Annual Report of HSE d.o.o. and HSE Group

2006

hse

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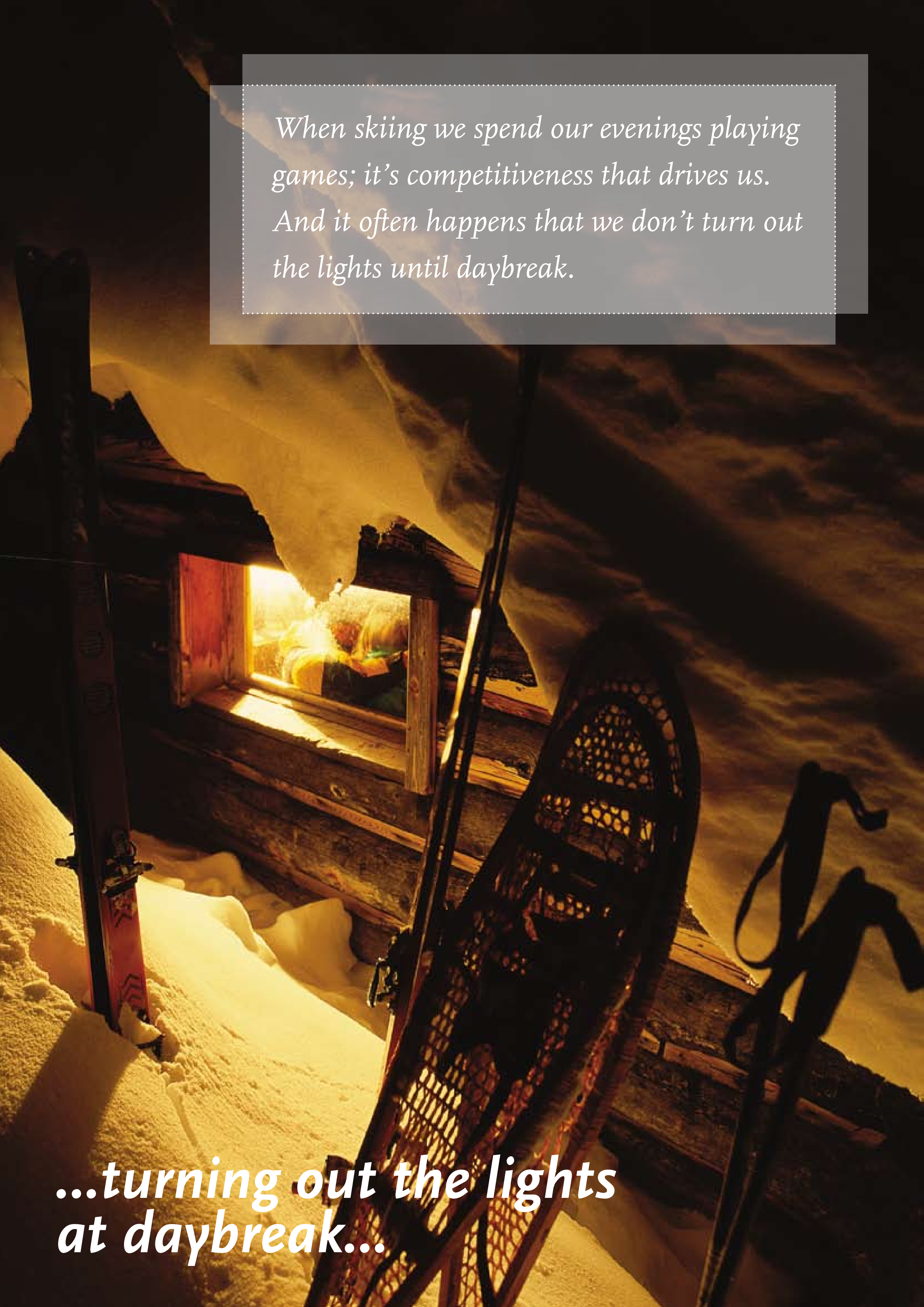
2006

CONTENTS

When skiing we spend our evenings playing games; it's competitiveness that drives us. And it often happens that we don't turn out the lights until daybreak.



...turning out the lights at daybreak...

1

Introduction

2006

1.1 KEY DATA

In 2006, the operation of the HSE Group was successful and the objectives set were achieved and even exceeded.

Also in the year 2006, HSE kept the position of the main producer and trader in electrical energy in Slovenia and took care of its safe and reliable supply at competitive prices. The trading quantities have still increased and the presence on foreign markets has significantly increased.

The year 2006 was marked by the opening of the Boštanj Hydropower Plant, the first one in the chain of new hydropower plants on the lower Sava River.

The operating result of HSE d.o.o. and the HSE Group was better than in the previous year and better than budgeted for the year 2006.

HSE Group

	2006	2005	IND06/05
Net sales in 000 SIT	201,792,229	158,476,894	127
Revenues in 000 SIT	210,606,075	167,080,602	126
EBIT in 000 SIT	22,385,851	14,992,091	149
EBITDA in 000 SIT	40,802,932	32,697,674	125
Net profit in 000 SIT	18,607,594	14,414,704	129
Assets in 000 SIT	373,441,091	357,853,560	104
Equity in 000 SIT	279,633,944	250,744,708	112
Cash flows from operating activities in 000 SIT	37,479,789	30,151,140	124
Added value in 000 SIT	72,724,689	64,877,227	112
Electric energy produced (in GWh)	6,961	6,771	103
Electric energy sold (in GWh)	16,088	14,364	112
Number of employees as at 31st Dec	4,316	4,899	88
Number of group companies as at 31st Dec	27	24	113

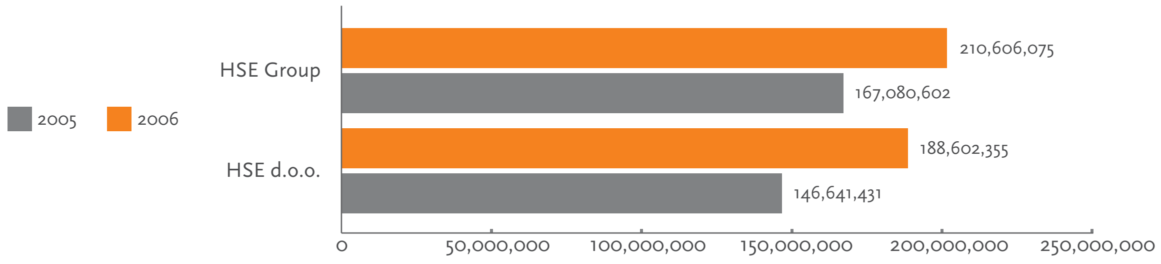
HSE Company d.o.o.

	2006	2005	IND06/05
Net sales in 000 SIT	188,191,375	146,067,922	129
Revenues in 000 SIT	188,602,355	146,641,431	129
EBIT in 000 SIT	12,042,273	7,022,273	171
EBITDA in 000 SIT	12,396,344	7,229,549	171
Net profit in 000 SIT	8,651,076	7,034,166	123
Assets in 000 SIT	260,563,063	256,902,085	101
Equity in 000 SIT	202,926,629	213,457,106	95
Cash flows from operating activities in 000 SIT	16,370,829	8,447,482	194
Added value in 000 SIT	13,604,692	8,317,904	164
Electric energy sold (in GWh)	16,318	14,645	111
Number of employees as at 31st Dec	97	90	108

1.2 FINANCIAL HIGHLIGHTS

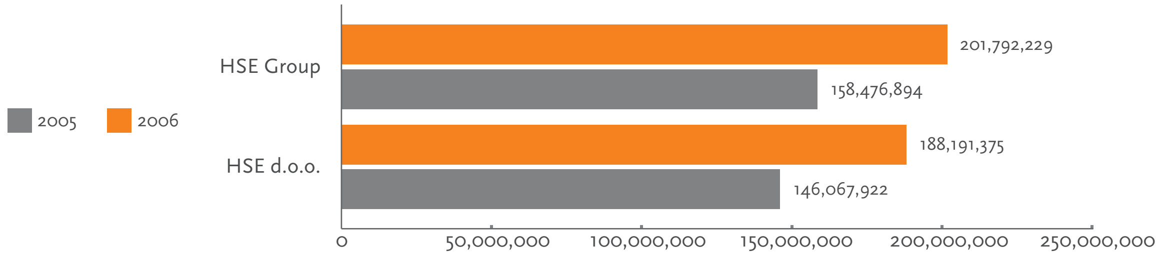
Total revenues

in 000 SIT



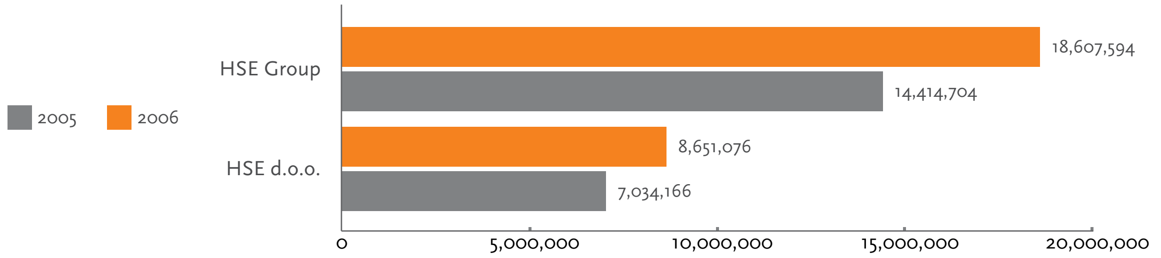
Net sales

in 000 SIT



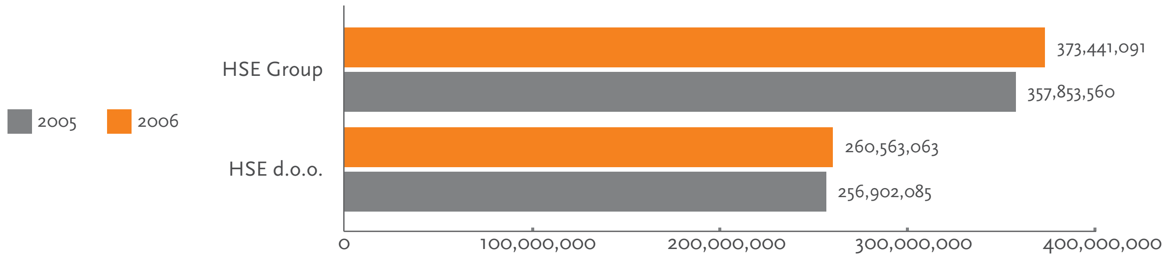
Net profit

in 000 SIT



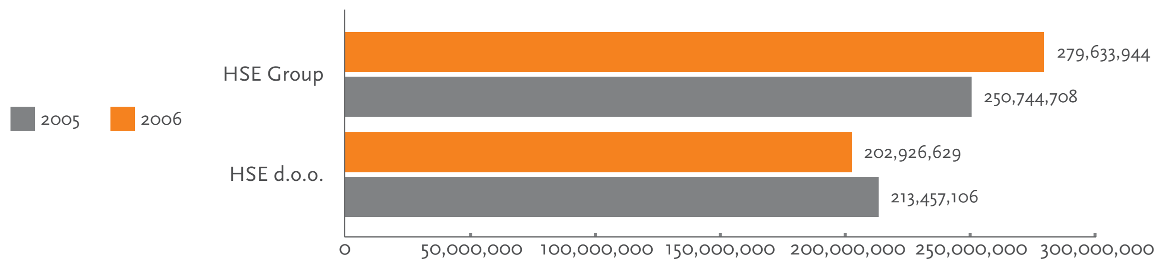
Balance sheet total

in 000 SIT



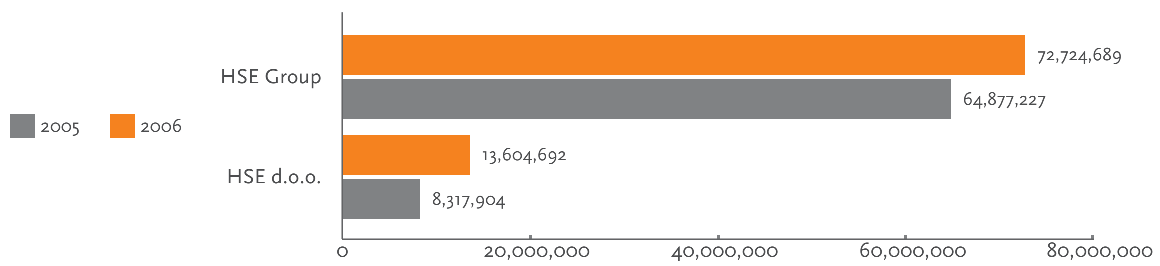
Equity

in 000 SIT



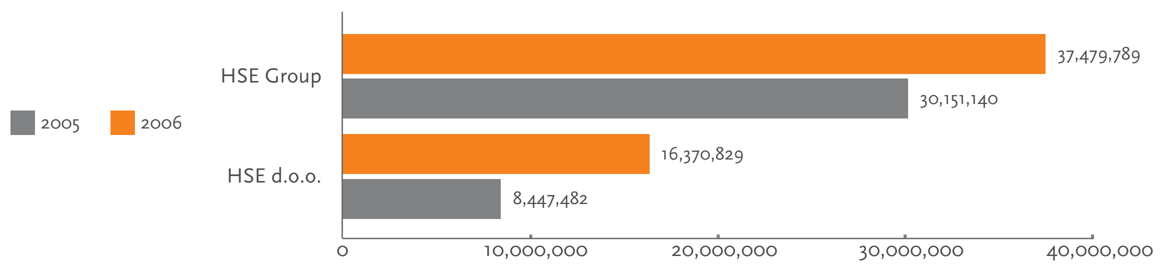
Added value

in 000 SIT



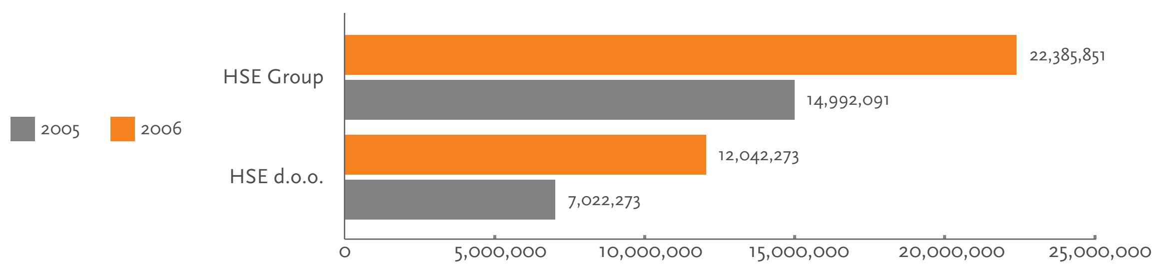
Cash flows from operating activities

in 000 SIT



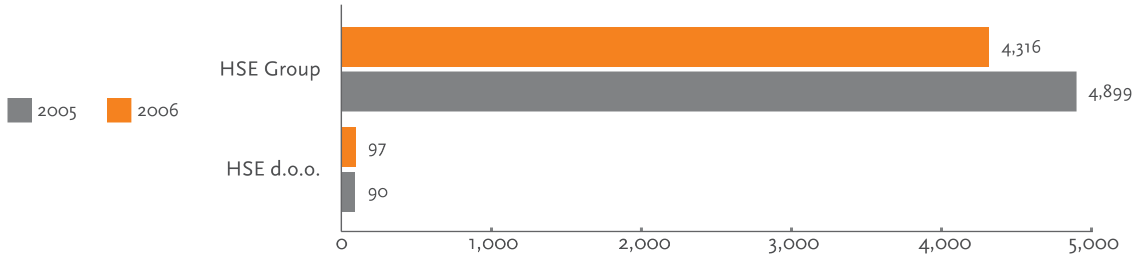
EBIT

in 000 SIT



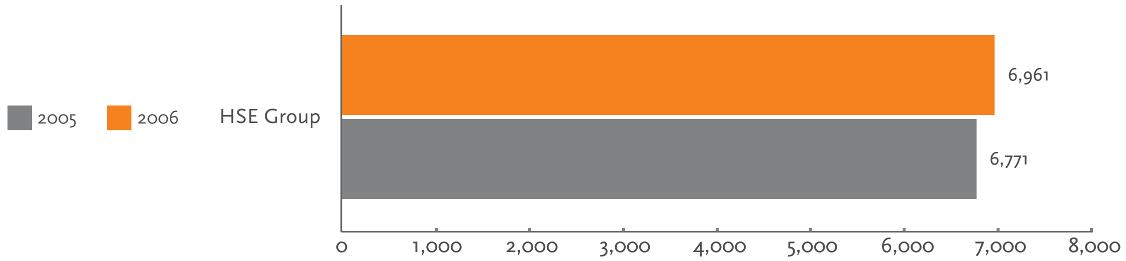
1.3 OTHER HIGHLIGHTS

Employees



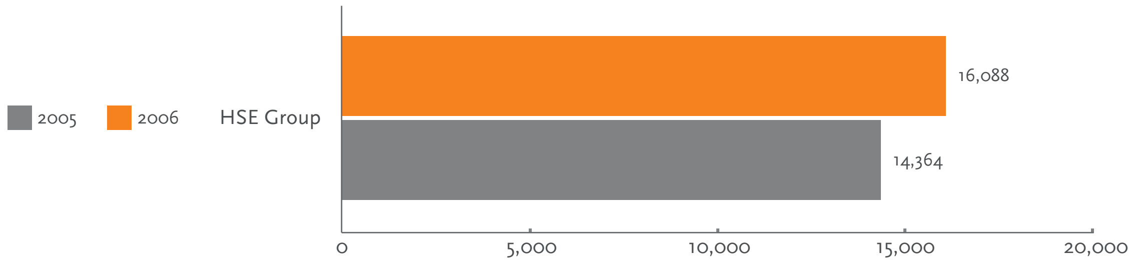
Production of group companies

in GWh



Sale of electric energy by HSE group

in GWh



1.4 STATEMENT ON THE MANAGEMENT OF HSE

Statement on the management of HSE

Pursuant to the provisions of Point 5 of Art. 70 of the Companies Act I, as the General Manager of HSE declare that the management of the Company has been carried out in accordance with the valid legal standards, Articles of Incorporation of the limited liability company Holding Slovenske elektrarne d.o.o. that the Republic of Slovenia as the founder and sole shareholder of Holding Slovenske elektrarne d.o.o. adopted on 14 February 2005 and in compliance with due professional care.

Under the Articles of Incorporation the management has been conducted directly through the founder and bodies of the Company, such as the Supervisory Board and the General Manager.

Founder

The founder independently decides on the following issues:

- changes and amendments to the Articles of Incorporation of HSE d.o.o.,
- adoption of the bases of business policy and Development Plan of HSE d.o.o.,
- adoption of the annual report, when the Supervisory Board has not approved it and when the General Manager and the Supervisory Board leave the resolution on the adoption of the annual report to the general meeting,
- use of accumulated profit,
- discharge given to the General Manager and the Supervisory Board,
- distribution and elimination of business shares,
- changes in the original capital of HSE,
- status changes and dissolution of the company,
- election and discharge of the members of the Supervisory Board of HSE,
- appointment of an auditor,
- appointment of the Assistant Vice-President and other authorised persons and
- other issues under the regulations and Articles of Incorporation.

Pursuant to Art. 526 of the Companies Act the founder enters its resolutions in the book of resolutions.

Supervisory Board

The Supervisory Board consists of 9 members; i.e. 6 members who represent the interests of the owner and are appointed and discharged by the owner and 3 members who represent the interests of employees and are appointed under the Act Regulating Workers' Participation in Management. Members of the Supervisory Board are appointed for a term of four years and can be re-appointed. Pursuant to the Articles of Incorporation the Supervisory Board is competent for the following issues:

- supervision over the management of the company,
- review of the structure of the annual report and proposal for the use of the accumulated profit,
- drawing-up a report on the results of the review of the annual report to be submitted to the general meeting,
- approval of the annual report or making remarks to it,
- expression of opinion on the bases of business policy and the Development Plan of HSE,

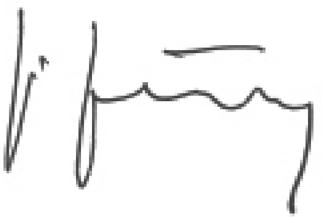
- agreement with the business plan of the company,
- proposal of resolutions for approval to the founder from its area of competence or expression of an opinion on the proposals of the General Manager to be accepted by the founder,
- appointment and removal of a general manager,
- conclusion of employment contract with the general manager,
- agreement with the General Manager about decision-taking at general meetings of subsidiaries in case of changes in the status or capital,
- adoption of the rules of procedure relating to the work of the Supervisory Board and
- possible request for a report on other issues.

The Supervisory Board can perform also other tasks in accordance with the regulations, documents of HSE and resolutions of the founder.

General Manager

The General Manager runs HSE and is appointed by the Supervisory Board on the basis of the contract notice for a term of 4 years. After the expiry of the term, the General Manager can be re-appointed. In accordance with the provision of the Companies Act the General Manager represents HSE independently and without limitations and is responsible for the conduct of business.

Holding Slovenske elektrarne d.o.o. follows no special code in its operation.



Jože Zagožen, D.Sc.
General Manager of HSE

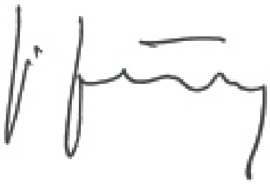
Ljubljana, 23 March 2007

1.5 LETTER BY THE GENERAL MANAGER

There are no limits for the energetic

The title of this years' introduction to the Annual Report is also the keynote of the corporate advertisement. It includes a picture of a tree whose branches overhang the top edge of the advertisement, and the pot it grows in breaks into small pieces due to its sudden expansion. Symbolism is simple: a tree cannot be limited; no one can prevent it from growing. In height and width. And HSE likes to identify with such »healthy« trees, as every company. This situation mainly applies to the year 2006 which can be described as the year of growth. Many important events occurred in the year that ended and made adequate provisions for the year 2007. The majority of events that took place marked our operation and contributed to the growth of HSE d.o.o. and the HSE Group. The Group grew and four new "members" were integrated into it in the year 2006: subsidiaries in Belgrade, Zagreb and Budapest and a branch office in Prague. Our business decisions relating to new investments and development projects that will - directly or indirectly - contribute to the assurance safe and reliable supply of electrical energy to our customers, were carried out in accordance with the goals set and the plans confirmed. In May, the first hydropower plant was opened in the chain of five new hydropower plants on the lower Sava River, the hardly expected Boštanj Hydropower Plant and the construction of the following four has continued. The implementation of the strategically extremely important Slovene energy project, i.e. the construction of the new 600 MW generator in Šoštanj Thermal Power Plant has already started and the preparations or initial project stages, such as the construction of Avče, the first pumped storage plant, and a chain of hydropower plants on the central Sava River have continued. Simultaneously, we have also studied the possibility of additional projects that would contribute to a high degree of self-supply of Slovenia with electrical energy when their feasibility and economic viability have been confirmed. The self-supply has constantly decreased due to a constant increase in consumption. Thus several promising agreements over the Slovene borders, exactly in the region of southeastern Europe, marked the year 2006 and HSE has asserted as a strategically important and reliable business partner. Republika Srbska, Kosovo, Serbia, Montenegro and Bulgaria are the markets where HSE has started appearing with its expertise and experience, but mainly with many good ideas and plans. Some important steps have been made which are necessary for successful penetration and thus the assumption of an active role in southeastern Europe.

In 2006, the HSE Group put a great deal of effort in the environmental protection and expansion of environmental awareness not only among producers, but also among the wide Slovene public. The promotion of "blue energy", the most relevant product in the area of renewable energy sources (by the way, last year the blue energy celebrated its thousandth customer) and the encouragement of economical use of energy that has been provided by the first informative education campaign in Slovenia - represented the major part of these activities. The campaign met with a wide response, as reflected in the advertising efficiency surveys. The majority of people who observed our advertisements thought about their implicit approach to the use of electrical energy for a moment at least. And sometimes a moment is enough. It may be a crucial one. It may mean a difference, it may bring about changes. Moments were decisive in history and wrote memories. We, at HSE would like that moments writing our history and memories would be as nice and useful as possible. We believe there were many such moments in the year 2006 and wish there will be many in the coming year. We will have to face serious challenges. By means of knowledge, experience and mostly good will, courage and commitment we will try to overcome the difficulties and show that there are no limits for energetic people. For the benefit of our employees, customers, owners and business partners. To the benefit of all I thank here sincerely for their contribution to good business results.



Jože Zagožen, D.Sc.
General Manager of HSE

1.6 REPORT OF THE SUPERVISORY BOARD

Pursuant to provisions of Art. 282 of the Companies Act the Supervisory Board of Holding Slovenske elektrarne d.o.o. informs the general meeting by this report about the following issues:

- the method and scope of reviewing the management of HSE during the financial year 2006,
- verification and approval of the Annual Report of HSE d.o.o. and the HSE Group,
- verification of the proposal for the use of accumulated profit,
- aspect of the Supervisory Board relating to the audit report.

The following members participated in the Supervisory Board of Holding Slovenske elektrarne d.o.o. as capital representatives in the year 2006: Andrej Vizjak, M.Sc. (Chairman), Andrej Aplenc, M.Sc. (Vice-Chairman), Franc Križanič D.Sc., Franc Bogovič, Franc Ervin Janežič, Janez Požar. Employee representatives were until 6 April 2006: Janez Keržan M.Sc., Branko Sevčnikar and Pavel Županc. Pavel Županc was discharged in the 12th session of the workers' council of HSE held on 6 April 2006 and Miran Božič was appointed an employee representative in the Supervisory Board instead of him.

In the 2nd regular session of the workers' council of HSE held on 12 September 2006 Janez Keržan, M.Sc. was discharged and Boštjan Jančar was appointed an employee representative in the Supervisory Board instead of him. In the period from 17 September 2006 to the end of the year the Supervisory Board included:

- capital representatives: Andrej Vizjak, M.Sc. (Chairman), Andrej Aplenc, M.Sc. (Vice-Chairman), Franc Križanič, D.Sc., Franc Bogovič, Franc Ervin Janežič, Janez Požar,
- employee representatives: Branko Sevčnikar, Miran Božič and Boštjan Jančar.

1.6.1 MONITORING AND SUPERVISION OF HSE OPERATIONS

In 2006, the Supervisory Board monitored and supervised the operation of HSE, the parent company of the HSE Group, within the legally defined powers and competence and in line with the Articles of Incorporation.

In total seven regular sessions the Supervisory Board discussed strategic issues as well as some other important operative matters and areas relating to the operations of HSE.

In its first regular session in the year 2006 held on 15 March 2006, the Supervisory Board was informed about the temporary non-audited financial report of HSE d.o.o. for the year 2005 and agreed with the proposal of the General Manager about the allocation of the half of net profit of the year 2005 to other revenue reserves. Simultaneously it was also informed about the planned appropriation of net profits or losses of the year 2005 in the companies within the HSE Group, about the operation of HSE in the first months of the year 2006, possibilities of investments in the markets of southeastern Europe, about the purchase of minority shares in TEB d.o.o. and TEŠ d.o.o., and the course of construction of the hydropower plant on the lower Sava River as well as starting points for the appointment of an audit committee within the Supervisory Board.

The Supervisory Board discussed and approved the Annual Report of HSE d.o.o. and the HSE Group for the year 2005 including the audit report in its 2nd session held on 9 June 2006. Then, it also adopted the view about the audit report and supported the endeavours of the General Manager about the use of the accumulated profit. During the session, the Board was also informed about the proposal of the Development Plan of the HSE Group 2006 / 2015 with a view to the year 2025 and the sales procedure of the equity investment of HSE d.o.o. in TDR-Metalurgija d.o.o. It appointed an audit committee with four members: France Križanič, D.Sc. as the Chairman of the committee and Andrej Aplenc, M.Sc. and Branko Sevčnikar as the members. The Supervisory Board also decided that that the audit committee shall select its fourth external member.

In its third regular session held on 4 July 2006 the Supervisory Board appointed the fourth member of the committee - Alenka Podbevšek - in accordance with the proposal of the audit committee and adopted an outline plan of the work of the audit committee. The Supervisory Board and the General Manager proposed the adoption of the resolution on the information about the annual report of HSE d.o.o. and the HSE Group and the audit report, on the use of accumulated profit and discharge given to the General Manager, approval and adoption of the Development Plan of the HSE Group 2006 / 2015 with a view to the year 2025, on the appointment of the audit company for auditing of financial statements and the Annual Report of HSE d.o.o. and the HSE Group for the financial years 2007 and 2008 as well as on the determination of meeting fees for the members of the audit committee within the Supervisory Board. At the same time, it was informed about the topical projects.

The Supervisory Board discussed the report on the operation of HSE d.o.o. and the HSE Group in the period January - June 2006 and alternative resolutions relating to the investment of HSE d.o.o. in TDR-Metalurgija d.d. in its third regular session held on 8 September 2006. It was also informed about the preparation of the 4th strategic conference of the HSE Group and the information about the up-to-date events relating to strategic orientation of the Government of the Republic of Slovenia concerning privatisation of the Slovene electrical energy industry.

An agreement to the sale of the interest of HSE d.o.o. in TDR-Metalurgija d.d. was given by the Supervisory Board in its fifth regular session held on 27 October 2006. At that time, the Supervisory Board was also informed about the investment programme relating to the construction of the Krško Hydopower Plant and erection of generator no. 6 in the Šoštanj Thermal Power Plant. The information about the events in the Boštanj Hydropower Plant and conclusions of the 4th strategic conference of the HSE Group were given in the fifth session.

The Supervisory Board discussed contracts for the supply of electrical energy to distribution companies in the year 2007 in its 6 regular session held on 1 December 2006. During this session it was also informed about the report on the operation of HSE d.o.o. and the HSE Group in the period January - September 2006, adopted the Rebalanced Business Plan of HSE d.o.o. for the year 2006 and was informed about the summaries of Rebalanced Business Plans for the year 2006 of the HSE Group companies. It took note also of the resolution of the Government of the Republic of Slovenia relating to the transfer of equity investments, transfer of investment of HSE to the joint venture - i.e. a newly established company and the course of activities in southeastern Europe.

