

**PUBLIC ENTERPRISE
“ELEKTROMREŽA SRBIJE,” BELGRADE**

**Consolidated Financial Statements
For the Year Ended December 31, 2009 and
Independent Auditors’ Report**

CONTENTS

	Page
Independent Auditors' Report	1 - 2
Consolidated Financial Statements	
Consolidated Income Statement	3
Consolidated Balance Sheet	4
Consolidated Statement of Changes in Equity and Reserves	5
Consolidated Cash Flow Statement	6
Notes to the Consolidated Financial Statements	7 - 44

Translation of the Auditors' Report issued in the Serbian language

INDEPENDENT AUDITORS' REPORT

TO THE MANAGEMENT BOARD OF THE PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE

We have audited the accompanying consolidated financial statements (pages 3 to 44) of the Public Enterprise Elektromreža Srbije, Belgrade (the "Company") and its subsidiaries, which comprise the consolidated balance sheet as at December 31, 2009, and the related consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of the significant accounting policies and other explanatory notes.

The consolidated financial statements of the Company as of December 31, 2008, were audited by another auditor whose report dated June 18, 2009, expressed a qualified opinion due to the matter of appraisal of property, plant and equipment.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the accounting regulations of the Republic of Serbia. 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 and the Law on Accounting and Auditing of the Republic of Serbia. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

INDEPENDENT AUDITORS' REPORT

TO THE MANAGEMENT BOARD OF THE PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE (Continued)

Basis for Qualified Opinion

As disclosed in Note 16 to the accompanying consolidated financial statements, in 2008, property, plant and equipment were appraised and revalued amounts have been determined by applying the weighted average of the values determined based on the income approach, replacement cost method and market-based approach, which was not substantiated by sufficient evidence. As a result, we were unable to quantify the effect of this matter on the value of property, plant and equipment, revaluation reserves and deferred tax liabilities as at December 31, 2009.

As disclosed in Note 28 to the accompanying consolidated financial statements, borrowings from the Export-Import Bank of China stated as of December 31, 2009 in the amount of RSD 893,891 thousand entirely relate to matured but outstanding borrowings. The negotiations on the reschedule of these debts, as increased by accumulated interest, in the amount of RSD 331,194 thousand (Note 30) are currently underway. Accordingly, given the uncertainty over the outcome of negotiations, we were unable to satisfy ourselves as to the fairness of disclosures regarding the liabilities arising from borrowing and interest accrued thereof, or to determine the effects of such adjustments, if any, on the Company's results of operations disclosed in the accompanying consolidated financial statements.

Qualified Opinion

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the matters referred to in the preceding paragraphs, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Public Enterprise "Elektromreža Srbije," Belgrade as of December 31, 2009, and its consolidated financial performance and cash flows for the year then ended, in accordance with the accounting regulations of the Republic of Serbia.

Emphasis of Matter

Without further qualifying our opinion, we draw attention to the following matters:

- a) As disclosed in Note 16 to the consolidated financial statements, the Company is in the ownership registration process of its rights of use over the property assumed from the Public Enterprise "Elektroistok," as well as from other entities within the Public Enterprise – Electric Power Industry of Serbia ("JP EPS"). At the issuance date of this Report, the aforementioned rights are still vested in these public enterprises.
- b) As disclosed in Note 24 to the consolidated financial statements, the amount of the Company's core capital is not reconciled with the amount inscribed in the Business Register maintained within the Serbian Business Registers Agency.

Belgrade, May 4, 2010

Miroslav Tončić
Certified Auditor

**PUBLIC ENTERPRISE
“ELEKTROMREŽA SRBIJE,” BELGRADE**

CONSOLIDATED INCOME STATEMENT
Year Ended December 31, 2009
(thousands of RSD)

	<u>Notes</u>	<u>2009</u>	<u>2008</u>
			<i>Audited by Another Auditor</i>
OPERATING INCOME			
Sales	5	10,903,170	11,454,210
Own work capitalized		914,101	661,663
Other operating income	6	238,108	232,578
		<u>12,055,379</u>	<u>12,348,451</u>
OPERATING EXPENSES			
Cost of commercial goods sold		(3,094)	(3,761)
Cost of material	7	(3,326,076)	(3,585,865)
Staff costs	8	(2,027,782)	(1,906,987)
Depreciation, amortization and provisions	9	(3,018,236)	(3,036,583)
Other operating expenses	10	(3,344,281)	(2,835,957)
		<u>(11,719,469)</u>	<u>(11,369,153)</u>
OPERATING PROFIT		<u>335,910</u>	<u>979,298</u>
Finance income	11	823,668	832,071
Finance expenses	12	(936,952)	(2,026,748)
Other income	13	256,238	734,492
Other expenses	14	(24,054)	(333,434)
PROFIT BEFORE TAX		<u>454,810</u>	<u>185,679</u>
INCOME TAXES	15		
- current tax expense		(65,039)	(60,779)
- deferred tax benefits		72,248	90,957
NET PROFIT		<u>462,019</u>	<u>215,857</u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

These consolidated financial statements were approved by the management of the Public Enterprise Elektromreža Srbije, Belgrade and filed with the Serbian Business Registers Agency on April 30, 2010.

Signed on behalf of the Company by:

Miloš Milanković
General Manager

Jovan Ećimović
Chief Financial Officer

Mirjana Krstić
Head of Accounting

**PUBLIC ENTERPRISE
“ELEKTROMREŽA SRBIJE,” BELGRADE**

CONSOLIDATED BALANCE SHEET
As at December 31, 2009
(thousands of RSD)

	Notes	December 31, 2009	December 31, 2008
			<i>Audited by Another Auditor</i>
ASSETS			
Non-current assets			
Intangible assets	16	42,532	40,891
Property, plant and equipment	16	54,152,361	54,165,221
Advances for property, plant and equipment	16	151,899	671,751
Equity investments	17	8,267	8,267
Other long-term financial placement	18	1,195,282	1,887,430
		<u>55,550,341</u>	<u>56,773,560</u>
Current assets			
Inventories	19	452,302	385,406
Accounts receivable	20	1,229,878	1,960,882
Short-term financial placements	21	3,490,826	1,495,344
Cash and cash equivalents	22	2,461,847	2,052,247
Value added tax and prepayments	23	943,124	692,018
		<u>8,577,977</u>	<u>6,585,897</u>
Total assets		<u><u>64,128,318</u></u>	<u><u>63,359,457</u></u>
EQUITY AND LIABILITIES			
Equity			
	24		
State-owned and other capital		30,540,088	30,540,088
Reserves		1,072	1,072
Revaluation reserves		12,192,270	12,207,156
Retained earnings		2,822,641	2,434,495
		<u>45,556,071</u>	<u>45,182,811</u>
Long-term provisions	25	273,577	184,128
Non-current liabilities			
Long-term borrowings	26	12,007,349	10,788,336
Other long-term liabilities	27	263,823	268,007
Current liabilities			
Short-term financial liabilities	28	1,397,877	1,255,637
Accounts payable	29	1,096,676	1,827,943
Other short-term liabilities	30	529,028	516,682
Value added tax and other duties payable and accruals	31	1,636,822	1,872,796
Income taxes payable		9,014	32,788
		<u>4,669,417</u>	<u>5,505,846</u>
Deferred tax liabilities	15	1,358,081	1,430,329
Total equity and liabilities		<u><u>64,128,318</u></u>	<u><u>63,359,457</u></u>
Off-balance-sheet items	32	<u><u>15,867,935</u></u>	<u><u>14,370,767</u></u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

**PUBLIC ENTERPRISE
“ELEKTROMREŽA SRBIJE,” BELGRADE**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
Year Ended December 31, 2009
(thousands of RSD)

	State- Owned Capital	Other Capital	Reserves	Revaluation Reserves	Retained Earnings	Total
<i>Audited by Another Auditor</i>						
Balance at January 1, 2008	30,506,506	33,582	1,072	-	602,699	31,143,859
Appraisal effects	-	-	-	13,561,914	-	13,561,914
Deferred taxes based on appraisal of property, plant and equipment	-	-	-	(1,354,747)	-	(1,354,747)
Profit for the year	-	-	-	-	215,857	215,857
Profit distribution	-	-	-	-	(225,628)	(225,628)
Adjustment of the tax base of property, plant and equipment	-	-	-	-	1,844,409	1,844,409
Other	-	-	-	(11)	(2,842)	(2,853)
Balance at December 31, 2008	<u>30,506,506</u>	<u>33,582</u>	<u>1,072</u>	<u>12,207,156</u>	<u>2,434,495</u>	<u>45,182,811</u>
Balance at January 1, 2009	30,506,506	33,582	1,072	12,207,156	2,434,495	45,182,811
Opening balance adjustments	-	-	-	-	(6,179)	(6,179)
Reversal of revaluation reserves	-	-	-	(14,886)	14,886	-
Profit distributed to the founder	-	-	-	-	(78,032)	(78,032)
Profit for the year	-	-	-	-	462,019	462,019
Other	-	-	-	-	(4,548)	(4,548)
Balance at December 31, 2009	<u>30,506,506</u>	<u>33,582</u>	<u>1,072</u>	<u>12,192,270</u>	<u>2,822,641</u>	<u>45,556,071</u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT
Year Ended December 31, 2009
(Thousands of RSD)

	2009	2008
		<i>Audited by Another Auditor</i>
CASH FLOWS FROM OPERATIONS		
Cash provided by operating activities		
Cash receipts from customers	13,193,128	12,511,478
Interest received	364,841	168,564
Other receipts from operating activities	30,917	1,949
Cash used in operating activities		
Cash paid to suppliers	(7,780,867)	(6,080,787)
Cash paid to and on behalf of employees	(1,882,453)	(1,792,464)
Interest paid	(445,895)	(52,060)
Income taxes paid	(86,375)	(31,079)
Other public duties paid	(712,697)	(972,031)
<i>Net cash provided by operating activities</i>	<u>2,680,599</u>	<u>3,753,570</u>
CASH FLOWS FROM INVESTING ACTIVITY		
Cash provided by investing activities		
Sale of shares and equity investments (net inflows)	-	483
Sale of intangible assets	909	939
Interest received	-	6,215
Dividends received	293,848	106,747
Cash used in investing activities		
Purchase of intangible assets, property, plant and equipment	(2,267,824)	(2,175,353)
Other financial placements (net outflows)	(693,746)	-
<i>Net cash used in investing activities</i>	<u>(2,666,813)</u>	<u>(2,060,969)</u>
CASH FLOWS FROM FINANCING ACTIVITY		
Cash used in financing activities		
Long- and short-term loans and other liabilities (net inflows)	298,655	141,198
Dividends paid	(78,032)	(208,772)
<i>Net cash provided by/(used in) financing activities</i>	<u>220,623</u>	<u>(67,574)</u>
NET CASH INCREASE	234,409	1,625,027
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	2,052,247	371,673
Foreign exchange gains and losses on translation	<u>175,191</u>	<u>55,547</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>2,461,847</u>	<u>2,052,247</u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

1. BACKGROUND INFORMATION

The Public Enterprise “Elektromreža Srbije,” Belgrade (hereinafter: “JP EMS” or the “Company”) was established pursuant to the Decision of the Republic of Serbia Government (no. 023-397/2005-1 dated January 27, 2005) on the establishment of a public enterprise involved in power transmission and in the management of the power transmission system, published in the Official Gazette of the Republic of Serbia no. 12/2005.

