
JP "ELEKTROMREŽA SRBIJE" BEOGRAD

***CONSOLIDATED FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED
31 DECEMBER 2006***

Contents

Independent Auditor's Report	1-2
Consolidated Income Statement for the year ended 31 December 2006	3
Consolidated Balance Sheet as of 31 December 2006	4
Consolidated Cash Flow Statement for the year ended 31 December 2006	5
Consolidated Statement of Changes in Equity for the year ended 31 December 2006	6
Notes to the Consolidated Financial Statements for the year ended 31 December 2006	7-34

INDEPENDENT AUDITOR'S REPORT

TO THE BOARD OF DIRECTORS OF JP ELEKTROMREZA SRBIJE BEOGRAD

We have audited the accompanying consolidated financial statements of JP Elektromreža Srbije, Beograd (hereinafter also referred to as "the Company"), which comprise the balance sheet as at 31 December 2006, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Accounting and Auditing Law and other applicable regulations in Republic of Serbia. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

We believe that, except as discussed in the following paragraphs (a) to (c), the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

- (a) We did not observe the counting of the physical inventories as of 31 December 2005, since that date was prior to the time we were initially engaged as auditors for the Company. Owing to the nature of the Company's records, we were unable to satisfy ourselves as to inventory quantities by other audit procedures.
- (b) The Company has not carried out a review of buildings and equipment to determine whether there is an indication that the assets may be impaired, and hence whether any impairment write down should be applied to the amounts recorded in the balance sheet at 31 December 2006 and 31 December 2005. In the absence of information to assess the recoverability of these assets, we were unable to satisfy ourselves as to the carrying amounts of buildings and equipment by other audit procedures.

- (c) As disclosed in Note 2 to the accompanying consolidated financial statements, no actuarial valuation has been performed to determine the present value of the employees' accrued entitlement to severance pay on retirement and jubilee awards and no provision for this liability has been made in the accompanying consolidated financial statements. We were not able to determine possible effects of recording the provision for this liability on consolidated financial statements of the Company.

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 paragraphs (a) to (c), the consolidated financial statements give a true and fair view of the financial position of the Company as of 31 December 2006 and of the results of its operations and its cash flows for the year then ended in accordance with Accounting and Auditing Law and basis set out in Note 2 to the accompanying consolidated financial statements.

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

1. As disclosed in Note 17 to the accompanying financial statements, the Company is in the process of registering its right to use properties with carrying amount of RSD 15,013,017 thousand taken over from JP Elektroistok and other State owned entities within Elektroprivreda Srbije. These rights are still registered under the name of other State owned entities as of the date of this report. Furthermore, the Company has not yet obtained formally the appropriate operating licence in respect of the buildings, included in property, plant and equipment as of 31 December 2005 in the amount of RSD 1,970,541 thousand.
2. As explained in Note 24 to the accompanying financial statements, the Company's capital, which is owned by the Government of the Republic of Serbia, was recorded as a difference between net book value of the assets and liabilities taken over from JP Elektroistok and JP Elektroprivreda Srbije at the date of the Company's foundation. On 1 July 2005 the state capital in the amount of EUR 516,017,205 was registered in the Register of business entities based on the valuation of assets of JP Elektroistok and JP Elektroprivreda as of 31 December 2004, which were afterwards transferred to the Company when it was founded.
3. The comparative amounts in the accompanying financial statements comprise the entire period from 1 January to 31 December 2005 including the period from 1 January 2005 to 30 June 2005 which preceded the date of the registration of the Company as JP "Elektromreza" Beograd on 1 July 2005. This registration has been treated in accordance with Serbian regulations as a "status change".

In Belgrade, 1 August 2007




Vladimir Filipović
Authorized Auditor

CONSOLIDATED INCOME STATEMENT
For the year ended 31 December 2006

	<i>Note</i>	<i>2006</i> <i>RSD'000</i>	<i>2005</i> <i>RSD'000</i>
Operating revenues			
Sales	3	4,766,380	3,731,718
Revenue from usage of own products and services	4	183,834	111,020
Other operating revenues	5	184,811	175,355
		5,135,025	4,018,093
Operating expenses			
Cost of goods sold		(3,600)	(1,469)
Cost of materials	6	(338,181)	(240,457)
Salaries and other benefits to employees	7	(1,447,591)	(1,132,617)
Depreciation, amortization and provisions	8	(1,850,457)	(1,754,112)
Other operating expenses	9	(697,504)	(413,099)
		(4,337,333)	(3,541,754)
Operating profit		797,692	476,339
Financial income	10	1,118,337	93,063
Financial expenses	11	(532,955)	(790,082)
Other income	12	34,025	76,693
Other expenses	13	(318,739)	(709,037)
Profit / (loss)		1,098,360	(853,024)
Net loss from discontinuing operations	14	(202,208)	-
Profit / (loss) before income tax		896,152	(853,024)
Current income tax expense	15	(27,383)	(72)
Deferred income tax revenue	15	277,958	124,313
Profit / (loss) for the period		1,146,727	(728,783)

CONSOLIDATED BALANCE SHEET
As of 31 December 2006

	Note	31.12.2006. RSD'000	31.12.2005. RSD'000
Non-current assets			
Intangibles	15	40,039	22,070
Property, plant and equipment	16	39,792,635	39,508,034
Long-term investments	17	1,637,475	1,027,913
		41,470,149	40,558,017
Current assets			
Inventories	18	468,259	346,592
Trade and other receivables	19	955,241	1,343,448
Short-term investments	20	245,507	45,332
Cash and cash equivalents	21	1,428,281	606,089
Value added tax and prepayments	22	86,242	83,496
		3,183,530	2,424,957
Deferred tax assets		481	-
TOTAL ASSETS		44,654,160	42,982,974
Equity			
State and other capital	23	30,540,089	30,420,410
Retained earnings		1,146,727	-
Accumulated loss		(541,316)	(541,316)
		31,145,500	29,879,094
Long-term liabilities and provisions			
Long-term provisions	24	89,624	41,345
Long-term loans	25	6,605,159	4,526,377
Other long-term liabilities	26	1,242,178	2,254,680
		7,936,961	6,822,402
Short-term liabilities			
Short-term financial liabilities	27	880,766	1,315,678
Operating liabilities	28	683,233	456,718
Other short-term liabilities and accruals	29	2,039,522	2,292,251
Taxes payables	30	81,927	80,341
Income tax payables	13	27,310	72
		3,712,758	4,145,060
Deferred tax liabilities	13	1,858,941	2,136,418
TOTAL EQUITY AND LIABILITIES		44,654,160	42,982,974
Off-balance sheet items	31	6,078,074	6,273,438