The objectives of the operation of HSE d.o.o. and the complete HSE Group for the year 2007 were set in the Business Plan that the Supervisory Board adopted in its last session in 2006 held on 20 December 2006 when it presented also summaries of business plans of the HSE Group companies for the year 2007.

The audit committee of the Supervisory Board in HSE held six sessions in the year 2006 and discussed legally defined areas as well as issues and the areas for which it is responsible in line with the special resolutions of the Supervisory Board.

The work of the Supervisory Board and the audit committee was very extensive in the year 2006, since HSE d.o.o. formulated a strategy of intensive appearance on the market. On the basis of quality and correct reports, analyses, and oral information as well as additional material prepared due to special requests of the Supervisory Board expressed in individual sessions the Supervisory Board got an insight in all key areas of the operation.

1.6.2 VERIFICATION OF THE ANNUAL REPORT AND VIEW ON THE AUDIT REPORT

On 6 April 2007, the General Manager of HSE submitted the audited annual report of HSE d.o.o. and the HSE Group to the Supervisory Board of HSE for its approval. The Supervisory Board discussed the Annual Report of HSE d.o.o. and the HSE Group for the year 2006 including audit reports and the proposal of the General Manager to be submitted to the owner about the use of accumulated profit in its 14th regular session held on 9 May 2007.

KPMG Slovenija, d.o.o. conducted the audit of financial statements of HSE d.o.o. and the HSE Group and the examination of conformity of the business report of HSE d.o.o. and the HSE Group for the year 2006.

In accordance with the opinion of the auditor of 30 March 2007 the financial statements of HSE d.o.o. and the HSE Group give a true and fair view of the financial position of HSE d.o.o. and the Group in all material respects as of 31 December 2006 and of their profit or loss and cash flows for the year then ended in compliance with the Slovene Accounting Standards. The business report complies with the audited financial statements.

In the fifth regular session in June 2006 the Supervisory Board of HSE d.o.o. and the HSE Group appointed the audit committee for the assurance of better transparency of the operation of HSE d.o.o. and the HSE Group. On 23 April 2007 the committee reviewed and checked the bases for the Annual Report. After the review of the bases for the Annual Report the audit committee has no remarks and recommends to the Supervisory Board that it should adopt the Annual Report of HSE d.o.o. and the HSE Group for the year 2006.

On the basis of the review of audit reports, assessment of the audit committee within the Supervisory Board, and on the basis of the explanations given during the session of the Supervisory Board, the Supervisory Board of HSE had no remarks to the audit reports. Based on the regular monitoring of operation of HSE d.o.o., unqualified audit opinions, good operating result of HSE d.o.o. and the HSE Group, the achieved objectives set in the Business Plan for the year 2006 and in line with its competence the Supervisory Board of HSE has no remarks and approves the Annual Report of HSE d.o.o. and the HSE Group for the year 2006 after the final review.

1.6.3 ESTABLISHMENT AND PROPOSAL FOR THE USE OF ACCUMULATED PROFIT

Holding Slovenske elektrarne d.o.o. ended the financial year 2006 by net profit amounting to SIT 8,651,076,385.26. Under the provisions of the Companies Act and while preparing the financial statements part of profit amounting to SIT 71,145,014.48 was used for covering of loss from previous periods that the company presented due to transition to the new Slovene Accounting Standards (SAS 2006).

In its 12th regular session held on 29 March 2007, the Supervisory Board agreed with the proposal of the General Manager that half of the remaining net profit amounting to SIT 4,289,965,685.39 should be used for the formation of other revenue reserves already during the preparation of financial statements for the year 2006.

The remaining net profit is the accumulated profit of the year 2006 amounting to SIT 4,289,965,685.39.

Pursuant to strategic objectives and the investment policy the Supervisory Board of HSE agrees with the proposal of the General Manager submitted to the owner that the accumulated profit amounting to SIT 4,289,965,685.39 or EUR 17,901,709.59 should be in its total amount used for the formation of other revenue reserves. Further on, the Supervisory Board proposes to the general meeting that it should give a discharge to the management board for the operation in the year 2006.

The Supervisory Board of HSE prepared the report in compliance with Art. 282 of the Companies Act. The report of the Supervisory Board is intended for the general meeting of HSE d.o.o.

Andrej Aplenc, M. Sc.
Vice-Chairman of the Supervisory Board of Holding Slovenske elektrarne d.o.o.

Ljubljana, 9 May 2007

Supplement/Amendment to the Report of the Supervisory Board

In the 17th regular session of the Supervisory Board of Holding Slovenske elektrarne d.o.o. held on 11 July 2007, the Resolution adopted by the Supervisory Board on 9 May 2007 was amended and consent was expressed by the Supervisory Board to the Management's proposal for the use the accumulated profit of HSE for 2006 in the amount of 4,289,965,685.39 SIT or 17,901,709.59 EUR so that the first half of the total amount be paid out to the shareholder (8,950,854.79 EUR) and the second half be used for the formation of other revenue reserves (8,950,854.80 EUR).

With the exception of the issue presented in the previous paragraph, no parts of the Report of the Supervisory Board of HSE dated 9 May 2007 have been changed.

Andrej Aplenc, M. Sc.
Vice-Chairman of the Supervisory Board of Holding Slovenske elektrarne d.o.o.

Ljubljana, 11. July 2007

1.7 SIGNIFICANT EVENTS IN THE HSE GROUP IN THE YEAR 2006

January

- Election of the new Supervisory Board of TEB.
- Beginning of discussion of the draft Development Plan of PV (the Velenje Coal Mine) for the period 2006 - 2011. Among others, the Plan foresees the coal price to the year 2011 amounting to 2.25 €/GJ and 1,400 employees as well as prolongation of the useful life of the coal mine to the year 2040. The Development Plan foresees also intensive privatisations of subsidiaries.
- When HSE has purchased shares of majority shareholders, it has become the only shareholder in TEB and TEŠ.

February

- Presentation of some most important Slovene investors was organised in Belgrade on the initiative of HSE and in co-operation with the Embassy of Slovenia in Serbia and Montenegro and in the wide area of southeastern Europe. Representatives of the leading Slovene companies in the area of energy industry, transport, civil engineering, trade and tourism presented their plans and readiness for investments.
- DEM organised the first spatial conference for the Kozjak Pumped Storage Plant, which should implement the idea of a pumped storage plant on the Drava River: The first spatial conference on the state detailed plan of a pumped storage plant on the Drava River and the over-head power line connection between the pumped storage plant and RTP Maribor held on 6 February marked the beginning of the procedure of the state detailed plan in the Office for Spatial Development within the Ministry of the Environment and Spatial Planning.
- The inspectorate of the Republic of Slovenia for energy conducted an inspection of the last restored generator in the Medvode Hydropower Plant in SEL and on the following day the first drilling with water flush was carried out in this hydropower plant.
- In its 4th regular session, the Supervisory Board of SEL re-appointed Drago Polak the present managing director of the company for a term of four years.
- For SENG, a loan agreement with the European Investment Bank was signed for the financing of Avče Pumped Storage Plant, the first pumped storage plant in Slovenia in the amount of 43 million EUR and the guarantee agreements for the security of this loan with Bank Austria Creditanstalt, trade union of banks and HSE.

March

- A new business establishment of HSE Invest was opened in Velenje.
- Three ministers visited the Boštanj Hydropower Plant during their visit to Posavje.
- A partial restoration of the command systems of the Formin Hydropower Plant was carried out in DEM; it was urgent from the aspect of assurance of reliable operation of individual generators of the power plant and the power plant as a unit until the planned reconstruction of the hydropower plant.

April

- The Minister of Economy Andrej Vizjak stopped in DEM for a short working visit. The management of the company informed him about the implementation of topical development projects.
- The started regular annual revision of the fourth gas generator was completed in TEB without any complications.
- There was 530,000 tons of coal on the disposal facility of the Velenje Coal Mine which is the top limit for the control of the disposal facility.

May

- On 27 May 2006 the first hydropower plant was opened in the chain of five new hydropower plants on the lower Sava River, i.e. Boštanj Hydropower Plant that can produce 115 GWh of electrical energy in a year on average.
- DEM set the production record; on 22 May the highest daily production in the year 2006 was achieved: 13,783 MWh or DEM generated 38.5 % of total Slovene consumption of the day (35,793 MWh). All generators on the Drava River operated at full power on that day.
- TEŠ celebrated the 50^{th} anniversary of the power plant operation. This jubilee was celebrated by the presentation of the book 50 years of light for Slovenia. On this occasion funds were donated to the hospital Topolščica and the municipality Šoštanj. An open-door day was organised.
- The revision of the fifth TEB gas turbine with the power of 14 MW was successfully completed.
- The Supervisory Board of TEB appointed Bogdan Barbič the managing director of the company for a term of four years.
- From the second half of the year 2005 to May 2006 the record average quality of coal was established in the Velenje Coal Mine - 11,672 KJ/kg.

June

- The Energy Agency of the Republic of Serbia festively granted the first seven licences for rendering of energy services in Serbia. HSE was among the first companies that acquired the licence; it obtained it through its subsidiary HSE Balkan Energy. Licence No. is 01/06-LE-10 which means it is the first company entered in the register of licences for trading in electrical energy in Serbia.
- PV Invest started operating; it is engaged in landscaping, geodetic services, etc., it should also offer 500 new jobs in the following years. Twenty employees from various departments of the Velenje Coal Mine have been transferred to the company.
- In its 5^{th} regular session the Supervisory Board of HSE approved the Annual Report of Holding Slovenske elektrarne d.o.o. and the HSE Group for the year 2005. It also appointed a four-member audit committee chaired by France Križanič, D.Sc., Andrej Aplenc, M.Sc. and Branko Sevčnikar as the members and Ms Alenka Podbevšek as an independent expert in accounting and finance area.
- The tender committee for the privatisation of the thermal power plant and the Plevlja mine in Montenegro published the proposal of the ranked list of bidders where HSE won the second place.
- Beginning of trial operation of the Boštanj Hydropower Plant.

July

- Jože Zagožen, D.Sc., the General Manager of HSE signed an agreement on long-term business and technical co-operation with Elektroprivreda of Republika Srbska (EPRS) in Banja Luka. The agreement signed in the presence of the Minister of Economy of the Republic of Serbia Milan Jelič, D.Sc., foresees co-operation between HSE and EPRS in the construction of a new 600 MW generator in the Ugljevik Thermal Power Plant, restoration of the old Ugljevik Thermal Power Plant, construction of hydropower plants and some other forms of business - technical co-operation.
- The Supervisory Board of the Velenje Coal Mine re-appointed Evgen Dervarič, D.Sc. the present director for a term of four years.
- The Velenje Coal Mine celebrated the 46th "Skok čez kožo". Jože Zagožen, D.Sc., General Manager of HSE made the honourable jump and Janez Janša, the President of the Government, and Milan Medved, D.Sc., Chairman of the Supervisory Board of the Velenje Coal Mine held speeches at the festive ceremony.
- In its 84th regular session the Government of the Republic of Slovenia adopted the strategic policies relating to the privatisation of the Slovene electrical energy industry.

August

- The Supervisory Board of DEM appointed Damjan Koletnik the new director of DEM for a term of four years.
- The Development Plan of the Velenje Coal Mine was adopted in the 10th regular shareholders' meeting.

September

- Under the auspices of HSE the first Slovene informative - educational campaign "Energy si" started.
- It was one of the basic findings of the fourth strategic conference of the HSE Group that business performance of the Group would importantly depend on investments in growth and development. Certain measures relating to this objective have already been taken.
- The project "Sustainable management of the Drava River Area" (TruD) was completed. It was carried out in scope of the Phare programme where DEM also co-operated.
- The largest photoelectric voltage power plant in Slovenia opened in SEL. The opening was organised on the occasion of the 20th anniversary of the operation of the Mavčiče Hydropower Plant.
- A major overhaul of the generator within the second generator in the Solkan Hydropower Plant was carried out in SENG.
- TEB purchased simulators for gas turbines that enable safe and reliable start-up of these two turbines. Besides the nuclear power station, TEB is the only power plant having a simulator in Slovenia.

October

- HSE as the largest Slovene producer of electrical energy and RWE Power AG as the largest German producer of electrical energy signed a co-operation agreement in the area of development and implementation of some investment projects in Macedonia.

- HSE opened a branch office in Prague.
- The Supervisory Board of HSE granted an approval for the sale of TDR - Metalurgija.
- The Supervisory Board re-appointed Vladimir Gabrijelčič a manager of SENG for a term of four years.
- The Minister of Economy Andrej Vizjak, M.Sc. visited TEŠ and on this occasion he emphasised that TEŠ would remain an important factor in the electrical energy system in long-term.
- Revision of gas generators 1, 2 and 3 was carried out in TEB.

November

- HSE officially opened a subsidiary in Hungary, HSE Hungary Kft., headquartered in Budapest.
- HSE submitted the best bid for the purchase of the thermal power plant and heating plant Rousse in Bulgaria.
- Damijan Koletnik started running DEM.
- The municipality of Šoštanj organised two spatial conferences; both were related to the construction of the 600 MW sixth generator of TEŠ.
- For the third time, PV (the Velenje Coal Mine) was ranked among the companies that make huge investments in training and won the TOP 10 recognition. Ten Slovene companies investing most in the training management received such recognition.
- In its 99th regular session the Government of the Republic of Slovenia adopted a resolution on the split-off of SEL and TEB (from HSE) and take-over by GEN energija and on a capital increase in HSE by shares of the Republic of Slovenia in DEM and TET.

December

- In its 100th session the Government of the Republic of Slovenia adopted the Development Plan of the HSE Group and granted a discharge to the Management Board and the Supervisory Board for the year 2005.
- On 20 December, after the fulfilment of all obligations of the buyer, 90.78 % shares of TDR-Metalurgija d.d. were transferred to a new customer, W & P Profil - Solarvalue holding, družba za upravljanje d.o.o., Ruše. Prior to the sale, the Supervisory Board of HSE and the Government of the Republic of Slovenia agreed about the sale of shares. Thus the sellers - HSE d.o.o., Kapitalska družba pokojninskega in invalidskega zavarovanja d.d., Holding Slovenske železnice d.o.o. and Tovarna dušika Ruše d.o.o. - in liquidation- enabled further development and operation to TDR - Metalurgija d.d. that has already faced bankruptcy.

...enlightening new perspectives...

There's nothing like an evening spent wrapped in a warm blanket reading a book. I love words that enlighten or bring new perspectives to life.

2

Business Report

2006

2.1 PARENT COMPANY – HSE D.O.O.

2.1.1 GENERAL INFORMATION ABOUT THE PARENT COMPANY

Company Profile of Holding Slovenske elektrarne d.o.o.

Full company name	Holding Slovenske elektrarne d.o.o.
Abbreviated name	HSE d.o.o.
Legal status	Limited liability company
Address	Koprska ulica 92, 1000 Ljubljana, Slovenia
Phone	01 470 41 00
Fax	01 470 41 01
Entry No.	1 / 35036 / 00, registered with the Ljubljana District Court
Share capital	1,156,216,668.00 SIT
Size	Large company
Ownership structure	100 % Republic of Slovenia
Year of establishment	2001
Transaction accounts	04302 – 0000317271 02924 – 0254805996
Transaction account of joint venture	04302 – 0001020424
TIN	99666189
VAT identification number	SI99666189
Registration number	1662970
Website	www.hse.si
E – mail	hse@hse.si; info@hse.si
General Manager	Jože Zagožen, D.Sc.
Deputy General Manager	Milan Medved, D.Sc.
Chairman of the Supervisory Board	Andrej Vizjak, M.Sc.

Articles of Incorporation

The Government of the Republic of Slovenia adopted the Articles of Incorporation of the limited liability company Holding Slovenske elektrarne d.o.o. in its 38th session held on 26 July 2001.

HSE was established with a view to:

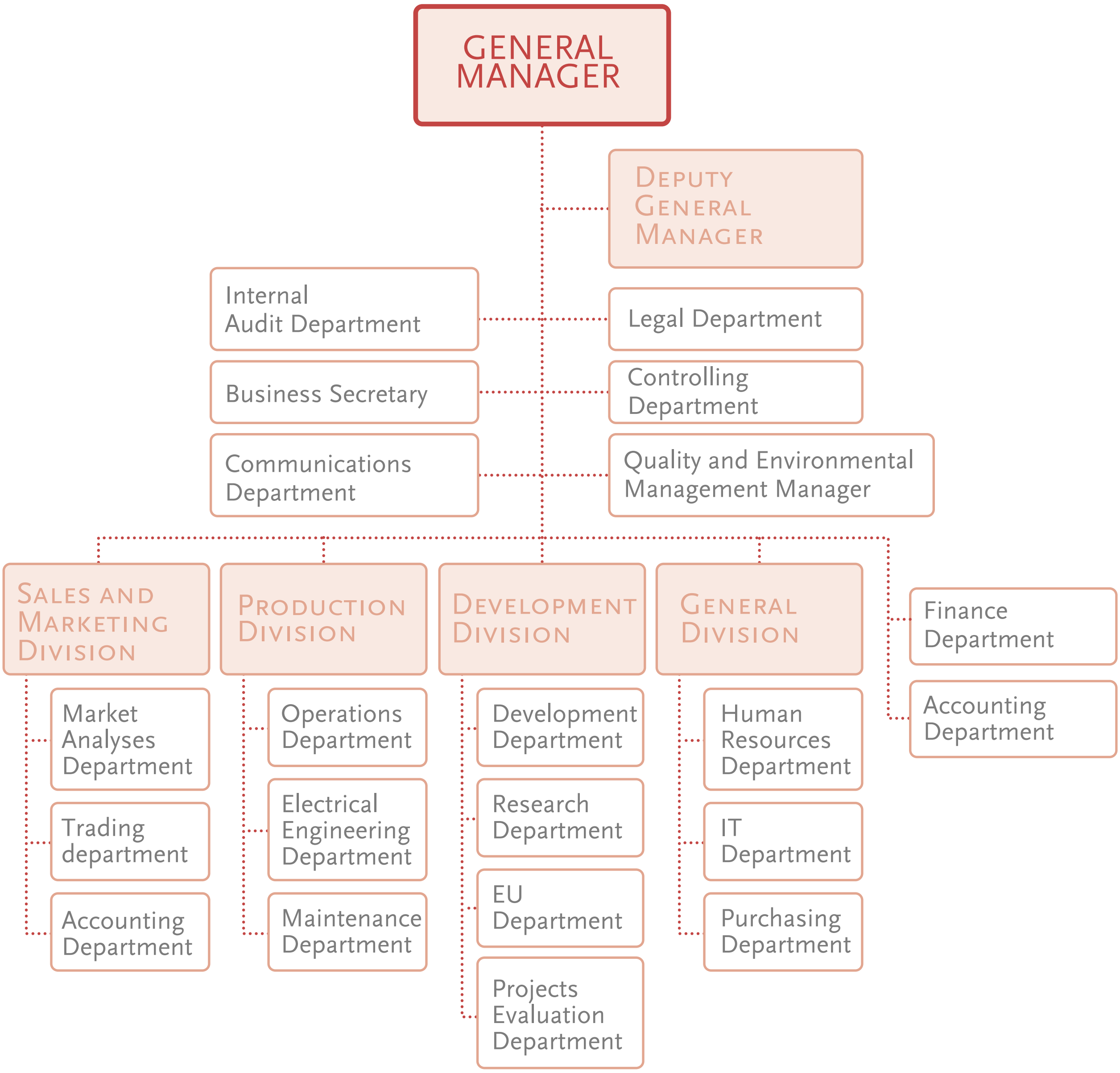
- provide for uniform market appearance of the companies integrated in the holding company as regards the sale of electrical energy,
- improve the competitiveness of Slovene power generation companies,
- implement the construction of hydropower plants on the lower Sava River.

Ownership structure

In HSE, the Republic of Slovenia agglomerated its shares in individual companies integrated in the holding.

The spare capital of HSE is represented by the contribution of the sole shareholder, namely the Republic of Slovenia, which thus holds one share and owns 100 % of the company.

2.1.2 ORGANISATION OF THE PARENT COMPANY HSE

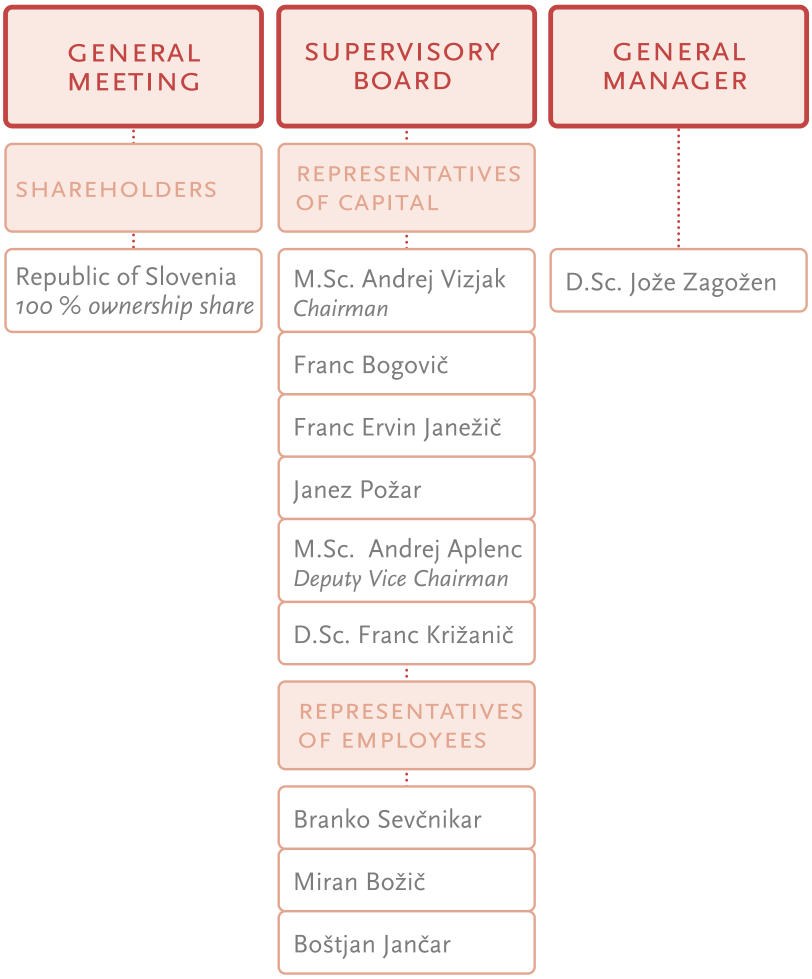


HSE d.o.o. is a controlling company of the HSE Group with its registered office in Ljubljana and business establishments in Maribor, Velenje, Nova Gorica and Sevnica. Business functions of the Group are divided by places where various advantages can be gained. The management board, sales and marketing division, general division, the departments of internal audit, public relations, legal affairs, controlling, finance and accounting are located in Ljubljana. The generation management centre, investment sector and telecommunications are in Maribor. The business establishment in Velenje is in charge of the domestic market, trade relations among the group companies, monitoring and calculation of deviations and long-term planning. The establishment in Nova Gorica is responsible for foreign markets, and the establishment in Sevnica for the activities related to the construction of hydropower plants on the lower Sava River.

2.1.1 MANAGEMENT OF THE PARENT COMPANY

The Republic of Slovenia as the only owner manages the patent company directly and through company bodies:

- the Supervisory Board and
- the General Manager.



Management of the parent company

Pursuant to the competence stipulated in the Articles of Incorporation the founder independently decides on strategic and development policies of the company, on the use of accumulated profit, changes in capital and all issues that are of vital importance for company's operation.

The Supervisory Board consists of nine members; six of them represent the interests of the owner and three members represent the interests of employees. The most important tasks of the Supervisory Board include supervision over the management of company transactions, proposal of resolutions - within its competence - to be adopted by the founder, review and adoption of annual reports and appointment of a general manager.

Audit committee

In order to assure complete transparency of the operation of HSE d.o.o. and the HSE Group the Supervisory Board of HSE appointed an audit committee in its 5th regular session held on 9 June 2006.

Members of the audit committee are:

- France Križanič, D.Sc., Chairman,
- Andrej Aplenc, M.Sc.
- Branko Sevčnikar,
- Alenka Podbevšek, independent expert in accounting.

The main tasks of the audit committee are:

- supervision over the integrity of financial information given by the company,
- control of the risk management system, internal audit and internal control system,
- assessment of the annual report structure, including the formulation of the proposal to the Supervisory Board,
- participation in determination of relevant auditing areas,
- participation in the selection of an independent external auditor and in the preparation of a contract between an auditor and HSE d.o.o.,
- monitoring of independence, objectivity and performance of external auditors,
- supervision over the character and scope of non-audit services and
- other tasks determined by the resolution of the Supervisory Board of HSE.

2.2 HSE GROUP PROFILE

Integrated diversity

HSE is the largest organisation in the area of electrical energy industry and the largest producer and trader in electrical energy on the Slovene wholesale market. It integrates five companies for electrical energy production, a mine, a company engaged in investments in the energy sector and four companies - in Italy, Croatia, Serbia and Hungary and a branch office in the Czech Republic - that take care for the integration of HSE in the international energy and business flows.

The integration of hydropower plants, thermal power plants and the mine under a single trademark - the HSE Group, uniform marketing of different sources of electrical energy, joint investments and development projects provide all HSE Group companies with enhanced flexibility, competitive advantage, and decreased risk exposure in operation and danger of possible power failures and measurable synergy effects.

In the five years since its establishment, HSE has become a driving force in the development of the Slovene electrical energy industry and through its constant growth and expansion to European markets on a par with the largest and the best competitors in its sector.

Primary activities of the Grouptegrated diversity

The HSE Group is primarily engaged in the management and control of energy supply as well as in environmental risk management processes related to its core business. This broad range of activities may be grouped into the following main categories of operations:

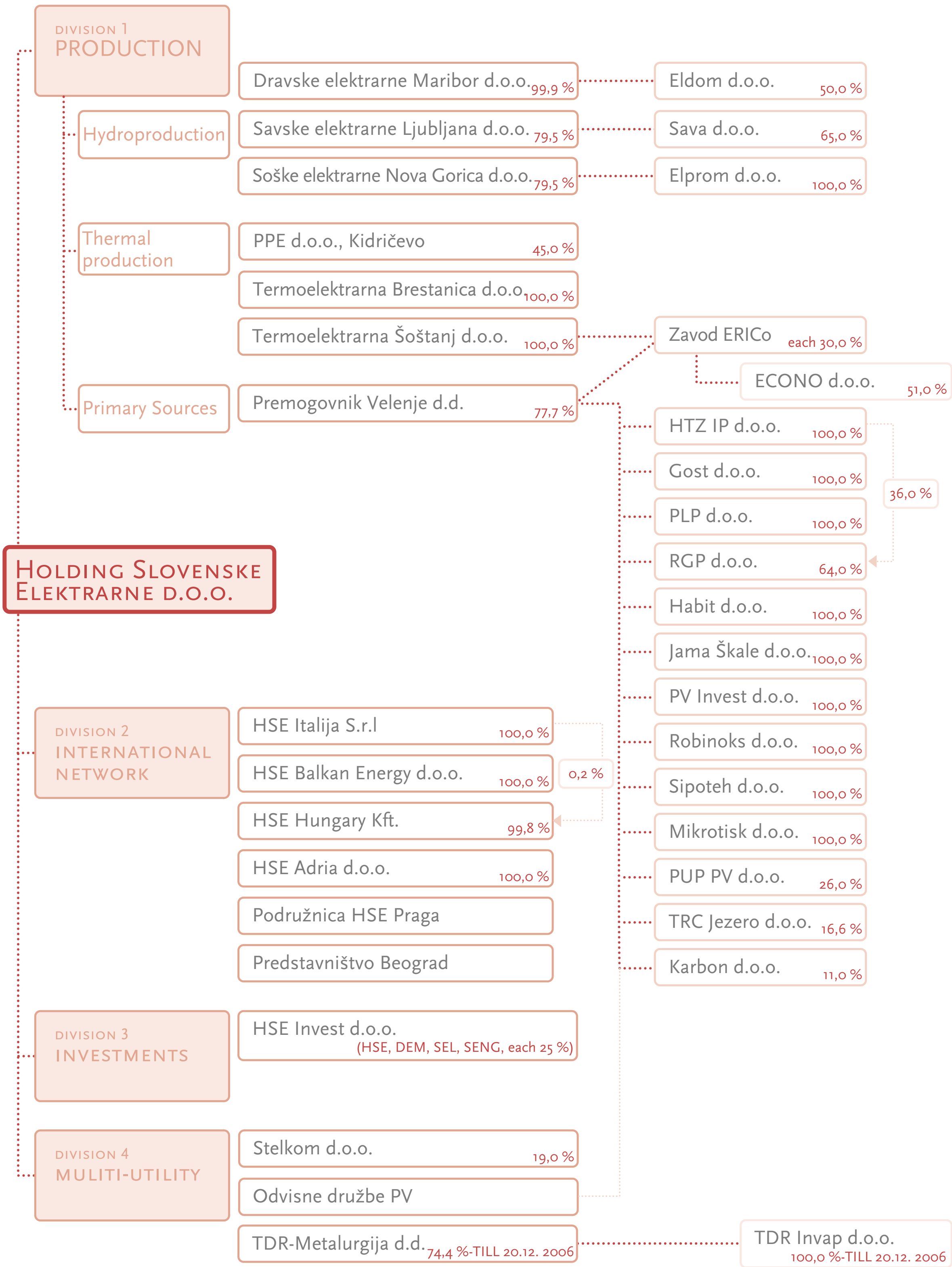
- production of electrical and thermal energy,
- mining of lignite,
- sale of and trade in electric and thermal energy,
- optimisation of production of the HSE Group,
- provision of system services needed for the operation of the electrical energy system,
- management and implementation of energy and environmental projects.

The core business of the Group pertains to the production of and trade in electrical energy, thus the major portion of this Annual Report refers to this same area.

