
The loan is repayable in 5 quarterly instalments of EUR 680 thousand each, which fall due as follows:
- the first instalment is due on the second anniversary of the agreement date; i.e. 31 December 2012;
- the second instalment is due on 31 March 2013;
- the third instalment is due on 30 June 2013;
- the fourth instalment is due on 30 September 2013;
- the fifth instalment is due on 31 December 2013.

The remaining loan amount of EUR 39,400,000.00 will be due on the ultimate repayment date.
The agreed collaterals comprise 20 blank accepted bills with the bill of exchange charges statement, a notarially authenticated debenture, a blank promissory note from Matija Martic with authorisation, lien established on the real estate and movable property of the Company, lien on the Company shares, insurance policies for real estate and movable property with restricted transferability.

(All amounts are expressed in thousands of kunas)

22. LONG TERM AND SHORT TERM BORROWINGS (continued)

On 31 December 2010 Zagrebačka banka d.d., Zagreb, approved to the Company a long-term loan with a principal of EUR 20,325 thousand. The loan is approved to settle the loan principal and a part of interest due under the agreement on a short-term loan in the amount of HRK 140,500 thousand, concluded on 29 August 2008. The loan is repayable on a one-off basis on the ultimate repayment date, which is 15 January 2014. The loan bears interest at a rate of 10 percent annually and is due on a one-off basis on the ultimate repayment date. The agreed collaterals comprise 20 blank accepted bills with the bill of exchange charge statement, a blank promissory note from Matija Martic with authorisation, lien established on the real estate and movable property of the Company, lien on the Company shares, insurance policies for real estate and movable property with restricted transferability.

The Company has committed, on a consolidation basis, to the following covenants over the term of the loans extended by Zagrebačka banka d.d. which are ultimately repayable in 2014:

	2011	**2012**	**2013**	**2014**
Minimum increased in total revenue	8%	13%	10%	6%
Minimum investment in tangible and intangible assets (% of total revenue)	6%	6%	6%	6%
Incremental EBITDA margin	32%	33%	34%	35%

In addition to the terms and conditions specified above, the Company has the obligation to notify of or provide a valid request in case of the following: capital expenditure, raising debt finance, liens, arm's-length transactions, profit or operation sharing agreements, investments, changes in the registered business, capital and Articles of Association/Statute, sale of assets, mergers and acquisitions, and ownership changes.

(All amounts are expressed in thousands of kunas)

23. ISSUED BONDS

	2011	2010
Nominal value	250,000	250,000
Deferred origination fees	(2,923)	(4,384)
Interest liabilities	20,874	20,875
	267,953	**266,491**

The Company issued bonds (OPTE-O-124 A) in nominal value of HRK 250 million on 5 February 2007. Bonds were issued on Zagreb Stock Exchange. Bonds have interest rate of 9.125% and their maturity date is 1 February 2014. The bonds have been issued with a price of 99.496%. Interest will be paid on annual basis starting from 1 February 2008. The effective interest rate is 9.226%.

The following covenants need to be complied with.:

	2007	2008	2009	2010	2011	2012
Consolidate EBITDA Margin (%) >=	5.00%	10.00%	15.00%	20.00%	25.00%	25.00%
Consolidated EBITDA/ Consolidated interest >=	0.30	1.20	1.75	2.00	4.00	5.00
Consolidate EBITDA (in HRK million) >=	17	45	75	125	150	200
CAPEX/Sales revenue <=	0.75	0.65	0.5	0.5	0.4	0.35
Consolidate total liabilities/ Consolidated EBITDA <=	30	15	10	6	5	3
No dividend payments	Yes	Yes	Yes	Yes	Yes	Yes

(All amounts are expressed in thousands of kunas)

23. ISSUED BONDS (continued)

The Agent, Zagrebačka banka d.d., is testing compliance of all terms at the end of each year based on the audited consolidated financial statements. The Group also took obligation to increase the value of its subscribed capital until 30 June 2009 through issuing of new shares that cannot be less then HRK 150 million. The bond owners had a first right to buy shares during increase of share capital. The bond owners have a right to call for early collection of nominal value of bonds if the Group is not in compliance with the covenants and other requirements. As explained in note 21 during 2007 the Company has increased its share capital for over HRK 150 million and satisfied requirement in relation to increase of share capital. The Group is not in compliance with above covenants as at 31 December 2011 and 2010.

As per International Accounting Standard 1 (the "IAS 1"), Article 65, when the company breaches a provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, it classifies the liability as current, even if the lender agreed, after the reporting period and before the authorization of the financial statements for issue, not to demand payment as a consequence of the breach. The Group classifies the liability as current because, at the end of the reporting period, it does not have an unconditional right to defer its settlement for at least twelve months after that date.

In accordance with this requirement as per the IAS 1 the Group has reclassified its liabilities from issued bonds to short term liabilities.

24. TRADE PAYABLES

	2011	2010
Domestic trade payables	86,600	128,710
Foreign trade payables	11,328	7,788
	97,928	**136,498**

The average credit period on purchases from suppliers was 103 days (2010: 151 days).