The RS Government Decision on the Company’s establishment sets forth that assets for the foundation and operation of the Company comprise movable and immovable assets, cash, securities, ownership rights and other assets comprising a founding contribution made by the Electric Power Industry of Serbia (“JP Elektroprivreda Srbije,” hereinafter “JP EPS”) upon the establishment of the Public Company “Elektroistok,” as well as assets acquired by this entity in its operations. Additionally, assets used for the establishment and operation of the Company also include a portion of assets that were used by JP EPS to perform the activities of power transmission system management, as well as the equity interest of JP EPS in the entity Elektroenergetski koordinacioni centar d.o.o. Beograd (Electricity Coordinating Center). All these assets are listed in the balance sheet as of December 31, 2004.

As in accordance with the Republic of Serbia Decision on the Company Establishment, effective as of July 1, 2005, the Serbian Business Registers Agency enacted a Decision on the Inscription of the Company into the Business Register, record number BD 80469/2005.

The Company’s core activities are the power transmission and transmission system management.

In order to perform these activities, the Company obtained from the Republic of Serbia Energy Agency the following licenses:

1. License for power transmission (no. 312-277/2006-L-I)
2. License for transmission system management (no. 312-278/2006-L-I)
3. License to organize electricity market (no. 312-58/2006-L-I)

The Company is the only entity in the Republic of Serbia holding licenses to perform the aforementioned activities.

The Company’s registration number is 20054182.

The Company’s tax identification number is 103921661.

At December 31, 2009, the Company had 1,355 employees (December 31, 2008: 1,355 employees).

The Company is headquartered in Belgrade, at number 11 Kneza Miloša Street.

The management bodies are the Management Board, General Manager and Supervisory Board. The representatives of the Company’s bodies are appointed by the Government of the Republic of Serbia.

Managing Board – by means of its decisions, it ensures the realization of all targets defined in the Company’s Statutes and is responsible for the achievement of the Company’s strategic goals.

General Manger – represents and acts in the name of the Company, organizes and manages the work process and coordinates the business activities of the Company; he is answerable for the regulatory compliance, proposes the basis for the business policies, the operation programs and development plans to the Managing Board, executes the decisions enacted by the Managing Board.

Supervisory Board – supervises the Company’s work and operations, reviews their annual reports, calculation and proposals for profit distribution.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION****2.1. Scope of Consolidation**

The accompanying financial statements represent the consolidation of the financial statements of the Public Utility "Elektromreža Srbije" (the "Company" or the "Parent Company") and the financial statements of the following legal entities:

	<u>% of Equity interests</u>
1 Elektroistok Izgradnja d.o.o., Beograd	100.00%
2 Elektroistok Projektni Biro d.o.o., Beograd	100.00%

All intercompany balances and transactions between the aforelisted subsidiaries have been eliminated upon consolidation.

2.2. Basis of Preparation and Presentation of Consolidated Financial Statements

Pursuant to the Law on Accounting and Auditing (Official Gazette of the Republic of Serbia no. 46 of June 2, 2006), legal entities and entrepreneurs incorporated in Serbia are required to maintain their books of account, to recognize and value assets and liabilities, income and expenses, and to present, submit and disclose financial statements in conformity with the prevailing legislation and professional rules which include: the Framework for the Preparation and Presentation of Financial Statements (the "Framework"), International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS), as well as the related interpretations representing an integral part of these standards which were in effect as at December 31, 2002.

The amendments to IAS, as well as the newly-issued IFRS and the related interpretations issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC"), in the period between December 31, 2002 and 2007, were officially adopted pursuant to a Decision enacted by the Ministry of Finance of the Republic of Serbia ("Ministry") and published in the Official Gazette of the Republic of Serbia number 16 of February 12, 2008. The Ministry also established (based on the Decision number 401-00-1456/2008-16) and published the official translation of the amendments to IAS 39 "Financial Instruments: Recognition and Measurement" and to IFRS 7 "Financial Instruments: Disclosures" in the RS Official Gazette number 116 as of December 17, 2008.

However, until the preparation date of the accompanying consolidated financial statements, not all amendments to IAS/IFRS and IFRIC in effect for annual periods beginning on or after January 1, 2009 had been translated (particularly subsequent to the aforementioned Decision of the Ministry). In addition, the accompanying consolidated financial statements are presented in the format prescribed under the "Guidelines on the Prescribed Form and Content of the Financial Statements of Enterprises, Cooperatives and Entrepreneurial Ventures" (Official Gazette of the Republic of Serbia, no. 114 of December 22, 2006, 119 as of December 26, 2008 and 2/10 as of January 15, 2010). Such statements represent the complete set of financial statements as defined under the law, which differ from those defined under the provisions of IAS 1, "Presentation of Financial Statements," and differ in some respects, from the presentation of certain amounts as required under the aforementioned standard. Standards and interpretations issued, but not yet adopted and translated in Republic of Serbia and standards and interpretations in issue not yet in effect are disclosed in Notes 2.3 and 2.4.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION (Continued)

2.2. Basis of Preparation and Presentation of Consolidated Financial Statements (Continued)

As in accordance with the Supplements and Amendment to Guidelines (Official Gazette of RS no. 2/10 as of January 15, 2010), in preparing the annual financial statements as of and for the year ended December 31, 2009, legal entities and entrepreneurs may decide not to disclose the effects of foreign exchange gains and losses and currency clause related to receivables and payables denominated in foreign currency within income and expenses of the current period. In the aforementioned case, the net effect of contractually agreed currency clauses is stated within other prepayments/accruals. The proportionate amount of deferred currency clause effects is transferred to the accounts of foreign exchange losses and gains as of the date upon which the respective payable if due for settlement and receivable is due for collection. The aforementioned accounting treatment departs from the provisions IAS 21 "Effects of Changes in Foreign Exchange Rates."

In accordance with the aforescribed, and given the potentially material effects which the departures of accounting regulations of the Republic of Serbia from IAS and IFRS may have on the fairness presentations made in the consolidated financial statements, the accompanying consolidated financial statements cannot be treated as a set of financial statements prepared in accordance with IAS and IFRS.

The consolidated financial statements were prepared at historical cost principle, unless otherwise stipulated in the accounting policies presented hereunder.

In the preparation of the accompanying consolidated financial statements, the Company adhered to the accounting policies described in Note 3. These accounting policies have been consistently applied to all presented reporting periods.

The Company's consolidated financial statements are stated in thousands of dinars (RSD). The dinar is the official reporting currency in the Republic of Serbia.

2.3. Standards and Interpretations in Issue, but not yet Adopted and Translated

As of the consolidated financial statements issuance date, the following standards, amendments were issued by the International Accounting Standards Board and Interpretations issued by the International Financial Reporting Interpretations Committee but were not officially adopted and translated in the Republic of Serbia for the annual accounting periods commencing on or after January 1, 2009:

- Amendments to IFRS 4 "Insurance contracts" and IFRS 7 "Financial Instruments: Disclosures" - Improving disclosures about financial instruments (effective for annual periods beginning on or after January 1, 2009),
- Amendments to IFRS 1 "First-time Adoption of IFRS" and IAS 27 "Consolidated and Separate Financial Statements" – Cost of investment in a subsidiary, jointly-controlled entity or associate (effective for annual periods beginning on or after January 1, 2009),
- Amendments to various standards and interpretations resulting from the Annual quality improvement project of IFRS published on May 22, 2008 (IAS 1, IFRS 5, IAS 8, IAS 10, IAS 16, IAS 19, IAS 20, IAS 23, IAS 27, IAS 28, IAS 29, IAS 31, IAS 34, IAS 36, IAS 38, IAS 39, IAS 40, IAS 41) primarily with a view to removing inconsistencies and clarifying wording (most amendments are to be applied for annual periods beginning on or after January 1, 2009),

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION (Continued)

2.3. Standards and Interpretations Issued, but not yet Adopted and Translated (Continued)

- Amendments to IAS 32 "Financial Instruments: Presentation" and IAS 1 "Presentation of Financial Statements" – Puttable financial instruments and obligations arising on liquidation (effective for annual periods beginning on or after January 1, 2009),
- IAS 1 (revised) "Presentation of Financial Statements" – A revised presentation (effective for annual periods beginning on or after January 1, 2009),
- IAS 23 (revised) "Borrowing Costs" (effective for annual periods beginning on or after January 1, 2009),
- Amendments to IFRS 2 "Share-based Payment" – Vesting conditions and cancellations (effective for annual periods beginning on or after January 1, 2009),
- Amendments to IFRIC 9 "Reassessment of Embedded Derivatives" and IAS 39 "Financial Instruments: Recognition and Measurement" -Embedded Derivatives (effective for annual periods ending on or after June 30, 2009),
- IFRIC 13 "Customer Loyalty Programmes" (effective for annual periods beginning on or after July 1, 2008),
- IFRIC 14 Interpretation on IAS 19 – The Limit on a Defined Benefit Assets, Minimum Funding Requirements and their Interaction (effective for the accounting periods starting January 1, 2008);
- IFRIC 15 "Agreements for the Construction of Real Estate" (effective for annual periods beginning on or after January 1, 2009),
- IFRIC 16 "Hedges of a Net Investment in a Foreign Operation" (effective for annual periods beginning on or after October 1, 2008).