HSE Group

In 2006, the HSE Group was comprised of the following companies:

- Holding Slovenske elektrarne d.o.o. as the controlling (parent) company and
- Dravske elektrarne Maribor d.o.o. with one subsidiary,
- Savske elektrarne Ljubljana d.o.o. with one subsidiary,
- Soške elektrarne Nova Gorica d.o.o. with one subsidiary,
- Termoelektrarna Brestanica d.o.o.,
- Termoelektrarna Šoštanj d.o.o.,
- Premogovnik Velenje d.d. with ten subsidiaries and one associated company,
- HSE Invest d.o.o.,
- HSE Italia S.r.l.,
- HSE Balkan Energy d.o.o.,
- HSE Hungary Kft.,
- HSE Adria d.o.o.,
- PPE d.o.o., Kidričevo as an associated company,
- TDR - Metalurgija d.d. with one subsidiary until 20 December 2006.



The companies TEŠ and PV (the Velenje Coal Mine) each hold a 30 % share in ERICo; although included in the scheme of the HSE Group, the financial operations of this institute are not included in the Group Annual Report. Likewise, the Annual Report does not include any performance-related information on the companies Eldom, Sava and Elprom.

Hydro production

Dravske elektrarne Maribor d.o.o.

Managing director	*Damijan KOLETNIK*
Address	Obrežna ulica 170, 2000 Maribor
Phone	02 300 50 00
Fax	02 300 56 65
E – mail	dem@dem.si
Website	www.dem.si
Primary activity	electricity production in hydropower plants
Composition of the Supervisory Board as at 31 December 2006	Igor MARINŠEK - chairman Aleksander BRUNČKO Bojan MAJHENIČ

DEM

DEM is the first production link in the HSE Group and the centre for operational control of the total production of electrical energy in the HSE Group. All power plants account for 25 % of total demand for electrical energy in Slovenia, and the threshold power amounts to 575 MW. DEM is also the largest producer of electrical energy from renewable sources. With eight hydropower plants on the Drava river and two small hydropower plants, the company produces as much as 80 % of the Slovene electrical energy which satisfies the criteria of renewable energy sources and the standards of the internationally recognised RECS certificate. Quality hydropower is provided in an environmentally friendly way and in line with the principles of sustainable development.

Eldom d.o.o.

A subsidiary of DEM. The company's activities include property management, organisation of meals in restaurants and management of holiday facilities of electrical energy industry in Slovenia.

Savske elektrarne Ljubljana d.o.o.

Managing director	*Drago POLAK*
Address	Gorenjska cesta 46, 1215 Medvode
Phone	01 474 92 74
Fax	01 474 92 72
E – mail	info@savske-el.si
Website	www.savske-el.si
Primary activity	electricity production in hydropower plants
Composition of the Supervisory Board as at 31 December 2006	Djordje ŽEBELJAN, M.Sc. – Chairman Anton GUNDE Marko BOGATAJ

SEL

SEL and its four hydropower plants are engaged in the production of electrical energy as well as in responsibility for the operation and maintenance of perfect energy production in hydropower plants, investment engineering for electrical energy facilities and installations, assembly, testing, measuring, start-up and elaboration of development tasks. Their total threshold power amounts to 117 MW.

Sava d.o.o.

A subsidiary of SEL, established to help meet the needs of constructing a chain of new hydropower plants along the lower Sava River.

Soške elektrarne Nova Gorica d.o.o.

Managing director	*Vladimir GABRIJELČIČ*
Address	Erjavčva 20, 5000 Nova Gorica
Phone	05 339 63 10
Fax	05 339 63 15
E – mail	seng@seng.si
Website	www.seng.si
Primary activity	electricity production in hydropower plants
Composition of the Supervisory Board as at 31 December 2006	Milan MEDVED, D.Sc. – Chairman Valentina LAVRENČIČ Alojz ISTINIČ

SENG

SENG with its total threshold power of 160 MW is in charge of optimal exploitation of the water potential of the Soča river, and their tributaries and other renewable sources under consideration of environmental conditions and demands of space users. At the level of the HSE Group the management centre in Nova Gorica is responsible for the provision of optimal and quality production of all power plants.

Next to production of electrical energy, SENG is also engaged in other activities: multi-use facilities related to water management, water supply, fish breeding, fishing, tourism and recreational activities.

Elprom d.o.o.

A subsidiary of SENG was established with the purpose of trading in electrical energy.

Thermal production

Termoelektrarna Brestanica d.o.o.

Managing director	*Bogdan BARBIČ*
Address	Cesta prvih borcev 18, 8280 Brestanica
Phone	07 481 60 00
Fax	07 492 22 62
E – mail	teb@teb.si
Website	www.teb.si
Primary activity	electricity production in thermal power plants
Composition of the Supervisory Board as at 31 December 2006	Milan MEDVED, D.Sc. – Chairman Nikola GALEŠA Anton GABRIČ

TEB

Total threshold power of TEB amounts to 312 MW. The power plant that has existed for over 60 years is next to system services and electricity production engaged also in the production of steam and hot water, storing, project engineering, technical consulting, technical testing, analyses and other services.

Termoelektrarna Šoštanj d.o.o.

Managing director	*Uroš ROTNIK, D.Sc.*
Address	Cesta Lole Ribarja 18, 3325 Šoštanj
Phone	03 899 31 00
Fax	03 588 24 85
E – mail	info@te-sostanj.si
Website	www.te-sostanj.si
Primary activity	electricity production in thermal power plants
Composition of the Supervisory Board as at 31 December 2006	Ivan ATELŠEK - Chairman Franc ROSEC Franc SEVER

TEŠ

TEŠ with the capacity of 755 MW on the generator and threshold power of 683 MW is the largest production facility among the HSE Group companies. It produces approx. a third of energy in the country, in critical periods it can meet more than half of the national demand. Besides electrical energy, it produces also thermal energy which is then supplied to the major part of the Šaleška valley. The power plant that utilises lignite from the nearby Velenje Coal Mine as the basic fuel consists of five production generators and two thermal stations. In accordance with the results the operation of TEŠ is comparable to equal European thermal power plants, but exceeds their operating generator availability.

Plinsko parna elektrarna d.o.o., Kidričevo	
Managing director	*Branko KOŽUH*
Address	Tovarniška cesta 10, 2325 Kidričevo
Phone	02 799 51 20
Fax	02 799 41 03
E – mail	brane.kozuh@talum.si
Website	/
Primary activity	other production of electrical energy
Composition of the Supervisory Board as at 31 December 2006	Metod PODKRIŽNIK, M.Sc. – Chairman Anton SMOLAK Zlatko ČUŠ

PPE Kidričevo

Plinsko parna elektrarna d.o.o., Kidričevo (CCGT power plant) was established in the year 2004 for the needs of construction planning of an 800 MW CCGT power plant in Kidričevo. The company's owners are HSE (45 %), Verbund (40 %) and Talum (15 %). In the phase of preparation, which will last until 2007, a decision will be adopted on the basis of appropriate studies whether to construct the power plant or not. If the decision is adopted that the plant should be constructed, the construction will take place in the years 2007 to 2009.

Primary sources

Premogovnik Velenje d.d.	
Managing director	*Evgen DERVARIČ, D.Sc.*
Address	Partizanska 78, 3320 Velenje
Phone	03 899 61 00
Fax	03 586 91 31
E – mail	info@rlv.si
Website	www.rlv.si
Primary activity	mining of lignite
Composition of the Supervisory Board as at 31 December 2006	Milan MEDVED, D.Sc. – Chairman Vida LORBER Branko MLINŠEK

The Velenje Coal Mine -PV

The Velenje Coal Mine is a technologically well-equipped mine that can be ranked among the most modern and safe mines in Europe. Its particularity is known all over the world, i.e. the "Velenje long wall method" with an adjusted top hydraulic system. Owing to the productivity, this method is proved to be most efficient for the extraction of thick coal layers and simultaneously it enables also filling and consolidation of the extraction area.

The quantity of the coal mined in the Velenje Coal Mine depends on the plans of the Slovene electrical energy sector; annually, it amounts to approx. 4 million tons of lignite on average and the total quantity is entirely intended for the needs of TEŠ. The Velenje Coal Mine performs also a variety of activities in the field of geo-technology such as project engineering of subterranean facilities, open mining and geo-mechanical research. Modern technical equipment and high professional level of the staff ensure safety of the employees and high productivity that is a basis for a competitive price of coal and consequently for the competitiveness of electrical energy of TEŠ and the complete HSE Group.

HTZ I.P. d.o.o.

HTZ I.P. d.o.o. is involved in the production, service and maintenance of products, equipment and installations. It is particularly distinguished by its rich experience and expertise in the maintenance and service of various mining devices. The company plays an important role in the training and employment of disabled persons.

Gost d.o.o.

Gost d.o.o. was initially solely engaged in the restaurant business and organised meals. Gradually, it has expanded its operation into the provision of tourist services.

PLP d.o.o.

PLP d.o.o. provides timber products for the needs of the mine. In order to ensure maximum safety, the products supplied have to meet the very highest quality standards.

RGP d.o.o.

RGP d.o.o. is involved in the engineering of penstocks, shafts, and similar subterranean civil engineering operations, including reinforcement and special mining construction works. The company is also engaged in the implementation of structural and static reinforcement of building constructions, project engineering and rendering of geometric and geo-mechanical services.

Habit d.o.o.

Habit d.o.o. is a real estate company which is specialised in its management. In addition to this, it handles organisation and management of specialist construction and installation works for residential and other civil engineering projects.

Jama Škale d.o.o.

The company was founded for the needs of closure of the Škale pit.

PV Invest d.o.o.

PV Invest d.o.o. is involved in landscaping, geodetic services, pulling-down of facilities, etc.

Robinoks d.o.o.

Robinoks d.o.o. is engaged in the manufacture of stainless steel products.

Sipoteh d.o.o.

Sipoteh d.o.o. is involved in the machine and production equipment, production of metal structures and their components.

Mikrotisk d.o.o.
Mikrotisk d.o.o. is a company performing services in the field of micro printing.

PUP PV d.o.o.
PUP PV d.o.o. is a company involved in cleaning and landscaping.

TRC Jezero d.o.o.
TRC Jezero d.o.o. wants to establish a tourist and recreational facility on the degraded land of the Šaleška valley. This developing lakeside reserve will be distinguished by its sports and leisure facilities, including a water park with thermal water. There shall be nothing to compare with in Slovenia.

Karbon d.o.o.
Karbon, čiste tehnologije d.o.o., was founded in 2002 and is active in the carbonisation of lignite, production of coal briquettes, and active charcoal. The company has been also establishing itself as a centre for clean coal technologies.

International network

HSE Italia S.r.l.	
Managing directors	*Milan MEDVED, D.Sc.* *Tomaž ŠTOKELJ, D.Sc.* *Damjan LIPUŠČEK*
Address	Via Roma 20 34179 Gorizia Italy
Phone	+ 39 0481 537 386
Fax	+ 39 0481 536 667

HSE Italia
The subsidiary of HSE headquartered in Italy is involved in the sale of electrical energy on the Italian market. It was founded in April 2003. HSE Italia connects HSE with (prospective) business partners for possible investments in the Italian territory and performs other activities related to trading in electrical energy.

HSE Balkan Energy d.o.o.	
Managing director	*Boris MEZGEC, M.Sc.*
Address	Makenzijeva 74 11000 Beograd Serbia
Phone	+ 381 11 3445 384
Fax	+ 381 11 3445 398

HSE Balkan Energy
The subsidiary of HSE in Belgrade is involved in the support to trading in electrical energy, research of possibilities of leasing or purchase of produc-

tion capacities and other investment possibilities, organisation and offering of consulting and contracting services of HSE in the field of operations in the electrical energy market, mining and hydro and thermal electrical energy, research of possibilities of operation in other energy fields such as oil, gas, thermal energy and research of possibilities of founding subsidiaries or co-owned companies for the implementation of basic strategic policies of HSE.

HSE Hungary Kft.

Managing directors	*Milan MEDVED, D.Sc.* *Tomaž ŠTOKELJ, D.Sc.*
Address	Károlyi Mihály u. 12 1053 Budapest Hungary
Phone	+ 36 1 486 2200
Fax	+ 36 1 486 2201

HSE Hungary

By founding the subsidiary HSE Hungary HSE has established efficient connections to the markets of Central and East Europe, mainly to Poland, Czech Republic and Slovakia and won the position of one of the most important international actors in the field of electrical energy industry in these countries. In this way, it has increased its flexibility and the scope of trading in electrical energy which it also one of the basic objectives of expansion of the company operation to foreign markets. HSE Hungary is involved in the purchase of electrical energy from qualified producers, sale of electrical energy to authorised consumers and other traders in electrical energy on the organised market whose member HSE is. Through its subsidiary in Hungary, HSE participates also in auctions for allocation of cross-border transfer capacities.

HSE Adria d.o.o.

Managing directors	*Tomaž ŠTOKELJ, D.Sc.* *Boštjan BANDELJ, M.Sc.*
Address	Miramarska 24 10000 Zagreb Croatia
Phone	+ 385 16 177 010
Fax	+ 385 16 177 010

HSE Adria

HSE Adria is a subsidiary of HSE in Croatia with headquarters in Zagreb. The main activities of the company include conclusion of contracts for the purchase and sale of electrical energy, establishment of business partnerships and other activities related to trading in electrical energy.

Branch office HSE Praga

Branch office manager	*Milan MEDVED, D.Sc.*
Address	Myslikova 28 121 02 Praha 2 Czech Republic
Phone	+ 420 224 920 607
Fax	+ 420 224 915 866

Branch office HSE Praga
On the basis of the obtained licence for trading in electrical energy the branch office in Prague is involved in the purchase of electrical energy from qualified producers, sale of electrical energy to authorised consumers, other traders in electrical energy and public trading companies as well as in trading in electrical energy on an organised market whose member it is. Simultaneously, HSE will be able to participate also in auctions for the allocation of cross-border transfer capacities.

Investments

HSE Invest d.o.o.

Managing director	*Miran ŽGAJNER*
Address	Obrežna 170 a, 2000 Maribor
Phone	02 300 58 92
Fax	02 300 58 99
E – mail	info@hse-invest.si
Website	www.hse-invest.si
Primary activity	leading and management of the pre-investment stage of development projects, management of new hydropower plants and restoration of the existing ones
Composition of the Supervisory Board as at 31 December 2006	Irena ŠLEMIC - Chairperson Marjan ŠMON Alida REJEC Janez NUČIČ

HSE Invest
HSE Invest makes investments in the energy sector. Nowadays, it plays an important role in the construction of a chain of hydropower plants on the lower Sava river.

Multi – utility

Stelkom d.o.o.

Managing director	*Lea BENEDEJČIČ, M.Sc.*
Address	Špruha 19, 136 Trzin
Phone	01 620 22 00
Fax	01 620 22 01
E – mail	info@stelkom.si
Website	www.stelkom.si
Primary activity	telecommunications
Composition of the Supervisory Board as at 31 December 2006	Gregor NOVAK - Chairman David VALENTINČIČ Mirko MARINČIČ, M.Sc. Simon TOT

Stelkom

Stelkom is a provider of telecommunications services and links for the telecommunications infrastructure of companies from the electric power industry. The infrastructure is based on the widely distributed optical of 2,500 km in total length.

TDR - Metalurgija d.d. [1]

Managing director	*Alojz CAJNKO, M.Sc.*
Address	Tovarniška cesta 51, 2342 Ruše
Phone	02 66 11 081
Fax	02 66 28 901
E – mail	info@tdr-metalurgija.si
Website	www.tdr-metalurgija.si
Primary activity	Production of calcium carbide, ferrosilicon, calcium silicon, and complex alloys
Composition of the Supervisory Board as at 31 December 2006	Irena STARE - Chairperson Janez KERŽAN Renata ŠTRITOF

[1] On 20 December 2006 HSE sold its ownership share in the company.

TDR-Metalurgija

TDR - Metalurgija is one of the earliest electro-chemical manufacturers in Central Europe. It is involved in the production of calcium carbide and ferroalloys. The company has a subsidiary which is engaged in training and employment of the disabled.

2.2.1 MANAGEMENT OF THE HSE GROUP

Governing bodies in subsidiaries

All subsidiaries, with the exception of HSE Italia, HSE Hungary and HSE Adria are managed by a single managing director or a management board. The majority of companies are supervised by a three-member Supervisory Board.

During 2006, regular and close co-operation with trade unions and workers' councils continued and has operated in HSE since its very beginning.

Trade union activities in the DEM, SEL, SENG, TEB and TEŠ companies are co-ordinated by Sindikat delavcev dejavnosti energetike Slovenije (SDE-Slovene Power Sector Union), one of the strongest within Zveza svobodnih sindikatov Slovenije (ZSSS - Association of Free Trade Unions of Slovenia). HSE d.o.o. and HSE Invest are in the process of establishing union representation.

In addition to SDE, two other trade unions operate within the HSE Group: Neodvisnost (representing some 10 % of SENG employees) and Sindikat pridobivanja energetskih surovin Slovenije (SPESS - Union of Coalminers) which is active in the PV Group (Group of the Velenje Coal Mine).

The SDE's Electrical Energy Sector Conference also encompasses the coordination of union activities within the HSE Group as well as the appointment of trade union representatives in the DEM, SEL, SENG, TEB, TEŠ companies. Union representatives communicate directly with the HSE management as well as with the managers of the subsidiaries. This spirit of co-operation ensures timely reaction and rapid solution to any problems as and when they arise as well as open discussion of suggestions and proposals. Such cooperation extends to the joint Workers' Council of the HSE Group.

Workers' councils in the HSE Group companies

Through the workers' councils, HSE Group employees enjoy their statutory right to participate in management. Each such workers' council elects representatives drawn from the workforce to the Supervisory Board of the company in which they operate.

Joint workers' council of the HSE Group

In compliance with the Workers' Participation in Management Act, the HSE Group also features a Joint Workers' Council, a body which further reinforces the statutory rights of employees. By way of this, various interests are taken into consideration, and broad consensus is achieved both in terms of the Group's Development Plans as well as with respect to implementation of various aspects of the social contract.

2.3 BUSINESS POLICY OF THE HSE GROUP

Mission

The mission of the HSE Group, one of the leading Slovene companies in the power sector, is growth and development by maintaining its position of market leader on the domestic market, increase of its shares on the south-eastern markets, and scientific and economic development of the Slovene power sector and its establishment in the international context.

Vision

The vision of the HSE Group is to ensure optimum utilisation of Slovene energy sources and personnel, to establish partnerships abroad - especially in southeastern Europe - and to assure long-term competitive advantage of the Group on the global energy market, while also expanding its business operations so as to benefit from additional synergy effects for the Group and Slovenia.

Values

The values of the HSE Group are reflected in the Group's attitude towards customers, the society, employees, business partners and company owners. The focus is on:

- customer satisfaction,
- building responsible, long-term partnerships with business partners,
- the protection of the environment and utilisation of renewable sources of energy,
- striving towards engineering excellence,
- continuous professional development and establishing a motivating work environment for HSE employees,
- providing safe and stable jobs and creative work environment,
- efficient operation and creation of profits for company owners,
- on-going improvement of the management system.

HSE Group Development Plan

Due to on-going increase in consumption of electricity at home and worldwide, the HSE Group has been since its establishment searching for new, additional projects and investments in order to ensure provision of safe, reliable competitive and environmentally friendly supply of electricity to domestic consumers also on a long-term basis.

Becoming a market leader in Southeastern Europe

The strategic orientation of the HSE Group is defined in the Development Plan of the HSE Group. Due to numerous changes in the field of electrical energy sector the management board of the HSE rebalanced the Development Plan of the Group at the beginning of 2006 as a response to many challenges and opportunities. The Development Plan now encompasses changes and amendments to the present strategic orientation that will enable further growth and development of the HSE Group and thus long-term effectiveness which will reflect in future safe, reliable, competitive and environmentally friendly electricity.

The Government of the Republic of Slovenia adopted the Development Plan of the HSE Group 2006 - 2015 in its 100th regular session held on 7 December 2006.

Next to safe, reliable, competitive and environmentally friendly electricity the core target of the Development Plan is also the development and growth of the HSE Group towards becoming a market leader in southeastern Europe.

2.3.1 PROJECTS OF THE HSE GROUP IN SLOVENIA

Investments of the HSE Group Companies until 2015 in Slovenia

	PROJECT	INSTALLED CAPACITIY (MW)	AVERAGE ANNUAL PRODUCTION (GWh)	INVESTMENT VALUE (MIO EUR) ***	BUILDING PERMIT	START OF OPERATIONS
I. PRIORITY						
1	HPP Boštanj	33	115	65	Nov 2002	May 2006
2	TPP B5 TEŠ ****	42	300	23	Apr 2006	May 2008
3	PSHPP Avče	178	426	86.9	Sep 2004	Nov 2008
4	HPP Blanca	42.5	160	85.6	Nov 2005	May 2009
5	Renovation of HPP Moste *	12.5	59.6	10.1	Dec 2006	Sep 2009
6	HPP Zlatoličje	24	45	57.2	Dec2005	May 2008
7	B6 TEŠ	600	3,234	598.7	Jun 2008	Feb 2011
8	HPP Krško	41.5	145	88.9	Jul 2007	May 2012
9	PSHPP Kozjak	400	776	153.3	Aug 2009	Aug 2015
10	HPP Brežice	41.5	161	57	Jul 2010	May 2015
11	HPP Mokrice	30.5	135	53.7	Jul 2013	May 2018
12	Renewable energy sources	15	35	20		2007-2018
13	Heat and electricity co-generation	100	600	53		2008-2015
TOTAL I. PRIORITY		1,560.50	6,191.60	1,352.40		
II. PRIORITY						DURATION OF CONSTRUCTION
1	CCGT Brestanica	163	1,037	66		29 months
2	Repowering of HE Moste *	49.4	98	75		36 months
3	CCGT Kidričevo	360	2,700	181		30 months
4	HPP Formin	10	32	50		36 months
5	HPP Učja	24	35	40		48 months
6	HPP on the middle Sava river	304	997	685		2009-2025
7	HPP on the Mura river	131.6	676.4	331		2010-2038
8	HPP on the Idrijca river	117	200	152		2012-2023
9	HPP Kobarid, HPP Kamno	81.2	268	96		2015-2025
TOTAL II. PRIORITY		1,237.80	6,043.40	1,676		
TOTAL I. AND II. PRIORITY		2,785.80	12,175.40	3,018.30		

Comment:
* The repowering of HPP Moste is not considered a restoration project (thus HE Moste was not accounted for in the total of both priorities)
** Renewably energy sources: small HPPs, solar power plants and geothermal energy
*** The investment value of individual investment includes solely its energy part at fixed prices without financing costs!
**** TEŠ – installation of additional gas turbine

The projects involving the restoration of existing and construction of new power facilities are - with regard to commercial, environmental, spatial and operational criteria - divided into two orders of priority. The comparative economic calculations justify the implementation of all the projects itemised under the first order of priority, whereas those listed under the second order of priority need to be additionally developed and researched.

When all investments in Slovenia have been made, all sub-systems of the HSE Group will become competitive, which is an urgent condition for long-term existence on a global energy market. The investments realised on the southeastern markets will enable HSE to become the market leader on these markets. The investments have been planned without endangering any investments necessary in Slovenia which remain the priority of the HSE Group.

2.3.2 PROJECTS OF THE HSE GROUP IN SOUTHEASTERN EUROPE

The region of southeastern Europe is of essential importance for HSE because of its need to grow and due to the fact that HSE is the main provider of electrical energy in Slovenia. Stable supply of Slovenia depends also on the fact whether HSE succeeds in becoming an important regional trader in and producer of electrical energy. Without its own production capacities in this region, HSE will not be able to accomplish its mission and enhance its sustainable development. Limitations in provision and transfer of electrical energy which HSE faces in the region can seriously influence the stability of trading and supply of customers. Stability can be significantly increased by:

- an increase in own production capacities,
- dispersion of locations and
- selection of adequate combinations of different types of power plants.

From the aspect of risk management related to trading, balance between own and foreign sources is extremely important as well as dispersion of facilities over the complete trading area. HSE has already made important steps in this area since they are needed for successful penetration. Over 100 potential investments were carefully studied and 20 projects were focused on since their technical and economic feasibility has been proved and return on invested assets is ensured.

Simultaneously, we should be well aware that the interest of large companies in this area has grown and the countries of southeastern Europe have imposed increasingly demanding conditions.

2.4 MANAGEMENT SYSTEM POLICY

The Management System Policy encompasses quality, environmental management and occupational health and safety. The Management System Manual is in conformity with the following standards: ISO 9001:2000, ISO 14001:2004 and OHSAS 18001:1999. Information security management in compliance with standard ISO 27001 has been at the stage of preparation. The information security management will be also integrated into the Group.

The total quality management is based on the following principles:
- responsibility for the implementation of specific tasks arising from certain direct and unequivocal mandates,
- accountability for the achievement of objectives in relation to quality, environmental management and occupational safety, represents an integral part of the core requirements for the implementation of individual tasks,
- each individual, irrespective of his/her position, be it at the strategic, tactical or operational level, is accountable for the implementation of objectives in relation to quality, environmental management, occupational safety and information security subject to and in accordance with his/her responsibilities and authority.

2.4.1 ACHIEVING THE OBJECTIVES IN RELATION TO QUALITY

Our on-going objectives regarding quality are as follows:
- meet customer requirements,
- achieve set strategic and tactical business objectives,
- establish the optimum organisation and transparency of business operation,
- operate in accordance with applicable regulations, and
- exercise continuous vigilance over the economic aspects of the business so as to ensure sound company performance.

In the year 2006, the set objectives were achieved. Internal audits were conducted and system procedures required due to the introduction of OHSAS 18001 and ISO 14001:2000 amended. An assessment of the operation of the management system was made and orientations for the future were adopted. The management system documents were introduced in the ODOD data storage and distributions computer system. Likewise ongoing was the training of employees in the field of quality and organisation of work.

Besides the internal audit, an external audit was also performed in 2006.

2.4.2 ACHIEVING THE OBJECTIVES RELATING TO ENVIRONMENTAL MANAGEMENT

The HSE Group is well aware that high level of environmental awareness ensures pleasant working environment and good relations with our neighbours. Intensive efforts towards sustainable development in terms of environmental management are being made on the local as well as on the government levels. We aim for continuous improvement of working and living conditions of HSE employees and population residing in the vicinity of HSE companies. To this end, our environmental policy has been developed so as to conform to the requirements of the new standard ISO 14001:2004. Special attention has been devoted to indirect environmental aspects arising in the HSE Group companies. The key objective of the HSE environmental policy is to establish a permanent balance, which can be achieved by implementing preventive measures, by preventing any environmental contamination, by sharing responsibility, as well as by making environmental management a part of individual business processes.

The year 2006 marks the period of intensive preparations for the adoption of the National Allocation Plan and the related allocation of quotas of emission coupons for the 2nd Kyoto period. A study "Support to the acquisition of rights to the emission of greenhouse gases in the period 2008 to 2012 and involvement of flexible organisms in the HSE business practice" has been ordered.

Financing of the study "Land use, changes in land use and forestry - selection and preparation of the methodology and calculation of CO_2 sinks in Slovenia" continued. The study contributed to the increase in allocation for complete area of Slovenia by 1.3 million tons CO_2/year.

In the year 2006, the elaboration of the study »Possibilities of capturing and storing CO_2 in thermal energy facilities« started and in scope of these activities HSE joined the international organisation CO_2net and the Slovene technological platform for the development of power plants without harmful emissions.

2.4.3 ACHIEVING THE OBJECTIVES RELATING TO OCCUPATIONAL HEALTH AND SAFETY

Concern for the improvement of Occupational Health and Safety conditions in the working environment, by taking into account the specifics of the HSE processes and subsidiaries of the HSE group, is an integral part of the Group and reflects our care for our employees and the company's attitude towards the social environment where we live and operate. Compliance with the relevant applicable legislation represents merely the minimum level to be achieved and improved upon, as evidenced by our introducing and following the requirements of the OHSAS 18001 standard.

In the year 2005, a safety council of the HSE Group was constituted. It shall coordinate the domain of occupational health and safety in all HSE Group companies. Members of the safety council of the HSE Group met in sessions and discussed their joint work. The Manual relating to the work of this council was changed. In the second half of the year, activities relating to the purchase of the software package of occupational health and safety were in progress. It was agreed that all the HSE Group companies should purchase this software package and thus monitoring of occupational health and safety could be uniform in all HSE Group companies.

A contract was ready to be signed until the end of the year 2006. The introduction of the software package will be carried out in the parent company in the first half of the year 2007 and then it will be introduced also to other Group companies.

2.4.4 ACQUIRED CERTIFICATES IN THE HSE GROUP

Free competition on the domestic electricity market and in particular on foreign markets necessitates certified quality in terms of system and environmental management, as well as a responsible approach to production of electricity and other energy products. Appropriately certified products result in an improved sales performance, and in order to penetrate an increasing number of markets the provisions of such warranties is mandatory.

Acquired certificates in the HSE Group

COMPANY	ISO 9001	ISO 14000	OHSAS 18001	EE TÜV 08/02[2]	RECS[3]	HACCP[4]	USP 210[5]
HSE	✓	✓	✓	✓	✓		
DEM	✓	✓		✓	✓		
SEL	✓	✓		✓	✓		
SENG	✓	✓		✓	✓		
TEB	✓	✓					
TEŠ	✓	✓	✓			✓	
PV	✓	✓	✓				✓
TDR - Metalurgija	✓						

[2]EE – 08/02 – Certificate for the production of electrical energy from renewable sources acquired from TÜV.
[3]RECS – Renewable Energy Certificate System, TÜV and Energy Agency of the R of Slovenia.
[4]HACCP – Risk analysis of critical control points; Standard for measuring laboratories.
[5]USP 210 – Standard of a learning company of the USP Institute.

2.4.5 ACHIEVING THE OBJECTIVES RELATING TO INFORMATION SECURITY

In the year 2006, the project of introducing the information security standard ISO 27001 started at the level of the parent company.

The bases for the beginning of the project ISO 27001 were elaborated; among them were the basic scheme of the project, the prepared basic list of required activities relating to the introduction and a schedule of project development, etc.