Belgrade, 1 August 2007



On behalf of JP Elektromreza Srbije Beograd:

Dragan Vignjevic
General Manager

CONSOLIDATED CASH FLOW STATEMENT
For the year ended 31 December 2006

	2006	2005
	RSD '000	RSD '000
Cash inflows from operating activities		
Sales and receipts from customers	4,914,350	2,931,418
Interests received from operating activities	160,823	-
Other inflows from ordinary operations	117,287	147,972
Cash outflows from operating activities		
Payments to suppliers and advances paid	(1,439,409)	(506,321)
Salaries, compensations and other personnel expenses	(1,005,476)	(1,109,905)
Interests paid	(213,763)	(303)
Income tax paid	(145)	-
Other duties paid	(413,042)	(457,643)
Net cash inflow from operating activities	2,120,625	1,005,218
Cash inflow from investing activities		
Sales of property, plant and equipment	1,997	508
Other financial investments, net inflow	-	40
Interests received from investing activities	-	77
Cash outflows from investing activities		
Purchases of intangibles, property, plant and equipment	(820,276)	(419,102)
Net cash outflow from investing activities	(818,279)	(418,477)
Cash outflows from financing activities		
Long-term and short-term borrowings and other liabilities, net outflows	(335,059)	-
Net cash outflow from financing activities	(335,059)	-
Total cash inflows	5,194,457	3,080,015
Total cash outflows	(4,227,170)	(2,493,274)
Net cash inflow	967,287	586,741
Cash at the beginning of the period	606,089	18,051
Foreign exchange gains on cash	4,437	1,330
Foreign exchange losses on cash	(149,532)	(33)
Cash at the end of the period	1,428,281	606,089

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006

<i>RSD'000</i>	<i>State capital</i>	<i>Other capital</i>	<i>Retained earnings</i>	<i>Accumulat ed loss</i>	<i>Total</i>
At 1 January 2005	21,590,587	33,582	9,275,974	-	30,900,143
Net effect of restructuring process	(294,028)	-	-	-	(294,028)
Loss for the year	-	-	-	(728,783)	(728,783)
Transfers	9,090,269	-	(9,275,974)	185,705	-
At 31 December 2005	30,386,828	33,582	-	(543,078)	29,877,332
Adjustment of opening balance	-	-	-	1,762	1,762
At 1 January 2006, adjusted	30,386,828	33,582	-	(541,316)	29,879,094
Capital increase	119,679	-	-	-	119,679
Profit for the year	-	-	1,146,727	-	1,146,727
At 31 December 2006	30,506,507	33,582	1,146,727	(541,316)	31,145,500

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

1. Corporate information

The consolidated financial statements of JP Elektromreza Srbije, Beograd (hereinafter referred to as "the Company") for the year ended 31 December 2006 have been authorised by the Company's Board of directors dated 1 August 2007.

The consolidated financial statements comprise financial statements of JP Elektromreza Srbije, Beograd and its fully owned subsidiaries Elektroistok – Izgradnja d.o.o. Beograd and Elektroistok – Projektni biro d.o.o. Beograd.

JP Elektromreza Srbije, Beograd with short-term JP EMS, Beograd was founded based on the Decision of the Government of Republic of Serbia (No. 023-397/2005-1 as of 27 January 2005) on formation of State owned company for electricity transmission and transmission system management announced at Official Gazette RS No. 12/2005.

According to the Decision of the Government of the Republic of Serbia on foundation of the Company, the assets used for the Company's foundation and operations comprise movable and immovable properties, cash and cash equivalents, securities, property law and other assets Elektroprivreda Srbije invested as the founder's stake in Elektroistok as well as the assets that Elektroistok acquired during its business operations. The assets used for the Company's foundation and operations also include part of the assets used by Elektroprivreda Srbije for transmission system management and Elektroprivreda's stake in the company „Elektroenergetski koordinacioni centar" d.o.o. Beograd. The above assets were determined by the balance of assets as of 31 December 2004.

According to the Decision of the Government of the Republic of Serbia on foundation of the Company, it was determined that the Company will take over the following:

1. Assets, rights and liabilities of the State owned company for electricity transmission "Elektroistok", Beograd, as well as all employees of that company,
2. Part of the assets and rights of the State owned company "Elektroprivreda Srbije", as determined in the balance of assets as of 31 December 2004,
3. Part of liabilities of the State owned company "Elektroprivreda Srbije" which that company has took over in relation with the business operations of State owned company for electricity transmission "Elektroistok", Beograd and in relation with construction, reconstruction and modernization of buildings, plants and equipment for electricity transmission system and transmission system management. Those liabilities should be determined by balance on dividing of liabilities as of 30 June 2005.
4. Part of the employees in the State owned company "Elektroprivreda Srbije" who were involved in the transmission system management until 30 June 2005.

In line with the Decision of the Government of Republic of Serbia on the Company's formation dated 1 July 2005, Serbian Business Register Agency made a Decision No. BD 80469/2005 on recording the Company's formation in Register of business entities.

The Company's main activities are transmission of electricity and operation of the electricity transmission system.

The Company's Head Office is located in Belgrade, Kneza Miloša Street no.11.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

1. Corporate information (continued)

Decision-making body of the Company consists of Board of Directors, Executive Director and Supervisory Board. The members of decision-making body of the Company are appointed by the Government of the Republic of Serbia.

Subsidiaries Elektroistok – Izgradnja d.o.o. Beograd and Elektroistok – Projektni Biro d.o.o. Beograd were departments in company JP Elektroistok, Beograd which were on 30 June 2005 separated and became separate legal entities. The main activity of company Elektroistok – Izgradnja d.o.o. Beograd is the construction of electric power systems, devices, lines and plants while the main activity of the company Elektroistok – Projektni Biro d.o.o. Beograd is design of electric power systems and devices.

As of 31 December 2006 the Company had 1,527 employees (31 December 2005 – 1,510).

2. Summary of significant accounting policies

Regulatory

The Company is regulated by the Ministry of Energy, as regulator, pursuant to the Energy Law and Law on establishment of Serbian Transmission Systems Operator "Elektromreza".

The Regulatory Authority (an Energy Agency) was founded in year 2005 by Decision of the Government of the Republic of Serbia. According to the Energy Law, the Energy Agency brought Methodology for setting tariff elements for calculating prices for access to and use of system for electricity transmission and Tariff system for electricity transmission system access and utilisation.