2.4. Standards and Interpretations in Issue not yet in Effect

At the date of issuance of these consolidated 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 January 1, 2013),
- IFRS 3 (revised) "Business Combinations" (effective for annual periods beginning on or after July 1, 2009),
- IFRS 1 (revised) "First-time Adoption of IFRS" (effective for annual periods beginning on or after July 1, 2009),
- Amendments to IFRS 1 "First-time Adoption of IFRS"- Additional Exemptions for First-time Adopters (effective for annual periods beginning on or after January 1, 2010),

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION (Continued)

2.4. Standards and Interpretations in Issue not yet in Effect (Continued)

- Amendments to IFRS 2 "Share-based Payment" - Group cash-settled share-based payment transactions (effective for annual periods beginning on or after January 1, 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 January 1, 2011),
- Amendments to IAS 27 "Consolidated and Separate Financial Statements" (effective for annual periods beginning on or after July 1, 2009),
- Amendments to IAS 32 "Financial Instruments: Presentation" – Accounting for rights issues (effective for annual periods beginning on or after February 1, 2010),
- Amendments to IAS 39 "Financial Instruments: Recognition and Measurement" – Embedded derivatives (effective for annual periods beginning on or after July 1, 2009),
- Amendments to various standards and interpretations resulting from the Annual quality improvement project of IFRS published on April 16, 2009 (IFRS 2, IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 18, IAS 36, IAS 38, IAS 39, IFRIC 9, IFRIC 16) primarily with a view to removing inconsistencies and clarifying wording, (most amendments are to be applied for annual periods beginning on or after January 1, 2010),
- 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 January 1, 2011),
- IFRIC 17 "Distributions of Non-Cash Assets to Owners" (effective for annual periods beginning on or after July 1, 2009),
- IFRIC 18 "Transfers of Assets from Customers" (effective for transfer of assets from customers received on or after July 1, 2009),
- IFRIC 19 "Extinguishing Liabilities with Equity Instruments" (effective for annual periods beginning on or after July 1, 2010).

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1. Revenues

Revenue is recognized up to the amount of economic benefits that will flow to the entity on condition that this amount may be reliably measured. Income is stated at fair value, net of discounts and value added taxes.

Income from power transmission system access and use is entirely realized in transactions with entities operating within the Electric Power Industry of Serbia.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.1. Revenues (Continued)

Income from Power Transmission System Access and Use

Based on the calculation methodology, income from power transmission system access and use also includes fees paid for the cost of electricity purchased to cover losses incurred in power transmission and costs of system services, i.e. power transmission system maintenance expenses.

Income from the access and use of power transmission system is invoiced based on tariffs for the access and use of power transmission system approved by the Energy Agency of the Republic of Serbia in its communication number 495/2008-D-I/2, adopted at the session of the Republic of Serbia Government held on July 31, 2008.

Interest income is recognized when earned.

3.2. Foreign Exchange Translation

Transactions denominated in foreign currencies are translated into dinars at the official exchange rates, as determined on the Interbank Market as of the date of each transaction.

Assets and liabilities denominated in foreign currencies are translated into dinars by applying the official exchange rates, as determined on the Interbank Market that are prevailing as of the balance sheet date.

Foreign exchange gains and losses earned or incurred in business transactions in foreign currency funds are carried through profit and loss account. Foreign exchange gains and losses arising from the recalculation of balance sheet items denominated in foreign currency are credited or charged as foreign exchange gains and losses, except in the case of foreign exchange differences and effects of currency clauses calculated for receivables and payables which are in accordance with Guidelines' Amendments and Supplements, stated on the line item of prepayments. The proportionate amount of deferred foreign exchange differences is transferred to foreign exchange gains and losses as of the maturity date, i.e. receivables underlying the calculation.

3.3. Borrowing Costs

Borrowing costs are recognized as an expense in the period in which they are incurred, regardless of how the borrowings are applied.

3.4. Income Taxes

Current Income Taxes

In the Republic of Serbia, income tax is payable at the rate of 10% on the tax base reported in the annual corporate income tax return as reduced by any applicable tax credits. The taxable base stated in the income tax return includes the profit shown in the statutory statement income, as adjusted for the differences that are specifically defined under statutory tax rules.

The tax regulations effective in the Republic of Serbia do not envisage that any tax losses of the current period be used to recover taxes paid within a specific carryback period. However, any current year losses may be used to reduce or eliminate taxes to be paid in future periods, but only for the duration of no longer than ten ensuing years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.4. Income Taxes (Continued)

Deferred Income Taxes

Deferred income taxes are provided using the balance sheet liability method, for temporary differences arising between the tax bases of assets and liabilities and their carrying values in the consolidated financial statements. The currently-enacted tax rates or the substantively-enacted rates at the balance sheet date are used to determine the deferred income tax amount. Deferred tax liabilities are recognized for all taxable temporary differences.

Deferred tax assets are recognized for all deductible temporary differences, and the tax effects of income tax losses and credits are available for carryforward, to the extent that it is probable that taxable profit will be available, against which the deductible temporary differences and the tax loss/credits of the carryforwards can be utilized.

Indirect Taxes and Contributions

Indirect taxes and contributions include property taxes and various other taxes and contributions on employee salaries paid pursuant to republic and municipal regulations.

3.5. Grants

Grants are recognized at their fair value when there is reasonable assurance that the entity will comply with the conditions attaching to them or that the grants will be received. Grants shall be recognized as income over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis. In case grants relate to an asset, the fair value of the grant is recorded on the accounts of deferred income which is then recognized in the income statement on a systematic and rational basis over the useful life of the asset in equal annual amounts.

3.6. Employee Benefits

a) Employee Taxes and Contributions for Social Security

Pursuant to the statutory provisions, the Company has an obligation to pay contributions to various state social security funds. These obligations involve the payment of contributions on behalf of the employee, by the employer in an amount calculated by applying the specific, legally-prescribed rates. The Company is also legally obligated to withhold contributions from gross salaries to employees, and on their behalf to transfer the withheld portions directly to the appropriate government funds. These contributions payable on behalf of the employee and employer are charged to expenses in the period in which they arise.

Long-Term Employee Benefits

Pursuant to the provisions of the Labor Law, the Company is under obligation to pay retirement benefits to a retiree in the amount of 1.67 of an average salary earned in the Company in the month preceding the payment of such benefits and the amount cannot be below three average gross monthly salaries realized in the Republic of Serbia in the month preceding the retirement. In addition, the Company is under obligation to pay jubilee awards for each 10, 20 and 30 years of service with the Company payable in the amount of 0.56, 1.12 and 1.67 of average monthly salaries in the Company for three months preceding the payment of jubilee awards.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Employee Benefits (Continued)

a) Employee Taxes and Contributions for Social Security (Continued)

Long-Term Employee Benefits (Continued)

Employee retirement benefits and jubilee awards are not provided by funds. Expenses arising from these benefits are determined by applying the actuarial Projected Unit Credit Method. Actuarial gains and losses are recognized within income and expenses in the profit and loss account of their respective period.

Costs of labor dating from previous periods are accrued in the income statement on a straight-line basis until the entitlement to the benefit has been established. If benefits become vested immediately after the introduction of a new plan or change in the existing plan, costs of labor realized in the preceding periods are instantly recognized. The liability for benefits includes the present value of benefits payable net of realized but unrecognized costs of labor dating from prior periods.

3.7. Property, Plant and Equipment

Items of property, plant and equipment are initially measured at their cost. The cost of an item of property, plant and equipment comprises its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Subsequent expenditure is recognized as an increase in cost of the respective assets, when it is probable that future economic benefits, in excess of the originally assessed standard of performance, will flow to the Company. Repairs and maintenance are expensed as incurred. Self-constructed assets are carried at cost which must be below the asset's market value. Cost of assets does not include interest, administrative expenses and overheads which cannot be directly ascribed to the construction of such asset.

Subsequent to initial recognition, land, buildings and equipment for transmission and transmission system management are carried at fair value net of accumulated depreciation of buildings and equipment and any possible impairment losses following the revaluation date. Revaluations is made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

If an asset's carrying amount is increased as a result of a revaluation, the increase is credited directly to equity under the heading of revaluation surplus. However, the increase is recognized in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss. If an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognized in profit or loss except to the extent of any credit balance existing in the revaluation surplus in respect of that asset.

In 2008, property, plant and equipment were appraised and revalued amounts have been determined by applying the weighted average of the values determined based on the income approach, replacement cost method and market-based approach, which was not substantiated by sufficient evidence.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.7. Property, Plant and Equipment (Continued)**

Revaluation reserves presented as a line item within equity relating to an item of property, plant and equipment are directly transferred to retained earnings upon disposal and sale of respective assets.

Office and other equipment which are not used in power transmission and transmission system management are stated at cost net of accumulated depreciation and impairment losses, if any.

Depreciation is calculated on the straight line basis to the cost of asset over its useful life, by applying the following depreciation rates:

Buildings	1.5%-2%
Equipment for substations	4%-5.56%
Overhead lines	2.86%-4%
Trucks and cars	14.3%-15.5%
Computers and computer equipment	20%-25%
Office furniture	10%-50%

The carrying amount of an item of property, plant and equipment is derecognized on disposal or when no future economic benefits are expected from its use or disposal. Gains or losses arising on the disposal or retirement of an asset are determined as the difference between the estimated net sales proceeds and the carrying amount of the asset, and is recognized when earned or incurred in the income statement.

3.8. Intangible Assets

Intangible assets acquired separately are initially recognized at cost. Cost represents the prices billed by suppliers together with all costs incurred in bringing new assets into use net of trade rebates and discounts.

Subsequently, intangible assets are carried at cost decreased by any allowance for accumulated amortization and impairment losses, if any.

Amortization of intangible assets is calculated by applying the straight-line method over the estimated useful life of an asset at the annual rate of 20%. Amortization commences when an intangible asset is placed in use. Net book value of intangible assets is reexamined at the end of each accounting period for assets that have not yet been placed in use.

3.9. Inventories

Inventories of material and spare parts are carried at the lower of cost or net realizable value.

Cost of inventories comprises the purchase price, import duties and other non-refundable taxes, and transport, handling and other costs directly attributable to the acquisition of inventories and bringing them to the location and condition necessary for them to be used. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase. The cost of inventories of materials and spare parts is assigned by using the weighted average method.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.9. Inventories (Continued)

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Provisions are made where appropriate in order to reduce the value of inventories to management's best estimate of net realizable value as well based on other documented decreases of inventories.

3.10. Impairment of Non-Monetary Assets

At each balance sheet date, the Company's management reviews the carrying amounts of the Company's assets. If there are any such indications, the Company formally assesses their recoverable value. If the recoverable amount of an asset is estimated to be less than its carrying value, the carrying amount of the asset is reduced to its recoverable amount. The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use. For the purpose of assessing value in use, estimated future cash flows are discounted to the present value by applying the discount rate before tax reflecting the present market estimate of time value of cash and risks specifically related to the asset in question. The Company uses the valuation technique which is the most adequate for determining the fair value net of costs to make the sale.