A contract for the assistance in project management was concluded. Various appropriate resolutions were adopted by the system management council and a team for the introduction of ISO 27001 was appointed. In mid- October 2006 one employee took part in the seminar for a leading auditor in compliance with standard ISO 27001 and acquired a title of an »Information Security Manager« and »Information Security Auditor« which is a condition for internationally recognised registration of leading auditors of information security.

2.5 MARKET POSITION

2.5.1 GENERAL ECONOMIC OUTLOOK IN SLOVENIA[6]

In the year 2006, the considerable economic growth marked the period and culminated in the second half of the year. From the aspect of demand, foreign trade remained the driving force of economy, but investments took over the leading position in accordance with the estimates for the year 2006. Increased investment activities were expected due to the abolition of investment bonuses from the beginning of 2007. This situation reflected in investments made in equipment and transport. Due to environmental requirements which some hundred large Slovene companies had to meet in relation to the European directive the so-called environmental investments were heavier. Unusually warm autumn and the beginning of winter created favourable conditions for the continuation of impressive growth of scope of civil engineering works, in the field of housing and infrastructure.

This year's inflation higher than in 2005

Unlike in the year 2005, when the Slovene inflation reached the European level and amounted to 2.3 %, the year 2006 ended with a slightly higher inflation rate amounting to 2.8 %, and the average annual inflation to 2.5 %. In spite of that, the movement of prices was still above average in some groups.

Like in the year 2005 the prices of services grew faster than prices of goods in 2006. On average, prices of services went up by 4.3 % over December 2005 and those of goods by 2.1%. The prices of non-durable goods increased by 3% in the year, followed by prices of semi-durable goods that went up by 2.4 %, but prices of durable goods decreased by 2 % over 2005.

Economic growth in 2006 estimated at 5.2 %

In accordance with the first estimate, an increase of 5.2 % in GDP was observed in fixed prices in 2006. Thus GDP in current prices amounted to 7,126,012 million SIT in 2006, which is an increase of 7.6 % over the year 2005. BDP translated at current rates amounted to 29,741 million € or 14,811 € per capita in 2006.

Significant growth of exports and imports

Similarly as in the year 2005, the export grew rapidly in 2006 (10.0 %). The growth was fastest at the beginning of the year and then it stabilised at approx. a 9 % annual rate. In 2006, export contributed 6.5 % to the economic growth. The increase in import (10.4 %) was slightly higher than the increase in export, and thus the balance of trade in goods and services with foreign countries amounting to 0.3 % had a negative influence on the economic growth (influence of the balance on real growth of GDP was positive in the first half of the year and negative in the second one).

Increase in gross investments in fixed assets almost 12 %

In real terms, gross investments in fixed assets increased by 11.9 % when compared to the year 2005, which is a significantly higher increase than in 2005 (1.5 %). The increase was high mainly in the last two quarters when investments in fixed assets were by approx. 15 % higher than in the second half of 2005. Considerable growth of investments was achieved in both main groups, in construction facilities and in machines and equipment. Investments in construction facilities increased significantly at the end of the year due to high increase in investments in non-housing facilities (in third quarter by 16.4 %, and in the fourth one by 20.2 %), and investments in machines and equipment at the beginning of the year. The growth of both investment components was very similar in the year (11.8 and 12.5 %).

[6]Source: SURS and SKEP GZS

Increase in final consumption similar to the year 2005

Expenses for final consumption increased in real terms by 3.4 % (in 2005 by 3.1 %) and they lagged behind the increase in GDP for the third successive year. The expenses of the state increased most among the categories of final consumption (by 3.8 %), household expenses went up by 3.3 %, and expenses of non-profitable institutions by 2.3 %.

Total domestic consumption higher by 5.5 %

Total domestic consumption (final consumption and gross investments) increased by 5.5 % in real terms over the year 2005 which is mainly due to significant growth of gross investments in 2005 (2.0 % growth). In the first two quarters of the year the domestic consumption increased by over 4 % and in the second half of the year by 6.5 % due to accelerated growth of investments. Domestic consumption contributed 5.5 % to the increase in GDP in total in the year 2006.

Added value increased most in civil engineering

Added value increased most in civil engineering (by 11.8 %). In the first half of the year the growth of civil engineering was similar as in the year 2005, but it increased enormously in the second half; it achieved 15.3 % in the third quarter and 23.5 % in the fourth quarter. Impressive growth of added value was observed also in processing industry (7.4 %), which is a significant increase over the year 2005 (2.8 %). The growth was similar in all quarters, except in the second one, when the situation calmed-down. In 2006, processing activities contributed 1.6 % to the economic growth amounting to 5.2 %.

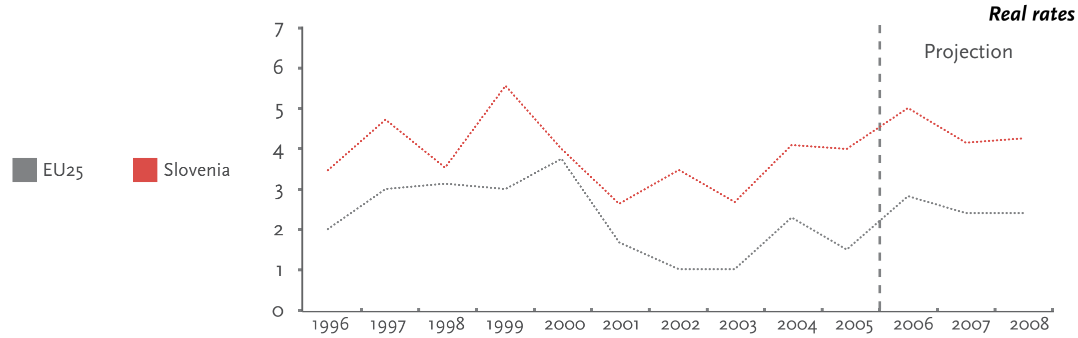
Added value was higher than GDP in the field of financial intermediation (8.9 %), in traffic (6.3 %), trade and catering industry (5.6 %). In real terms, the added value in basic activities (from A to F) increased by 6.7 %, in trading by 5.5 %, and non-trading (mainly the state) by 1.9 %.

Total employment higher by 1.2 %

In 2006, total employment amounted to 927 thousand people in accordance with the estimates of national survey and was by 1.2 % higher than a year ago. The number of employees increased most in civil engineering (by 7.5 %) and services (by 5.4 %). In spite of the high added value, the employment rate decreased in processing activities (by 1.7 %). In 2006, non-financial and financial companies employed 1.4 % more staff and an increase of 1.2 % was observed in the state sector over the year 2005.

Gross domestic product: Slovenia and EU25, 1996 – 2008

Real rates of growth in %



Source: SURS, EU25 - EC, autumn 2006 and Eurostat, February 2007 SKEP GZS

2.5.2 ELECTRICITY MARKET

The year 2006 brought no significant changes in the field of regulatory framework. In 2005, the new Energy Act was adopted, but it contained no novelties that would significantly influence the Slovene wholesale market of electrical energy. The novelty, introduced by the new Energy Act is that no company registered in Slovenia is required for trading in electrical energy. Thus, the Slovene wholesale market has become more accessible for foreign traders in electrical energy since administrative obstacles and costs of entering the Slovene wholesale market are low.

Under the European Directive on the allocation of cross-border transfer capacities the Slovene operator of transfer and distribution network continued allocating transfer capacities from the year 2005 also in 2006. Through daily, weekly and bimonthly auctions those transfer capacities were distributed that had not distributed previously in accordance with the pro rata system. A transitional period with the possibility of allocation of cross-border transfer capacities on internal EU borders in accordance with the pro rata system will end on 1 July 2007. After this date the Slovene operator of transfer network can allocate cross-border transfer capacities on market bases only.

The Slovene market of electrical energy is open in line with the European policy. Only households are classified as tariff customers until mid 2007; their price of electricity was regulated and determined on the basis of coverage of production and supply costs. All non-household customers are now entitled to freely choose their energy supplier and the price of electricity is thus determined by supply and demand on the market.

CO_2 emission coupons serve as an important factor in determination of prices on the market of electrical energy. In 2005, they were one of the most important factors in determining prices of electrical energy in Continental Europe. The cost of emissions on European wholesale markets of electrical energy has in many ways changed the manner of offering production from the facilities using fossil fuels as primary source, and caused a considerable increase in electricity prices. The cost of emissions in cost prices of electricity production strongly linked the electricity market to very volatile global oil and natural gas markets. Volatile prices of long-term deliveries in 2006 went up significantly.

During the year, intensive preparations for the establishment of the 2nd Slovene UCZTE zone were in progress. The zone was finally established at the end of 2006 and it will take over part of production capacities from the company. This situation resulted in some uncertainty in company operation, especially in trading and conclusion of delivery contract for the following years.

2.5.3 ELECTRICITY MARKETS IN 2006

The electricity markets were indirectly marked by the European trading scheme with emission coupons and the sharp oil price increase.

2.5.3.1 Slovenia

Last year was characterised by a strong increase in activities and trading quantities on the Slovene wholesale market.

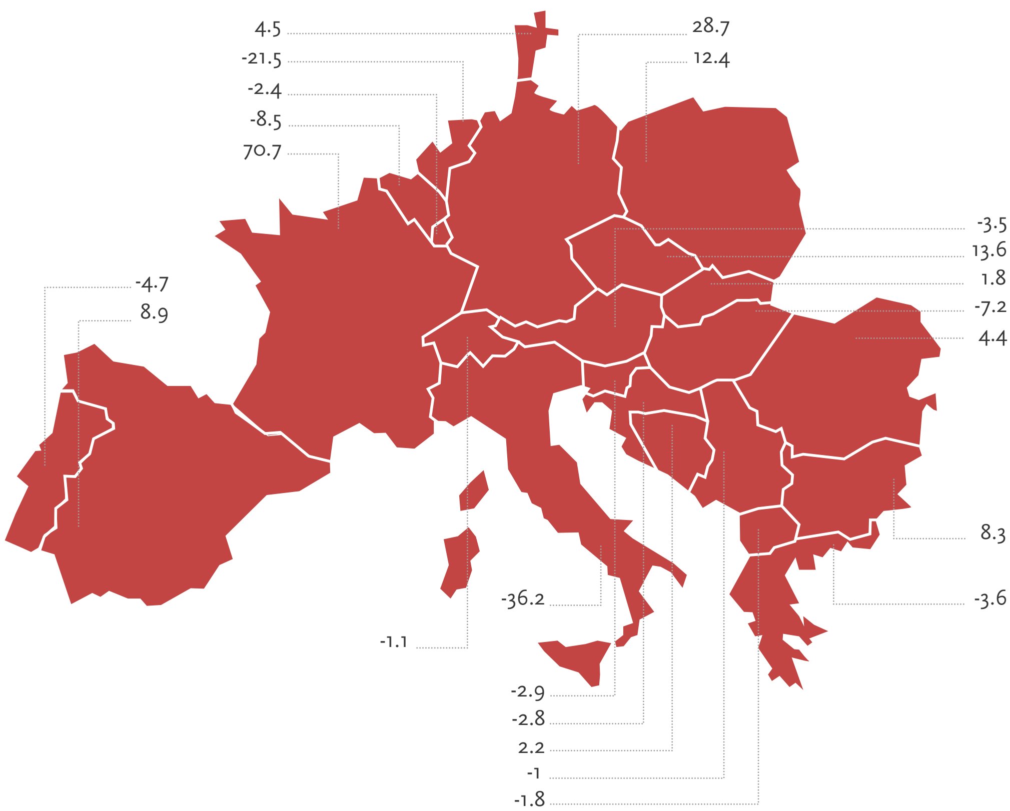
At the beginning of the year, high prices in auctions for the import of electricity from the southern border to Slovenia were of essential importance for the Slovene wholesale market as well as occasional high prices of export transfer capacities from Slovenia to Austria. A favourable offer of electrical energy at relatively low prices in southeast Europe resulted in the energy flow from the southeastern markets to the market of Continental Europe and Italy.

In the first half of April 2006 a major overhaul in the nuclear power station started and lasted until mid May. The overhaul had no significant influence on the Slovene wholesale prices due to a favourable offer of electrical energy on the wholesale market.

High prices in Continental Europe also enabled placing on the market additional quantities of electricity produced in TEŠ at prices which were considerably higher than expected at the end of the previous year.

Balance of European Electricity Markets in 2006

in TWh

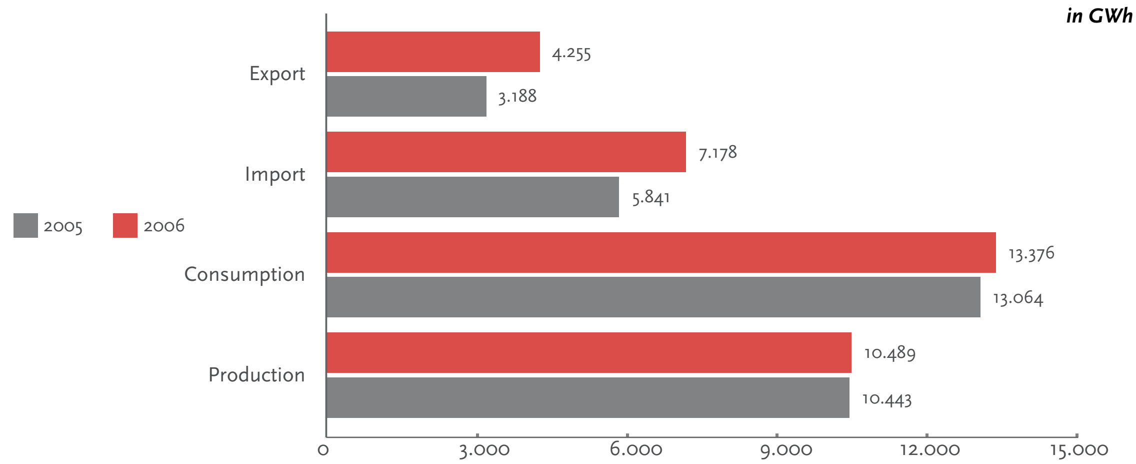


In the last quarter the sources on the southeastern markets were not available and the prices on the Slovene market went up and exceeded the price levels of Continental Europe and came close to the Italian levels. Similar price trends were also observed in prices of long-term deliveries.

Last year was also characterised by a below average production of electricity in hydropower plants which was lower by 11.6 % or 420 GWh as compared with the planned production of the year 2006.

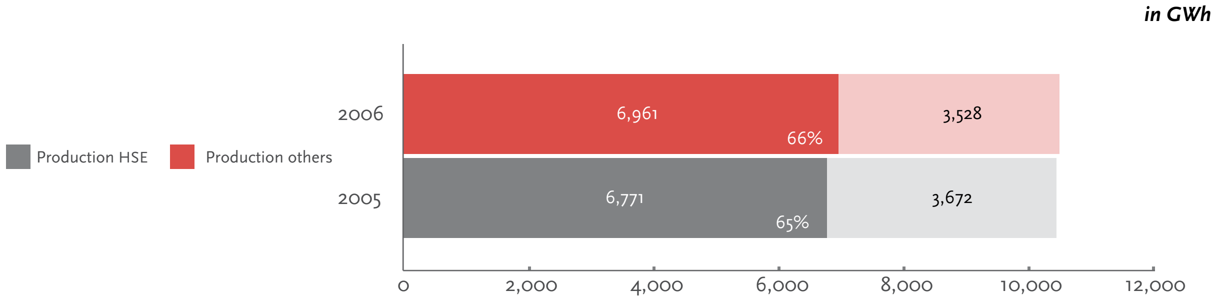
The growth of Slovene consumption was steady in 2006. When compared to the year 2005, Slovene consumption of electricity again witnessed an increase of 2.4 % in 2006 (including losses in the network).

Slovene Electricity Market[7]



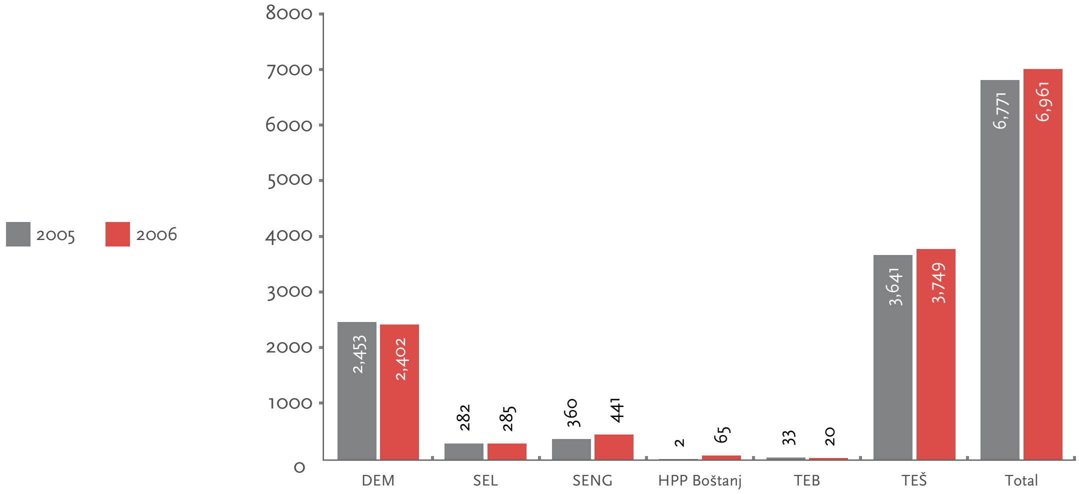
[7]Source: Report of Eles in December 2006. Only the Slovene part of the nuclear power station and losses in transfer network were considered.

Production share of the HSE Group in total production of electrical energy in Slovenia in the years 2006 and 2005



Production of net electrical energy in the HSE Group in the years 2006 and 2005

in GWh



2.5.3.2 Continental Europe

On the market of Continental Europe, the year 2006 can be assessed as a year of concrete changes which brought a lot of dynamic activities to the electricity market. It can be also said that at the beginning of the year all ratios revealed continuous rapid growth of prices of long-term deliveries from the previous years which increased the price of a futures contract for the year 2007 to a level of 60 €/MWh. After the collapse of the emission coupon market the growth of energy prices slowed down. At the beginning of April the public was informed about the data relating to the use of coupons for the first emission period and it became evident that the quantity of coupons used did not reach the quantity in accordance with the allocation plan of distributed coupons. This situation caused an immediate reduction in coupon prices amounting to 10 €/ton. Slightly less dramatic was the reduction of coupons planned for the second allocation period, nevertheless the prices dropped significantly. The reduction in prices of emission coupons caused the reduction in prices of electrical energy and the delivery for 2007 dropped to less than 50 €/MWh. The market of emission coupons had the strongest influence on long-term markets, but the reduction in coupons on the day-ahead market had no such immediate drastic influence.

In 2006, the price of Brent crude oil for the delivery in the following months achieved a historic value since it exceeded 75 $/barrel which is an absolute price record. Since oil prices are followed by gas prices in a period of 6 - 9 months, high oil prices announced high prices of gas at the end of the year. Due to such circumstance the loading of thermal power plants would increase and result in an increase in prices of emission coupons from 10 €/ton to 16 €/ton.

In summer months we again witnessed price records for deliveries of electrical energy on a day-ahead market when the consumption strongly increased due to the influence of a heat wave, but the production of thermal power plants and the nuclear power plant, cooled by river flows, was limited due to their heating. The price of daily band deliveries on the Leipzig Exchange exceeded the value of 300 €/MWh. At the end of the year, the above average temperatures and sufficient production capacities caused a reduction in energy prices. An additional factor in energy prices was prices of emission coupons that dropped from at the middle of the year and reached the level of about 5 €/ton at the end of the year. Unlike in 2005 when daily prices rose in winter, the mild winter in the year 2006 resulted in low prices on the day-ahead market.

In the year 2006, the optimisation of marketing activities and production continued under consideration of market prices of electrical energy at an hourly level. Advantage was taken of price margins in individual hours, of purchases at less expensive time and sale in more expensive hours in order to maximise revenue.

2.5.3.3 Southeastern Europe

At the beginning of the year, prices of electrical energy on the markets of southeastern Europe were far below the prices in Continental Europe due to favourable hydrological circumstances. The situation changed in the second half of the year 2006 since the excessive offer of electrical energy practically vanished.

Due to the increase in prices on the market of Continental Europe under the influence of the European trading scheme with CO_2 emission coupons and other energy products the energy supplies were even more expensive than those on the southern border in the first half of the year. Price relationships among markets were successfully utilised since the energy purchased on the southeastern markets was delivered to Continental Europe. Unfortunately, high prices of cross-border transfer capacities reduced profits of such transactions.

In spite of auctions for the allocation of cross-border transfer capacities on Slovene borders that significantly increased the prices of imported electrical energy from southeastern Europe to Slovenia, these markets were for HSE the principal foreign purchasing markets in 2006.

Nevertheless, any increase in the volume of trade is still hindered by a variety of costs and restraints pertaining to transits of electricity, which are - contrary to the European legislation - imposed on the electricity traders by transmission systems operators. However, the liquidity of trading in southeastern markets increased significantly although some other Slovene operators have also introduced auctions for cross-border trading in accordance with the Slovene model. It shall be emphasised that trading on the Hungarian market has become transparent and the liquidity on this market has improved which is contributed also by providers of portal trading.

The high rate of economic growth in southeastern Europe has increased the demand for electrical energy. More consumption reduces the amount of surplus production capacity, which in turn enhances growth in prices. Besides that, a major part of production capacities of electrical energy is based on hydropower production which increases the volatile character of prices. Poor hydrology and constant growth of consumption in the second half of the year influenced the exceptional increase in prices of electrical energy in this area. The prices of long-term contracts on southeastern markets exceeded those in Continental Europe and came close to the prices on the Italian market in spite of the fact that producers in this part of Europe are not involved in the CO_2 trading scheme.

2.6 SALES AND CUSTOMERS

2.6.1 ELECTRICAL ENERGY

Price of electrical energy

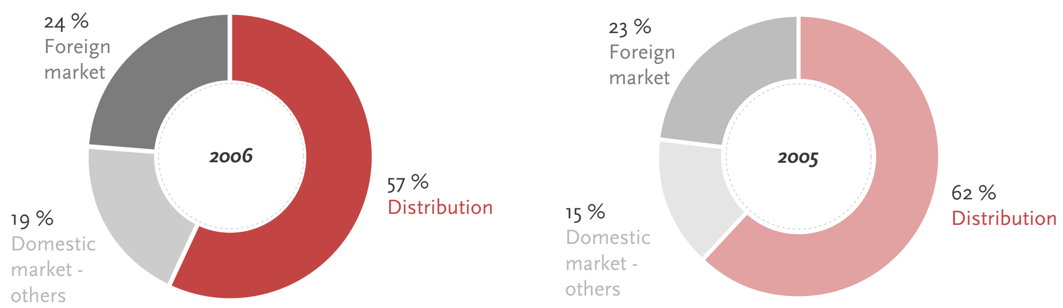
In 2006, electrical energy pricing was subject to market conditions, so that the margin price was again determined on the basis of the most expensive unit of energy at a specific moment. The factors affecting pricing were: the price of CO_2 emission coupons, atmospheric factors, in particular temperature, wind and hydrology, available cross-border transfer capacities, and the growth of energy consumption both within the country and abroad.

In order to maximise the operating result of the Company at acceptable risk exposure, coordinated activities were conducted in connection with the sale of electrical energy generated by HSE Group companies, trading in electrical energy from other sources, and managing the generating plants of HSE Group companies.

Sales volume

In 2006, the total sales volume of the HSE Group in both domestic and foreign markets amounted to 16,088 GWh of electrical energy. The most important was the domestic market, which accounted for 76.2 % of the total sales, of which 57.2 % to five distribution companies, 17.7 % to other direct customers, and 1.3 % to GEN energija, GEN I, and ELES as tertiary and secondary control energy, and deviations. Exports accounted for 23.8 % of sales, mostly to Italy. The HSE Group successfully participated in auctions for the allocation of cross-border transfer capacities for the export of electrical energy to Italy, and thereby increasing its presence in the Italian market, which is, owing to its high electricity prices, the Group's most lucrative market.

Structure of sales in 2006 and 2005



Long-term contracts and day-ahead market

The HSE Group generated the bulk of its sales revenue under long-term contracts. Trading on day-ahead markets was carried out for the purpose of balancing contractual obligations with the production possibilities of HSE Group companies, as well as optimising the Group's portfolio and taking advantage of market opportunities. The energy surpluses generated during periods of increased streamflows and additional quantities of electrical energy were sold on day-ahead markets, when market prices exceeded the costs of additional production.

Ancillary services

In addition to electrical energy, the following contracted ancillary services were provided in 2006:

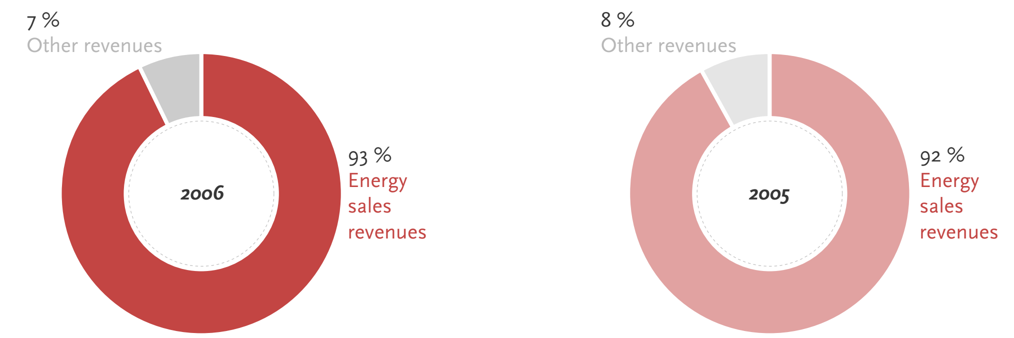
- secondary frequency control in a range of ± 67 MW in the period from 3 January to 28 July and from 19 September to 31 December, in a range of ± 77 MW in the period from 1 January to 29 July, from 29 July to 4 August, and from 22 August to 18 September, and in a range of ± 80 MW in the period from 5 August to 21 August;
- tertiary frequency control with the inclusion of non-spinning and spinning reserves in the amount of 163 MW in the period from 1 January to 31 December 2006;
- black start capability;
- reactive power support;
- secondary control services.

2.6.2 OTHER ACTIVITIES

Structure of total sales revenue

In 2006, the HSE Group generated a sales revenue in the amount of 202 billion SIT, of which 31% was generated abroad. In the structure of sales revenues, electrical energy accounted for 93 % of net sales revenue, and other products and services accounted for 7 % of net sales revenue of the HSE Group.

Sales revenue in 2006 and 2005



Other products and services

Other activities comprise, as their major part, the production of calcium carbide, ferrosilicon, and complex alloys.

Other activities also comprise the production and sale of thermal energy as well as other services and products provided or produced by the Group companies within the scope of their activities

Thermal energy

In 2006, the HSE Group sold 425 GWh of thermal energy.

2.7 PURCHASES AND SUPPLIERS

Power plants in the HSE Group in 2006

DEM		Dravograd	Vuzenica	Vuhred	Ožbalt	Fala	MB otok	Zlatoličje	Formin	Small HPPs	Total
	Nr of agregats	3	3	3	3	1+2	3	2+1	2	1	
Net capacity	MW	26	56	72	73	58	60	114	116	0,7	576
Rated generation capacity	MVA	36	78	90	90	74	78	148	148	1,2	743
Gross head Hbr.	m	8,9	13,7	17,4	17,4	14,6	14,2	33	29		148
Rated flow Qi	m³/s	405	550	550	550	505	550	463	500		

SEL		Moste I.	Moste II.	Mavčiče	Medvode	Vrhovo	Small HPPs	Total
	Nr of agregats	3	1	2	2	3	1	
Net capacity	MW	13	8	38	26	34	0,05	119
Rated generation capacity	MVA	22,5	11	50	27	42	0,09	153
Gross head Hbr.	m	70,45	177,2	17,5	21,2	8,12	-	294
Rated flow Qi	m³/s	28,5	6	260	142	500	-	

SENG		Doblar I.	Doblar II.	Plave I.	Plave II.	Solkan	Zadlaščica	Small HPPs	Total
	Nr of agregats	3	1	2	1	3	2	26	
Net capacity	MW	30	40	15	19	32	8	11	155
Rated generation capacity	MVA	48	50	22	23	39	10	12	204
Gross head Hbr.	m	47,2	48,5	27,5	27,5	23			174
Rated flow Qi	m³/s	90	105	75	105	180	2,2		

TEB		Parna 1	Parna 2	PB I.	PB II.	PB III.	PB IV.	PB V.	Total
	Nr of agregats								
Net capacity	MW	10	11	21	21	21	114	114	312
Rated generation capacity	MVA	16	15	32	32	32	155	155	437

TEŠ		Blok1	Blok2	Blok3	Blok4	Blok5	Total
	Nr of agregats						
Net capacity	MW	25	25	69	248	305	672
Rated generation capacity	MVA	37,5	37,5	94	324	377	870

TEŠ Generator 1 and 2: Due to the exhaustion of generators the anticipated availability is lowered to 25 MW
TEŠ Generator 5 has a capacity of 377 MVA at 3 bar of hydrogen pressure.

2.7.1 ELECTRICAL ENERGY

Synergy

With the objective of maximising performance, the HSE Group endeavours to take advantage of synergies associated with a wide spectrum of production capacities. Because the operating and cost-related characteristics of individual generating plants differ, the cost-effective production of electrical energy can be achieved by appropriate production scheduling. And since the price of electrical energy fluctuates on the market, the economical dispatching of production units while observing technical criteria is all the more important.