The Company accounts for certain transactions in accordance with applicable regulations (regulatory accounting) when the following criteria are met: (a) the rates for regulated services provided are established by or are subject to approval by an independent, third-party regulator (the Ministry); (b) the regulated rates are designed to recover the cost of providing the services; and (c) in view of the demand for the regulated services, it is reasonable to assume that rates are set at levels that will recover the cost that can be charged to and collected from end-users. Under regulatory accounting, the timing of the Company's recognition of certain assets, liabilities, revenues and expenses may differ from that otherwise expected under Serbian generally accepted accounting principles for non-regulated businesses.

Contract signed between State owned Power Electricity Company (JP EPS) and the Company for the period from January to December 2006, regulates criteria and prices for services of transmission of electricity and operation of the electricity transmission system, as well as the manner and payment terms for services provided. Price for the service of transmission of electricity and operation of the electricity transmission system for 2006 year amounts to 0.0814 RSD/kWh and has not changed as compared to 2005 year. Invoicing for 2006 year has been done per planed amounts from electro energetic balance.

When the regulator issues decisions affecting the financial statements, the effects of the decision are recorded in the period in which the decision is received.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)

Basis of preparation

The financial statements are presented in Republic of Serbia Dinar (RSD), being domicile currency of the Company, and all values are rounded to the nearest thousand (RSD'000) except when otherwise indicated. The financial statements have been prepared on a historical cost basis, except for financial instruments that have been measured at fair value.

The Company maintains its records and prepares financial statements in accordance with the Accounting and Auditing Law of the Republic of Serbia (Official Gazette of the Republic of Serbia No: 46/06), Rulebook on chart of accounts and contents of chart of accounts for companies, cooperatives, other legal entities and entrepreneurs (Official Gazette of the Republic of Serbia No: 114/2006) and Rulebook on format and contents of financial statements for companies, cooperatives, other legal entities and entrepreneurs (Official Gazette of the Republic of Serbia No: 114/2006).

Bases of consolidation

As stated in Note 1 to the accompanying financial statements, the consolidated financial statements comprise financial statements of JP Elektromreza Srbije, Beograd and its fully owned subsidiaries Elektroistok – Izgradnja d.o.o. Beograd and Elektroistok – Projektni biro d.o.o. Beograd.

The financial statement of subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognised in assets, are eliminated in full.

Subsidiaries are fully consolidated from the date of foundation, or acquisition, being the date on which parent company obtains control, and continue to be consolidated until the date such control ceases.

Foreign currency translation

The functional and presentation currency of the Company is the Republic of Serbia Dinar (RSD). Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency shall be translated using the exchange rates at the date when the fair value was determined.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)**Intangibles**

Intangible assets acquired separately are initially measured at cost of purchase or development cost. The cost of purchase comprises the invoice value, possible import duties and other costs directly attributable to the acquisition of intangible asset. Trade discounts and rebates deducted in determining the costs of purchase. Interest expenses that occur during the period of development of intangible assets are not capitalised.

Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Depreciation of the intangible assets is calculated on a straight-line basis over its estimated useful life of the intangible asset by applying the annual depreciation rate of 20%. Amortization begins when asset is available for use. The carrying value of intangible assets is reviewed annually when the asset is not yet in use.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment in value.

Subsequent expenditures are capitalised when they appreciably extend the life, increase the earning capacity or improve the efficiency of property, plant and equipment. Repairs and maintenance are charged to expenses as incurred.

Self-developed assets are stated at cost if does not exceed the market value. Cost does not include interest, administrative and general expenses which are not directly related to development of the asset.

Depreciation is calculated on a straight-line basis over the remaining estimated useful life of the asset as follows:

Buildings	15-76 years
Transformers	12-34 years
Long-distance power transmission lines	14-46 years
Lorries and cars	2-5 years
Computers and computer equipment	3-4 years
Office equipment	5-9 years

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year the item is derecognised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)

Investments

All investments are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investment.

Available for sale financial instruments

Financial instruments available for sale comprise investment in shares of other legal entities and banks. After initial recognition, financial instruments available for sale are measured at fair value. For instruments that are actively traded in organised financial markets, fair value is determined by reference to Stock Exchange quoted market bid prices at the close of business at the balance sheet date. Instruments, which are not quoted at active market and where their fair value cannot be reliably determined, are measured at cost less impairment in value, if any.

Loans and receivables originated by the Company

Loans and receivables originated by the Company are measured at amortised cost using the effective interest rate method. Gains and losses are recognized in income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Recoverable amount of non-current assets

As at each balance sheet date, the Company assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Company makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount. Recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

Inventories

Inventories of material and spare parts are valued at the lower of cost of purchase and net realisable value.

The cost of purchase comprises the invoice value, import duties, transport, handling and other costs incurred in bringing inventories to its present location and condition. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase. Cost of materials and spare parts is assigned by using the weighted average cost method.

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

Provision against inventories is recorded when it is estimated that value should be reduced to net realizable value and on the basis of other documented decrease in value of inventories.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)

Trade and other receivables

Trade receivables are recognised and carried at original invoice amount, less an allowance for any uncollectible amounts. Bad debt allowance is recognised against receivables being overdue more than 60 days. The assessment of the possibility of collection can be conducted for individual cases. Bad debts are written off when there is no possibility of their collection.

Provision against trade receivables is not made for the receivables from legal entities to which the Company has liabilities as well.

Cash and cash equivalents

Cash and cash equivalents comprise cash at bank, cash in hand and high liquid securities with a maturity of three months. For the purposes of the Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognized at cost, being the fair value of the consideration received net of disbursement costs associated with the borrowing. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any disbursement costs, and any discount or premium on settlement. Gains and losses are recognized in net profit or loss when the liabilities are derecognized or impaired, as well as through the amortization process.

Donations

Donations ("grants") are recognised at their value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where appropriate a part of a financial asset or a part of a group of financial assets) is derecognized when the Company does not have any more control over an asset or part of a financial asset.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Employee Benefits

The Company, in the normal course of business, makes payments on behalf of its employees for pensions, health care, employment and personnel tax that are calculated on the basis of gross salaries and wages, as well as food allowances, travel expenses and vacation allowances according to the local legislation.

The Company makes these contributions to the Government's health and retirement funds, at the statutory rates in force during the period, based on gross salary payments. The cost of these payments is charged to the income statement in the same period as the related salary cost. There is no additional liability for these plans.