3.11. Provisions

A provision should be recognized when, and only when an entity has a present obligation (legal or constructive) as a result of a past event, when it is probable (i.e., more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation. The amount recognized as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date. If the effect of the time value of money is significant, provisions are discounted by applying the discount rate before taxation which reflects the risk specific for the liability in question.

3.12. Financial Assets

Financial assets are classified as at fair value through profit and loss, loans and receivables, placements held to maturity or financial assets held for sale. The Company classifies its financial assets upon initial recognition. Financial assets are recognized in the Company's balance sheet on the date upon which the Company becomes counterparty to the contractual provisions of a specific financial instrument. Financial assets are initially recognized at fair value as increased by the costs to make the transaction, except in the case of financial assets carried at fair value through profit and loss.

Financial assets of corporate entities include cash and cash equivalents and short-term deposits, financial instruments which are not quoted and accounts receivable and other receivables.

Equity Investments in Subsidiaries

Equity investments in subsidiaries and associates are stated at cost net of accumulated allowance for impairment, if any.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.12. Financial Assets (Continued)

Financial Instruments Available for Sale

Financial instruments available for sale comprise equity investments in other legal entities and banks. Subsequent to initial recognition, financial instruments available for sale are stated at fair value. For those instruments traded on the organized financial market, the fair value is determined based on the assets value quoted on an active market as of the balance sheet date. Instruments for which values quoted on an active market do not exist and whose fair value cannot be readily and reliably determined are stated at cost net of allowance for impairment, if any.

Interest-Bearing Loans and Borrowings

Loans and borrowings extended by the Company are measured at amortized value by applying the effective interest method. Income and expenses are recognized in the income statement as arising from impairment and derecognition in the same way as through amortization process.

Short-Term Accounts Receivable

Accounts receivable are recognized and recorded at their invoiced value, net of provisions for bad debts. Provisions are formed for receivables that are at least 60 days past their due date and the collectability of such receivables is assessed individually. Receivables are written off when determined to be irrecoverable in full.

Cash and Cash Equivalents

Cash and cash equivalents comprise cash held on the account held with banks, cash on hand, demand deposits and other highly liquid securities with up to three month maturities. For the purpose of preparing the cash flow statements, cash and cash equivalents encompass the abovementioned line items.

3.13. Impairment of Financial Assets

At each balance sheet date, the Company's management reviews the carrying amounts of the Company's financial assets. The value of a financial asset is impaired if there is objective evidence of impairment related to an event occurring after the asset was recognized which affects the estimated future cash flows arising from the financial asset. Objective evidence that a financial asset is impaired includes observable data with reference to significant financial difficulty of the issuer or obligor, a breach of contract, such as a default or delinquency in interest or principal payments, as well as other objective evidence.

If there is objective evidence that assets have been impaired, the amount of loss is calculated as the difference between the carrying value of assets and the present value of estimated future cash flows. The value of asset or assets is decreased using the allowance for impairment account and impairment loss is carried through profit and loss. Assets are written off when collection is no longer probable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.14. Financial Liability

Financial liabilities are initially recognized at fair value as increased, in case of loans and borrowings, by the costs to make transaction.

Financial liabilities of the Company include accounts payable and other liabilities from operations, loans and borrowings.

Interest Bearing Loans and Borrowings

All loans and borrowings are initially recognized at cost, being the fair value of amount received net of borrowings costs. Following the initial recognition, interest bearing loans and borrowings are measured at amortized value by applying the effective interest rate. Amortized value is calculated taking into account all costs of payments, as well as discounts and premiums applied in loan repayment. Gains and losses are recognized in the income statement upon derecognition or impairment of liabilities, as well as in the amortization process.

3.15. Derecognition of Financial Assets and Liabilities

Financial Assets

The Company derecognizes a financial asset (or a portion of financial assets or a group of financial assets) when, and only when:

- (a) the contractual rights to the cash flows from the financial asset expire;
- (b) the Company retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to one or more entities based on a transfer agreement; or
- (c) the Company transferred rights to the cash inflows from an asset and (a) transferred all risks and rewards arising from the asset or (b) has neither transferred not retained all risks and rewards in connection with the asset, but it transferred the control over the asset.

Financial Liabilities

The Company removes a financial liability from its balance sheet when, and only when, it is extinguished i.e., when the obligation specified in the contract is discharged or cancelled or expired. An exchange between an existing borrower and lender of debt instruments with substantially different terms shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount of a financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognized in profit or loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

4. SUMMARY OF SIGNIFICANT ACCOUNTING ESTIMATES

Independent Estimates

The basic assumptions relating to the future events and other sources of uncertainties in making estimates as of the statement of financial position date carrying risk that may give rise to materially significant adjustments to the present value of assets and liabilities in the following fiscal year are presented in the following passages:

Appraisal of Property, Plant and Equipment

The Company carries land, building and equipment for power transmission and power transmission system management at their revalued amounts with the changes in their fair values recognized within equity. The Company engaged an independent appraiser to determine the fair value as of January 1, 2008.

Employee Benefits

The present value of retirement benefits, jubilee awards and unused annual leaves is determined in an actuarial assessment. Actuarial assessment relies upon the assumptions in connection with a discount rate, envisaged salary growth, mortality rate and employee turnover. In determining an adequate discount rate, the Company relies on an interest rate equaling the rate applied to corporate bonds. The mortality rate is based on the publicly available mortality tables. The future salary growth is based on expected inflation rates.

5. SALES

	Year Ended December 31,	
	2009	2008
Income from electricity transmission and transmission system management	8,564,368	8,371,770
Income from reservations of transmission capacities on interconnections	1,789,393	2,351,788
Income from cross-border exchange based on ITC methodology	177,859	419,689
Other revenues from the sale of products and services	371,550	310,963
	<u>10,903,170</u>	<u>11,454,210</u>

6. OTHER OPERATING INCOME

	Year Ended December 31,	
	2009	2008
Income from grants	125,474	184,418
Income from insurance claims	103,624	38,086
Other operating income	9,010	10,074
	<u>238,108</u>	<u>232,578</u>

PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

7. COST OF MATERIALS

	Year Ended December 31,	
	2009	2008
	<hr/>	<hr/>
Cost of electricity purchased to cover transmission losses	2,897,112	2,986,371
Cost of material	191,946	350,405
Fuel and energy	128,726	128,179
Office material and other overhead material	52,264	61,567
Small tools and fixtures	23,970	42,511
Other staff costs	32,058	16,832
	<hr/>	<hr/>
	3,326,076	3,585,865
	<hr/> <hr/>	<hr/> <hr/>

8. STAFF COSTS

	Year Ended December 31,	
	2009	2008
	<hr/>	<hr/>
Gross salaries	1,524,687	1,458,515
Taxes and contributions charged to employer	305,059	269,490
Business trip expenses	103,829	84,861
Transportation expenses	40,700	31,723
Retirement benefits	398	998
Jubilee awards	633	11,597
Remunerations to the members of Management and Supervisory Boards	11,437	11,746
Other staff costs	41,039	38,057
	<hr/>	<hr/>
	2,027,782	1,906,987
	<hr/> <hr/>	<hr/> <hr/>

Remunerations to Management

In 2009, the Company paid remunerations to key management, which entails the members of Management Board, directors and other managers (2009: the total number is 30; 2008: 32) in the gross amount of RSD 48,358 thousand (2008: RSD 53,183 thousand).

	December 31,	December 31,
	2009	2008
	<hr/>	<hr/>
<i>Management</i>		
Salaries	36,921	41,437
	<hr/>	<hr/>
<i>Management Board</i>		
Remunerations to the members of the Management Board	11,437	11,746
	<hr/>	<hr/>
	48,358	53,183
	<hr/> <hr/>	<hr/> <hr/>

PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

9. DEPRECIATION, AMORTIZATION AND PROVISIONS

	Year Ended December 31,	
	2009	2008
Depreciation	2,900,737	2,935,903
Amortization	4,882	6,971
Provisions for litigations	112,617	46,555
Provisions for unused accumulated annual leaves (Note 31)	-	47,154
	<u>3,018,236</u>	<u>3,036,583</u>

10. OTHER OPERATING EXPENSES

	Year Ended December 31,	
	2009	2008
System services	1,748,223	1,496,273
Production services	459,999	194,360
Maintenance	222,412	176,278
Taxes and other duties payable	248,106	208,839
Insurance premiums	127,388	153,936
Electricity exchange expenses for the needs of system stability	156,456	204,070
Telecommunications	54,278	79,856
Public utilities and maintenance of business premises	13,245	12,036
Security	42,984	42,219
Professional services	18,136	19,255
Entertainment	28,757	28,341
Research	1,129	14,074
Membership fees	23,591	10,188
Rentals	13,544	10,882
Environment protection	9,796	9,470
Professional education	11,838	9,780
Bank charges	7,658	6,698
Other expenses	156,741	159,402
	<u>3,344,281</u>	<u>2,835,957</u>

11. FINANCE INCOME

	Year Ended December 31,	
	2009	2008
Interest received	556,561	431,175
Foreign exchange gains	254,549	380,712
Foreign currency clause gains	12,432	20,015
Other finance income	126	169
	<u>823,668</u>	<u>832,071</u>

PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

11. FINANCE INCOME (Continued)

The Company stated interest income in the amount of RSD 556,561 thousand as of December 31, 2009 which mostly relates to interest charged on assets held on current accounts totaling RSD 254,146 thousand and interest charged to rescheduled receivables from Electric Power Industry of Serbia in the amount of RSD 198,435 thousand.

12. FINANCE EXPENSES

	Year Ended December 31,	
	2009	2008
	<hr/>	<hr/>
Foreign exchange losses	438,384	344,705
Interest expenses	399,924	490,915
Foreign currency clause losses	96,777	1,190,982
Other finance expenses	1,867	146
	<hr/>	<hr/>
	936,952	2,026,748
	<hr/>	<hr/>

Interest expenses stated in the amount of RSD 399,924 thousand arise from interest accrued on long-term borrowings.