(All amounts are expressed in thousands of kunas)

25. OTHER CURRENT LIABILITIES

	2011	2010
Payables on advances	8,130	-
VAT payable	4,245	3,180
Net payroll	2,532	2,434
Taxes and contributions on salaries	1,862	1,795
Other state payables	1,505	814
Other payables	87	1,031
	18,361	**9,254**

26. ACCRUED EXPENSES AND DEFERRED INCOME

	2011	2010
Accrued interest	15,646	-
Deferred revenues from equipment rental	14,500	-
Accrued invoices from domestic suppliers	12,613	16,331
Deferred income from notary charges	3,337	920
Accrued invoices from foreign suppliers	531	1,438
Other accruals	-	865
	46,627	**19,554**

Movement in accrued expenses and deferred income:

	2011	2010
1 January	19,554	21,774
Increase in accrued expenses and deferred income	83,440	66,059
Reversed during the year	(56,367)	(68,279)
Closing balance	**46,627**	**19,554**

(All amounts are presented in thousands of kunas)

27. RELATED PARTY TRANSACTIONS

Receivables and payables and income and expenses from related party transactions for the Group are provided in the table below:

	2011	2010
Receivables		
Matija Martić	12,913	12,180
Payables		
Matija Martić	-	-

In 2011 compensations paid to all Management Board members and Supervisory Board members amounted to HRK 5,491 thousand (2010: HRK 2,550 thousand) as follows:

- Total amount of compensations paid to Management Board members and Supervisory Board members in OT-Optima Telekom d.d. amounted to HRK 189 thousand (including compensation to the majority owner of the Company).
- Total amount of compensations paid to Management Board members and Supervisory Board members in Optima Direct d.o.o. amounted to HRK 5,302 thousand.

(Please note that Supervisory Board members are only receiving compensation related to their regular work in the Group. No additional compensation is paid for the function of Supervisory Board member)

Compensations paid in 2010 to the majority owner of the Company Matija Martić were HRK 2,009 thousand (2010: HRK 1,595 thousand). Compensations relate to his work in the Company. Loans given to the majority owner of the Company amounted to HRK 12,913 thousand as at 31 December 2011 (2010: HRK 12,180 thousand) and are disclosed in Note 14 to the consolidated financial statements.

Members of key management have signed the Statement of Independence, confirming that neither they nor their close family members have any equity interests in any of the companies.

The Members of the Management and Supervisory Boards who were at the same time the Company's shareholders at 31 December 2011 were as follows:

- Matija Martić, President of the Management Board, with a share of 65.94% comprising 1,850,569 ordinary shares;
- Goran Jovičić, Member of the Management Board, with a share of 0.71% comprising 20,000 ordinary shares.

(All amounts are presented in thousands of kunas)

28. FINANCIAL INSTRUMENTS

During the period, the Group used most of its financial instruments to finance its operations. Financial instruments include loans, bills of exchange, cash and liquid assets, and other various instruments, such as trade receivables and trade payables, arising directly from the ordinary activities.

Capital risk management

Net debt to equity ratio (Gearing ratio)

The Management Board reviews the capital structure on a quarterly basis. As part of this review, the Management considers the cost of capital and the risks associated with each capital class.

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

The capital structure of the Group consists of net debt (borrowings as detailed in Note 22 offset by cash and bank balances) and equity of the Group (comprising issued capital, reserves and retained earnings as detailed in Note 21).

The Management Board reviews the capital structure of the Group on a quarterly basis. As part of this review, the Management Board considers the cost of capital and the risks associated with each class of capital.

The gearing ratio at 31 December was as follows:

	2011	**2010**
Debt (long-term and short-term borrowings)	918,157	855,575
Cash and cash equivalents	(1,395)	(1,216)
Net debt	916,762	854,359
Equity	(486,679)	(419,215)
Net debt to equity ratio	**(188.37%)**	**(203.80%)**

Debt is defined as liability for long-term and short-term borrowings and for issued bonds. Equity includes all capital and reserves of the Group.

(All amounts are presented in thousands of kunas)

28. FINANCIAL INSTRUMENTS (continued)

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instruments are disclosed in note 3 to the consolidated financial statements.

Categories of financial instruments

	2011	2010
Financial assets		
Loans	48,628	44,278
Cash and cash equivalents	1,395	1,216
Receivables	83,488	78,851
	133,511	**124,345**
Financial liabilities at amortized cost		
Issued bonds	267,953	266,491
Borrowings	650,204	589,084
Trade payables and other liabilities	155,304	159,527
	1,073,461	**1,015,102**

(All amounts are expressed in thousands of kunas)

28. FINANCIAL INSTRUMENTS (continued)

Currency risk (continued)

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

	2011	2010	2011	2010
	Liabilities		Assets	
EUR	585,805	585,746	23,459	18,864
USD	2,967	290	-	110
	588,772	**586,036**	**23,459**	**18,974**

Foreign currency sensitivity analysis

The Group is mainly exposed to the fluctuations in the exchange rate of Croatian kuna to Euro and US dollar.