In accordance with the Collective Agreement, the Company is obliged to pay employees retirement indemnity in accordance with law (in accordance with Labour Law there is a mandatory retirement indemnity equal to 3 gross monthly salaries, based on the country average salary earned in the month prior to retirement) i.e. regardless of their will in case of loss of working ability, in the amount of 1.67 average salary earned in the Company in the month prior to retirement The retirement indemnity cannot be lower than 1.67 average salary earned in the Company in the month prior the retirement indemnity is paid if that is more favourable for the employee.

Incentive retirement indemnities are determined and paid to employees on the basis of the programme approved by the Board of Directors.

Employees are entitled to jubilee awards upon completion of:

- 10 years of service – 0.56 the average monthly salary earned in the Company in the month prior to jubilee award payment
- 20 years of service – 1.12 the average monthly salary earned in the Company in the month prior to jubilee award payment
- 30 years of service – 1.67 the average monthly salary earned in the Company in the month prior to jubilee award payment

No actuarial valuation has been performed to determine the present value of these liabilities and no provision for these liabilities has been made in the accompanying financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

2. Summary of significant accounting policies (continued)

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Revenue from sales of services

Revenue from sales of services is recognised when the service is provided.

Interest income

Interest income is recognised for the period it refers to.

Other income and expenses

Borrowing costs are recognised as an expense when incurred.

Other operating income and expenses are recognised on accrual basis.

Income tax

Current income tax is provided for in accordance with local fiscal regulations in the Republic of Serbia using the prescribed tax rate on tax based determined by tax return. Tax losses stated in annual tax returns can cover future tax profit in ten-year period.

Deferred income taxes are calculated and recognised, using the liability method, on all temporary differences at the balance sheet date between tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income liabilities are recognised on all taxable temporary differences.

Deferred income tax assets are recognized for all deductible temporary differences, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized.

Deferred income tax assets and liabilities are measured at the tax rates expected to be applied in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Value added tax

Revenues, expenses and assets are recognized in net amount without applicable value added tax, except when amount of value added tax cannot be recovered from tax authorities. In that case value added tax is recognized as part of cost of purchase or expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

3. Sales

Sales for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Income from electricity transmission, transmission system management and capacity allocation	4,654,254	3,695,882
Income from sales of products and services	112,126	35,836
	4,766,380	3,731,718

4. Revenues from usage of own products and services

Revenues from usage of own products and services for the years ended 31 December 2006 and 31 December 2005 amounting to RSD 183,834 thousand and RSD 111,020 thousand relate to investments performed by the Company on its transmission capacities.

5. Other operating income

Other operating income for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Income from insurance indemnities	86,843	81,087
Amortization of deferred income - Note 27	83,956	75,616
Rental income	5,279	5,511
Other operating income	8,733	13,141
	184,811	175,355

6. Cost of materials

Cost of materials for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Cost of materials	159,205	95,659
Cost of spare parts	45,372	57,231
Cost of small tools	36,125	20,454
Cost of office and other overhead material	33,147	21,276
Cost of fuel and energy	64,332	45,764
Cost of other materials	-	73
	338,181	240,457

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

7. Salaries and other benefits to employees

Salaries and other benefits to employees for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Gross salaries	1,061,601	766,572
Taxes and contributions on salaries	201,071	171,341
Business trips	72,188	62,591
Termination benefits	59,035	84,453
Transportation of employees	25,639	17,135
Jubilee awards	6,794	7,487
Severance pay on retirement	3,826	8,187
Other personal expenses	17,437	14,851
	<u>1,447,591</u>	<u>1,132,617</u>

8. Depreciation, amortization and provisions

Depreciation, amortization and provisions for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Depreciation of property, plant and equipment - Note 17	1,771,659	1,722,934
Amortization of intangibles - Note 16	14,107	3,976
Provision for litigations - Note 25	64,691	27,202
	<u>1,850,457</u>	<u>1,754,112</u>

9. Other operating expenses

Other operating expenses for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Maintenance	231,109	122,264
Taxes and other duties	133,145	81,323
Insurance premiums	127,626	115,693
Postage and telephone expenses	40,377	17,856
Utility services and maintenance of business premises	28,139	14,459
Security expenses	20,445	11,388
Entertainment	16,363	11,608
Production services	13,741	-
Bank charges	4,582	3,535
Rental expenses	3,921	9,869
Other expenses	78,056	25,104
	<u>697,504</u>	<u>413,099</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

10. Financial income

Financial income for years ended 31 December 2006 and 31 December 2005 relates to the following:

	<i>2006</i> <i>RSD'000</i>	<i>2005</i> <i>RSD'000</i>
Interest income	208,588	87,595
Foreign exchange gains	906,414	4,208
Other financial income	3,335	1,260
	<u>1,118,337</u>	<u>93,063</u>

Interest income amounting to RSD 157,820 thousand for the year ended 31 December 2006 (RSD 85,912 thousand for the year ended 31 December 2005) relate to interest on rescheduled receivables from Elektroprivreda Srbije – Note 17.

11. Financial expenses

Financial expenses for years ended 31 December 2006 and 31 December 2005 relate to the following:

	<i>2006</i> <i>RSD'000</i>	<i>2005</i> <i>RSD'000</i>
Foreign exchange losses	215,964	686,072
Interest expenses	304,688	103,947
Other financial expenses	12,303	63
	<u>532,955</u>	<u>790,082</u>

12. Other income

	<i>2006</i> <i>RSD'000</i>	<i>2005</i> <i>RSD'000</i>
Cancellation of long-term provisions – Note 25	14,887	3,390
Gains from sales of property, plant and equipment	6,969	548
Collection of previously provided receivables	2,613	3,237
Surpluses	592	5,660
Gains from sales of materials	80	3,114
Cancellation of provision for obsolete inventories	-	4,519
Income from write-off of liabilities	-	432
Other income	8,884	55,793
	<u>34,025</u>	<u>76,693</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

13. Other expenses

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Provision against trade receivables - Note 19	208,763	177,833
Loss on write-off and sales of property, plant and equipment and materials	87,267	56,578
Inventories impairment	2,938	-
Non-current assets impairment	2,168	32,551
Provision against other receivables	675	1,272
Minuses	90	233
Rescheduling of the loan Kapital Hilfe - Note 25	-	434,424
Other expenses	16,838	6,146
	<u>318,739</u>	<u>709,037</u>

14. Loss from discontinuing operations

Structure of loss from discontinuing operations can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Rescheduling of loan Kapital Hilfe (Note 26)	(160,638)	-
Contributions for beneficiary work	(87,659)	-
Interest on rescheduled receivables from EPS	36,099	-
Rescheduling of loan IBRD 2338-7 (Note 26)	24,729	-
Rescheduling of loan EIB (Note 26)	6,411	-
Rescheduling of loan IBRD 2338-5 (Note 26)	2,178	-
Other income and expenses, net	(23,328)	-
	<u>(202,208)</u>	<u>-</u>