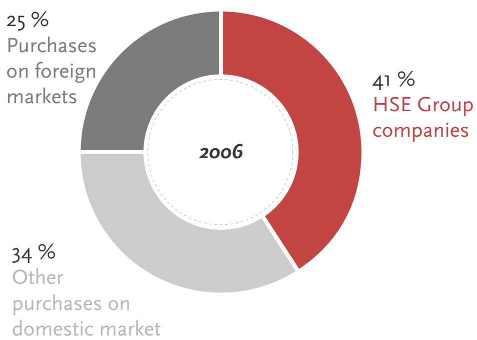
Structure of purchases

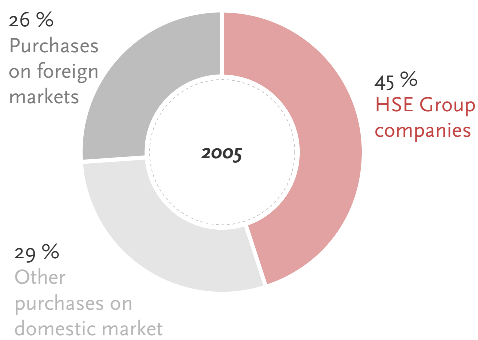
In 2006, electrical energy supplied by the HSE Group to its customers was mainly purchased from its subsidiaries (41.3 %), while 24.8 % was purchased abroad. Electrical energy purchases in the remainder of the domestic market accounted for 33.9 % of the total purchases, the major portion representing purchases from GEN energija.

Electrical energy purchase in 2006 and 2005

Source	2006		2005	
	GWh	Share	GWh	Share
HSE Group companies	6,647	41.3%	6,423	44.7%
Other purchases on domestic market	5,455	33.9%	4,187	29.1%
Purchases on foreign markets	3,986	24.8%	3,754	26.1%
TOTAL	16,088	100.0%	14,364	100.0%

Electrical energy purchases in 2006 and 2005

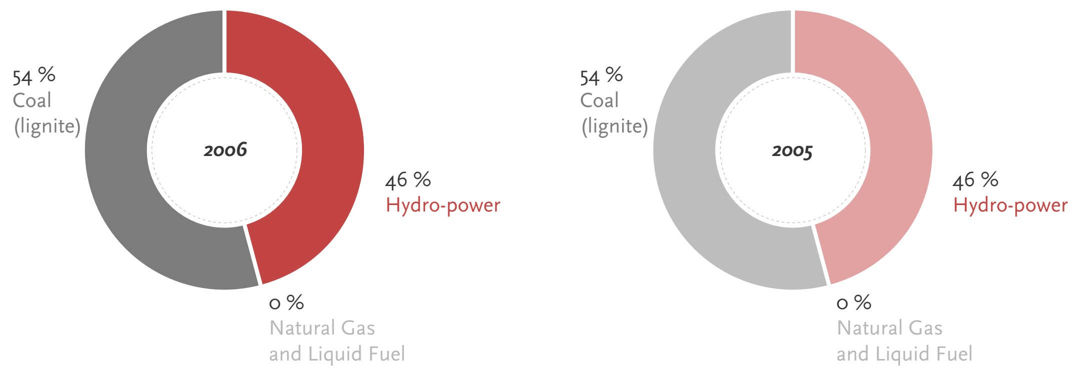




Primary raw materials

In 2006, primary raw materials for electrical energy production included water potential (45.9 %), coal (53.9 %), and natural gas and liquid fuel (0.3 %).

Primary raw materials for electrical energy production in 2006 and 2005



Purchase optimisation

The average attained purchase price of electrical energy increased in 2006 in comparison with the 2005 figure. The higher purchase price is mainly due to:

- the worsening hydrological situation, resulting in an 11.6 % lower production of cheaper hydropower in HSE Group companies compared to the planned output, and
- unfavourable conditions in the electricity market.

With the help of the balance group and electrical energy production management system, appropriate electricity market products, such as base load, peak, off-peak, and hourly power, were developed and included in the product portfolio of the HSE Group.

Coal

To meet the needs of electrical energy production in TEŠ, 42,982 TJ of coal was purchased in Premogovnik Velenje (Velenje Coal Mine). At year end, the coal stock amounted to 3,957 TJ.

2.8 INVESTMENTS

In line with its investment plans and projects, the HSE Group undertakes to ensure the reliable supply of electrical energy in Slovenia as well as its gradual expansion to foreign markets.

The HSE Group is aware of the following key facts:

- the HSE Group's customers are dependent on the quality of electrical energy,
- electrical energy must primarily be generated at home and an adequate capacity provided,
- greater efficiency may only be achieved by the efficient utilisation of primary sources,
- a high degree of supply reliability can only be achieved by appropriate diversification of sources,
- new sources and know-how should be developed.

The investments of the HSE Group are aimed at modernising the existing thermal power plants and hydro-electrical power plants, and constructing new power facilities in order to upgrade the existing good structure of power generating sources and improve the long-term competitiveness of all subsystems of the HSE Group.

The HSE Group's commitment to streamline the production process is not only demonstrated by cost reductions, but also by the implementation of an optimal policy of new investments in line with the strategic objectives of the HSE Group.

In 2006, the construction of new production facilities and the professional maintenance of existing facilities progressed according to plan.

A period of intensive investments previously initiated by the HSE Group continued in 2006 with further investments in intangible assets and property, plant and equipment.

2.8.1 TOP PRIORITY INVESTMENTS

2.8.1.1 Hydropower Plant on the Lower Sava River

Joint venture agreement

In 2003, a joint venture agreement was signed by the companies HSE, DEM, SEL, SENG, and TEB for the construction of hydropower plants on the lower Sava River. Under this agreement, the contracting parties undertook to contribute funds in the following shares:

- HSE 51.00 %
- DEM 30.80 %
- SEL 12.60 %
- SENG 2.80 %
- TEB 2.80 %

Accounting for joint venture

On the basis of the above-mentioned Agreement, the controlling company set up in its financial statements, for the period from 2004 to 2006, long-term provisions for liabilities arising from investments made by DEM, SEL, SENG and TEB.

Boštanj Hydropower Plant

The construction of the Boštanj Hydropower Plant - the first in a series of five new hydropower plants on the lower Sava River - was after 42 months completed at the end of May 2006 according to schedule. On 5 June 2006, a one-year trial run of the hydropower plant was started. During the trial run, any defects found in built-in equipment will be remedied, guarantee measurements performed, and the group and remote management of the hydropower plant will be tested.

Due to certain defects found in generators, there is a possibility that the repair of all three generators will not be completed during the trial run. For this reason, the trial run will be extended for another year. Given the anticipated scope of repairs required in generator no. 2, the reconnection of generator no. 2 to the network may be realistically expected in May 2007. Repairs on the other two generators are expected to be completed by the end of 2007. Following their rehabilitation, measurements of guaranteed values will be carried out and an application for the acquisition of a use permit will be filed.

In the period from 5 June, when the trial run was begun, to the end of 2006, the Boštanj Hydropower Plant generated 47.9 GWh of electrical energy.

Blanca Hydropower Plant

Preparatory works have been completed. Intensive construction works are in progress on the dam structures. In line with a decree issued by the Slovene Government, the execution designs and the Infrastructure Development Program were amended. A contract for the supply of main technological equipment was signed.

Krško Hydropower Plant

The National Spatial Plan was adopted. An understanding was reached and an agreement signed on the construction and co-financing of a bridge and a by-pass road. The purchases of required land plots were started.

Brežice Hydropower Plant

The first environmental conference was held, and pre-investment studies and documents were commissioned.

Mokrice Hydropower Plant

Pre-investment studies and documents for HE Mokrice were commissioned. The elaboration of outline plans and pre-investment plans was started.

2.8.1.2 Avče Pumped Storage Plant

Pumped storage plant

In periods of low electricity prices (at night and on weekends), energy is used to pump water to the reservoir. In periods of high electricity prices (work-day peaks), the accumulated water is used for the generation of electrical energy.

An investment project has been under way since 2003, when design and investment documents serving as a basis for the adoption of a relevant decision were elaborated. In 2004, the investment program was approved.

In 2005, a tender for works on individual segments of the project was called and the main construction works were started.

In 2006, works were begun on the upper reservoir, which included soft soil excavations and the transport of materials to a permanent dumpsite in the vicinity of the reservoir.

42 meters of access tunnel and 10 meters of lower surge chamber were constructed. Works were continued on the pipeline route, which included excavations for deep foundation with wells.

The main engine shaft was entirely excavated, followed by the installation of siphon lining and the concreting of siphon.

Investor

The project investor is SENG.

In the course of 2006, working drawings were prepared by the supplier of equipment and the basic designs for mechanical and electrical installations were handed over by the engineering company. Further reconciliations were performed in the design of pressure piping and other hydro-mechanical equipment. Model research studies of the lower intake/discharge facility were prepared and successfully completed

2.8.1.3 Restoration of Medvode Hydropower Plant

Investor
The project investor is SEL.

After the successful completion of rehabilitation works on generator no. 2 at the beginning of 2005, generator no. 1 stopped running at the end of May of the same year. The generator was dismantled, and the installation of a new turbine up to the free turbine shaft was started in the beginning of December. After installation of the generator, an internal technical inspection and the first drilling with water flush were performed. The secondary equipment and safety speeders were then tested, and the generator was synchronised to the power network in March 2006. Since the end of March 2006, generator no. 1 has been operating on a regular basis. A technical inspection of restored generators and joint facilities of the Medvode Hydropower Plant was conducted in July 2006. A new use permit was issued in September 2006.

Following the rehabilitation of the two generators, the engine house roof was also restored. Restoration works comprising the replacement of waterproofing, fitting of new floor coverings and troughs, and the installation of a new electric heating system for drains were completed at the end of July. The last phase of restoration of the Medvode Hydropower Plant will include the restoration of mechanical parts of portal crane drives, whose completion is scheduled in May 2007.

2.8.1.4 Rehabilitation of Zlatoličje Hydropower Plant

Investitor
The project investor is DEM.

The Zlatoličje Hydropower Plant, the largest channel power plant in Slovenia, has been operating reliably since 1969. Its restoration is urgent due to the deterioration of generator and turbine equipment. The objectives of the restoration plan also include increased electrical energy production and increased safety for persons and the environment.

In 2005 and 2006, most of the contracts with suppliers of equipment and contractors were concluded. A major portion of the equipment for secondary systems has already been supplied. In 2006, construction works on the Melje Dam, Melje Mini-Hydropower Plant, inflow channel, and the engine room were started.

The technically most complex phase of restoration works involving the replacement of turbine and generator equipment will be carried out in the period from July 2007 to March 2009.

2.8.1.5 Generator No. 6, 600 MW, in TEŠ

Investor
The project investor is TEŠ.

The pre-investment plan for generator no. 6 was presented at the HSE strategic conference in September 2005, where the construction of generator no. 6 in TEŠ was ranked among the priority projects of the HSE Group.
On the basis of the above-mentioned, an investment program was com-

piled for the new power plant - generator no. 6 in TEŠ. The investment program was originally compiled for a 520 MW power plant, but was subsequently amended and now presents and deals with a 600 MW power plant.

Parallel to the preparation and processing of investment documents, other procedures and activities are under way for incorporating the planned investment in the energy system and the environment. In November 2005, the Ministry of Economy issued an energy permit for a 520 MW energy plant, which was subsequently changed in May 2006 to apply to a 600 MW energy plant.

The placing of the above-mentioned power plant in the environment calls for the adoption of relevant spatial documents. The procedure for issue of two site plans is progressing in line with the time schedule. Procedures for the supply of equipment and services have also been started.

According to the current schedule, the completion of this project is foreseen in 2012.

2.8.1.6 Upgrade of Generator No. 5 in TEŠ

Owing to obsolete technology, the plant's efficiency needs to be increased and coal consumption reduced. This will result in lower emissions of greenhouse gases.

Investor

The project investor is TEŠ.

The optimal solution for generator no. 5 in TEŠ has proved to be the enlargement of two gas turbines into a combined gas/steam turbine plant whose process is based on the heating of feed water by a steam generator.

The enlargement of two gas turbines in generator no. 5 will increase the installed capacity of the generator by 84 MW and improve its efficiency.

The objective of the investment is to increase electrical energy production while consuming the entire planned quantity of coal in accordance with the long-term coal supply contract, lower the CO_2 emission factor per kWh, reduce the price of electrical energy, and fulfil the obligations under the Kyoto Protocol.

In 2006, the Government adopted the National Spatial Plan for the construction of the Šentrupert-Šoštanj gas pipeline. A long-term sales/purchase contract for natural gas was concluded with Geoplin, as well as contracts for the supply of gas turbines and utilisers.

2.8.1.7 Kozjak Pumped Storage Plant

The Kozjak Pumped Storage Plant will increase the competitive strength of DEM and HSE in terms of production and economy. It will enable the pumping of water to the reservoir during periods of low electricity prices, and the generation of electrical energy during periods of higher electricity prices. The higher reliability of power will result in favourable economic effects for HSE and DEM.

Investor

The project investor is DEM.

The activities conducted in 2006 included the implementation of the National Spatial Plan, research projects, and the revision of conceptual design solutions.

2.8.2 OTHER MAJOR INVESTMENTS OF THE CONTROLLING COMPANY

Kidričevo gas-fired thermal power plant

Plinsko parna elektrarna d.o.o., Kidričevo was incorporated in 2004 for the purpose of planning the construction of 800 MW gas-fired thermal power plant in Kidričevo. The owners of the company are HSE (45%), Verbund (40%), and Talum (15%).

In 2006, the conceptual plan required in the elaboration of the National Spatial Plan was prepared.

The project sponsor is PPE Kidričevo d.o.o.

Control Centre of the HSE Balance Group

In the beginning of 2006, the hardware and software for the new control centre were transferred from Sweden to the provider of services in Ljubljana. This was followed by database preparation and the elaboration of operator images. For the needs of HSE, the signal lists of DEM, SENG, TEB, TEŠ, and SEL were checked and the execution of commands for DEM was approved. A flowchart of schedule was prepared for all HSE members. Hydrological models of all river basins and thermal power plants were elaborated for the optimisation model.

In the spring of 2006, the majority of training programmes for system administrators were completed. A workshop for database preparation and image elaboration was also organised. In June, factory tests of equipment for the control centre were performed at the manufacturer's plant. The testing of functional sets, such as SCADA, automatic production control, and log book, was successfully completed, while planning and optimisation tests showed a need for some corrections.

Following the delivery of hardware and software to the site in Maribor, the servers, workstations, and communication system were installed. Connections were established with hydropower plants, ELES, and HEP. A connection was also established with the metering system and the security centre.

In December, the final acceptance of the control centre system in Maribor and the factory acceptance of equipment for the SEL control centre were simultaneously conducted.

HSE Fault and Event Analysis Centre

The construction of the HSE Fault and Event Analysis Centre was completed. All computer-related works on protective relay connections from facilities of the HSE Group to the communication junction were completed. Software was tested during the preparation of individual protective relay modules in the plants of the HSE Group. Within the scope of this project, the Boštjan Hydropower Plant was connected to the remote control system, but not to the HSE security centre. In 2007, the connection of the Trbovlje Thermal Power Plant to the HSE security centre is planned.

HSE Telecommunications Network

In January 2006, the final acceptance of the HSE and DEM telecommunications networks was conducted and the guarantee period began to run. At the end of September, ELES released a pair of optical fibres on the Dravograd-Šoštanj route, thus putting into operation the last missing part of the telecommunications ring. Redundant operation has now been made possible in the eastern part of the telecommunications network. The Boštanj telecommunications junction was also commissioned. The completion of this telecommunications junction was delayed because part of the supplied passive equipment, i.e. optical filters, differed from the filters built into other junctions, as the supplier was unable to meet our demands for the harmonisation of equipment. The technical documents for the Boštanj telecommunications junction were handed over by the contractor. The installation and commissioning of continuous power supply to the Brestanica telecommunications junction were carried out. The continuous supply system was relocated from the abandoned HSE telecommunications junction system in Velenje, thus ensuring redundant power supply to the telecommunications junction. Inspections were conducted at the telecommunications junctions in order to examine and correct relevant documents. The connections between HSE members were transferred to the telecommunications network. The existing connections leased from ELES were cancelled.

Underground natural gas storage facility

In 2006, the preliminary study & research documents were prepared. These comprised the elaboration of studies and the conduction of field and laboratory research activities. In future it will be necessary to prepare a draft design, environmental studies together with impact assessments, an investment programme for a connecting pipeline with accompanying facilities, and to supplement the feasibility study relating to the construction of this facility. In accordance with the agreement reached between HSE, Geoplin-plinovodi and the Brestanica Thermal Power Plant, these activities will be continued and will include the preparation of study documents (draft design of underground storage facility and investment program), which will serve as a basis for the final decision on the continuation of this project.

Hydropower plant on the central Sava River

The preparation of technical documents for the construction of a hydropower plant on the central Sava River is in the final phase. These documents have been prepared in several versions, both in respect of construction (derivation principle, overflow principle) and in respect of location of the hydropower plant (in the region of the upper Sava River from Medvode to Zalog, and in the Litija region). Several versions have also been prepared in respect of equipment used and construction of planned buildings. In order to obtain as realistic data as possible for the design and economic assessment of the project, measurements of the gravimetric courses of "fixed points of altitude" and river profiles were conducted. Project assignments were also prepared on the basis of conclusions derived from previously prepared technical documents (geological investigations), environmental protection, and water habitats, which will be used in the continuation of the project. The works are scheduled for completion in May 2007, when a pre-investment plan will be drawn up, providing answers for the economic part of the project as well. A basis will therefore be given for deciding on the further course of the project. The documents prepared so far will be presented to the local communities. A good cooperation network has been established. Owing to the problems relating to Nature 2000, a detailed program of measures will be prepared in cooperation with the Fishing Association of Slovenia, in particular for the upper part of the central Sava River, as well as an inventory of the habitat area, and an awareness and acceptability program.

Activities relating to the drawing up of a concession agreement are also in progress.

2.8.3 OTHER MAJOR INVESTMENTS OF SUBSIDIARIES

DRAVSKE ELEKTRARNE MARIBOR

The reconstruction of the Zlatoličje Hydropower Plant is, next to investments in the construction of a hydropower plant on the lower Sava River, the second largest investment of DEM. Within the scope of this reconstruction project, construction works were started in 2006 on the Melje Dam, Melje Mini Hydropower Plant, supply channel, and on the hydropower plant's engine room. Final works were also completed on the reconstruction of the Vuhred and Ožbalt Hydropower Plants. Within the scope of reconstruction works on the Kozjak Pumped Storage Plant, activities relating to the implementation of the National Spatial Plan, research studies, and the revision of conceptual design solutions were conducted.

SAVSKE ELEKTRARNE LJUBLJANA

Investment projects were implemented in line with the approved business plan. In addition to the construction of a hydropower plant on the lower Sava River, major investments included the reconstruction of the Medvode Hydropower Plant and the Moste Hydropower Plant, the upgrade of control equipment at the Vrhovo Hydropower Plant, and the modernisation of the SEL Control Centre.

SOŠKE ELEKTRARNE NOVA GORICA

Two thirds of the planned investments for 2006 were realized. The majority of funds were earmarked for the construction of the Avče Pumped Storage Plant, the construction of a hydropower plant on the lower Sava River, and the elaboration of design and investment documents.

TERMOELEKTRARNA BRESTANICA

Alongside investments in the construction of a hydropower plant on the lower Sava River, the company carried out some minor modifications in the automation of existing facilities, prepared design and development documents, and completed the development of the TEB complex information system.

TERMOELEKTRARNA ŠOŠTANJ

Investment activities were conducted in line with the adopted business plan. The highest investments were earmarked for the combined gas/steam system of generator no. 5 and the construction of a new steam generator no. 6. Major investments in generator no. 5 are connected to the planned major overhaul of generator no. 5 in 2007.

PREMOGOVNIK VELENJE

In 2006 the company exceeded the planned investments by 2 percent. Most of the funds were used for underground structures, i.e. the construction of a main railway transport route for coal removal from the bottom of the basin and for rehabilitation of the central tunnel - excavation of railway route and installation of panels, acquisition of digging equipment. This was followed by works on underground structures and investments in IT equipment.

2.9 INFORMATION TECHNOLOGY

The following main IT objectives were achieved in 2006:

- increased in speed and reliability of data links,
- introduction of electronic document system to support business processes,
- continuing development of the management information system,
- regular upgrading and modernisation of system equipment and installation of all security corrections, assuring reliable and safe system operation,
- implementation of effective control and management systems for active and passive networks and all platforms,
- continuing development of a uniform information platform in the HSE Group.

ODOS Electronic Document System

The electronic document system was further implemented in 2006. ODOS provides for quick access to documents, easier document search and retrieval, processing and management, shortens business processes and records them accurately. All functions that are interrelated or related to other information systems are performed automatically, thus facilitating the work of system users.

MIS-MAKS Management Information System

The MAKS web application is designed to monitor the financial-accounting data of the HSE Group companies. All data is stored in the same place and adequately classified. The application provides for the generation of standard reports, defines indicators, and points out deviations.

Maximo Maintenance Information System

The working group, together with the contractor, prepared a proposal of joint starting points for the introduction of a computer-supported maintenance information system in the HSE Group for the following areas:

- record keeping and monitoring of devices and facilities by site,
- maintenance management and control supported by working documents,
- record keeping of maintenance personnel,
- management, integration, and analysis of information.

The contractor united all the discussed contents into a final document that was approved by members of the working group and the security council. Alongside the DEM, TEB, and TEŠ companies, which have already implemented this software, the SEL and SENG companies have also started to implement the software designed to support maintenance processes.

Security control

Security control of the information system is a process based on the execution of special, previously prepared tests with the goal of detecting security problems in IS. By use of verified methods, the contractor attempted to identify any potential weaknesses in the system. All the necessary works needed to eliminate deficiencies were performed.

Consolidation of Oracle Databases

The greater stability, reliability, and security of data were ensured at a lower price by the consolidation of databases. The high availability of all databases in the system is achieved by a smaller number of servers that are now united in a cluster and therefore less vulnerable.

2.10 FINANCIAL OPERATIONS

Principle Activities

In 2006, the financial operations of the HSE Group were primarily aimed at:

- ensuring solvency and optimising liquidity of the HSE Group,
- implementing financial policy with respect to banks and other financial institutions,
- managing related risks.

The basic function of financial operations is to ensure the solvency of the HSE Group and, consequently, the undisturbed performance of other business activities. The current solvency of the HSE Group was ensured in 2006 by monitoring and optimising current cash surpluses and deficits in HSE Group companies. In addition, cash flows were managed effectively by the implementation of a liquidity reserve policy based on credit lines granted by domestic and foreign banks, diversification of investments and liabilities, maturity adjustment of receivables and liabilities, and the consistent collection of receivables.

In 2006, both the controlling company and the HSE Group as a whole were very active in the field of financing, particularly in ensuring the necessary financial sources under favourable terms for the implementation of the HSE Group's development projects. HSE Group companies borrow funds independently in accordance with the conditions and procedures of the Decree on the conditions and procedures of borrowing, as stipulated in Article 87 of Public Finance Act. The HSE Group carefully examines various financing options and, by choosing the most favourable financial sources, lowers the value of necessary project investments and costs of financing. In the beginning of 2006, SENG signed a Loan Contract with the European Investment Bank (EIB) in the amount of 43 million EUR for an investment in the Avče Pumped Storage Plant. At the same time, a guarantee contract serving as security for the EIB loan was concluded between SENG, HSE as the controlling company, and a syndicate of domestic and foreign banks.

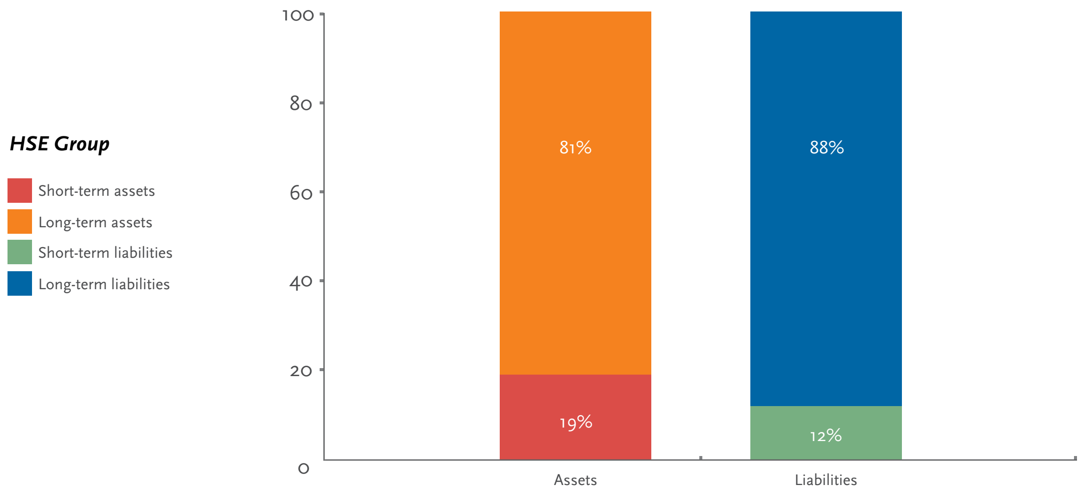
At the end of 2006, financial liabilities were recorded by the HSE Group in the amount of 45.9 billion SIT, of which long-term financial liabilities accounted for 77 % and short-term financial liabilities for 23 %. The long-term financing to long-term assets ratio of the HSE Group was 109 %. The financial liabilities denominated in SIT, EUR and CHF were recorded separately. In 2006, the share of EUR borrowings increased considerably. This was due to Slovenia's admission to the European Monetary Union as well as to costs of borrowing, since foreign currency borrowings within the country and abroad were cheaper than borrowings in SIT. For this reason, a large portion of borrowings is linked to a variable interest rate requiring the use of financial instruments to hedge against interest rate risks.

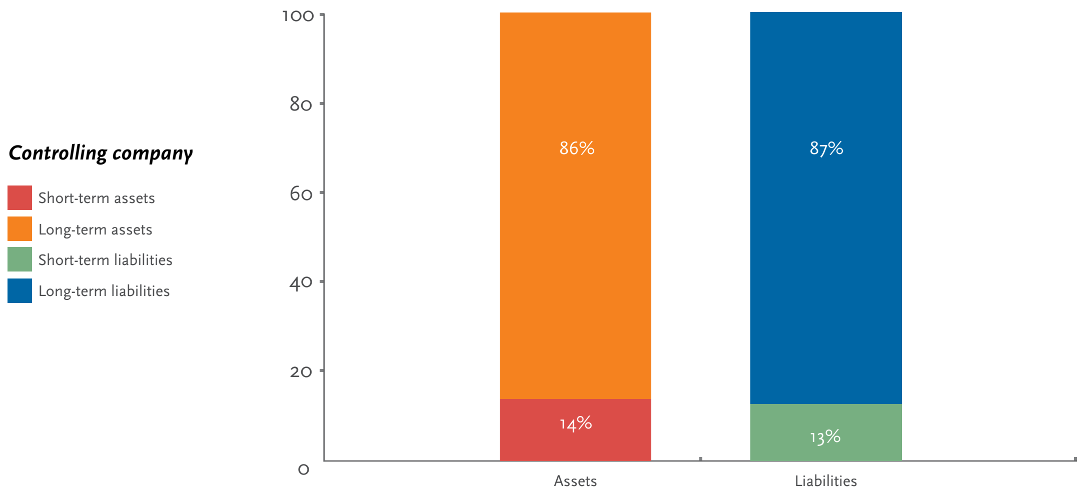
In the risk management process, special attention was paid to interest rate risk, credit risk, currency risk, and liquidity risk. Liquidity risk was effectively managed by monitoring and optimising current cash surpluses and deficits in HSE Group companies. Within the scope of interest rate risk management, derivative financial instruments provided by banks were used to change a portion of variable interest rates into fixed interest rates.

Achieved Goals

An analysis of the financial operations of HSE Group companies shows that all set goals and objectives were achieved. HSE Group companies did not have any solvency problems, and the financial resources required for the implementation of investments were provided. Observing the principle of diversification within the scope of the safety principle, placements of free cash ensured adequate returns.

Balance sheet structure of the HSE Group and the controlling company as at 31 December 2006





2.11 RISK MANAGEMENT

The HSE Group is fully aware that risk management consists of two interrelated components:

- identification of risk,
- adequate control of all significant types of risks.

In 2006, the upgrading of risk management systems in the HSE Group was continued. For this purpose, a Risk Management Committee was established for the purpose of creating an effective environment, guidelines, strategies, processes, methods and controls for risk measurement. The Risk Management Committee is composed of experts from various departments in the company, which ensures a complete overview of risk exposure. The Risk Management Committee will upgrade the existing risk management system and risk management organisation.

In 2006, the most intensive efforts were devoted to preparing a methodology, processes and controls for measuring the credit, price and volume risks to which the HSE Group is most exposed.

The HSE Group is exposed to risks in all areas of operation, particularly in electrical energy production and marketing. These may roughly be classified in the following groups:

- price or market risk,
- volume risk,
- financial risk,
- human resources risk,
- information system risk.

MARKET RISK

The HSE Group continued to develop the market and volume risk monitoring model, which is based on computation of the trading portfolio's open position, optimisation of the Group's production units and the company's trading activities, automated monitoring and assessment of price fluctuations on the Group's electrical energy wholesale markets. The model enables monitoring of the company's trading portfolio risk exposure in real time.

In line with the market risk management strategy, the company's exposure to unfavourable market conditions was managed by conclusion of several long-term contracts for electrical energy supply with different partners and by standardised futures contracts. Long-term contracts were concluded in different markets in line with the company's portfolio coverage strategy.

Long-term contracts for electrical energy supply as a means of decreasing market risk are contracts with a delivery term of one year or more. Long-term contracts are concluded on different regional markets via trading portals, directly with partners on the basis of inquiries and quotations, or by participation in tenders. The conclusion of long-term contracts guarantees the supply of electrical energy to the company at fixed prices over specific periods of time, regardless of the conditions on the daily energy market.

Standardised futures contracts for electrical energy supply as another significant means of managing exposure to electrical energy market price fluctuations represent an increasingly more liquid financial instrument in the electrical energy market, particularly when trading is conducted for two or more years in advance. Futures contracts are traded on the European Energy Exchange (EEX). This type of trading involves no physical supply of electrical energy, thus eliminating the need for formalities regarding the submission of schedules, membership in balance groups, etc. For this reason, futures contracts are not only traded by participants of the electrical energy spot market, but also by banks and other financial institutions, which ensures the liquidity of this market. To hedge against risks, it is important to be able to settle the futures contract with regard to the daily market, where energy is supplied against a long open position. The final price of energy supply is equivalent to the price of opening a long position.