13. OTHER INCOME

	Year Ended December 31,	
	2009	2008
	<hr/>	<hr/>
Reversal of allowance for impairment	2,981	577,726
Penalties and fines from commercial contracts	115,083	64,194
Collected guarantees for failure to perform	80,335	-
Reversal of impairment in property, plant and equipment	-	28,759
Reversal of long-term provisions	14,912	20,729
Write-off of liabilities	4,661	20,034
Gains on the sale of material	20,136	8,297
Surpluses	7,715	7,958
Other income	10,415	6,795
	<hr/>	<hr/>
	256,238	734,492
	<hr/>	<hr/>

Penalties and fines from commercial contracts stated in the amount of RSD 115,083 thousand mostly, in the amount of RSD 78,896 thousand relate to the collections of performance bonds from the entity SAG GmbH, Germany.

PUBLIC ENTERPRISE “ELEKTROMREŽA SRBIJE,” BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

14. OTHER EXPENSES

	Year Ended December 31,	
	2009	2008
Impairment of property, plant and equipment	19	291,240
Allowance for impairment of accounts receivable	4,944	7,401
Losses on disposal and sale of equipment	4,054	7,593
Shortages	909	226
Other expenses	14,128	26,974
	24,054	333,434

15. INCOME TAXES

a) Components of Income Taxes

	Year Ended December 31,	
	2009	2008
Current income taxes	(65,039)	(60,779)
Deferred income taxes	72,248	90,957
	7,209	30,178

b) Numerical reconciliation between the tax expense and the product of accounting results multiplied by the applicable tax rate

	December 31, 2009	December 31, 2008
Profit before taxation	454,810	185,679
Income tax at the statutory tax rate of 10%	45,481	18,568
Tax effects of expenses not recognized in the tax balance	11,224	5,501
Tax credits for capital expenditures realized in the current year	(64,252)	(54,247)
Other	338	-
	7,209	30,178

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

15. INCOME TAXES (Continued)

c) Deferred tax assets / liabilities

	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Present value of property, plant and equipment the value of which is systematically written off on a time basis as included in the financial statements	42,928,688	45,043,771
Present value of property, plant and equipment recognized for tax purpose	(30,469,563)	(31,870,529)
Deductibles based on which deferred tax assets are recognized	<u>1,121,685</u>	<u>1,130,048</u>
Taxable temporary difference	<u>13,580,810</u>	<u>14,303,290</u>
Deferred tax (10%)	1,245,913	1,317,324
Deferred tax liabilities	<u>1,358,081</u>	<u>1,430,329</u>

At December 31, 2009, the Company had tax credits from capital expenditures carried forward in the amount of RSD 198,093 thousand. The Company did not recognize deferred tax assets based on intangible assets as it was uncertain that it will be able to use them in the ensuing periods.

PUBLIC ENTERPRISE “ELEKTROMREŽA SRBIJE,” BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

16. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

	Land	Buildings	Plant, Equipment and Other Assets	Construction in Progress	Total	Intangible Assets
Cost						
Balance, January 1, 2008, before adjustments	111,888	49,819,401	63,734,797	6,182,729	119,848,815	59,754
Opening	-	-	-	4,537	4,537	-
Balance, January 1, 2008, after adjustments	111,888	49,819,401	63,734,797	6,187,266	119,853,352	59,754
Appraisal effects	1,121,680	10,073,818	13,021,645	(35,401)	24,181,742	-
Additions	-	639	216,540	2,906,658	3,123,837	4,400
Activation of construction in progress	-	343,549	419,639	(763,188)	-	-
Transfers	-	(678)	678	(45,878)	(45,878)	-
Sale	-	(1,584)	(7,061)	(8,293)	(16,938)	-
Write-offs (disposals)	-	-	(68,555)	-	(68,555)	(2,160)
Shortages	-	-	(96)	(135)	(231)	-
Other changes	-	924	(1,082)	(122,406)	(122,564)	-
Balance, December 31, 2008	1,233,568	60,236,069	77,316,505	8,118,623	146,904,765	61,994
Balance, January 1, 2009	1,233,568	60,236,069	77,316,505	8,118,623	146,904,765	61,994
Additions	-	-	59,801	2,832,417	2,892,218	7,250
Activation of construction in progress	11,060	135,490	672,010	(818,560)	-	-
Transfers	-	-	(305,312)	14,120	(291,192)	-
Self-constructed assets	-	-	-	60,755	60,755	-
Grants	-	73,252	66,288	-	139,540	-
Sale	-	(288)	(21,279)	-	(21,567)	-
Write-offs (disposals)	-	-	(35,265)	-	(35,265)	(2,334)
Shortages	-	-	(86)	(844)	(930)	-
Balance, December 31, 2009	1,244,628	60,444,523	77,752,662	10,206,511	149,648,324	66,910
Accumulated Depreciation/Amortization						
Balance, January 1, 2008	8,371	34,650,729	44,071,884	267,933	78,998,917	16,089
Appraisal effects	-	3,215,851	7,628,431	72,801	10,917,083	-
Charge for the year	-	1,041,968	1,893,935	-	2,935,903	6,971
Transfers	-	(619)	619	(37,413)	(37,413)	-
Sale	-	(1,174)	(6,960)	-	(8,134)	-
Write-offs (disposals)	-	-	(65,617)	-	(65,617)	(1,957)
Shortages	-	-	(96)	-	(96)	-
Other changes	-	943	(1,082)	(960)	(1,099)	-
Balance, December 31, 2008	8,371	38,907,698	53,521,114	302,361	92,739,544	21,103
Balance, January 1, 2009	8,371	38,907,698	53,521,114	302,361	92,739,544	21,103
Charge for the year	-	1,044,584	1,856,153	-	2,900,737	4,882
Transfers	-	-	(209,095)	-	(209,095)	-
Sale	-	(260)	(20,512)	-	(20,772)	-
Write-offs (disposals)	-	-	(33,294)	-	(33,294)	(1,607)
Shortages	-	-	(27)	-	(27)	-
Transfers to third parties	-	56,793	63,579	-	120,372	-
Other changes	-	-	-	(1,502)	(1,502)	-
Balance, December 31, 2009	8,371	40,008,815	55,177,918	300,859	95,495,963	24,378
Net book value						
December 31, 2009	1,236,257	20,435,708	22,574,744	9,905,652	54,152,361	42,532
January 1, 2009	1,225,197	21,328,371	23,795,391	7,816,262	54,165,221	40,891

In accordance with the Law on Public Enterprises of the Republic of Serbia, the Company has the right of use over the state-owned assets. In accordance with the RS Government Decision on Establishment, the Company cannot sell or acquire buildings or other immovables, plant and equipment to be used in electricity transmission and transmission system operation, without the previously obtained consent from the Republic of Serbia Government.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***16. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS (Continued)**

The right to use the assets assumed from the Public Enterprise "Elektroistok" and other public entities within JP EPS, has not been transferred to the Company and is still vested in these public enterprises.

The Company stated additions on the constructions in progress in the amount of RSD 2,832,417 thousand where the amount of RSD 1,078,547 thousand refers to the acquisition of transformers for substations in Leskovac, Jagodina 4, Smederevo 3 and Belgrade 8.

Advances for property, plant and equipment under construction as of December 31, 2009 totaled RSD 151,899 thousand which are associated with the acquisition of fixed assets used in the reconstruction of substations.

17. EQUITY INVESTMENTS

	<u>% Interest</u>	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Equity investments in related parties:			
Electricity Coordinating Center	25%	5,246	5,246
Equity investments in other legal entities			
Elektroprivreda Srbije – Kosovo		236,027	236,027
Recreators d.o.o., Beograd		3,200	3,200
Privredna banka a.d., Beograd		163	163
Stanogradnja		98	98
		<u>239,488</u>	<u>239,488</u>
<i>Less: Allowance for impairment</i>			
- equity investments in related parties		(342)	(342)
- equity investments in other legal entities		<u>(236,125)</u>	<u>(236,125)</u>
		<u>8,267</u>	<u>8,267</u>

The entity - Electricity Coordinating Center, a Limited Liability Company from Belgrade (EKC) is involved in consulting services in the field of regulating and calculating power realized. This company was established in 1993 and operated as a coordinator of the regulatory and computation block of the Public Enterprise - Electric Power Industry of Serbia (Elektroprivreda Srbije – JP EPS), the Power Utility of the Republic of Macedonia (Elektroprivreda Makedonije), the Power Utility of the Republic of Montenegro and the Power Utility of the Republic of Srpska (Elektroprivreda Republike Srpske). The aforementioned Public Enterprises are the founders of the Electricity Coordinating Center with 25% equity investments. From December 1, 2007, the function of EKS has been performed by the Public Utility Elektromreža Srbije, whereas the Electricity Coordinating Center assumed the consulting services in the field of regulations and calculation of energy.

Equity investment in the Public Utility Elektromreža Srbije amounting to RSD 236,027 thousand relates to the founding investments of JP EPS in the Kosovo 2100MW Project and TSU Priština Project. Pursuant to the RS Government Decision, based on the split-off balance as of June 30, 2005 these investments were transferred to the Public Utility Elektromreža Srbije in full. Due to the uncertainty over the availability of future economic benefits arising on these placements, they were provided for in full.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

18. LONG-TERM FINANCIAL PLACEMENTS

	December 31, 2009	December 31, 2008
Receivables from JP EPS	2,370,342	2,704,051
Receivables for apartments sold and residential loans	79,680	78,478
Rescheduled accounts receivable	11,062	-
Other long-term financial placements	-	359
	<u>2,461,084</u>	<u>2,782,888</u>
Current portions:		
- receivables from EPS	(1,260,637)	(889,865)
- receivables for apartments sold	(5,114)	(5,441)
- receivables from employees	(51)	(152)
	<u>1,195,282</u>	<u>1,887,430</u>

Rescheduled receivables from JP EPS stated as of December 31, 2009 in the amount of RSD 2,370,342 thousand (including current portions of RSD 1,260,637 thousand) comprise rescheduled receivables arising from the Agreement regulating the collection of outstanding receivables from the use and access to the power transmission system signed with the Public Company Jugoistok, Niš, as well as receivables associated with the distribution of income jointly earned with JP EPS as stipulated in the split-off balance. The structure of the aforementioned receivables is presented in the table below:

	December 31, 2009	December 31, 2008
Receivables based on the split-off balance between JP EMS and JP EPS	701,892	1,010,725
Receivables from debt outstanding from		
- 2005	171,975	343,950
- 2007	755,090	1,349,376
- 2009	741,385	-
	<u>2,370,342</u>	<u>2,704,051</u>

19. INVENTORIES

	December 31, 2009	December 31, 2008
Material	322,870	300,312
Spare parts	81,617	81,813
Tools and fixtures	194,746	183,580
Goods	1,913	1,157
Advances paid	66,453	19,384
	<u>667,599</u>	<u>586,246</u>
Less: Allowance for impairment		
- inventories	(214,694)	(200,109)
- advances paid	(603)	(731)
	<u>452,302</u>	<u>385,406</u>

PUBLIC ENTERPRISE “ELEKTROMREŽA SRBIJE,” BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

20. ACCOUNTS RECEIVABLE

	December 31, 2009	December 31, 2008
Accounts receivable:		
- domestic	1,184,552	1,525,132
- foreign	2,441	3,892
Interest receivables	24,416	128,495
Receivables from employees	16,079	27,982
Receivables for prepaid taxes and contributions	1,599	6,710
Other receivables	22,622	287,977
	<u>1,251,709</u>	<u>1,980,188</u>
Allowance for impairment:		
- accounts receivable	(1,372)	-
- interest receivables	(19,600)	(18,353)
- other receivables	(859)	(953)
	<u>(21,831)</u>	<u>(19,306)</u>
	<u>1,229,878</u>	<u>1,960,882</u>

Domestic accounts receivable stated in the amount of RSD 1,184,552 thousand as of December 31, 2009 mostly, in the amount of RSD 1,134,339 thousand relate to receivables from the entities operating within the Public Enterprise Electric Power Industry of Serbia (JP EPS).