15. Income tax

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Current income tax	(27,383)	(72)
Deferred income tax	277,958	124,313
	<u>250,575</u>	<u>124,241</u>

Current income tax for the year ended 31 December 2006 and 31 December has been calculated in accordance with local tax regulations, in accordance with separate tax returns of the Company and subsidiaries. The Company does not perform tax consolidation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

15. Income tax (continued)

Summarized, calculation of current income tax for the year ended 31 December 2006 is as follows:

	<i>2006</i>
	<i>RSD'000</i>
Profit / (loss) before income tax	896,152
<i>Capital gains and losses</i>	
Capital gains	(5,277)
Capital losses	-
<i>Adjustment for non-deductible expenses</i>	
<i>Adjustment for depreciation</i>	
Accounting depreciation	1,785,766
Tax depreciation	(1,524,147)
Taxable profit / (tax loss)	1,231,961
Utilization of tax losses from prior years	(681,935)
Capital gain exceeding prior years capital losses	2,977
Tax base	553,003
Current income tax rate	10.00%
Calculated income tax	55,300
Tax credit	(27,917)
Current income tax expense	27,383

Changes in deferred income tax liabilities were as follows:

	<i>Balance sheet</i>		<i>Income statement</i>	
	<i>31.12.2006.</i>	<i>31.12.2005.</i>	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>	<i>RSD'000</i>	<i>RSD'000</i>
Deferred tax liability				
Difference in net carrying value of property, plant and equipment for tax and accounting purposes	1,858,941	2,136,418	277,958	124,313
	1,858,941	2,136,418	277,958	124,313

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

16. Intangibles

<i>In RSD'000</i>	Software licenses	Intangible assets under construction	Total
Cost			
At 1 January 2005	9,664	-	9,664
Transfer from other companies within EPS during restructuring	-	3,493	3,493
Additions	-	13,735	13,735
Transfer	13,735	(13,735)	-
Other	(71)	-	(71)
At 31 December 2005	23,328	3,493	26,821
Additions	-	22,882	22,882
Transfers	1,749	(1,749)	-
Disposals	(325)	-	(325)
Other	274	-	274
At 31 December 2006	25,026	24,626	49,652
Accumulated amortization			
At 1 January 2005	1,887	-	1,887
Current year amortization	3,977	-	3,977
Other	(1,113)	-	(1,113)
At 31 December 2005	4,751	-	4,751
Current year amortization	4,887	-	4,887
Disposals	(25)	-	-
At 31 December 2006	9,613	-	9,613
Net book value:			
At 31 December 2006	15,413	24,626	40,039
At 31 December 2005	18,577	3,493	22,070
At 1 January 2005	7,777	-	7,777

Intangibles under construction as of 31 December 2006 amounting to RSD 21,133 thousand relates to licence for SAP.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

17. Property, plant and equipment

<i>In RSD'000</i>	Land	Buildings	Equipment	Assets under construction and advances for PP&E	Total
Cost					
At 1 January 2005	109,489	45,973,823	58,142,550	3,807,395	108,033,257
Transfer of assets from other companies within EPS during restructuring	230	2,871,822	3,600,098	458,559	6,930,709
Additions	-	-	-	1,020,040	1,020,040
Transfers from CIP	963	115,214	658,858	(775,035)	-
Transfer of assets to companies within EPS during restructuring	-	(107,928)	(125,749)	(684)	(234,361)
Disposals and write-offs	-	(14,720)	(251,477)	(10,271)	(276,468)
Other	-	-	-	(139,013)	(139,013)
At 31 December 2005	110,682	48,838,211	62,024,280	4,360,991	115,334,164
Additions	-	-	-	2,329,297	2,329,297
Transfer from Termo Power Plant Nikola Tesla	-	-	113,028	-	113,028
Transfers from CIP	-	144,767	178,316	(323,083)	-
Transfer	-	147,374	(147,374)	-	-
Transfer to inventories	-	-	-	(283,412)	(283,412)
Disposals and write-offs	-	(56,604)	(90,908)	(193,858)	(341,370)
Other	-	(3,963)	(175)	-	(4,138)
At 31 December 2006	110,682	49,069,785	62,077,167	5,889,935	117,147,569
Accumulated depreciation and impairment					
At 1 January 2005	8,409	31,230,834	38,960,809	412,361	70,612,413
Transfer of assets from other companies within EPS during restructuring	-	1,537,031	2,327,908	-	3,864,939
Depreciation for the year	-	614,130	1,108,803	-	1,722,933
Transfer of assets to companies within EPS during restructuring	-	(98,674)	(111,805)	-	(210,479)
Disposals and write-offs	(40)	(734)	(194,985)	-	(195,759)
Impairment of investment material	-	-	-	32,083	32,083
At 31 December 2005	8,369	33,282,587	42,090,730	444,444	75,826,130
Transfer from Termo Power Plant Nikola Tesla	-	-	1,939	-	1,939
Depreciation for the year	-	627,794	1,153,085	-	1,780,879
Transfer	-	94,959	(94,959)	-	-
Disposals and write-offs	-	(36,208)	(70,526)	(147,120)	(253,854)
Other	-	-	(160)	-	(160)
At 31 December 2006	8,369	33,969,132	43,080,109	297,324	77,354,934
Net book value:					
At 31 December 2006	102,313	15,100,653	18,997,058	5,592,611	39,792,635
At 31 December 2005	102,313	15,555,624	19,933,550	3,916,547	39,508,034
At 1 January 2005	101,080	14,742,989	19,181,741	3,395,034	37,420,844

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**For the year ended 31 December 2006****17. Property, plant and equipment (continued)**

According to the Law on State owned enterprises in the Republic of Serbia, the Company has a right to use the assets owned by the State. Based on the Decision on Company Foundation issued by the Government of the Republic of Serbia, the Company cannot purchase or sell the buildings and other properties, plants or devices used for conducting the activities of electricity transmission and transmission system management. The consent of the Government of the Republic of Serbia is required in order to purchase and sell high-value assets used for conducting the activities of electricity transmission and transmission system management and for the purpose of replacing obsolete assets, modernization or technical and technological improvements.

The right of usage of the assets taken from Elektroistok and other State owned companies within Elektroprivreda Srbije has not been transferred to the Company, but is still on the name of these State owned enterprises (RSD 15,013,017 thousand as of 31 December 2006). Furthermore, as of 31 December 2006 buildings amounting to RSD 1,970,461 thousand are not legalized yet.