Risks are assessed using standard risk assessment methods, such as the Monte Carlo method and the VaR method. The results of the model are summarised in the Analysis of Trading Portfolio and Risks, which is prepared bi-weekly as a tool for deciding on further product trading in the electrical energy market.

The Management Board is regularly briefed on the results of analyses and the management of key risks in this area, and informs the Supervisory Board thereof as the need arises.

The Management estimates that the market risk was well-managed in 2006 by the implementation of planned activities, established information support, and by the regular exchange of relevant information and experiences with other domestic and foreign energy supply companies. Risk exposure was moderate due to a further internationalisation.

VOLUME RISK

Volume risk consists of risks arising from production uncertainty, consumption uncertainty, and energy supply uncertainty.

- Production uncertainty is mainly associated with the question whether or not electrical energy will be available on the market. It is also linked to operational risk, which tries to assess the probability and effect of breakdown of a generator or any other production unit. Particularly important is the impact of uncertain hydrology, because more than one half of electrical energy is provided by hydropower plants.
- Consumption uncertainty is due to the impact of weather and temperature, load flexibility, seasonal cycles, and stochastic consumption growth.
- Energy supply uncertainty is due to random failure of power lines and other equipment, or to interventions by an operator of the power transmission network as the result of transmission path overload.

Electrical energy production is exposed to the following risks of deviation from planned supplies:

- the risk of non-supply of electrical energy from hydropower plants due to hydrological and meteorological conditions;
- the risk of non-supply of electrical energy from thermal plants due to outages or technological and ecological limitations to production;
- the risk of non-supply of coal from the Velenje Coal Mine due to production hold-up caused by outages, breakdowns of technological systems, accidents, or other geological disturbances;

- the risk of non-supply of gas to TEB is possible due to restraint on supply in case of failure to notify in advance of required quantities, particularly in winter, when there is not enough gas available. The gas may be replaced with extra light fuel oil, which considerably increases the production price;
- in periods of increased production in thermal plants, economic limitations should also be considered, i.e. any changes in the method of CO_2 tax payment and the introduction of trading in CO_2 emission coupons, in line with the implementation of the Kyoto Protocol and the EU Directive on trading in greenhouse gases.

In 2006, the volume of electrical energy generated by hydropower plants was lower by 420 GWh compared to the projected figure due to unfavourable hydrology conditions. The volume of electrical energy generated by TEŠ was higher by 349 GWh compared to the projected figure. TEB realised 19.5 % of the projected volume (80 GWh less than planned). The low generation of electrical energy by TEB is due to the mild winter and favourable market prices.

The deviations of actual daily water inflows from the daily forecasts were also a problem. These deviations were expressed as deviations of hydropower plant production from the forecasted schedules. To the extent possible, the deviations were balanced by adjusting the production of thermal power plants, and by increasing sales and purchases. The objective of the HSE Group is to decrease the risks to which the newly formed balance group is exposed.

Electrical energy production in the HSE Group is controlled by the Control Centre in Maribor. The main objectives of production control are:

- to ensure minimum deviations of production and the balance group from the schedules,
- to ensure optimal appropriation of power among available generators,
- to promptly activate reserve capacities in emergency situations.

The quality of controlling the HSE balance group is reflected in the minimisation of deviation costs, as the deviations of balance group members are reduced by adapting their production. In 2006, the members of the HSE balance group were: the production units of the HSE Group, NEK, TET, direct consumers, the Velenje Coal Mine, and the balance subgroups of four distribution companies. The balance group's deviations include all deviations of generated production and consumption from the forecasted schedules. In our opinion, the control of the HSE balance group was successful in 2006.

FINANCIAL RISK

Special attention is paid by the HSE Group to the financial risks to which the Group is exposed in its operations, and adopting measures for managing such risks.

The Group is not exposed to any significant currency risks through its foreign currency operations. The major net exposure is in EUR. Following Slovenia's admission to the ERM2 exchange rate mechanism and introduction of the euro in 2007, its exposure in EUR is negligible. The country's exposure to euro currency risk was additionally mitigated by natural hedge, i.e. by offsetting euro liabilities against revenues from euro receivables. The volume of operations in other currencies, alongside the euro, is negligible and thus the currency risk of these currencies is low.

Liquidity risk is the risk that an enterprise will encounter difficulties in raising funds to meet its commitments in due time. Current liquidity is provided by matching and planning cash flows. In the HSE Group, current cash surpluses and deficits are monitored and optimised by the Group companies. The management of cash flows is enabled by the above-mentioned system, a liquidity reserve policy based on credit lines granted by domestic and foreign banks, the diversification of investments and liabilities, maturity adjustment of receivables and liabilities, and the consistent collection of receivables, all of which ensures the company's and the Group's payment capacity and low level of current liquidity risk.

Trade receivables under annual contracts are mostly secured by bills or bank guarantees. Trade receivables due from certain customers are regulated in detail through EFET Agreements. In some cases collateralisation is not required due to a specific customer's strategic position and/or financial stability.

Short-term electrical energy trading is carried out on stock exchanges - related receivables are secured by the obligatory membership system, through trading portals, and by bilateral agreements. EFET Agreements are concluded with most of these customers, except those for which collateralisation is not required due to a customer's specific position, as in the case of trading under annual contracts.

The collateralisation of other receivables is not required due to their specific nature.

In our opinion, the trade receivables risk is well managed thanks to the above- mentioned management measures.

Interest rate risk exposure is the possibility of increased costs of financing at the source, linked to a variable interest rate, due to changing interest rates in the market. Interest rates charged on long-term borrowings and linked to EURIBOR are hedged by appropriate derivative financial instruments due to a forecasted increase in the key interest rate in the euro zone. A portion of variable interest rates has been changed to fixed interest rates. In our estimate, the interest rate risk is low due to the above-mentioned measures aimed at hedging against interest rate risk, a large share of own equity, and a low debt to asset ratio (5% of the balance sheet sum of the company and 12 % of the balance sheet sum of the Group).

HUMAN RESOURCES RISK

The Group's activities, intensive growth, and the implementation of its strategic plans require that its employees steadily upgrade their existing knowledge, acquire new skills and competences, and demonstrate a dynamic, multidisciplinary approach, self-initiative, and ability to work in a team.

Loss of key employees is considered to be the main human resources risk. This can be prevented by good management and communications with/among employees, continuous professional growth and education, and stimulating working conditions and environment. Human resources risk exposure is estimated as low.

INFORMATION SYSTEM RISK

Risks having significant impact on operations are:

- Internet access failure,
- E-mail failure,
- OpenLink (on-line marketing support) failure
- Network connections failure.

Internet access failure

To provide for the required system availability, a platform and connections were established that are able to provide for system availability in case of failure of any of the system components. The NSPOF (No Single Point Of Failure) solution was implemented, ensuring undisturbed internet access in case of hardware failure or Internet provider failure. For this purpose, all systems providing Internet access are duplicated. This solution also ensures undisturbed Internet access in case of hardware failure or Internet provider failure. Exposure to Internet access failure risk is assessed as very low due to the above- mentioned measures.

E-mail failure

The 5-year old computer system was upgraded by an additional server in order to provide for high availability of the message system. The server cluster consists of two active servers: one is always ready and waiting to take on the load if any of the others fail. In our opinion, E-mail failure risk was successfully managed in 2006.

OpenLink (on-line marketing support) failure

Risk mitigation activities and measures included the purchase of a new application server, transfer to a new version of OpenLink Endur, monitoring of the operating system and services using the MOM and TERRA monitoring systems, and hardware control by HP SIM. Exposure to OpenLink (on-line marketing support) failure risk is estimated as very low due to the above- mentioned measures.

Network connections failure

The transition of all data links to the umbrella telecommunications network was implemented in February 2006. Eles's data links were redirected to the backup links. Simultaneously at the Ljubljana location, a router Cisco 6500 with optical GE interfaces for connection to the umbrella telecommunications network was installed and a new module with 48 inputs was added to the network switch. The backup radio connection TEŠ-Lubela-HSE Velenje was upgraded to a velocity of 54 GBps. A connection with Boštanj Hydropower Plant and SEL was set up via the umbrella telecommunications network. Exposure to network connections failure is estimated as very low due to the above-mentioned measures.

Effective monitoring and management systems were implemented for the active and passive networks and for all platforms. Each year, the quantity of hardware and software equipment is enlarged together with other system support services by approximately 20 %. Due to the growing IT infrastructure, effective systems for availability detection and preventive control are used.

2.12 PUBLIC RELATIONS

Public relations activities were performed in 2006 in line with current events and HSE business policies. Mention should be made of the "Energija" (Energy) informative education campaign organised by HSE with the goal of informing the general Slovene public on the importance of the rational use of electrical energy. The campaign was carried out in the autumn months and included a wide variety of communication tools ranging from PR activities in which relevant issues were addressed in cooperation with the media, to advertising activities and the creation of an interactive website for collecting advice on the rational use of electrical energy. The campaign met with a wide response, as reflected in the advertising efficiency surveys.

Promotional activities were continued in the spring and autumn of 2006 to increase the sale of Blue Energy, HSE's top product in the area of renewable energy sources, which at year end celebrated its thousandth customer.

Other public relations activities in 2006 included the opening of a branch office in Prague and a subsidiary in Budapest, as well as other international activities conducted by HSE, particularly in southwestern Europe. As a tender participant or business partner, HSE was active in the markets of Croatia, Bosnia and Herzegovina, Serbia, Montenegro, Rumania, and Bulgaria. From the aspect of ensuring an adequate supply of electrical energy, international activities are a must, as is the construction of new production facilities in Slovenia. The central event organised by HSE in 2006, which was responsible for its content and communications, was the opening of the first in a series of hydropower plants on the lower Sava River, i.e. the Boštanj Hydropower Plant.

Simultaneously with the above-mentioned activities, regular public relations activities were carried out throughout 2006, both in the public relations and advertising areas. Advertisements were made in the media and in supplements covering topics linked to the HSE's area of operation. Eight editions of Energija magazine were issued, and the Company's website was redesigned and its contents refreshed.

2.13 RESEARCH AND DEVELOPMENT

In 2006, research and development projects were conducted in line with the Group's development objectives and policies focused on acquiring new skills in all prospective areas, which will provide for the safe and quality supply of electrical energy.

The Group is aware that the need to preserve the environment is a growing concern, and that negative environmental impacts accompanied by limited fossile fuel reserves are a strong criterion in the selection of new fuels.

The use of renewable energy sources, such as sun, wind and geothermal energy, is still in its early stages in Slovenia, which is why they should be thoroughly researched as soon as possible and their commercial use enhanced. Although research studies are costly and of long duration, large energy supply companies are a suitable place for their conduction because they can provide, in cooperation with universities and research institutions, a solid base of knowledge and the capital required for such projects.

The HSE Group is the largest electrical energy producer in Slovenia, whose goal is to expand within existing markets and to tap new electrical energy markets. For this purpose the Group is devoting intensive efforts to research and development, which will open new prospective areas and point out new directions for the successful operation of the HSE Group in future. Each research activity has its own unique purpose and a different time horizon of effects. Not every development activity is measurable in monetary units, and only these activities can essentially change the quality of a company's services in the final phase of implementation.

R & D project structure

CATEGORY	*CRITERIA*
Value	A positive value added during basic operations (proved by products and services).
Significant impact	Significant impact on basic operations: • use of opportunity for expansion of the company and operations • avoidance of risks • increasing the value of a trademark – goodwill
Innovations / Know-how	R&D is required as a basis for successful operation in other company divisions, and as support in enforcing new regulations, laws, standards...
Legally binding	Legal obligation towards: • laws • other legally binding state requirements • concluded contracts

Research activities

The HSE Group wishes to acquire, in an original and systematic way, new knowledge that is important for the development of new activities and the discovery of new areas of operation. Newly acquired knowledge will be used in the development of new and the improvement of existing business processes in electrical energy generation. In the open electricity market,

the HSE Group is exposed to strong pressures from competitors and demands to reduce environmental impacts. For this reason, solutions need to be found for streamlining operations and developing new methods of electrical energy production from renewable energy sources. The research areas dealt with by the HSE Group in its research activities are:
- research activities of strategic importance for companies,
- research activities in the energy development area,
- research activities in the environmental protection area, and
- research activities in operating issues.

Due to the large scope of areas to be covered, optimisation of resources, and the required response time, research cannot be conducted only within the HSE Group. Contacts need to be made with research and development institutions outside the HSE Group in order to establish a creative partnership based on constructive criticism of the existing partnership with the purpose of achieving a new partnership and creating long-term solutions that will guarantee the reliability of electrical energy supply in the market and a stable environment for capital improvement and knowledge development.

Cooperation with research institutions should not end with the handover of a product (study) or with the presentation, explanation of results, or informing about the contents of a study, but with the opening of new horizons on both sides.

Projects
The activities associated with projects are the following:
- participation in the preparation and elaboration of documents for the acquisition of funds,
- participation and coordination of procedures for the elaboration of investment documents, evaluation of investment programs, and the introduction of uniform evaluation criteria,
- introduction of uniform methods for the preparation of documents and start-up studies,
- preparation of investment documents for renewable sources production projects in the HSE Group,
- introduction of project controlling,
- preparation of development plans of Group companies and reconciliation with the development plan of the HSE Group.

Training
The main activities associated with training include:
- employee training for the execution of assignments relating to research and development projects,
- organisation and conduction of professional meetings and seminars held for the presentation of expert documents required for the implementation of OVE projects and others,
- organisation of training programmes on new technologies.

EU legislation
Slovene laws and regulations were drawn up in compliance with EU legislation and adapted to the local circumstances. Preparations for Slovenia's EU Presidency in the area of energy were carried out.

2.14 PLANS FOR THE FUTURE

The HSE Group and the entire Slovene electrical energy industry are facing serious challenges, and their existence and development will depend on their ability to respond to these challenges. A key role in the HSE Group's future will be played by further growth and expansion to foreign markets, in particular its penetration into Central and southeastern Europe. The HSE Group's ambitious development plan envisages an increase in the total trading volume of electrical energy from 16.1 TWh in 2006 to 39.3 TWh by 2018. This scope of trading is a condition for the HSE Group to become an important player in the region of southeastern Europe, with the possibility of active and equal participation in shaping the above-mentioned markets.

For the present, the Group's own production located exclusively in Slovenia accounts for one half of the structure of energy sources, and purchases in domestic and foreign markets account for the other half. In 2018, the Group's own sources in Slovenia are expected to account for one fourth, own sources in southeastern Europe for one fourth, and other purchases in the market for the remaining half of the structure of energy sources. The projected structure is undoubtedly favourable from the point of view of trading risk management. Emphasis should be given to the significance of a balance between our own and foreign energy sources, as well as the spread of our own facilities throughout the entire trading region. The HSE Group has already closely examined more than a hundred potential investments in southeastern Europe and is now focused on twenty projects which, according to expert analyses, are technically and economically justified and ensure an adequate return on investment.

Despite its activities abroad, the HSE Group will not disregard its development role in the Slovene market, where it is the leading investor in the construction of new electrical energy production facilities. Besides its presently most important domestic energy project, i.e. the construction of hydropower plants on the lower Sava River, another strategically significant project of the HSE Group is the construction of a new 600 MW generator in TEŠ and a series of hydropower plants on the Mura River and on the central Sava River.

In future, the HSE Group will focus its efforts on environmental protection and promoting environmental awareness, not only among producers, but also among the general Slovene public. Since its establishment, the HSE Group's strategies and development plans have been based on reconciling the exploitation of natural resources with their natural renewal ability, as well as on the development of technologies and processes which reduce the detrimental impact of energy production on the natural and living environments. This has been proven by the ISO 14001 international environmental certificate, which has been obtained by all production companies in the HSE Group and the controlling company HSE d.o.o.

Also awaiting HSE are numerous structural changes. In first place is by all means the privatisation process, which will be implemented within the process of integral privatisation of the Slovene electrical energy industry. The capital consolidation of the Group and vertical integration with electrical energy distribution companies need to be completed. In view of growing competition, HSE Group companies will have to rationalise operations, reduction of costs without threatening the safety and reliability of production, manage all types of risks, and implement development projects. Through its internal reorganisation, the HSE Group will be able to secure its own human resources and, armed with its own know-how and expertise, strengthen its position in the domestic market and conquer shares in foreign markets.

2.15 SIGNIFICANT EVENTS AFTER THE BALANCE SHEET DATE

Euro introduction

The euro, the European Union's single currency, was introduced in Slovenia as the legal means of payment on 1 January 2007.

The euro should improve competitiveness in Slovenia as a result of comparable prices in the euro-currency zone and the creation of a more stable environment for the entire industry, because a single currency eliminates currency risks and currency exchange costs.

The transition from the tolar to the euro caused companies to incur certain short-term costs relating in particular to IT adjustment, accounting and financial statements transformation, and additional training of employees. However, the microeconomic reasons for entry into the single currency zone are based on the assumption that the savings due to the use of a single currency will outweigh the one-off costs of transition to a common currency.

Split-off of SEL and TEB

At its 99th regular session on 30 November 2006, the Government of Slovenia adopted a resolution on the split-off of a part of Holding Slovenske elektrarne d.o.o. as the transferor company to GEN energija d.o.o. as the transferee company.

In line with the resolution of the Government of Slovenia, the managements of Holding Slovenske elektrarne and GEN energija had to prepare the transfer of HSE's capital investments in the Brestanica Thermal Power Plant and the Sava River Hydropower Plants Ljubljana to GEN energija under the split-off procedure by way of split-off and take-over.

The decision on the procedure of split-off by take-over was adopted after close examination of the advantages and disadvantages of other procedures. The split-off will be effected in the phases foreseen by applicable legislation. Under the resolution, the date of split-off is 31 December 2006 and the procedure is scheduled for completion in the first half of 2007.

The resolution is the first step in the implementation of the Government's Strategic Policies relating to the privatisation of the Slovenian electrical energy industry, which were adopted at its 84th regular session on 27 July 2006.

Capital increase of DEM and TET, and adjustment of share capital of HSE

The Government of the Republic of Slovenia as the founder and sole shareholder of Holding Slovenske elektrarne, d.o.o. adopted at its 99th regular session held on 30 November 2006 a resolution on capital increase by the payment of additional contributions (effective capital increase) in kind, representing:

- a share of the Republic of Slovenia in Termoelektrarna Trbovlje d.o.o. (Trbovlje Thermal Power Plant) equal to 80.34 percent, and
- a share of the Republic of Slovenia in Dravske elektrarne Maribor d.o.o. (Drava River Hydropower Plants Maribor) equal to 0.14 percent.

Simultaneously with the capital increase, HSE adjusted the share capital and basic contributions to the euro.

The procedure will foreseeably be completed in the first half of 2007.

Amendment of the Articles of Incorporation of HSE

The Government of the Republic of Slovenia, as the founder and sole shareholder, adopted at its 112th regular session held on 7 March 2007 the Act amending the Articles of Incorporation of the limited liability company Holding Slovenske elektrarne d.o.o. and approved the final text of the Articles of Incorporation of the limited liability company Holding Slovenske elektrarne d.o.o.. The Government also adopted a statement on the acceptance of a new contribution for capital increase and a report on contributions in kind, and authorised Andrej Vizjak, Minister of Economy, to sign the above-mentioned Acts, statement, and report.

Due to the extensive tasks defined in the HSE Group's development plan relating to large and accelerated investments in Slovenia and abroad, reliable electrical energy supply, changes in the electrical energy market, and the complexity of all set business objectives, the Government approved the proposal for a two-member management board in HSE.

Purchase of minority interests in SENG

The Government of the Republic of Slovenia, at its 84th regular session held on 27 July 2006, approved a proposal of strategic policies to be applied in the privatisation of the Slovenian electrical energy industry. Pursuant to these policies, HSE shall purchase the remaining minority interests in Soške elektrarne Nova Gorica d.o.o. (Soča River Hydropower Plants). To finance this purchase, HSE raised a loan in the beginning of 2007, with the consent of the Ministry of Economy and the Ministry of Finance, in an amount of 29 million EUR for a period of 10 years, with a 2-year moratorium on the repayment of principal.

The purchase procedure is expected to be completed in the first half of 2007.

...a delicious radiance...

It's great to gaze into the glowing oven, the deliciousness within. Can hardly wait until its ready: »Mum, is it done yet, is it done?«

3

CORPORATE SOCIAL RESPONSIBILITY REPORT

2006

3.1 RESPONSIBILITY TO EMPLOYEES

Power is in the people

If the HSE Group's slogan is "The power of energy", then the slogan of human resources management is "Power is in the people". All companies that not only manage to survive in the market, but also to grow and create added value with their own "sources of power", are aware of the importance of this "power". This is also the guiding principle of the HSE Group.

Today's lifestyle, in which changes are the only constant, requires that the management of HSE Group companies carefully monitor the present situation and, in particular, play an active role in shaping the future. Continuous changes are occurring in all spheres of life: technology, products, competition, owners, markets, customers, trade and industry, business environment, company objectives, employees and, ultimately, relations between all shareholders in a company.

If, until recently, suppliers, buyers and owners were considered the most important partners, today the most important partners are the employees and members of the HSE Group, who are the suppliers of knowledge, carriers of value, and important "architects" of organisational culture, and thus a source of competitive advantages and the Group's heralds both inside and outside the company.

Human resources policy

Systematic human resources management has remained one of the most important aspects of our business strategy. The objectives of employee development are, as in the past, oriented towards accomplishing the strategic goals of the HSE Group. The principal employee development activities - from the professional integration of new employees, systematic and continuous professional and personal development of employees to the transfer of knowledge on all levels and, ultimately, the creation of conditions ensuring the simultaneous fulfilment of needs of the HSE Group and individual employees - are subordinated to these objectives.

Of high importance are the following characteristics of human resources policy: satisfaction of employees, their confidence and striving, and their loyalty to the Group. The company needs enthusiastic individuals who are willing to strive for noticeable and measurable operating results, and realise business visions and strategies. The HSE Group endeavours to clearly define its expectations and objectives, to sincerely and authentically care for its employees, and to stimulate achievements. We are aware that strategies alone do not lead to success. Success is achieved by people and the values directing them.

The HSE Group observed these basic principles in 2006, laying major emphasis on:

- recruitment,
- investments in employee development,
- maintaining a favourable organisational climate and employee satisfaction,
- concern for a quality and healthy working environment and the continuation of a program for the protection and strengthening of health in the working and living environments,
- ensuring an optimal number of employees and an optimal human resources structure.

In 2006, the HSE Group continued its regular and close cooperation with trade unions and workers' councils, thus achieving a balance between various interests and broad consent both in respect of the Group's development plans and the provision of social welfare.

3.1.1 EMPLOYEES IN THE CONTROLLING COMPANY

Recruitment

Thanks to its leading role in the electrical energy sector, the Company is also attractive as an employer. Employment applications are received from applicants with developed career paths as well as those at the start of their career. The recruitment policy is based on a combination of external recruitment, which provides for the inflow of fresh ideas, energies, and different viewpoints, and internal recruitment within the HSE Group, which ensures quality experts of various profiles with a wide range of general and specific knowledge and competences. As regards executives and experts, the company pursues a policy of training its own staff.

The Group's intensive growth and realisation of development plans called for an increase in manpower. In 2006, ten new staff members were employed in marketing, production, research & development, and general administration. The employment of three employees was terminated: one on the basis of a mutual agreement, one replacing a full-time employee returning from maternity leave, and one who retired. On 31 December 2006, the Company had 97 employees, which is 8 % more than at the end of 2005.

As of 1 February 2006, a new job classification has been in force. The actual number of employees is lower by 7 %, or 7 employees, in comparison with the projected number in the Rebalanced 2006 Business Plan, in particular due to:

- the notice terms of new employees who will commence employment in the first quarter of 2007 on the basis of calls for job applications in the third quarter of 2006,
- unsuccessful calls for job applications in the Legal Division, IT Division, and Secretary's Office of the Company,
- a job invitation that was not carried out for the position of Market Analyst in the Marketing Division,
- The retirement of an employee as of 30 December 2006.

Job recruitments were most intensive in the first half of the year, when 7 new staff members were employed. The other 3 staff members were employed in the third quarter of 2006.

Number of employees in HSE d.o.o.	
1 January 2006	90
31 December 2006	97

Voluntary pension insurance

Like other companies in the electrical power sector, the controlling company has its own retirement scheme and voluntary supplementary pension insurance program, in which most of the employees participate. The program has been implemented since 2002, when the first employees were transferred to HSE from its subsidiaries. On the basis of long-term savings on an employee's personal account, a supplementary pension will be paid to employees upon reaching a certain age.

Employees and social community

Employees have obligations not only to their employer and themselves, but also to the wider community. For this reason they are active members of numerous industrial, professional, and sports associations.

3.1.2 EMPLOYEES IN THE HSE GROUP

At the end of 2006, the HSE Group employed 4,316 employees, which represents a 12 % decrease compared to the number of employees on 31 December 2005. This data does not include the TDR - Metalurgija Group, which was sold at the end of 2006.

Employees in HSE Group

COMPANY	31 Dec 2006	%	31 Dec 2005	%	IND 06/05
HSE	97	2.2	90	1.8	108
DEM	288	6.7	294	6	98
SEL	124	2.9	126	2.6	98
SENG	126	2.9	126	2.6	100
TEB	121	2.8	123	2.5	98
TEŠ	537	12.4	561	11.5	96
PV Group	2,984	69.2	3,162	64.5	94
TDR - Metalurgija Group	-	-	386	7.9	0
HSE Invest	36	0.8	31	0.6	116
HSE Italia	0	0	0	0.0	0
HSE Balkan Energy	2	0	0	0.0	0
HSE Hungary	0	0	0	0.0	0
HSE Adria	1	0	0	0.0	0
TOTAL	4,316	100.0	4,899	100.0	88

Education structure

The employee education structure in the HSE Group has been improving from year to year. The share of employees with a higher education and a university education has increased in comparison with the previous year.

Number of employees as at 31 December 2006 and average number of employees in 2006 by education level

Educational leve	Employees as at 31 Dec 2006		Av. no. of employees in 2006	
	Controlling company	HSE Group	Controlling company	HSE Group
I.	0	330	0	341
II.	0	271	0	280
III.	0	17	0	20
IV.	1	1,832	2	1,902
V.	11	1,135	12	1,165
VI.	12	308	12	306
VII.	55	391	52	391
VIII. and IX.	18	32	17	31
TOTAL	97	4,316	95	4,436

3.1.3 CONCERN FOR EMPLOYEE EDUCATION AND TRAINING

Employee education is one of our primary human resources activities. This is more than evident in available records on investments in knowledge, since a significant part of investments by companies in the developed world are investments in the upgrading of knowledge, which is the basic source of economic efficiency. However, by the term "upgrading knowledge" we are not only referring to the quantity of such education, but above all to the benefits gained by both the individual and the company. These are reflected in the satisfaction of employees, increased creativity, quality of work and, last but not least, greater loyalty to the company. The HSE Group is aware that through systematic education and training, we are preserving the competences of our employees, i.e. helping them to acquire new knowledge, skills, and ability to use such knowledge, as well as to develop relations, motives, opinions, and desires.

In addition to acquiring knowledge, it is crucial to be able to use such knowledge in practice, and to transfer and spread it among other Group members. This is also one of the key objectives of the HSE Group in human resources management, and one of the key tools for establishing and creating a culture of life-long learning, which is based on the principle of responsibility and reciprocity for one's own education and development, as well as for education and development of co-workers and the entire HSE Group.

Education in the controlling company

In 2006, several external and internal training programmes were organised within the HSE Group in the areas of finance and accounting, auditing, marketing, production, legislation, communications, ISO standards, health and safety at work, IT, and various language courses.

Internal training programmes were organised for all employees in individual business units, as follows:

- quality system courses were conducted by the employees of HSE and TEŠ,
- training courses on the ODOS electronic document system and computer workshops for working in the HSE environment were conducted by employees from the IT division, and
- an advanced business English course.

External and internal training programmes were attended by 90 % of employees. The programmes comprised a total of 3,547 hours, with an average 37 hours per employee. Several types of courses were organised, the majority of which involved extended professional training, followed by computer and IT training, foreign language courses, management training, quality system training, environmental management training, and courses on health and safety at work.

Thematic workshops

Since 2004, thematic workshops on different levels have been organised for the entire HSE Group. These were continued in 2006, and have become an effective part of the education system in HSE. Internal training programmes leading to a Qualification Certificate were organised within the HSE Group for members of the Supervisory Board and the Management Board. These training programmes were conducted by the Association of Supervisory Board Members. Several workshops on the topic of electrical energy production were also organised.

Off-the-job training

In addition to the upgrading of knowledge and employee training, HSE's education activities also comprised off-the-job training and the granting of scholarships.

In 2006, three employees enrolled in part-time studies, two of them on the under-graduate level to acquire a university education (level VII), and one employee on the post-graduate level to acquire a Master's degree in mechanical engineering. At present, twelve employees are undergoing off-the-job training, two of them to obtain a higher-level education, five to obtain a university-level education, and five employees are enrolled in post-graduate studies.

Scholarships

Students involved in research activities contribute new ideas and views on solving work-related problems. HSE provides support to students of technical, social and natural sciences both in the form of financing as well as practical training and gradual integration into the organisational environment.

In 2006, the controlling company granted a scholarship to one technical science student.

3.2 RESPONSIBILITY TOWARDS THE NATURAL ENVIRONMENT

Environment-friendly

Slovenia entered the European Union with a comparatively well-preserved natural environment, as well as with the awareness that the environment is one of the pillars of sustainable future development.

At the very beginning of its operations, the HSE Group designed an environmental policy whose basic components can be summarized in the following points:

- to produce electrical energy having minimum impacts on the environment,
- to observe all statutory standards and recommendations,
- to introduce the best technologies available in order to minimise impacts on the environment,
- to boost the development of renewable electrical energy sources,
- to achieve a partner relation with local communities and jointly solve environmental issues and plan the sustainable development of electrical energy production,
- to achieve the sustainable operation and development of energy facilities.