21. SHORT-TERM FINANCIAL PLACEMENTS

	December 31, 2009	December 31, 2008
Current portion		
- Rescheduled receivables from JP EPS	1,260,637	889,865
- Long-term receivable for apartments sold and housing loans	3,790	3,442
Short-term deposits with banks (in RSD)	1,400,000	600,000
Short-term deposits with banks (in foreign currency)	801,542	-
Portion of rescheduled accounts receivable (currency clause)	24,857	2,037
	<u>3,490,826</u>	<u>1,495,344</u>

Term deposits placed with banks are associated with deposits placed for the period shorter than a year at an interest rate fluctuating between 5.25% and 15.75% annually.

22. CASH AND CASH EQUIVALENTS

	December 31, 2009	December 31, 2008
Foreign currency account	1,593,566	1,550,490
Current account	835,213	483,329
Cash on hand	3,498	2,963
Letters of credit and special purpose cash funds	20,191	12,463
Other cash and cash equivalents	9,379	3,002
	<u>2,461,847</u>	<u>2,052,247</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***23. VALUE ADDED TAXES AND PREPAYMENTS**

	December 31, 2009	December 31, 2008
Value added tax	77,656	-
Accrued uninvoiced expenses	72,556	466,184
Deferred value added taxes	112,052	195,345
Prepaid value added taxes	3,756	4,351
Prepaid expenses	3,514	14,013
Net effects of accrued currency clause effects	603,714	-
Other prepayments	69,876	12,125
	<u>943,124</u>	<u>692,018</u>

Net effects of accrued currency clause effects as of December 31, 2009 totaling RSD 603,714 thousand represent the currency clause effects arising in connection with long-term borrowings which are recorded in the books of account pursuant to the Rules on the Amendments and Supplements to the Rules on the Chart of Account for Companies, Cooperatives and Other Legal Entities ("RS Official Gazette, number 4/10).

24. CAPITAL**State-Owned Capital**

The Company's core capital is state-owned and is inscribed upon the establishment of the Company as a difference between the book value of assets and liabilities assumed from the Public Enterprise "Elektroistok" and JP EPS. State-owned capital is registered with the Serbian Business Registers Agency on July 1, 2005 in the amount of EUR 516,602,312. The registration was performed pursuant to the appraisal of state-owned capital contributed in kind. The appraisal was performed by the local certified appraiser and comprises the assets of the Public Enterprise "Elektroistok" and other public entities within JP EPS as of December 31, 2004. As a consequence of the aforementioned, the Company's core capital stated at December 31, 2009 in the amount of RSD 30,506,506 thousand is not reconciled with the amount inscribed with the Serbian Business Registers Agency by an amount of RSD 10,346,515 thousand.

Other Capital

Other capital presented in the Company's balance sheet as of December 31, 2009 relates to the Company's own non-business resources transferred upon the first time application of the newly-adopted accounting regulations of the Republic of Serbia at January 1, 2004.

Distribution of Profit

On July 21, 2009, the Company's Managing Board enacted a Decision with reference to the distribution of profit presented in the financial statements for the year ended December 31, 2008. Pursuant to the July 22, 2009 Decision, RSD 78,032 thousand was paid to the RS Government as the Company's founder, whereas the balance of net profit earned in 2008 remained undistributed.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

25. LONG-TERM PROVISIONS

The movements on long-term provisions in the years ended December 31, 2009 and 2008 were as follows:

	Provision for Employee Benefits	Provision for Litigation	Total
Balance, January 1, 2008	95,081	64,701	159,782
Charge for the year	17,556	28,999	46,555
Reversal of provisions	-	(20,729)	(20,729)
Release of provisions	-	(1,480)	(1,480)
Balance, December 31, 2008	<u>112,637</u>	<u>71,491</u>	<u>184,128</u>
Charge for the year	-	112,617	112,617
Reversal of provisions	(4,388)	(10,523)	(14,911)
Release of provisions	(6,339)	(1,918)	(8,257)
Balance, December 31, 2009	<u><u>101,910</u></u>	<u><u>171,667</u></u>	<u><u>273,577</u></u>

Provision for Employee Benefits

The movements on the provisions for employee benefits as of December 31, 2009 and 2008 are as follows:

	December 31, 2009	December 31, 2008
Jubilee awards	54,064	59,333
Retirement benefits	<u>47,846</u>	<u>53,304</u>
	<u><u>101,910</u></u>	<u><u>112,637</u></u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

26. LONG-TERM BORROWINGS

	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Foreign long-term loans		
EIB I	2,423,312	1,816,320
EBRD I	2,118,983	1,926,983
IDA	152,612	132,153
	<u>4,694,907</u>	<u>3,875,456</u>
Domestic long-term loans (preagreed with the Deposit Insurance Agency)		
IBRD 2338-5	1,309,363	1,264,930
IBRD 2338-7	374,387	361,682
IBRD 14695	155,313	150,042
EIB 692 YU	218,555	201,944
Kapital Hilfe (Investbanka)	4,626,122	4,302,475
Kapital Hilfe (Vojvodanska banka)	1,075,816	1,000,652
	<u>7,759,556</u>	<u>7,281,725</u>
<i>Current portions:</i>		
EBRD I	(325,997)	(256,931)
IBRD 2338-5	(59,612)	(55,082)
IBRD 2338-7	(17,045)	(15,750)
IBRD 14695	(7,071)	(6,534)
Kapital Hilfe (Investbanka)	(30,249)	(27,950)
Kapital Hilfe (Vojvodanska banka)	(7,140)	(6,598)
	<u>(447,114)</u>	<u>(368,845)</u>
	<u>12,007,349</u>	<u>10,788,336</u>

Long-Term Foreign Borrowings

Based on the Agreement on funding the project of operating the electric power system of Serbia and Montenegro, entered by and between Serbia and Montenegro, on one side, and the European Investment Bank, on the other, on August 31, 2002, JP EPS was approved a framework loan of EUR 59 million. On December 21, 2006, an Agreement between JP ERS and the Company was closed, based on which all rights and liabilities related to this loan are transferred to the Public Enterprise "Elektromreža Srbije." The loan is to be drawn in tranches at the Company's requests, where the total loan funds must be disbursed in no more than 9 tranches of no less than EUR 3 million. The limit for the use of the framework loan approved is set to be June 30, 2008. The loan is to be repaid in semi-annual installments maturing on May 10 and November 10 in the period between November 11, 2011 and January 20, 2027 at an annual interest rate of 2.3%. Until December 31, 2009, an amount of EUR 25,272,000 was drawn. The balance of the agreed borrowing was cancelled.

Loan from the European Bank for Reconstruction and Development has been approved in the amount of EUR 60,400,000 and until December 31, 2009, the portion amounting to EUR 31,805,000 has been drawn. The loan has been initially agreed between the European Bank for Reconstruction and Development and Public Enterprise Electric Power Industry of Serbia and in 2008, it was transferred to the Company. In accordance to the Loan Agreement, the Company is under obligation to maintain the following ratios:

- Debt services cover ratio should at all times be above 1.3
- Current ratio should at all times be above 1.2
- Debt to equity ratio should at all times be below 2.3
- Ratio between amounts collected and amounts invoiced should at all times be above 0.9.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***26. LONG-TERM BORROWINGS (Continued)**

On September 8, 2005, Serbia and Montenegro and International Association for Development executed the Agreement on Development Loan no. 4090 YF for the purpose of realization of the project on improving the access to electricity market for consumers and suppliers. The funds planned for the realization of the part of the project that is to be carried out by the Company and regarding the construction of inter-connected transmission lines and related activities, amounts to SDR 1,660,000 (SDR – Special Drawing Rights). Until December 31, 2009, the amount of SDR 1,476,466 has been drawn.

Long-Term Loan Preagreed with the Deposit Insurance Agency

The loan from the International Bank for Reconstruction and Development was initially approved to the Electric Power Industry of Serbia (JP EPS). In accordance with the Loan Agreement between the Socialist Republic of Yugoslavia and the International Bank for Reconstruction and Development as of December 17, 2001, the total liabilities of the Company arising from the loan principal, interest and other expenses accrued by the end of 2001 represent the principal of the new loan, repaid to the RS Government. On May 17, 2006, JP EPS entered into an Agreement on reschedule of liabilities with the Deposit Insurance Agency, which regulates the liabilities to the Republic of Serbia arising from the loan reschedule. In accordance with the aforementioned Agreement a portion of liability of 81% of debt was transferred to the Public Utility Elektromreža Srbije. The aforementioned debt is rescheduled over the period until December 15, 2031. The repayment is to be executed in semi-annual annuities, the first one being due on June 15, 2006 at a variable interest rate.

The loan from the European Investment Bank was initially approved to the Public Enterprise "Elektroistok." In conformity with the Law on the Debt of the Federal Republic of Yugoslavia towards the European Union, the loan was rescheduled in 2001 to the amount of EUR 2,065,511. On April 12, 2006, the Public Enterprise "Elektromreža Srbije" as the legal successor of the Public Enterprise Elektroistok, closed an Agreement governing the liabilities towards the Republic of Serbia. Based on the aforementioned Agreement, the loan principal was increased by interest accrued in the amount of EUR 222,742 which was discharged by the Republic of Serbia by October 17, 2005. The related grace period lasts 10 years, and the loan is payable in 5 equal annual installments starting from October 17, 2012. The interest rate is variable and is calculated semi-annually.