The following table details the Group's sensitivity to a 10 % increase in Croatian kuna against the relevant foreign currencies (2010: 10%). The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for percentage change in foreign currency rates. The sensitivity analysis includes monetary assets and monetary liabilities in foreign currencies. A negative number indicates a decrease in profit where HRK changes for above mentioned percentage against the relevant currency. For a reverse proportional change of HRK against the relevant currency, there would be an equal and opposite impact on the profit.

	2011	2010	2011	2010
	Liabilities		Assets	
EUR	58,580	58,575	2,346	1,886
USD	297	29	-	11
	58,877	**58,604**	**2,346**	**1,897**

The exposure to the fluctuations in exchange rates by 10% is mainly attributable to the borrowings, trade payables and receivables from related companies denominated in Euro (EUR) and US dollar (USD).

28. FINANCIAL INSTRUMENTS (continued)

Interest rate risk

Interest rate cash flow risk is the risk that the interest cost of financial instruments will fluctuate over the time.

The Group has long-term borrowings at variable interest rates in the amount of HRK 368,636 thousand which exposed it significantly to the interest rate risk. In case that the interest rate was higher for 1%, the effect of HRK 3,686 thousand would debit the income statement for the year ended 31 December 2011.

The issued bonds are valued at amortized cost and changes in the interest rate that could effect change in the fair value of the bonds are not effecting the carrying amount of issued bonds.

Other price risks

The Group is not exposed to equity price risks arising from equity investments. There are no significant equity instruments held by the Group.

Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted procedures which it applies in dealing with customers. The Group obtains sufficient collaterals, where appropriate, as a means of mitigating the risk of financial loss from defaults.

Trade receivables are followed on regular basis to determine their risk status and appropriate risk procedures are taken for trade receivables. The credit ratings of Group counterparties are continuously monitored and credit exposure is controlled by counterparty limits that are reviewed at least annually. The Group transacts with a large number of customers from various industries and of various size, as well as with retail customers that have specific credit risk. The Group has developed procedures for each specific customer group to insure that credit risk is addressed in most appropriate way.

(All amounts are presented in thousands of kunas)

28. FINANCIAL INSTRUMENTS (continued)

Credit risk (continued)

In the table below the Group presented the balances of 6 major counterparties at the end of the reporting period.

Counterparty	Headquarters Country	2011	2010
Telekom Slovenije	Slovenija	6,051	2,097
HT	Hrvatska	2,548	3,466
VIPnet	Hrvatska	970	997
Tele2	Hrvatska	963	102
CARnet	Hrvatska	208	646
IT –TEL	Slovenija	155	2,404
		10,895	**9,712**

(All amounts are presented in thousands of kunas)

28. FINANCIAL INSTRUMENTS (continued)

Liquidity risk

Ultimate responsibility for liquidity risk management rests with the Board of directors, which has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate reserves and credit lines, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

Liquidity rate tables and interest rate risks

The following tables detail the Group's remaining contractual maturity for its financial liabilities at the end of the period. The tables have been drawn up based on the undiscounted cash flows of financial liabilities on maturity date. The table includes both interest and principal cash flows.

	up to 1 year	1-5 years	Over 5 years	Total
2011				
Non-interest bearing	147,247	-	-	147,247
Interest bearing	120,063	795,850	2,243	918,156
	228,740	**795,850**	**2,243**	**1,065,403**
2010				
Non-interest bearing	159,527	-	-	159,527
Interest bearing	66,352	786,708	2,515	855,575
	225,879	**786,708**	**2,515**	**1,015,102**

Majority of non-interest bearing liabilities in 2011 represent trade payables in the total amount of HRK 97,928 thousand (2010: HRK 136,498 thousand).

Interest bearing liabilities are short-term and long term borrowings, finance leases as well as bonds issued.

(All amounts are expressed in thousands of kunas)

28. FINANCIAL INSTRUMENTS (continued)

Liquidity risk (continued)

The following tables detail the Group's remaining contractual maturity for its financial assets at the end of the period.

The tables have been drawn up based on the undiscounted cash flows of financial assets on maturity date. The table includes both interest and principal cash flows.

	up to 1 year	1-5 years	Over 5 years	Total
2011				
Non-interest bearing	84,883	-	-	84,883
Interest bearing	750	43,004	4,874	48,628
	85,726	**43,004**	**4,874**	**133,511**
2010				
Non-interest bearing	80,067	-	-	80,067
Interest bearing	610	31,488	12,180	44,278
	80,677	**31,488**	**12,180**	**124,345**

The balance of cash and cash equivalents is shown under non-interest bearing financial assets due to low interest rate of these assets.

29. APPROVAL OF FINANCIAL STATEMENTS

The financial statements set out on pages 4 to 63 were approved by the Board of directors and authorized for issue.

Signed on behalf of the Group on 27 March 2012:

Matija Martić	Goran Jovičić	Jadranka Suručić
President of the Management Board	Member of the Management Board	Member of the Management Board

OT-Optima Telekom d.d.
ZAGREB