All HSE Group companies producing electrical energy as well as the controlling company have been awarded the ISO 9001 international quality certificate and the ISO 14001 international environmental certificate. By consistent observance of these standards, the companies are ensuring the safe and environment- friendly production of electrical energy in all hydropower plants. Through environmental rehabilitation and various modernisations, the two thermal power plants have also achieved a more environment-friendly technological level. The Velenje Coal Mine was among the first coal mines in the world to achieve integral and responsible environmental management in compliance with the requirements of the respective standard.

Kyoto Protocol

The Kyoto Protocol, which came into force in February 2005, has laid heavy requirements on the HSE Group. Namely, the future development of electrical energy production is to be aimed at lowering specific greenhouse gas emissions per unit of electrical energy. It will above all be necessary to build, renewable energy production units (water and wind energy, biomass). In energy production from fossile sources, technologies with lower greenhouse gas emissions will have to be introduced.

The HSE Group is aware that its present development must not endanger the development and environmental needs of present and future generations. This is also embodied in the 2006/2015 Development Plan of the HSE Group.

Renewable energy sources

The area of renewable energy sources is a comparatively new area in Slovenia. However, following the example of European countries, it is developing quickly. Under the Slovene Energy Act, renewable energy sources are sources which are entirely or predominantly renewable in the natural environment and cannot be depleted. The five renewable sources most frequently used are hydropower, wind, biomass, and geothermal and unaccumulated solar energy. The Act is based on the guidelines of the EU directives. In compliance with EU Directive 2001/77/EC, Slovenia as an EU member country is obliged to increase the use of electrical energy from renewable energy sources from 29.9 % in 1999 to 33.6 % by 2010.

Energy from hydropower plants is, in terms of volume, the most important source of electrical energy from renewable sources in Slovenia, and the HSE Group is the largest producer of hydropower in Slovenia. The area of renewable energy sources is therefore highly important, both for the operation and the future image of the Group. With respect to electrical energy supply from renewable sources, in 2004 activities were started in connection with the setup of a domestic market for electrical energy supply from renewable sources (Blue Energy), participation in the drawing up of implementing regulations covering this area, and international activities relating to the sale of renewable certificates abroad.

RECS system

HSE is also a member of the international organisation RECS (Renewable Energy Certificate System), which encourages and promotes international trading with renewable energy certificates. Within the framework of this system, all hydropower plants of the HSE Group were certified, and the first quantities of certificates were issued and sold abroad. In 2005, the first RECS certificates were sold in Slovenia within the framework of the Blue Energy project.

Guarantee of Origin (GoO) and labelling of energy source structure

In addition to RECS, the international organisations RECS International (traders and system users) and AIB (issuers of RECS certificates) developed an international trading system for guarantees of origin (GoO) within the EECS umbrella system. Trading in GoO under the EECS system has been conducted for the past two years. At present, seven countries have adopted the system and are participating in it. HSE intends to join the EECS system for GoO trading in 2007. In this way, Slovenia will participate in this international system with both GoO and RECS certificates.

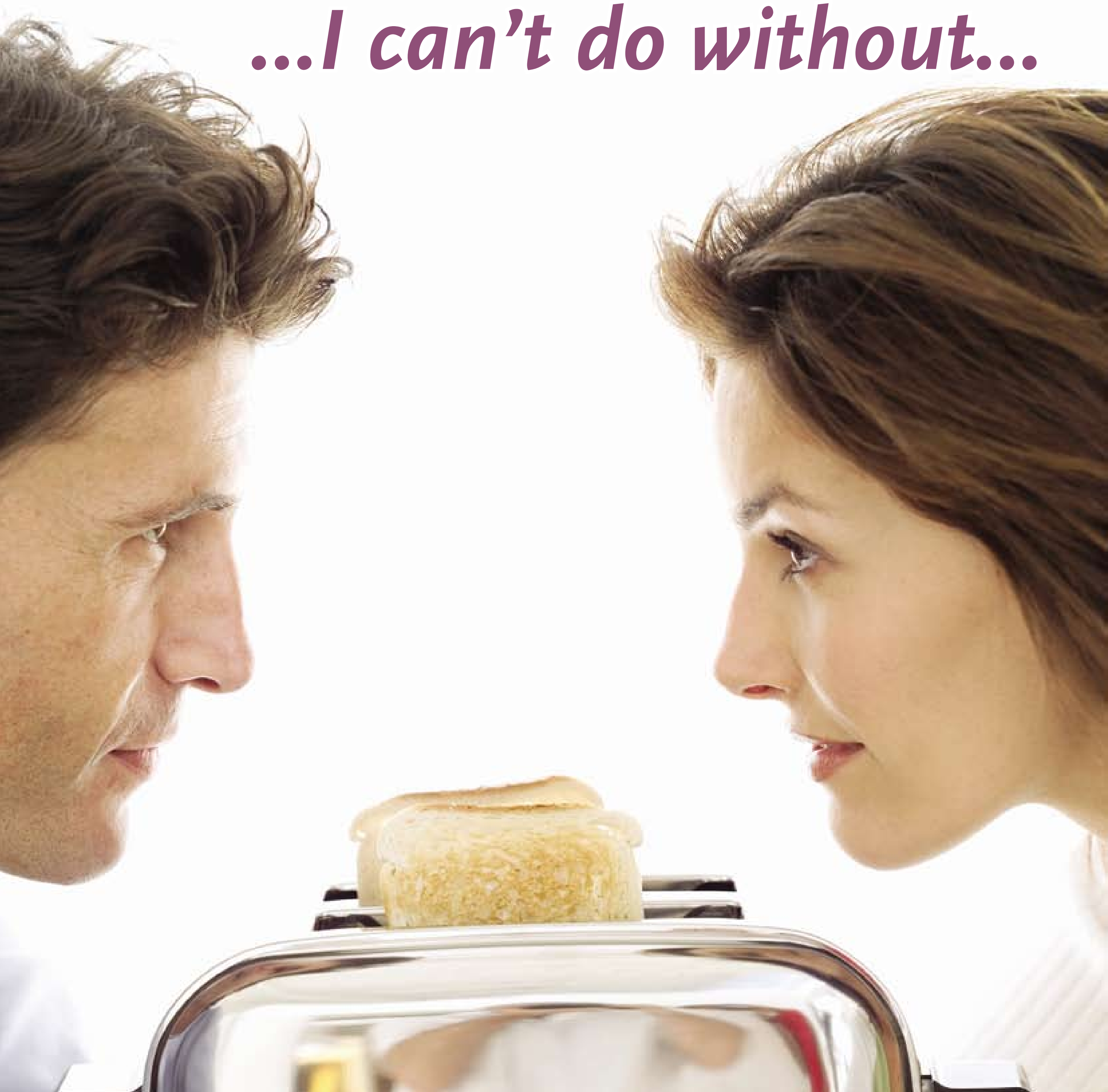
In May 2005, the Act on the method of defining the shares of electricity production sources and the mode of their presentation. The wording of the Act was drawn up by the Energy Agency of RS, which also gave due consideration to international findings. The Act stipulates that both GoO and market certificates may be used to determine the shares of renewable energy sources. Those renewable energy sources for which market certificates or GoO have been issued may be considered as such only against the presentation of documents proving that they were claimed in the calendar year for which the structure of energy sources is being proven.

3.3 RESPONSIBILITY TO THE BROADER SOCIAL COMMUNITY

HSE's relations with the broader social environment are reflected in the form of sponsorships and donations given to those in need of help. In 2006, HSE supported numerous athletes, cultural projects, health projects, societies, and individuals requiring additional funds for their operation and life in general. At HSE we are aware that our business results do not depend solely on the figures standing behind our business performance, but also - and above all - on the support of those who directly or indirectly enable us to achieve such results, and with them the reputation of the company.

Clock radio. Shower. Hairdryer. Electric toothbrush. Electric razor. Kettle. Toaster. Fridge. At breakfast, she asks: »Would it be easier for you to live without electricity or without me?«

...I can't do without...



4

Financial Statements of HSE d.o.o.

2006

4.1 GENERAL NOTES

Basis for the preparation of financial statements

Financial statements and the notes thereto have been prepared in accordance with provisions of the Companies Act (hereafter ZGD-1) and the Slovenian Accounting Standards 2006 (hereafter SAS 2006).

Financial statements have been prepared using the Slovene tolar (SIT) as the unit of currency, rounded to the nearest thousand.

Fundamental accounting principles and qualitative characteristics of accounting

During the preparation of financial statements following fundamental accounting assumptions have been take into account:

- accrual basis;
- going concern;

as well as qualitative characteristics:

- going concern;
- consistency;
- prudence;
- consideration of revenues and expenses irrespective of their payment;
- individual valuation of assets and liabilities.

Exchange rate and method of translation into domestic currency

Items in financial statements that are denominated in foreign currencies are translated into local currency in the income statement on the day of accrual, using the middle exchange rate of the Bank of Slovenia.

The balance of assets and liabilities expressed in a foreign currency have been translated into Slovene tolars at the middle exchange rate of the Bank of Slovenia as at 31 December 2006.

The resulting exchange gains and losses are accounted under financial revenue or financial expenses, respectively.

Balances of assets and liabilities expressed in a foreign currency have been translated as at 31 December 2006 by using following exchange rates:

- middle exchange rate as at 31 December 2005: 1 euro = 239,5756 SIT (basis for previous year's items);
- middle exchange rate as at 31 December 2006: 1 euro = 239,6400 SIT;
- middle exchange rate as at 31 December 2006: 1 CZK = 8,7208 SIT;
- middle exchange rate as at 31 December 2006: 1 USD = 181,9314 SIT;
- middle exchange rate as at 31 December 2006: 1 CHF = 149,0299 SIT;
- middle exchange rate as at 31 December 2006: 1 HUF = 0,9524 SIT;
- middle exchange rate as at 31 December 2006: 1 HRK = 32,6374 SIT;
- monthly exchange rate for December 2006: 1 RSD = 3,0349 SIT.

Accounting policies

In the recording and valuation of items in the financial statements, SAS (2006) stipulations have been followed directly, except in the valuation of items for which SAS (2006) allow various options. In such cases, the Company applies valuation methods that comply with its own Accounting Rules or resolutions adopted by the General Manager.

Transition to SAS (2006)

Pursuant to the new Slovenian Accounting Standards, effective 1 January 2006, in some cases the recognition of assets and liabilities, revenues and expenses differs from the previously applicable SAS (2001).

In this regard, transitional provisions set out in Item 15 of the Introduction to SAS 2006 were applied upon the Company's transition to SAS 2006, and appropriate adjustments and restatements were made.

Energy Act

Pursuant to the Energy Act, the legal entities carrying out more than one business activity within the industry of electric energy supply are obliged to assure separate accounting supervision of every of the Company's registered activities in compliance with SAS 2006.

Intangible assets

Intangible assets are long-term assets enabling the performance of the Company's registered activities, whereas physically they do not exist. Intangible assets include concessions, patents, licenses, trade marks and similar rights with finite useful lives.

Upon initial recognition intangible assets are valued at cost, which is inclusive of import and other non-refundable duties and costs, and exclusive of interest expenses incurred.

After recognition, intangible assets are carried at cost.

The amount is subsequently lowered by the amount of amortisation, recorded under accumulated amortisation. In the balance sheet, intangible assets are recorded at the carrying amount i.e. as the difference between the purchase cost and accumulated amortisation.

An item of intangible assets is amortised using the straight-line amortisation method (single-asset amortisation). Amortisation shall begin when the intangible asset is available for use.

Amortisation rates applied to the individual types of intangible assets are based on their planned useful lives.

Property, plant and equipment

Property, plant and equipment are long-term assets owned by the Company and used for the performance of the Company's registered activities.

An item of property, plant and equipment is initially recognised at cost comprising its purchase price, import duties and non-refundable purchase taxes, as well as directly attributable costs of bringing the asset to working condition for its intended use. The cost does not include the borrowing costs related to the acquisition of the item of property, plant and equipment to bring the asset to its working condition.

Individual items of property, plant and equipment of great value with different useful lives are stated and accounted for separately at cost.

The cost does not include the costs incurred upon the dismantling and removing the items of property, plant and equipment.

Spare parts of higher value are accounted for under property, plant and equipment and depreciated over the useful life of the related asset.

The cost model is applied for measurement of items of property, plant and equipment after initial recognition.

In the bookkeeping records the cost as well as the accumulated depreciation is recorded separately for items of property, plant and equipment, whereas in the balance sheet they are recorded at carrying amount i.e. as a difference between the cost and accumulated depreciation.

Subsequent expenditure on an item of property, plant and equipment increases its cost when it increases its future economic benefits in excess of the originally assessed future economic benefits.

The subsequent expenditure enabling extension of the useful life of the asset initially reduces the accumulated depreciation.

Recognition of an item of property, plant and equipment in the bookkeeping records and the balance sheet is reversed when an asset has been disposed of. Gains on disposal of an asset are recorded under operating revenues from revaluation; the carrying amount of the asset is recorded under revaluation operating expenses.

The depreciation of an item of property, plant and equipment begins on the first day of the following month after it has been available for use.

An item of property, plant and equipment is depreciated using the straight-line depreciation method (single-asset amortisation).

Amortisation rates applied to the individual types of property, plant and equipment are based on their planned useful lives.

Investments

Investments are considered as Company's assets. The proceeds from investments are to increase the Company's revenues.

Upon initial recognition, investments are recorded at their initial cost, increased by the costs attributable directly to the investment (except for investments carried at fair value through profit and loss).

Upon their recognition in the books of account, the investments are stated at their settlement date (payment date).

After initial recognition, investments are carried at cost.

Considering the planned settlement or the reason for the investment being held, the investments are carried in the balance sheet under long- or short-term assets.

Inventories

As part of the short-term assets of the Company, inventories are initially recognised at cost, comprising its purchase price, import duties and non-refundable purchase taxes, as well as direct costs of purchasing. The purchase price is reduced by any discounts that have been granted.

If latest purchase prices or the cost of the latest produced items in the accounting period differ from the prices and/or the costs of items of inventory of the same class, the first-in first-out (FIFO) method is applied to recognise declining quantities of inventories.

Receivables

Receivables are the rights, emanating from property and other legal relationships, to claim the settlement of a debt, the payment for deliveries or rendered services from a specific person or entity.

Initially receivables of all categories are carried at amounts recorded in the relevant bookkeeping documents under the assumption that the amounts owed will also be collected.

Advances paid for property, plant and equipment and inventories are not recorded in the balance sheet among receivables but among assets which they refer to.

In terms of their maturity, receivables may be classified into long-term and short-term receivables.

Cash

Cash includes deposit money, i.e. cash deposited in accounts with a bank or another financial institution that can be used for payment purposes. It is classified into cash readily available for disbursement and cash held in demand deposits.

The carrying amount of an item of cash is the same as its initial nominal value until the need for its revaluation arises.

Short-term deferred cost and accrued revenue

Short-term deferred costs and accrued revenue include short-term deferred costs or short-term deferred expenses as well as short-term accrued revenue.

Short-term deferred costs or short-term deferred expenses are amounts incurred but not yet charged against an entity's activities and they do not yet affect profit or loss

Short-term accrued revenues are amounts that have been considered in the income statement but not yet charged to third parties.

Equity

The total equity is defined by the amounts invested by owners and the amounts generated during operation that belong to the owners.

Share capital is held in local currency. Share capital and capital reserves represent owner's cash contributions and contributions in kind.

Other revenues reserves are formed on the basis of resolutions adopted by the Supervisory Board and the Shareholders' Meeting.

Net profit represents the undistributed part of the net operating result for the financial year.

Retained earnings represent the result of the changes in the books of account incurred upon transition to SAS 2006.

Revaluation surplus includes the values of derivatives used for risk hedging.

Provisions

Provisions are formed for obligations expected to arise from obligating past events in a period exceeding one year and whose amounts can reliably be estimated. They are formed when the obligation can reliably be measured.

Long-term liabilities

Long-term liabilities are recognised obligations of an enterprise associated with the financing of its assets the settlement of which is expected, usually by payment of cash, in a period of more than one year. They are carried at cost.

The part of matured long-term liabilities and long-term liabilities due to be settled within twelve months of the balance sheet date is recorded in the balance sheet under current liabilities.

Long-term financial liabilities are long-term loans received on the basis of loan contracts, repayable in a period longer than one year. An item of long-term liabilities is initially recognised at the amount arising from the relevant document, which evidences the receipt of cash. They are subsequently decreased by principal repayments.

Accounted but not yet due interest on long-term financial liabilities are recorded among other short-term operating liabilities.

Long-term operating liabilities result from transactions between the Company and business partners based on contracts concluded.

Short-term liabilities

Short-term liabilities are recognised obligations of an enterprise associated with the financing of its assets the settlement of which is expected, usually by payment of cash, in a period of no more than one year. They are carried at cost.

The carrying amounts of short-term liabilities are equal to the amounts arising from the relevant documents adjusted for their increases or decreases agreed by the creditors.

The item of short-term financial liabilities includes a portion of long-term liabilities that matures in a period less than a year after the balance sheet date.

Accrued cost and deferred revenue

Short-term accrued cost and deferred revenue comprise short-term accrued costs, short-term deferred revenues and value added tax on advance payments.

As the activity is evenly charged, the costs and expenses that have not occurred but are expected are recorded among accrued costs.

Derivative financial instruments

Derivative financial instruments are financial instruments whose value changes in response to the change in a specified interest rate or commodity price and which require no initial net investments.

The derivatives used by the Company are derivatives held for trading purposes (standard futures) and risk hedging derivatives (interest rate swaps and standard futures).

The gains and losses associated with derivatives held for trading are recognised directly in the income statement.

The derivative financial instruments are used as cash flow hedge, hence the portion of the gain or loss from a hedging item considered as successful hedging shall be recognised directly in equity, and the difference shall be recognised in profit or loss.

The profit or loss recognised directly in equity shall be transferred to the profit or loss in the period in which the profit or loss is affected by the hedged item.

The futures are recorded at the 'net' principle which means that the value of futures is recorded off the balance sheet.

Off balance sheet items

Off-balance sheet items include business events that have no direct impact on items in the financial statements but are significant in view of informing the users of the annual report.

Revenues

Revenues are recognised if an increase in economic benefits during the accounting period is related to an increase in assets or a decrease in liabilities, and the increase can be measured reliably

Revenues are recognised when it is probable that cash receipts will flow from them, unless they were achieved on origin.

Revenues from the sale of services and merchandise are recognised at selling prices stated in invoices or other documents, less discounts and rebates approved either when the sale is made or subsequently, including those granted for early payment.

Capitalised own services are services provided by the company itself that are accounted for under property, plant and equipment.

Revaluation operating revenues are revenues recognised upon the disposal of property, plant and equipment and revenues recorded upon a decrease in the reversal of allowances for receivables in connection with short-term receivables.

Off balance sheet items are the revenues arising in association with investments, as well as in association with receivables and liabilities.

Financial revenues are recognised when statements of account are prepared, regardless of cash receipts associated with them, unless there exists significant uncertainty as to their amount, maturity date and collectability.

Interest is accounted in proportion to the previous year, unsettled amount of the principal and the agreed-upon interest rate.

Other revenues comprise extraordinary items. They are recorded in actual amounts.

Expenses

Expenses are recognised when decreases in economic benefits during the accounting period are associated with decreases of assets or increases of liabilities and the decreases can be measured reliably.

Operating expenses are recognised upon the purchase of merchandise or upon the rendering of services.

Revaluation operating expenses comprise the surplus of the carrying amount over the selling price, and the amounts incurred in the write-off of operating receivables.

Financial expenses incur in association with debts, short-term investments and short-term receivables.

They are recognised when statements of account are prepared, regardless of cash payments associated with them.

Interest is accounted in proportion to the previous year, unsettled amount of the principal and the agreed-upon interest rate.

Segment reporting

The Company presented the net sales results separately by two geographical segments, domestic market and foreign market. No detailed segmentation within the two markets has been reported, nor the results for the period per individual geographical segments, since the Company understands that the disclosure of such information might have a detrimental effect upon the Company. In terms of segment reporting, the Company's assets and liabilities represent an indivisible unit.

As terms of operation and risks for individual groups of products are similar, the Company does not itemise operations by segment.

Taxation

The Company is subject to the Value Added Tax Act and the Corporate Income Tax Act.

Deferred taxes

Deferred taxes are earmarked for covering temporary differences between carrying amount and tax values of assets and liabilities. The deferred tax assets represent the currently recorded corporate income tax and deductible temporary differences, which will result in lower tax payable in future periods.

4.2 STATEMENT BY THE MANAGING DIRECTOR

The Managing Director of Holding Slovenske elektrarne d.o.o. hereby confirms the financial statements of HSE for the financial year ended 2006, the notes thereto as well as the accounting policies applied.

The Managing Director confirms that the accounting policies have consistently been applied during the preparation of the financial statements, that accounting estimates were prepared on the principal of prudence and best business practice and that the Annual Report gives a true and fair view of the financial position of the Company and the results of its operations for the year ended 31 December 2006.

The Managing Director confirms that the financial statements have been prepared in accordance with provisions of the Companies Act, the Slovenian Accounting Standards and other regulations managing the accounting area. The financial statements were prepared on a going concern basis.

Managing Director
Jože Zagožen, Ph.D.

Ljubljana, 23 March 2007

4.3 AUDITOR'S REPORT

KPMG

Independent Auditor's Report

To the Shareholders of Holding Slovenske elektrarne d.o.o.

We have audited the accompanying financial statements of the Holding Slovenske elektrarne d.o.o., which comprise the balance sheet as at 31 December 2006, the income statement, the statement of changes in equity, the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

We also read the Management Report.

Management's responsibility for the financial statements

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

Auditor's responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Holding Slovenske elektrarne d.o.o. as at 31 December 2006, the result of its operations and its cash flows for the year then ended in accordance with the Slovenian Accounting Standards.

The Management Report is in conformity with the audited financial statements.

KPMG SLOVENIJA,
podjetje za revidiranje, d.o.o.

Marjan Mahnič, B.Sc.Ec.
Certified Auditor
Partner

Ljubljana, 30th March 2007

KPMG Slovenija, d.o.o.
1

4.4 BALANCE SHEET

BALANCE SHEET

ITEM					in 000 SIT
		Note	31 Dec 2006	1 Jan 2006	31 Dec 2005
	ASSETS		260,563,063	239,420,036	256,902,085
A.	*LONG-TERM ASSETS*		*223,820,826*	*205,433,918*	*222,916,112*
I.	Intangible assets and long-term deferred costs and accrued revenues	1	1,356,234	471,925	473,912
1.	Concessions, patents, licences, trademarks and similar rights		1,356,234	471,687	473,674
3.	Advances for intangible assets		0	238	238
II.	Property, plant and equipment	2	24,039,589	17,755,531	17,749,472
1.	Land and buildings		7,811,805	440,930	440,930
	b) Buildings		7,811,805	440,930	440,930
2.	Manufacturing plant and equipment		8,003,473	0	0
3.	Other plant and equipment		728,238	312,728	312,728
4.	Property, plant and equipment being acquired		7,496,073	17,001,873	16,995,814
	a) Property, plant and equipment in course of construction		5,975,234	16,965,522	16,965,522
	b) Advances for acquisition of property, plant and equipment		1,520,839	36,351	30,292
IV.	Long-term investments	3	197,934,832	187,158,569	204,662,728
1.	Long-term investments excluding loans		197,934,832	187,158,569	204,662,728
	a) Shares and interests in group companies		197,777,504	187,130,624	204,634,786
	b) Shares and interests in associates		130,328	945	942
	c) Other shares and interests		26,600	26,600	26,000
	d) Other long-term investments		400	400	400
V.	Long-term operating receivables	4	30,000	30,000	30,000
3.	Long-term operating receivables due from others		30,000	30,000	30,000
VI.	Deferred tax assets	5	460,171	17,893	0
B.	*CURRENT ASSETS*		*36,463,596*	*33,928,461*	*33,928,316*
II.	Inventories		785	733	729
1.	Material		462	379	379
4.	Advances for inventories		323	354	350
III.	Short-term investments	6	7,977,307	7,487,134	7,487,134
1.	Short-term investments excluding loans		1,247,698	1,394,963	1,394,963
	b) Other shares and interests		1,238,423	1,238,423	1,238,423
	c) Other short-term investments		9,275	156,540	156,540
2.	Short-term loans		6,729,609	6,092,171	6,092,171
	a) Short-term loans to group companies		734,609	12,812	12,812
	b) Short-term loans to others		5,995,000	6,079,359	6,079,359
IV.	Short-term operating receivables	4	27,483,706	25,436,281	25,436,140
1.	Short-term operating receivables due from group companies		551,497	275,508	275,508
2.	Short-term trade receivables		22,330,458	15,352,082	15,352,082
3.	Short-term operating receivables due from others		4,601,751	9,808,691	9,808,550
V.	Cash	7	1,001,798	1,004,313	1,004,313
C.	*DEFERRED COSTS AND ACCRUED REVENUES*	*8*	*278,641*	*57,657*	*57,657*
	OFF BALANCE SHEET ASSETS	*9*	*52,792,017*	*20,798,417*	*20,798,417*

BALANCE SHEET (continuation)

ITEM					in 000 SIT
		Note	31 Dec 2006	1 Jan 2006	31 Dec 2005
	LIABILITIES		***260,563,063***	***239,420,036***	***256,902,085***
A.	***EQUITY***	***10***	***202,926,629***	***195,881,872***	***213,457,106***
I.	Called-up capital		1,156,217	1,156,217	1,156,217
1.	Share capital		1,156,217	1,156,217	1,156,217
II.	Capital surplus		166,070,501	166,070,501	166,070,501
III.	Revenue reserves		29,514,702	24,707,653	24,707,653
5.	Other revenue reserves		29,514,702	24,707,653	24,707,653
IV.	Revaluation surplus		1,895,244	501,563	18,005,652
V.	Retained profit		0	3,445,938	0
VI.	Net profit for the period		4,289,965	0	3,517,083
B.	***PROVISIONS AND LONG-TERM ACCRUED COSTS AND DEFERRED REVENUES***	11	***1,677,170***	***4,377,913***	***4,290,932***
1.	Provisions for pensions and similar liabilities		95,546	86,981	0
2.	Other provisions		1,581,624	4,290,932	4,290,932
C.	***LONG-TERM LIABILITIES***	12	***23,074,461***	***10,569,618***	***10,569,618***
I.	Long-term financial liabilities		12,221,092	7,394,595	7,394,595
2.	Long-term financial liabilities to banks		12,221,092	7,394,595	7,394,595
II.	Long-term operating liabilities		10,853,369	3,175,023	3,175,023
1.	Long-term operating liabilities to group companies		10,770,512	3,175,023	3,175,023
2.	Long-term trade payables		82,857	0	0
D.	SHORT-TERM LIABILITIES	13	***32,293,619***	***28,227,123***	***28,227,123***
II.	Short-term financial liabilities		1,174,629	5,212,002	5,212,002
2.	Short-term financial liabilities to banks		1,174,629	5,212,002	5,212,002
III.	Short-term operating liabilities		31,118,990	23,015,121	23,015,121
1.	Short-term operating liabilities to group companies		12,869,261	11,262,982	11,262,982
2.	Short-term trade payables		15,552,966	11,085,868	11,085,868
4.	Short-term operating liabilities from advances		36	0	0
5.	Other short-term operating liabilities		2,696,727	666,271	666,271
E.	***SHORT-TERM ACCRUED COSTS AND DEFERRED REVENUES***	***14***	***591,184***	***363,510***	***357,306***
	OFF BALANCE SHEET LIABILITIES	9	***52,792,017***	***20,798,417***	***20,798,417***

4.5 INCOME STATEMENT

INCOME STATEMENT

ITEM		in 000 SIT 2006	2005
1.	Net sales	188,191,375	146,067,922
a)	Domestic market	133,594,958	108,994,689
b)	Foreign market	54,596,417	37,073,233
3.	Capitalised own products and/or services	37,797	36,409
4.	Other operating revenues (inclusive of revaluation operating revenues)	3,392	3,596
5.	Costs of goods, materials and services	172,233,601	137,406,708
a)	Cost of goods and materials sold and cost of materials used	171,107,510	136,658,884
b)	Cost of services	1,126,091	747,824
6.	Labour costs	1,204,319	1,083,304
a)	Payroll costs	831,592	738,745
b)	Social security costs	174,740	154,934
	- of which for pension insurance costs	110,578	97,802
c)	Other labour costs	197,987	189,625
7.	Write-downs in value	358,100	212,327
a)	Depreciation and amortisation expense	354,071	207,276
b)	Revaluation operating expenses associated with intangible assets and property, plant and equipment	3,690	2,769
c)	Revaluation operating expenses associated with current assets	339	2,282
8.	Other operating expenses	2,394,271	383,315
OPERATING PROFIT		***12,042,273***	***7,022,273***
9.	Financial revenue from shares	35,737	23,588
a)	Financial revenue from shares and interests in group companies	0	2,451
c)	Financial revenues from shares and interests in other companies	35,737	21,137
10.	Financial revenue from loans	239,648	206,404
a)	Financial revenue from loans to group companies	2,050	3,223
b)	Financial revenue from loans to others	237,598	203,181
11.	Financial revenue from operating receivables	93,537	211,612
a)	Financial revenue from operating receivables due from group companies	2	0
b)	Financial revenue from operating receivables due from others	93,535	211,612
12.	Financial expenses due to impairment and write-offs of investments	1,123,099	5
13.	Financial expenses for financial liabilities	672,087	432,926
a)	Financial expenses for loans received from group companies	114	3
b)	Financial expenses for loans received from banks	671,973	432,923
14.	Financial expenses for operating liabilities	42,216	88,678
a)	Financial expenses for operating liabilities due to group companies	39	0
b)	Financial expenses for trade payables and bills payable	4,010	3,658
c)	Financial expenses for other operating liabilities	38,167	85,020
PROFIT FROM ORDINARY ACTIVITIES		***10,573,793***	***6,942,268***
15.	Other revenues	869	91,900
16.	Other expenses	6	2
PROFIT FROM EXTRAORDINARY ACTIVITIES		***863***	***91,898***
TOTAL OPERATING PROFIT		***10,574,656***	***7,034,166***
17.	Income tax	2,365,858	0
18.	Deferred taxes	-442,278	0
19.	***NET PROFIT FOR THE PERIOD***	***8,651,076***	***7,034,166***