Out of total purchases of property, plant and equipment for the year ended 31 December 2006 the biggest portion amounting to RSD 2,227,270 thousand relate to purchases of overhead lines and substations.

Accumulated depreciation of fixed assets under construction relates to the provision of spare parts used for investment maintenance.

Insurance of Assets

The Company carries insurance for loss or damage to substations, transmission lines, towers, poles, telecommunication facilities, and physical damage to automobiles. However, there is no assurance that available insurance will cover all losses or liabilities that might arise in the conduct of the Company's business. In the event of an uninsured loss or liability, the Company would apply to the Ministry of Energy to recover the loss (or liability) through an increased tariff. However, there is no assurance that the regulator would approve any such application, in whole or in part. Any major damage to the Company's facilities could have a material adverse effect on the Company's business, results of operations, financial position and prospects.

Damage from Weather and Other Disasters

The Company's facilities are exposed to the effects of severe weather conditions and other acts of nature. Although those facilities have been constructed, operated and maintained to withstand certain levels of severe weather and natural phenomena, the Company cannot ensure that they will successfully do so in all circumstances. In addition, many facilities are located in remote areas, making access for repair of damage due to weather conditions or other natural phenomena difficult. Further, losses arising from damage to assets and facilities could result from other sources beyond the Company's control, such as acts of vandalism, sabotage or terrorism. Any major damage to the Company's facilities could result in repair costs that are substantial in amount, any of which might adversely affect the Company's business, results of operations, financial position and prospects.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

18. Long-term financial investments

Long-term financial investments as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i> <i>RSD'000</i>	<i>31.12.2005.</i> <i>DIN'000</i>
Investments in shares of other legal entities	245,100	241,900
Other long-term financial investments	1,629,027	1,022,630
Long-term financial investments, gross	1,874,127	1,264,530
Provision against investments in shares of other legal entities	(236,652)	(236,617)
Long-term financial investments, net	1,637,475	1,027,913

Other long-term financial investments as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i> <i>RSD'000</i>	<i>31.12.2005.</i> <i>RSD'000</i>
Rescheduled receivables from Elektroprivreda Srbije	1,836,909	1,010,725
Receivables for sold flats and loans for flats	30,650	24,194
Time deposits	5,600	-
Receivables from State owned companies within EPS-a in respect of loan received from IBRD	-	26,087
Other long-term financial investments	840	931
	1,873,999	1,061,937
Less: Current portion of rescheduled receivables from Elektroprivreda Srbije - Note 21	(244,972)	(39,306)
	1,629,027	1,022,631

Part of rescheduled receivables from Elektroprivreda Srbije as of 31 December 2006 amounting to RSD 977,034 thousand relate to receivables in respect of allocation of joint income within EPS until 31 December 2004. Based on the balance on dividing of liabilities accepted by Elektroprivreda Srbije and the Company as of 30 June 2005, out of total receivables from EPS as of 31 December 2004 amounting to RSD 2,555,967 thousand part amounting to RSD 1,545,242 thousand was written off and part amounting to RSD 1,010,725 thousand was rescheduled. The rescheduled part of receivables is to be repaid in monthly instalments over the period of 15 years. The first instalment was due on 30 June 2006. The interest is calculated by applying the National Bank of Serbia discount rate. Second part of rescheduled receivables from Elektroprivreda Srbije amounting to RSD 859,875 thousand as of 31 December 2006 relates to receivables of Elektroistok as of 30 June 2005, which are rescheduled in accordance with the contract signed between the Company and EPS as of 1 November 2006. The rescheduled receivables are to be repaid in monthly instalments over the period of 5 years. First instalment is due on 31 January 2007. The interest is calculated by applying the National Bank of Serbia discount rate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

19. Inventories

Inventories as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Material	289,954	217,268
Spare parts	182,352	132,464
Tools and inventory	13,786	12,451
Goods	1,093	583
Advances	16,986	14,757
Inventories, gross	<u>504,171</u>	<u>377,523</u>
Provision for obsolete inventories of material	(35,432)	(28,985)
Provision for obsolete inventories of goods	(76)	(75)
Provision against advances paid	(404)	(1,871)
Inventories, net	<u><u>468,259</u></u>	<u><u>346,592</u></u>

20. Trade and other receivables

Trade and other receivables as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Receivables from local trade debtors	1,086,779	1,258,929
Receivables from foreign trade debtors	66,244	157,457
Receivables for interest	128,779	87,185
Receivables from employees	26,167	11,919
Receivables for over-paid taxes and contributions	2,300	733
Other receivables	4,252	14,531
	<u>1,314,521</u>	<u>1,530,754</u>
Provision against local trade receivables	(358,640)	(186,771)
Provision against other receivables	(640)	(535)
	<u><u>955,241</u></u>	<u><u>1,343,448</u></u>

As of 31 December 2006 the Company did not reconcile with customers part of trade receivables amounting to RSD 3,454 thousand.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

20. Trade and other receivables (continued)

Movements in provision against trade receivables for the years ended 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Balance at 1 January	186,771	11,436
Provision during the period - Note 13	208,763	177,833
Foreign exchange translation of previously provided receivables	(28,244)	921
Collection of previously provided receivables – Note 12	(2,613)	(3,237)
Write-off	(6,020)	-
Other	(17)	(182)
Balance at 31 December	358,640	186,771

21. Short-term investments

Short-term investments as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Current portion of rescheduled receivables from EPS - Note 17	244,972	39,306
Other short-term investments	535	6,026
	245,507	45,332

22. Cash and cash equivalents

Cash and cash equivalents as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Foreign currency accounts	1,372,912	564,684
Current accounts	48,400	38,342
Cash in hand	2,635	1,753
Letters of credits and cash held for special purposes	2,229	652
Other cash and cash equivalents	2,105	658
	1,428,281	606,089

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

23. Value added tax, deferred expenses and accrued income

Value added tax, deferred expenses and accrued income as of 31 December 2006 and 31 December 2005 relate to:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Accrued income not invoiced	74,474	46,554
Value added tax	1,554	7,794
Prepaid expenses	2,038	1,176
Other deferred expenses and accrued income	8,176	27,972
	86,242	83,496

24. State-owned capital

State-owned capital represents the capital owned by the State, recorded at the foundation date as a difference between the carrying value of the assets and liabilities taken over from JP Elektroistok and JP Elektroprivreda Srbije. On 1 July 2005 the state-owned capital was registered at Register of business entities in the amount of EUR 516,017,205. The registration was based on the independent appraisal of “in-kind” capital contribution of the State, performed by local certified valuer as of 31 December 2004, which comprised assets of JP Elektroistok and other companies within JP Elektroprivreda Srbije.