The loan from Kapital Hilfe Bank was approved to the Public Enterprise "Elektroistok" by the Federal Republic of Germany in 1974. The loan was realized through Invest banka a.d., Beograd and Vojvodanska banka a.d., Novi Sad. The grace period lasted from 1992 to December 31, 2005.

a) Invest banka a.d., Beograd

On April 12, 2006, the Company entered into an Agreement on debt reschedule with the Deposit Insurance Agency. In accordance with the aforementioned Agreement, the Company's liabilities related to this loan as of December 31, 2005 amounted to EUR 49,033,292 (EUR 46,825,100 of the principal, EUR 2,208,192 of related interest). The loan is to be repaid in semi-annual annuities commencing from September 22, 2014, accruing interest at the rate of 2.3% per annum. The loan falls due on March 22, 2041.

b) Vojvodanska banka a.d., Novi Sad

On December 29, 2006, the Company entered into the Agreement on Reschedule of Liabilities towards the Republic of Serbia with the Deposit Insurance Agency. According to the aforementioned Agreement, the Company's liabilities arising from this loan as of September 22, 2006 amounted to EUR 11,405,597 (EUR 10,884,349 of the principal, EUR 521,247 of related interest). The loan is to be repaid in semi-annual annuities starting from September 22, 2018, at an interest rate of 2.3% annually. The loan matures on March 22, 2041.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

27. OTHER LONG-TERM LIABILITIES

	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Liabilities to JP EPS based on long-term loans	309,596	286,066
Liabilities to the RS Government based on rescheduled public duties	-	6,820
Other long-term liabilities	8,096	18,832
	<u>317,692</u>	<u>311,718</u>
<i>Current portion:</i>		
- liabilities to JP EPS based on long-term loans	(53,869)	(38,504)
- liabilities to the RS Government	-	(722)
- other long-term liabilities	-	(4,485)
	<u>263,823</u>	<u>268,007</u>

28. SHORT-TERM FINANCIAL LIABILITIES

	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Current portions:		
- Long-term foreign loans	325,997	256,931
- Domestic long-term loans (preagreed with the Deposit Insurance Agency)	121,117	111,914
- liabilities to JP EPS based on long-term loans	53,869	38,504
- liabilities to the RS Government	-	722
- other long-term liabilities	-	4,485
- Import-Export Bank of China	893,891	842,605
Other short-term financial liabilities	3,003	476
	<u>1,397,877</u>	<u>1,255,637</u>

Liabilities arising from the loan obtained from the Export-Import Bank of China stated as of December 31, 2009 in the amount of RSD 893,891 thousand (USD 13,395,945) entirely relate to a matured loan outstanding. In fact, the loan was approved on December 23, 1999 with a grace period of 5 years with the first installment due on January 21, 2004. The Company failed to repay the loan in accordance with the annuity schedule, so the loan fully matured at June 21, 2008. The negotiations on the reschedule of these liabilities, increased by interest accrued thereto, in the amount of RSD 331,194 thousand (Note 30) are currently underway. The Company did not calculate the penalty interest that may be assessed based on matured but unsettled annuities.

PUBLIC ENTERPRISE "ELEKTROMREŽA SRBIJE," BELGRADE

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

29. ACCOUNTS PAYABLE

	December 31, 2009	December 31, 2008
Advances received	106,197	147,074
Accounts payable:		
- domestic	677,850	770,621
- foreign	312,020	893,939
Other accounts payable	609	16,309
	<u>1,096,676</u>	<u>1,827,943</u>

30. OTHER SHORT-TERM LIABILITIES

	December 31, 2009	December 31, 2008
Interest payable	445,061	406,055
Liabilities for salaries and taxes and contribution on salaries	77,832	104,261
Other liabilities	6,135	6,366
	<u>529,028</u>	<u>516,682</u>

31. VALUE ADDED TAX AND OTHER DUTIES PAYABLE, AND ACCRUALS

	December 31, 2009	December 31, 2008
Deferred income from grants	1,310,212	1,404,899
Other deferred income	106	79,045
Value added tax and VAT accrual	160,113	209,291
Accrued interest	96,847	110,634
Accrued annual leave allowances	46,608	47,154
Other accruals	11,603	17,829
Other taxes	10,525	3,693
Other liabilities	808	251
	<u>1,636,822</u>	<u>1,872,796</u>

Movements on the account of deferred income from grants received for the years ended December 31, 2009 and December 31, 2008 were as follows:

	December 31, 2009	December 31, 2008
Balance, January 1	1,404,899	1,552,187
New grants during the year	30,787	37,130
Release to income – Note 5	(125,474)	(184,418)
Balance, December 31	<u>1,310,212</u>	<u>1,404,899</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***32. OFF-BALANCE SHEET ITEMS**

	December 31, 2009	December 31, 2008
Issued bills of exchange	8,149,103	7,525,677
Estimated war damage	6,937,398	6,410,137
Received bills of exchange and guarantees	680,286	338,469
Written off equity investments of banks in bankruptcy	48,974	48,974
Leased equipment	36,952	36,952
Other off-balance sheet items	15,222	10,558
	<u>15,867,935</u>	<u>14,370,767</u>

Bills of exchange issued as of December 31, 2009 in the amount of RSD 8,149,103 thousand relate to own bills of exchange issued to the Deposit Insurance Agency as collateral for the regular repayment of borrowings (Note 26).

Estimated war damage as of December 31, 2009 and 2008 are fully associated with the damage caused by the bombing of electric supply structures by NATO estimated at RSD 6,937,398 thousand.

33. CONTINGENT LIABILITIES AND COMMITMENTS**Litigation**

As disclosed in Note 25, as of December 31, 2009, the Company made provisions for legal proceedings in the amount of RSD 171,667 thousand. The final outcome of these legal proceedings is uncertain. The Company's management assesses that the litigations for which no provisions have been formed will not have adverse effects on the Company.

Contingent Liabilities

In 2009, an Agreement was signed for a new loan with the European Investment Bank (EIB II) in the amount of EUR 24,500. The amount borrowed is to be repaid over the period of 20 years with a 5-year grace period at an interest rate indexed to 6-month EURIBOR. The borrowing will be used to improve electricity network, i.e. for the construction of six substations and accompanying overhead lines.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT**Equity Risk Management**

There is no formal frame delineating the Company's risk management. The Company's management considers equity risk and tries to relieve the risk effects, under the assumption that the Company will be able to continue its operations as a going concern, at the same time maximizing profits earned and optimizing debt to equity ratio. The Company's equity includes borrowings explained in Note 26, other long-term liabilities, cash and cash equivalents and capital, which includes state-owned capital, other capital, reserves and retained earnings.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)****Equity Risk Management (Continued)**

Persons in control of finances on the Company level review the equity structure on annual basis. As a part of the review at issue, the Company's management considers the price of capital and risk originating in the type of capital.

The debt to equity ratios of the Company as of the year end was as follows:

	December 31, 2009	December 31, 2008
Indebtedness a)	13,669,049	12,311,980
Cash and cash equivalents	2,461,847	2,052,247
Net indebtedness	11,207,202	10,259,733
Equity b)	45,556,071	45,182,811
Debt to equity ratio	0.25	0.23

a) Debt is related to long-term loans, other long-term liabilities and short-term financial liabilities.

b) Equity includes state-owned and other capital, revaluation reserves and retained earnings.

Significant Accounting Policies regarding Financial Instruments

The details of significant accounting policies, as well as basis for measurement and recognition of income and expenses for each category of financial assets and liabilities, are set out in Note 3 to the accompanying consolidated financial statements.

Categories of Financial Instruments

	December 31, 2009	December 31, 2008
Financial assets		
Long-term financial placements	1,203,549	1,895,697
Accounts receivable	1,212,200	1,925,991
Short-term financial placements	3,490,826	1,495,344
Cash and cash equivalents	2,461,847	2,052,247
	<u>8,368,422</u>	<u>7,369,279</u>
Financial liabilities		
Long-term liabilities	12,271,172	11,056,343
Current portion of long-term liabilities	1,397,877	1,255,637
Accounts payable	990,479	1,680,825
Other liabilities	559,646	540,884
	<u>15,219,174</u>	<u>14,533,689</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)****Categories of Financial Instruments (Continued)**

Basic financial instruments held by the Company comprise cash and cash equivalents, receivables, financial placements arising directly from the Company's business operations, as well as long-term borrowings, accounts payable and other liabilities primarily used to finance the Company's current operations. In the regular course of business, the Company is exposed to the risk enumerated and delineated in the following passages.

Financial Risk Management

Financial risks include market risk (foreign currency risk and interest rate risk), credit risk and liquidity risk. These risks are considered on time basis and are diminished by decreasing relevant exposures. The Company does not make use of any financial instruments so as to avoid the adverse effect of these risks on the Company's business operations, due to the fact that such instruments are not commonly used on the Republic of Serbia market, nor is there an organized market for such instruments in the Republic of Serbia.

Market Risk

In its business operations, the Company is exposed to financial risks inherent in fluctuations of foreign currencies and interest rates.

Market risk exposure is measured by means of sensitivity analysis. There have been no changes in the manner in which the Company alleviates and measures the exposure.

Foreign Currency Risk

The Company is exposed to foreign currency risks inherent in cash and cash equivalents, accounts receivable, long-term borrowings and accounts payable denominated in foreign currency. It does not make use of any special hedging instruments given that such instruments are uncommon in the Republic of Serbia.

The stability of economic environment in which the Company operates is greatly dependent upon the economic measures taken by the Republic of Serbia's Government including the establishment of an adequate legal and legislative framework.

The carrying values of the Company's monetary assets and liabilities denominated in foreign currency as of the balance sheet date were as follows:

	Assets		Liabilities	
	December 31, 2009	December 31, 2008	December 31, 2009	December 31, 2008
EUR	2,475,762	1,791,934	13,283,005	12,535,929
USD	19,664	19,012	1,225,086	1,225,086
	<u>2,495,426</u>	<u>1,810,946</u>	<u>14,508,091</u>	<u>13,761,015</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Market Risk (Continued)

Foreign Currency Risk (Continued)

The Company is sensitive to the movements in the EUR and American Dollar (USD) exchange rates. The following table gives details on the Company's sensitivity analysis to the increase and decrease of 10% in the dinar to foreign currency exchange rate. These sensitivity rates were used to report on the foreign currency risk and represent the management's best estimate of reasonably expected fluctuations in exchange rates. The sensitivity analysis includes only the outstanding foreign currency assets and liabilities denominated in foreign currency and it adjusts their translation at the period end for the fluctuation of 10% in foreign exchange rates. The positive number from the table points to the increase in the result of the current period, being the case when RSD value grows stronger as opposed to the currency at issue. In case RSD decreases 10% as compared to the foreign currency at issue, the impact on the profit for the current period would be the exact opposite of the one calculated in the previous case.