Other capital

Other capital of the Company for the years ended 31 December 2006 and 31 December 2005 in the amount of RSD 33,582 thousand relates to the Company’s own non operating sources transferred to the capital as of 1 January 2004.

25. Long-term provisions

Long-term provisions for the years ended 31 December 2006 and 31 December 2005 in the amount of RSD 89,624 thousand and RSD 41,345 thousand, respectively, relate to provision for potential losses from pending litigations involving the Company as a defendant.

Movements in the provision against legal cases for the years ended 31 December 2006 and 31 December 2005 were as follows:

	<i>2006</i>	<i>2005</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Balance at 1 January	41,345	17,512
Provision during the period - Note 8	64,691	27,202
Cancellation of provision - Note 11	(14,887)	(3,390)
Payments	(1,525)	-
Other	-	21
Balance at 31 December	89,624	41,345

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

26. Long-term loans

Long-term loans as of 31 December 2006 and 31 December 2005 comprise the following:

	<i>Interest rate</i>	<i>Maturity</i>	<i>31.12.2006.</i> RSD'000	<i>31.12.2005.</i> RSD'000
· European Investment Bank	Variable	2009-2018	20,418	-
· Kapital Hilfe - Vojvodjanska banka a.d. Novi Sad	not defined	not defined	-	674,677
<i>Liabilities to the Government of the Republic of Serbia - Deposit Insurance Agency in respect of the loans:</i>				
· Kapital Hilfe - Investbanka a.d. Beograd	2.3%	2007-2014	3,873,630	4,192,347
· International Bank for Reconstruction and Development - 2338-5	Variable	2006-2031	1,208,885	-
· Kapital Hilfe - Vojvodjanska banka a.d. Novi Sad	2.3%	2007-2014	901,042	-
· International Bank for Reconstruction and Development - 2338-7	Variable	2006-2031	345,656	-
· Evropean Investment Bank - 16268	EURIBOR	2012-2016	180,061	175,831
· International Bank for Reconstruction and Development - 14695	Variable	2006-2031	143,393	163,125
			6,673,085	5,205,980
Less: current portion of long-term loans - Note 28			(67,926)	(679,603)
			6,605,159	4,526,377

Portion of the loan from European Investment bank amounting to RSD 20,428 thousand which was directly utilized by the Company is disclosed under long-term loans. Portion of loan as of 31 December 2006 which was utilized by Elektroprivreda Srbije for the Company's needs and is disclosed under other long-term liabilities – Note 27. As of 26 March 2007 entire liabilities towards European Investment Bank in respect of this loan are transferred from Elektroprivreda Srbije to the Company.

Loan Kapital Hilfe – Investbanka a.d. Beograd was rescheduled during the year ended 31 December 2005. Recorded liabilities in respect of this loan were lower as compared to liabilities determined during rescheduling by RSD 434,425 thousand, which was recorded in the year ended 31 December 2005 by charging other expenses - Note 13.

Loans from International Bank for Reconstruction and Development 2338-5 and 2338-7, as well as the loan from European Investment Bank was rescheduled during the year ended 31 December 2006. Recorded liabilities exceeding liabilities determined by rescheduling agreements were cancelled crediting income – Note 14. As of 31 December 2006 liabilities in respect of loans from International Bank for Reconstruction and Development 2338-5 and 2338-7 were disclosed as liabilities towards Elektroprivreda Srbije, under Other long-term liabilities. It is expected loan from International Bank for Reconstruction and Development 2338-6 to be rescheduled soon and transferred from liabilities towards Elektroprivreda Srbije to liabilities towards Government of the Republic of Serbia – Deposit Insurance Agency.

Loan Kapital Hilfe – Vojvodjanska banka has been rescheduled during the year ended 31 December 2006 resulting in higher liabilities then recorded ones in the amount of RSD 160,638 thousand which was recorded by charging expenses – Note 14.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

26. Long-term loans (continued)

Other loans

On 8 September 2005 Serbia and Montenegro and International Association for Development signed 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). The loan is to be repaid in the period from 2015 to 2025. The Company has not withdrawn any amount in respect of this loan.

27. Other long-term liabilities

Other long-term liabilities as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Liabilities towards Elektroprivreda Srbije for long-term loans	2,005,687	2,840,203
Liabilities towards the Government of the Republic of Serbia for rescheduled duties	48,538	49,699
Other long-term liabilities	793	853
	<u>2,055,018</u>	<u>2,890,755</u>
Current maturity of long-term loans to Elektroprivreda Srbije – Note 28	(807,832)	(633,072)
Current maturity to the Government of the Republic of Serbia - Note 28	(4,455)	(2,158)
Current portion of other long-term liabilities - Note 28	(553)	(845)
	<u>1,242,178</u>	<u>2,254,680</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

27. Other long-term liabilities (continued)

Liabilities towards JP Elektroprivreda Srbije relate to the portion of long-term loans used by the Company. These liabilities relate to the loans granted by the following banks:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
European Bank for Reconstruction and Development 1	934,180	130,765
Export-Import Bank of China	803,431	967,440
International Bank for Reconstruction and Development - portion 2338 – 6	255,068	276,054
European Investment Bank	13,008	-
International Bank for Reconstruction and Development - portion 2338 – 5	-	1,139,988
International Bank for Reconstruction and Development - portion 2338 – 7	-	325,956
	2,005,687	2,840,203

The liabilities towards Elektroprivreda Srbije regarding the loan granted by the European Bank for Reconstruction and Development 1 relate to the unused part of the loan in respect of the Loan Agreement signed on 25 October 2001 by EPS and the Bank for the purpose of realization urgent reconstruction project in the energy power sector. The total amount of the granted loan is EUR 100,000,000 out of which the Company should use the amount of EUR 60,400,000. The loan should be repaid in six-month instalments from 7 September 2005 to 7 March 2016. The interest rate is variable.

Liabilities for the loan granted by Export-Import bank of China relate to the portion of this loan used for the needs of the Company. The Company settles its liabilities towards Elektroprivreda Srbije in the same manner as the latter mentioned settles its own.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

28. Short-term financial liabilities

Short-term financial liabilities as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i> <i>RSD'000</i>	<i>31.12.2005.</i> <i>RSD'000</i>
• International Bank for Reconstruction and Development - 2338 -5	37,396	-
• Kapital Hilfe - Investbanka a.d. Beograd	12,460	-
• International Bank for Reconstruction and Development - 2338 -7	10,693	-
• International Bank for Reconstruction and Development – 14695	4,436	4,926
• Kapital Hilfe - Vojvodjanska banka a.d. Novi Sad	2,941	674,677
<i>Current maturity of long-term loans - Note 25</i>	<u>67,926</u>	<u>679,603</u>
• Export-Import bank of China	642,745	580,464
• International Bank for Reconstruction and Development – 1	145,247	-
• International Bank for Reconstruction and Development - 2338 -6	15,355	8,337
• European Investment Bank	4,485	-
• International Bank for Reconstruction and Development – 2338 -5	-	34,427
• International Bank for Reconstruction and Development – 2338 -7	-	9,844
<i>Current maturity of liabilities towards EPS - Note 26</i>	<u>807,832</u>	<u>633,072</u>
Current maturity of liabilities towards the Government of the Republic of Serbia	4,455	2,158
Other short-term financial liabilities	553	845
	<u>880,766</u>	<u>1,315,678</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

29. Operating liabilities

Operating liabilities as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Advances received	71,026	86,275
Domestic trade creditors	93,225	72,217
Foreign trade creditors	397	-
Other operating liabilities	518,585	298,226
	683,233	456,718

The biggest portion of other operating liabilities as of 31 December 2006 in the amount of RSD 517,793 thousand (RSD 228,544 thousand as of 31 December 2005) relates to the liabilities towards Elektroprivreda Srbije in respect of delivered equipment by the supplier for the realization of the urgent reconstruction project in the sector of energy industry, financed by the loan of European Bank for Reconstruction and Development, as well as other costs of purchase and purchases financed from European Investment Bank loan.

30. Other short-term liabilities and accruals

Other short-term liabilities and accruals as of 31 December 2006 and 31 December 2005 relate to the following:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Deferred income from received donations	1,791,721	1,745,760
Interest payable	323,875	748,206
Liabilities for salaries and compensations	168,327	60,958
Accrued liabilities	128,613	30,125
Other liabilities	10,175	6,504
<i>Other short-term liabilities and accruals, gross</i>	2,422,711	2,591,553
Amortization of deferred income from received donations	(383,189)	(299,302)
<i>Other short-term liabilities and accruals, net</i>	2,039,522	2,292,251

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

30. Other short-term liabilities and accruals (continued)

Movements in donations received during the years ended 31 December 2006 and 31 December 2005 were as follows:

<i>RSD'000</i>	<i>Gross Value</i>	<i>Depreciation</i>	<i>Net value</i>
As of 1 January 2005	1,597,654	(226,624)	1,371,030
Donation in kinds	146,528	-	146,528
Other donations	5,791	-	5,791
Release to income statement - Note 4	(4,213)	(71,403)	(75,616)
Other	-	(1,275)	(1,275)
As of 31 December 2005	1,745,760	(299,302)	1,446,458
Donation in kinds	25,961	-	25,961
Other donations	20,000	-	20,000
Release to income statement - Note 4	-	(83,956)	(83,956)
Other	-	69	69
As of 31 December 2006	1,791,721	(383,189)	1,408,532

The amortization of received donations relates to the proportional part of the depreciation of fixed assets and used material from the donations.

Interest payable as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Kapital Hilfe – Vojvodjanska banka	-	97,329
International Bank for Reconstruction and Development	-	28,496
European Investment Bank	-	25,126
Interest for long-term loans - Note 25	-	150,951
Liabilities towards EPS - International Bank for Reconstruction and Development	56,581	317,116
Liabilities towards EPS - Export-Import Bank of China	266,305	279,151
Interest for other long-term liabilities - Note 26	322,886	596,267
Other interest payable	989	988
	323,875	748,206

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
For the year ended 31 December 2006

31. Taxes payable

Taxes payable as of 31 December 2006 and 31 December 2005 consist of the following:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Value added tax	45,289	77,841
Fee for city land usage	26,850	-
Other taxes payable	9,788	2,500
	<u>81,927</u>	<u>80,341</u>

32. Off-balance sheet items

Off-balance sheet as of 31 December 2006 and 31 December 2005 can be further analysed as follows:

	<i>31.12.2006.</i>	<i>31.12.2005.</i>
	<i>RSD'000</i>	<i>RSD'000</i>
Written-off estimated war damage	5,715,521	6,185,785
Received notes and guarantees	265,137	-
Written-off investments in banks in bankruptcy	48,974	48,974
Rented equipment	36,952	36,952
Other off-balance sheet	11,490	1,727
	<u>6,078,074</u>	<u>6,273,438</u>

Estimated war damage as of 31 December 2006 and 31 December 2005 entirely relates to the damage estimated in the amount of EUR 7,235 thousand caused by NATO bombing of electric-power buildings.

33. Commitments and contingencies

Capital commitments

As of 31 December 2006 the Company has concluded major contracts for construction and purchases of plant and equipment amounting to approximately EUR 62 millions, out of which part of purchases amounting to approximately EUR 25 millions have been completed. Purchases of equipment are mainly financed through loans from European Bank for Reconstruction and Development and European Investment Bank.

Legal cases

As stated in Note 25, as of 31 December 2006 the Company made provisions for legal proceedings initiated against the Company in the amount of RSD 89,624 thousand. As of 31 December 2006 the total amount of legal proceedings against the Company amounts to RSD 91,405 thousand, plus accrued interest until the date of the proceedings settlement that is by the date of payments according to the proceedings. The Company's management is of the opinion that on the basis of legal proceeding exceeding already created provision cannot cause materially negative consequences for the Company.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006

33. Commitments and contingencies (continued)

Financial Instruments

Interest rate risk

The Company's exposure to market risk for changes in interest rates relates primarily to long-term loans. The Company does not use interest rate swaps to hedge its risks associated with interest rate fluctuations.

Foreign currency risk

The Company is exposed to the risk associated to foreign currency fluctuations due to liabilities arising from foreign currency loans. The Company does not use any instruments to hedge its risks associated with foreign currency fluctuations.

Credit risk

The extent of the Company's credit exposure is represented by the aggregate balance of trade and other receivables (as they appear on the balance sheet). Trade receivables mostly relate to receivables from JP Elektroprivreda Srbije.

Fair value risk

Financial assets and liabilities should be recognized on the balance sheet and subsequent to initial measurement at cost; they should be remeasured to its fair value. The fair value of financial instruments is determined with reference to relevant market information, where appropriate. At 31 December 2006, management believes that the fair values of financial assets and liabilities held by the Company did not differ materially from their recorded values in these financial statements.