	December 31, 2009				December 31, 2008			
	EUR influence		USD influence		EUR influence		USD influence	
	+10%	-10%	+10%	-10%	+10%	-10%	+10%	-10%
Profit/Loss	(1,080,724)	1,080,724	(120,542)	120,542	(1,074,399)	1,074,399	(113,578)	113,578

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Market Risk (Continued)

Interest Rate Risk

The Company is exposed to interest rate risk inherent in assets and liabilities with floating interest rate. This risk depends upon the financial market since the Company does not have any instruments that could alleviate its influence.

The carrying values of financial assets and liabilities at the end of the period under review are presented in the following table:

	December 31, 2009	December 31, 2008
Financial assets		
<i>Non-interest bearing</i>		
Long-term financial placements	8,267	8,267
Accounts receivable	1,212,200	1,925,991
Cash and cash receivables	2,461,847	2,052,247
	<hr/>	<hr/>
<i>Fixed interest rates</i>		
Long-term financial placements	1,195,282	1,887,430
Short-term financial placements and loans	3,490,826	1,495,344
	<hr/>	<hr/>
	8,368,422	7,369,279
	<hr/>	<hr/>
Financial liabilities		
<i>Non-interest bearing</i>		
Accounts payable	990,479	1,680,825
Other liabilities	17,738	20,674
	<hr/>	<hr/>
<i>Fixed interest rates</i>		
Long-term liabilities	10,033,459	8,887,104
Current portion of long-term liabilities	1,257,280	1,134,084
Other liabilities	371,267	355,615
	<hr/>	<hr/>
<i>Variable interest rates</i>		
Long-term liabilities	2,237,713	2,169,239
Current portion of long-term liabilities	140,597	121,553
Other liabilities	170,641	164,595
	<hr/>	<hr/>
	15,219,174	14,533,689
	<hr/>	<hr/>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

*All amounts are expressed in thousands of RSD, unless otherwise stated.***34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)****Market Risk (Continued)***Interest Rate Risk (Continued)*

The sensitivity analysis presented in the following text has been established based on the Company's exposure to interest rate risk inherent in non-derivative instruments as of the balance sheet date. For the liabilities with variable interest rate, the analysis has been prepared under the assumption that the outstanding balance of assets and liabilities as of the balance sheet date remained constant throughout the year. The increase or decrease in interest rates of 1 percentage point represents the fluctuation reasonably anticipated by the management. If the interest rates were 1 percentage point higher/lower and other variables remained unchanged, the Company would incur a loss/realized profit in the year ended December 31, 2009 in the amount of RSD 25,379 thousand (December 31, 2008: RSD 24,369 thousand). Such situation is ascribed to the Company's exposure arising from the variable interest rates applied to long-term borrowings and other long-term liabilities.

Credit Risk*Managing Accounts Receivable*

Credit risk relates to the exposure inherent in the possibility that the contractual party fails to act upon its contractual commitments and cause the Company to suffer a financial loss. The Company's exposure to this risk is limited to the amount of accounts receivable as of the balance sheet date.

The most significant customers are presented in the following table:

	December 31, 2009	December 31, 2008
JP Elektrovojvodina, Novi Sad	271,233	271,686
JP Elektrosrbija, Kraljevo	262,458	242,777
Elektrodistribucija Beograd	248,088	273,568
Company for distribution of electricity Centar, Kragujevac	201,539	190,481
Company for distribution of electricity Jugoistok, Niš	150,868	426,301
Other	24,367	75,579
	<u>1,158,553</u>	<u>1,480,392</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Credit Risk (Continued)

Managing Accounts Receivable (Continued)

The structure of accounts receivable as of December 31, 2009 is presented in the following table:

	<u>Gross Exposure</u>	<u>Allowance for Impairment</u>	<u>Net Exposure</u>
Accounts receivable not matured	1,072,461	-	1,072,461
Accounts receivable matured and provided for	21,831	(21,831)	-
Accounts receivable matured, but not provided for	<u>139,739</u>	<u>-</u>	<u>139,739</u>
	<u>1,234,031</u>	<u>(21,831)</u>	<u>1,212,200</u>

The structure of accounts receivable as of December 31, 2008 is presented in the following table:

	<u>Gross Exposure</u>	<u>Allowance for Impairment</u>	<u>Net Exposure</u>
Accounts receivable not matured	1,772,092	-	1,772,092
Accounts receivable matured and provided for	19,505	(19,505)	-
Accounts receivable matured, but not provided for	<u>153,899</u>	<u>-</u>	<u>153,899</u>
	<u>1,945,496</u>	<u>(19,505)</u>	<u>1,925,991</u>

Accounts Receivable Matured and Provided for

In the previous periods, the Company calculated an allowance for impairment of matured receivables in the amount of RSD 21,831 thousand (December 31, 2008: RSD 19,505 thousand) due from those customers whose creditworthiness has changed and which will not be collected in full.

Accounts Receivable Matured, but not Provided for

The Company failed to make an allowance for impairment of receivables matured as of December 31, 2009 in the amount of RSD 139,739 thousand (December 31, 2008: RSD 153,899 thousand) given that the customer creditworthiness has not changed, the Company holds that the present value of these receivables will be collected in full.

The average days' outstanding for accounts receivable in 2009 counted 44 days (2008: 81 days).

All receivables matured but unprovided for belong to the group from 31 to 90 days.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Credit Risk (Continued)

Managing Accounts Payable

Accounts payable as of December 31, 2009 stated in the amount of RSD 990,479 thousand (December 31, 2008: RSD 1,680,825 thousand) where the major portion of RSD 493,351 thousand relates to the liabilities to the Public Enterprise Electric Power Industry of Serbia. This supplier does not charge penalty against matured liabilities, whereas the Company duly settles accounts payable, as in accordance with financial risk management policies.

Liquidity Risk

The ultimate responsibility for liquidity risk management resides with the Company’s management, which is also responsible for managing the Company’s short-term, medium-term and long-term financing and liquidity management. The Company manages liquidity by maintaining the necessary level of cash reserves, based on continued monitoring over the planned and actual cash flows, as well as by matching the maturities of financial assets and liabilities.

Tables of Liquidity and Credit Risk

The following tables present details of outstanding contractual maturities of the Company’s financial assets. The amounts presented are based on the non-discounted cash flows from financial assets based on the earliest date for the Company’s collection of such receivables.

The following tables present details of outstanding contractual maturities of the Company’s financial liabilities. The amounts presented are based on the non-discounted cash flows from financial liabilities based on the earliest date upon which the Company’s may be expected to settlement such liabilities.

Maturities of Financial Liabilities

	December 31, 2009					
	Within a Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	Total
Interest bearing loans	-	-	1,405,373	255,727	12,007,949	13,669,049
Accounts payable	403,914	586,565	-	-	-	990,479
Other liabilities	547,232	12,358	56	-	-	559,646
	<u>951,146</u>	<u>598,923</u>	<u>1,405,429</u>	<u>255,727</u>	<u>12,007,949</u>	<u>15,219,174</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

34. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Liquidity Risk (Continued)

Tables of Liquidity and Credit Risk (Continued)

Maturities of Financial Liabilities (Continued)

	December 31, 2009					
	Within a Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	Total
Interest bearing loans	842,605	-	427,208	1,799,113	9,243,054	12,311,980
Accounts payable	1,680,825	-	-	-	-	1,680,825
Other liabilities	540,884	-	-	-	-	540,884
	<u>3,064,314</u>	<u>-</u>	<u>427,208</u>	<u>1,799,113</u>	<u>9,243,054</u>	<u>14,533,689</u>

Fair Value of Financial Instruments

The following table represents the present value of financial assets and liabilities and their fair value as of December 31, 2009 and 2008.

	December 31, 2009		December 31, 2008	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets				
Long-term financial placements	1,203,549	1,203,549	1,895,697	1,895,697
Accounts receivable	1,212,200	1,212,200	1,925,991	1,925,991
Short-term financial placements	3,490,826	3,490,826	1,495,344	1,495,344
Cash and cash receivables	2,461,847	2,461,847	2,052,247	2,052,247
	<u>8,368,422</u>	<u>8,368,422</u>	<u>7,369,279</u>	<u>7,369,279</u>
Financial liabilities				
Long-term liabilities	12,271,172	12,271,172	11,056,343	11,056,343
Current portion of long-term liabilities	1,397,877	1,397,877	1,255,637	1,255,637
Accounts payable	990,479	990,479	1,680,825	1,680,825
Other liabilities	559,646	559,646	540,884	540,884
	<u>15,219,174</u>	<u>15,219,174</u>	<u>14,533,689</u>	<u>14,533,689</u>

35. TAXATION RISKS

The Republic of Serbia tax legislation is subject to different interpretations and changes occur frequently. The interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company may not coincide with that of the management. As a result, transactions may be challenged by tax authorities and the Company may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for five years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2009

All amounts are expressed in thousands of RSD, unless otherwise stated.

36. CURRENT ECONOMIC SITUATION AND ITS IMPACT ON THE COMPANY

The Company’s operations were under the influence of the global financial crisis. It is expected that the Company will probably operate in a more difficult and uncertain economic environment in 2010. The impact of this crisis on the Company’s business operations is currently not possible to fully predict and therefore there is an element of general uncertainty.

So far, the ongoing financial crisis has had a limited impact on the financial position and performance of the Company.

The potential consequences of the financial crisis on the Company’s operations may reflect in the Company’s increased difficulties in obtaining additional sources of funds, and in particular, additional loan facilities. The aforementioned difficulty in obtaining loan facilities would also be a long-term consequence which, in the opinion of the Company’s management, cannot have decisive impact on the Company’s operations.

The deteriorating economic situation in the country will probably impact the position of certain industries and the ability of some clients to meet their obligations which may impact the amount of necessary allowance for impairment and provisions formed against potential losses incurred in 2010, as well as other fields which require significant estimates from the management, and where the actual results may depart from the estimates.

37. EXCHANGE RATES

The official exchange rates for the major currencies used in the translation of the balance sheet components denominated in foreign currencies, into Republic of Serbia Dinars (RSD) were as follows:

	In RSD	
	December 31, 2009	December 31, 2008
EUR	95.8888	88.6010
USD	66.7285	62.9000