4.6 CASH FLOW STATEMENT

CASH FLOW STATEMENT

ITEM	2006	2005
A. CASH FLOWS FROM OPERATING ACTIVITIES		
a) Items of income statement	15,716,532	7,817,339
Operating revenue (except from revaluation) and financial revenue from operating receivables	188,284,442	146,279,892
Operating expenses excluding depreciation or amortisation (except from revaluation) and financial expenses from operating liabilities	(172,567,910)	(138,462,553)
b) Changes in net operating assets in balance sheet items (including accruals and deferrals, provisions and deferred tax assets and liabilities)	654,297	630,143
Opening less closing operating receivables	(7,908,638)	(4,027,391)
Opening less closing deferred costs and accrued revenues	(220,984)	(31,953)
Opening less closing deferred tax assets	(442,278)	0
Opening less closing inventories	(52)	(486)
Closing less opening operating liabilities	9,005,197	4,702,071
Closing less opening accrued costs and deferred revenues and provisions	221,052	(12,098)
Net cash from operating activities (a+b)	16,370,829	8,447,482
B. CASH FLOWS FROM INVESTING ACTIVITIES		
a) Cash receipts from investing activities	208,761,019	180,368,876
Interest and dividends received from investing activities	278,274	325,130
Cash receipts from disposal of intangible assets	399,273	0
Cash receipts from disposal of property, plant and equipment	9,384	6,285
Cash receipts from disposal of long-term investments	45,101	2,502
Cash receipts from disposal of short-term investments	208,028,987	180,134,959
b) Cash payments from investing activities	(222,245,614)	(188,205,899)
Cash payments to acquire intangible assets	(1,459,646)	(1,382,906)
Cash payments to acquire property, plant and equipment	(6,026,966)	(7,245,407)
Cash payments to acquire long-term investments	(6,097,577)	(5,851,886)
Cash payment to acquire short-term investments	(208,666,425)	(173,725,700)
c) Net cash from investing activities (a + b)	-13,484,595	-7,837,023
C. CASH FLOWS FROM FINANCING ACTIVITIES		
a) Cash proceeds from financing activities	9,964,252	5,006,597
Cash proceeds from increase in long-term financial liabilities	999,881	0
Cash proceeds from increase in short-term financial liabilities	8,964,371	5,006,597
b) Cash payments from financing activities	(12,853,001)	(5,373,069)
Interest paid on financing activities	(677,873)	(441,655)
Cash repayments of short-term financial liabilities	(9,175,128)	0
Dividends and other profit shares paid	(3,000,000)	(4,931,414)
c) Net cash from financing activities (a + b)	-2,888,749	-366,472
D. CLOSING BALANCE OF CASH	***1,001,798***	***1,004,313***
x) Net cash inflow or outflow for the period	(2,515)	243,987
y) Opening balance of cash	1,004,313	760,326

4.7 STATEMENT OF CHANGES IN EQUITY - FINANCIAL YEAR 2006

in 000 SIT

	ITEM	Called-up capital		Capital surplus	Revenue reserves		
		Share capital	Uncalled capital		Legal reserves	Reserves for own shares and interests	Own shares and interests (deduction item)
	Balance at 31 Dec 2005	1.156.217	0	166.070.501	0	0	0
	Changes due to transition to SAS (2006)	0	0	0	0	0	0
A.	*Opening balance*	1.156.217	0	166.070.501	0	0	0
B.	*Movements to equity*	0	0	0	0	0	0
d)	Net profit or loss for the period						
f)	Other increases in components in equity						
C.	*Movements within equity*	0	0	0	0	0	0
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board						
b)	Allocation of net profit to additional reserves based on a resolution of the shareholders' meeting						
c)	Settlement of loss as a deduction component of equity						
D.	*Movements from equity*	0	0	0	0	0	0
a)	Payment of dividends						
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)						
e)	Other decreases in components of equity						
E.	*Closing balance*	1.156.217	0	166.070.501	0	0	0
	ACCUMULATED PROFIT	0	0	0	0	0	

in 000 SIT

	ITEM	Revenue reserves		Revaluation surplus	Retained profit or loss	Net profit or loss for the period		TOTAL
		Statutory reserves	Other revenue reserves		Retained net loss	Net profit for the period	Net loss for the period	
	Balance at 31 Dec 2005	0	24.707.653	18.005.652	0	0	0	213.457.106
	Changes due to transition to SAS (2006)	0	0	(17.504.089)	(71.145)	0	0	(17.575.234)
A.	*Opening balance*	0	24.707.653	501.563	0	0	0	195.881.872
B.	*Movements to equity*	0	0	4.230.249	0	8.651.076	0	12.881.325
d)	Net profit or loss for the period					8.651.076		8.651.076
f)	Other increases in components in equity			4.230.249				4.230.294
C.	*Movements within equity*	0	4.807.049	0	0	(4.361.111)	0	0
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board		4.289.966		0	(4.289.966)		0
b)	Allocation of net profit to additional reserves based on a resolution of the shareholders' meeting		517.083					0
c)	Settlement of loss as a deduction component of equity					(71.145)		0
D.	*Movements from equity*	0	0	(2.836.568)	0	0	0	(5.836.568)
a)	Payment of dividends			0				(3.000.000)
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)			35.082				35.082
e)	Other decreases in components of equity			(2.871.650)				(2.871.650)
E.	*Closing balance*	0	29.514.702	1.895.244	0	4.289.965	0	202.926.629
	ACCUMULATED PROFIT	0	0	0	0	4.289.965	0	4.289.965

FINANCIAL YEAR 2005

ITEM		Called-up capital		Capital surplus	Revenue reserves			in 000 SIT
		Share capital	Uncalled capital		Legal reserves	Reserves for own shares and interests	Statutory reserves	Other revenue reserves
A.	***Opening balance***	***1.156.217***	***0***	***166.070.474***	***0***	***0***	***0***	***21.190.570***
B.	***Movements to equity***	***0***	***0***	***0***	***0***	***0***	***0***	***0***
d)	Net profit or loss for the period						0	
f)	Specific equity revaluation adjustment						0	
C.	***Movements within equity***	***0***	***0***	***0***	***0***	***0***		***3.517.083***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board						0	3.517.083
D.	***Movements from equity***	***0***	***0***	***0***	***0***	***0***		***0***
a)	Payment of dividends							
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)							
E.	***Closing balance***	***1.156.217***	***0***	***166.070.474***	***0***	***0***		***24.707.653***
	ACCUMULATED PROFIT	***0***	***0***	***0***	***0***	***0***	***0***	***0***

ITEM		Retained net profit	Net profit for the period	Equity revaluation adjustment		in 000 SIT
				General equity revaluation adjustment	Specific equity revaluation adjustment	TOTAL
A.	***Opening balance***	***4.931.414***	***0***	***27***	***11.271.304***	***204.620.006***
B.	***Movements to equity***	***0***	***7.034.166***	***0***	***6.954.518***	***13.988.684***
d)	Net profit or loss for the period		7.034.166			7.034.166
f)	Specific equity revaluation adjustment				6.954.518	6.954.518
C.	***Movements within equity***	***0***	***(3.517.083)***	***0***	***0***	***0***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board		(3.517.083)			0
D.	***Movements from equity***	***4.931.414***	***0***	***0***	***220.170***	***5.151.584***
a)	Payment of dividends	4.931.414				4.931.414
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)				220.170	220.170
E.	***Closing balance***	***0***	***3.517.083***	***27***	***18.005.652***	***213.457.106***
	ACCUMULATED PROFIT	***0***	***3.517.083***		***0***	***3.517.083***

4.8 NOTES TO THE FINANCIAL STATEMENTS

4.8.1 BALANCE SHEET

General

Information regarding the basis for preparation of the balance sheet and the specific accounting policies, selected and applied with significant transactions and other business transactions of the Company, are presented in disclosures of individual assets and liabilities.

As for the transition to the SAS (2006) following changes have been disclosed:

- elimination of the increase of long-term investments due to the use of the equity method, recorded under specific equity revaluation adjustment in the amount of 17,504,159 thousand SIT;
- formation of deferred taxes in the amount of 17,893 thousand SIT due to the formation of provisions for jubilee benefits and termination benefits;
- elimination of long-term deferred costs of operation in the amount of 1,987 thousand SIT,
- transfer of a part of the investment in the hydroelectric power plants on the lower Sava river from intangible assets to property, plant and equipment (3,728,893 thousand SIT);
- transfer of a part of the investment in the hydroelectric power plants on the lower Sava river from 'long-term deferred costs' to 'concessions, patents, licences, trade marks and similar rights' (229,000 thousand SIT);
- transfer of VAT in the amount of 6,204 thousand SIT from advances for property, plant and equipment, inventories and other operating receivables to accrued costs and deferred revenues.

The Company has no additional information whose disclosure in the balance sheet is not obligatory though considered to be significant for a true and fair presentation of the Company's operations.

Assets and liabilities are recorded at fair value or at initial cost if the fair value of assets or liabilities cannot be defined.

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the balance sheet for 2005 are recorded in two columns, namely:

- under SAS (2001) and in items of the balance sheet under SAS (2006),
- under restated amounts as at 1 January 2006 in compliance with Point 15 of the Introduction to the SAS (2006).

(1)
Intangible assets
1,356,234 thousand SIT

Concessions, patents, licences, trademarks and similar rights include:

- transfer of the concession rights for the Boštanj and Blanca hydroelectric power plants;
- software under development and software in use; and
- CO_2 emission coupons (for trading).

Amortisation rates of intangible assets with finite useful lives range from 2 % to 33.33 %, depending on the expected useful lives.

COST AND ACCUMULATED AMORTISATION OF INTANGIBLE ASSETS

BALANCE AS AT 31 Dec 2006	*CONCESSIONS, PATENTS, LICENCES TRADEMARKS AND SIMILAR RIGHTS*	*TOTAL* (*in 000 SIT*)
Cost	1,876,846	1,876,846
Accumulated amortisation	520,612	520,612
Book value	1,356,234	1,356,234

MOVEMENT OF INTANGIBLE ASSETS

INTANGIBLE ASSETS	*CONCESSIONS, PATENTS, LICENCES TRADEMARKS AND SIMILAR RIGHTS*	*ADVANCES FOR INTANGIBLE ASSETS*	*TOTAL* (*in 000 SIT*)
Carrying amount as at 1 Jan 2006	471,687	238	471,925
Additions	1,497,241	0	1,497,241
Transfers	156,540	0	156,540
Decrease	-389,356	-238	-389,594
Amortisation	-54,593	0	-54,593
Revaluation	-325,285	0	-325,285
Book value as at 31 Dec 2006	1,356,234	0	1,356,234

(2)
Property, plant and equipment
24,039,589 thousand SIT

Buildings comprise:

- Production facilities in the Boštanj hydroelectric power plant;
- business premises in Ljubljana; and
- business premises in Sevnica.

Production plant and equipment comprise production equipment of the Boštanj hydroelectric power plant.

Under other plant and equipment the Company records equipment for collecting data about energy the production on the Group level, telecommunication network equipment, hardware, furniture, passenger cars and small tools.

Advances for property, plant and equipment refer to the supply of equipment for the Boštanj and Blanca hydroelectric power plants.

Property, plant and equipment in course of construction mostly refer to investments in production facilities and equipment of the power plant on the Lower Sava river and the centre of managing the balance sheet group.

Pursuant to the joint venture contract, the venturers have the right on the co-operation in the management of the funds invested in the joint venture project, i.e. the completed HPPs and the HPPs in construction and other assets, in the portion corresponding to their respective shares in the investment.

The Company records no property, plant and equipment under finance lease or mortgage.

No impairment or increase in value of property, plant and equipment was carried out in 2006.

DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

GROUPS OF PROPERTY, PLANT AND EQUIPMENT	*DEPRECIATION RATES*	*USEFUL LIFE*
Buildings	1.52% - 5%	20 - 66 let
Furniture	10% - 25%	4 - 10 let
Computer equipment	20% - 50%	2 - 5 let
Low-value assets	25% - 33.33%	3 - 4 leta
Cars	12.5% - 20%	5 - 8 let
Manufacturing plant and equipment	2% - 20%	5 - 50 let
Other equipment	20% - 25%	4 - 5 let

COST AND ACCUMULATED DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

BALANCE AS AT 31 Dec 2006 *in 000 SIT*

	BUILDINGS	*MANUFACTURING PLANT AND EQUIPMENT*	*OTHER PLANT AND EQUIPMENT*	*ADVANCES FOR PROPERTY, PLANT AND EQUIPMENT*	*PROPERTY, PLANT AND EQUIPMENT IN COURSE OF CONSTRUCTION*	*TOTAL*
Cost	7,898,657	8,165,639	1,223,538	1,520,839	5,975,234	24,783,907
Accumulated depreciation	86,852	162,166	495,300	0	0	744,318
Book value	7,811,805	8,003,473	728,238	1,520,839	5,975,234	24,039,589

MOVEMENT OF PROPERTY, PLANT AND EQUIPMENT

MOVEMENT OF PROPERTY, PLANT AND EQUIPMENT *in 000 SIT*

	BUILDINGS	*MANUFACTURING PLANT AND EQUIPMENT*	*OTHER PLANT AND EQUIPMENT*	*ADVANCES FOR PROPERTY, PLANT AND EQUIPMENT*	*PROPERTY, PLANT AND EQUIPMENT IN COURSE OF CONSTRUCTION*	*TOTAL*
Carrying amount as at 1 Jan 2006	440,930	0	312,728	36,351	16,965,522	17,755,531
Additions	7,437,272	8,165,639	606,612	1,566,946	5,219,234	22,995,703
Disposals	0	0	-12,219	-82,458	0	-94,677
Transfers	0	0	0		-16,209,522	-16,209,522
Depreciation	-66,397	-162,166	-178,883	0	0	-407,446
Book value as at 31 Dec 06	7,811,805	8,003,473	728,238	1,520,839	5,975,234	24,039,589

3) Long-term investments 197,934,832 thousand SIT

Shares and interests in group companies refer to the value of long-term investments in companies, where the Company has a majority interest (whether direct or indirect through other companies) and prepares consolidated financial statements for these Group companies

The item of shares and interests in associates records a 45 % capital contribution into the company Plinsko parna elektrarna.

The item of other shares and interests refers to the 19 % share in the company Stelkom.

The investment in Technological Centre for Research and Experimental Development (Tehnološki center za raziskave in eksperimentalni razvoj) was recorded under other long-term investments.

According to our estimates, the investments are not considered to be subject to risk.

COST AND VALUE ADJUSTMENT OF LONG-TERM INVESTMENTS

BALANCE AS AT 31 Dec 2006	SHARES AND INTERESTS IN GROUP COMPANIES EXCEPT ASSOCIATES	SHARES AND INTERESTS IN ASSOCIATES	OTHER SHARES AND INTERESTS	OTHER LONG-TERM INVESTMENTS	in 000 SIT TOTAL
Cost	229,249,533	130,328	26,600	400	229,406,861
Value adjustment	31,472,029	0	0	0	31,472,029
Book value	197,777,504	130,328	26,600	400	197,934,832

MOVEMENT OF LONG-TERM INVESTMENTS

MOVEMENT OF LONG-TERM INVESTMENTS	SHARES AND INTERESTS IN GROUP COMPANIES EXCEPT ASSOCIATES	SHARES AND INTERESTS IN ASSOCIATES	OTHER SHARES AND INTERESTS	OTHER LONG-TERM INVESTMENTS	in 000 SIT TOTAL
Carrying amount as at 1 Jan 2006	187,130,624	945	26,600	400	187,158,569
Additions	297,958	0	0	0	297,958
Disposals	-1,168,200	0	0	0	-1,168,200
Increase	11,517,122	129,383	0	0	11,646,505
Book value as at 31 Dec 2006	197,777,504	130,328	26,600	400	197,934,832

MOVEMENTS IN LONG-TERM INVESTMENTS IN GROUP COMPANIES

MOVEMENT OF LONG-TERM INVESTMENTS IN GROUP COMPANIES	*in 000 SIT*
	2006
Change of the investment in Termoelektrarna Brestanica d.o.o.	4,616,172
Change of the investment in Termoelektrarno Šoštanj d.o.o.	6,885,967
Change of the investment in TDR - Metalurgija d.d.	-1,153,217
New investment in HSE Hungary Kft.	45,729
New investment in HSE Balkan Energy d.o.o.	245,646
New investment in HSE Adria d.o.o.	6,583
Total changes in long-term investments	10,646,880

LONG-TERM INVESTMENTS IN GROUP COMPANIES

GROUP COMPANIES		*in 000 SIT*
	31. 12. 06	*1. 1. 06*
Dravske elektrarne Maribor d.o.o.	92,622,618	92,622,618
Savske elektrarne Ljubljana d.o.o.	27,646,798	27,646,798
Soške elektrarne Nova Gorica d.o.o.	26,270,717	26,270,717
Termoelektrarna Brestanica d.o.o.	6,927,950	2,311,778
Termoelektrarna Šoštanj d.o.o.	22,526,394	15,640,427
Premogovnik Velenje d.d.	21,480,247	21,480,247
HSE Invest d.o.o.	2,500	2,500
TDR - Metalurgija d.d.	0	1,153,217
HSE Italia S.r.l.	2,322	2,322
HSE Hungary Kft.	45,729	0
HSE Balkan Energy d.o.o.	245,646	0
HSE Adria d.o.o.	6,583	0
Total long-term investments in group companies	197,777,504	187,130,624

Long-term investments in Group companies

DRAVSKE ELEKTRARNE MARIBOR d.o.o.,
Obrežna ulica 170, 2000 MARIBOR

- share of HSE: 99.9 %
- total equity: 110,666,247 thousand SIT
- net profit for 2006: 4,999,272 thousand SIT.

SAVSKE ELEKTRARNE LJUBLJANA d.o.o.,
Gorenjska cesta 46, 1215 MEDVODE

- share of HSE: 79.5 %
- total equity: 35,487,560 thousand SIT
- net profit for 2006: 67,713 thousand SIT.

SOŠKE ELEKTRARNE NOVA GORICA d.o.o.,

Erjavčeva 20, 5000 NOVA GORICA

- share of HSE: 79.5 %
- total equity: 35,959,770 thousand SIT
- net profit for 2006: 1,070,358 thousand SIT.

TERMOELEKTRARNA BRESTANICA d.o.o.,

Cesta prvih borcev 18, 8280 BRESTANICA

- share of HSE: 100.0 %
- total equity: 10,941,677 thousand SIT
- net profit for 2006: 496,938 thousand SIT.

TERMOELEKTRARNA ŠOŠTANJ d.o.o.,

Cesta Lole Ribarja 18, 3325 ŠOŠTANJ

- share of HSE: 100.0 %
- total equity: 47,346,317 thousand SIT
- net profit for 2006: 395,489 thousand SIT.

PREMOGOVNIK VELENJE d.d.,

Partizanska cesta 78, 3320 VELENJE

- share of HSE: 77.7 %
- total equity: 32,014,746 thousand SIT
- net profit for 2006: 100,688 thousand SIT.

HSE INVEST d.o.o.,

Obrežna ulica 170a, 2000 MARIBOR

- share of HSE: 25.0 % (direct); 89.7 % (indirect)
- total equity: 7,039 thousand SIT
- net profit for 2006: 2,899 thousand SIT.

HSE Italia S.r.l.,

Via Roma 20, Gorizia, Italy

- share of HSE: 100.0 %
- total equity: 16,920.39 EUR or 4,055 thousand SIT
- net profit for 2006: 670.42 EUR or 161 thousand SIT.

HSE Hungary Kft.,

Karolyi Mihaly u. 12, Budapest, Hungary

- share of HSE: 99.8 % (0.2 % share held by HSE Italia)
- total equity: 51,959 thousand HUF or 49,486 thousand SIT
- net profit for 2006: 1,959 thousand HUF or 1,866 thousand SIT.

HSE Balkan Energy d.o.o.,

Makenzijeva 74, Beograd, Serbia

- share of HSE: 100.0 %
- total equity: 80,972 thousand RSD or 245,648 thousand SIT
- net profit for 2006: 511 thousand RSD or 1,475 thousand SIT.

HSE Adria d.o.o.,

Miramarska 24, Zagreb, Croatia

- share of HSE: 100.0 %
- total equity: 225,081.50 HRK or 7,346 thousand SIT
- net profit for 2006: 39,281 HRK or 1,278 thousand SIT.

Long-term investments in associates

Plinsko parna elektrarna d.o.o.,

Tovarniška 10, 2325 Kidričevo

- share of HSE: 45.0 %
- total equity: 289,539 thousand SIT
- net profit for 2006: 130 thousand SIT.

(4)
Receivables
27,513,706 thousand SIT

Long-term receivables due from others refer to the deposit given as collateral for trading with electricity on Slovenia's stock market.

Short-term operating receivables due from group companies comprise receivables from the sale of electricity and receivables referring to the operational cost of the Boštanj hydroelectric power plant.

The major part of short-term operating trade receivables comprises receivables from the sale of electricity in Slovenia and abroad.

Short-term operating receivables due from others include input VAT receivables, security deposits, receivables payable to the grantor of the concession for the funds provided as security during the process of acquisition the land for the Blanca hydroelectric power plant, as well as receivables for interest on deposits and default interest.

Receivables due by customers are mainly settled within the set terms or with minor delays. In case of default, the customers both in Slovenia and abroad are charged the default interest at the contractual rate. At year-end, the share of receivables that were not yet due accounted for 99% of the total receivables; all receivables were settled as at the date when this report has been prepared.

Receivables overdue for a period exceeding 180 days are considered as doubtful. The Company recorded no such receivables as at the balance sheet date.

The information referring to debt insurance has been presented in the Management Report.

SHORT-TERM OPERATING RECEIVABLES

	31 Dec 2006	1 Jan 2006
		in 000 SIT
Short-term receivables due from domestic customers	15,891,294	12,618,884
Short-term receivables due from foreign customers	6,989,350	3,008,670
Short-term advances for services not rendered - domestic market	896	873
Short-term advances for services not rendered - foreign market	132	9,591
Short-term advances for purchase of shares in companies	0	5,851,886
Short-term guarantees	612,630	0
Short-term operating receivables on the account of others	190,103	8,925
Short-term receivables associated with financial revenues	23,862	35,093
Short-term receivables due from the state	3,485,873	2,665,903
Short-term receivables due from other entities	289,566	1,236,456
Total	27,483,706	25,436,281

SHORT-TERM OPERATING RECEIVABLES DUE FROM GROUP COMPANIES

GROUP COMPANIES	31 Dec 2006	1 Jan 2006
		in 000 SIT
Dravske elektrarne Maribor d.o.o.	57,483	898
Savske elektrarne Ljubljana d.o.o.	23,515	898
Soške elektrarne Nova Gorica d.o.o.	5,226	898
Termoelektrarna Brestanica d.o.o.	5,226	898
Termoelektrarna Šoštanj d.o.o.	0	898
Premogovnik Velenje d.d.	58,815	50,875
TDR - Metalurgija d.d.	0	219,209
HSE Invest d.o.o.	123	925
HSE Balkan Energy d.o.o	13,489	0
HSE Hungary Kft.	387,614	0
HSE Italia S.r.l.	6	9
Total	551,497	275,508

RECEIVABLES BY MATURITY DATES

MATURITY	31 Dec 2006	1 Jan 2006
		in 000 SIT
Receivables not yet due	27,285,087	24,487,297
Receivables overdue for less than 3 months	198,036	953,855
Receivables overdue from 3 to 6 months	583	24,847
Receivables overdue for more than 6 months	0	2,242

(5)
Deferred tax assets
460,171 thousand SIT

Deferred tax assets were formed by the Company and result from the expenses which influence the Company's current result but are not deductible for tax purposes in the reporting year.

During the transition to SAS (2006) the Company formed provisions for jubilee benefits and termination benefits which resulted in the formation of deferred tax assets in the amount of 17,893 thousand SIT, as set out below:
- upon the formation of provisions 21,745 thousand SIT,
- due to the change in the tax rates in accordance with ZDDPO-2, deferred tax assets were decreased by 3,852 thousand SIT.

MOVEMENT OF DEFERRED TAX ASSETS

DEFERRED TAX ASSETS				*in 000 SIT*
	PROVISIONS	*IMPAIRMENT*	*DEPRECIATION*	*TOTAL*
Value as at 1 Jan 2006	17,893	0	0	17,893
Formation, increase	366,811	74,815	2,307	443,933
Utilisation	-1,655	0	0	-1,655
Value as at 31 Dec 2006	383,049	74,815	2,307	460,171

(6)
Short-term investments
7,977,307 thousand SIT

Other shares and interests include investments in shares of Slovenia's banks.

Other short-term investments refer to the fair value of the interest swap as at 31 December 2006.

Short-term loans to group companies comprise loans granted to three group companies.

Short-term loans to others comprise short-term Tolar and foreign currency deposits with major Slovenia's banks.

A part of the loans granted to group companies has been secured by blank bills and arrangements on loan repayment by offset against the debtor's receivables.

Short-term deposits in the local currency have not been secured. In accordance with the internal rules, the Company has complied with the principle of investment diversification per individual banks and monitors credit ratings.

The investments are not considered to be subject to risk.

(7) Cash 1,001,798 thousand SIT

Cash includes the Company's cash balances on Tolar and foreign currency accounts with domestic and foreign banks and money at call in foreign currencies deposited in foreign banks.

No automatic debit balances had been agreed with the banks for the transaction accounts as at year-end 2006.

(8) Deferred costs and accrued revenues 278,641 thousand SIT

DEFERRED COSTS AND ACCRUED REVENUES

DEFERRED COSTS AND ACCRUED REVENUES		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Short-term deferred and expenses	258,635	35,152
Short-term accrued revenues	20,000	22,505
VAT on advances received	6	0
Total	278,641	57,657

(9) Off balance sheet items 52,792,017 thousand SIT

In addition to the assets and liabilities presented within the off balance sheet items, the Company also signed two guarantees in 2006, as set out below:

- a guarantee issued to Geoplin referring to the fulfilment of liabilities and other obligations of the thermal power plant in Šoštanj arising from a long-term agreement on natural gas for a period until (incl.) 2012; furthermore, an agreement was signed with the thermal power plant in Šoštanj, stipulating that in case the payment is made to Geoplin by HSE, the receivables arising from the payment shall be offset by the liabilities due by HSE to the thermal power plant in Šoštanj.
- a guarantee provided by HSE in the guarantee agreement signed between HSE, SENG Nova Gorica and Bank Austria Creditanstalt, stating that HSE shall settle any outstanding liabilities arising from the loan obtained from the European Investment Bank for the Avče power plant; an additional agreement was signed with SENG, stating that in case a payment is made by HSE pursuant to the guarantee agreement, the receivables arising from the payment shall be offset by the liabilities due by HSE to SENG Nova Gorica.

OFF BALANCE SHEET ASSETS

in 000 SIT

	31 Dec 2006	1 Jan 2006
Bank guarantees received for electric energy	3,830,158	8,064,701
Bank guarantees received for investments	8,863,792	2,524,193
Bank guarantees received for investments - group companies	9,431	23,789
Insurance policies received for investments	120,834	710,060
Mutual fund (Modri sklad)	33,067	14,076
Total off balance sheet assets	12,857,282	11,336,819

OFF BALANCE SHEET LIABILITIES

in 000 SIT

	31 Dec 2006	1 Jan 2006
Bank guarantees granted for electric energy	2,006,482	1,652,085
Bank guarantees granted for electric energy - group companies	1,307,403	0
Bank guarantees granted for the concession of HPP Boštanj	24,000	0
Futures contracts - for insurance	36,551,760	7,807,082
Statement about the possibility of obtaining funds (AE licence)	2,000	2,000
Lawsuits	43,090	431
Total off balance sheet liabilities	39,934,735	9,461,598

(10) Equity 202,926,629 thousand SIT

The value of share capital remained unchanged in the reporting period.

Upon transition to SAS (2006), the amount previously recorded as general equity revaluation adjustment (27 thousand SIT) was transferred to capital surplus.

Other revenue reserves increased in the reporting period by:

- 517,083 thousand SIT based on the resolution adopted by the shareholders' meeting of the Company (part of accumulated profit of 2005) and
- a part of the net profit for 2006 in the amount of 4,289,966 thousand SIT.

Retained earnings and losses in the amount of 71,145 thousand SIT refer to the loss arising from the change in the balance sheet items upon the transition to SAS (2006), as set out below:

- the formation of provisions for termination payments and jubilee benefits in the amount of 69,087 thousand SIT;
- reversal of long-term deferred development costs in the amount of 1,987 thousand SIT;
- reversal and recognition of the exchange differences arising from a long-term investment abroad, amounting to 74 thousand SIT and
- reversal of impairment of a long-term investment in associates in the amount of 3 thousand SIT.

Under revaluation surplus, the results of standardised futures used as hedges and the fair value of interest swaps.

Standardised futures refer to closing deals on the purchase of electricity on foreign stock markets in the future, on the basis of which the Company secured deals already concluded for the sale of electricity in the same period.

The revaluation surplus was decreased by the amounts of deals on the purchase of electric energy in 2006, secured by standard futures contracts (35,082 thousand SIT). The cost of goods sold was increased by the same amount.

The index of euro exchange rate was recorded at 0.027 % in the reporting period. In case equity were revalued by the factor of euro exchange rate index, the net profit or loss for the accounting period would be higher by 51,867 thousand SIT. This amount of capital is exclusive of the net profit for the period, distributed profit from previous periods, the loss incurred upon the transition to SAS (2006) and the increase in revaluation surplus in 2006.

By taking into account the said calculation, the Company would record a net profit in the amount of 8.599.209 thousand SIT.

The cost of living index was recorded at 2.8 % in the reporting period. By taking the cost of living index into account, the total capital of the Company would increase by 5,402,684 thousand SIT. Hence this amount of capital is exclusive of the net profit for the period, distributed profit from previous periods, the loss incurred upon the transition to SAS (2006) and the increase in revaluation surplus in 2006.

By taking into account the said calculation, the Company would record a net profit in the amount of 3,248,392 thousand SIT.

COMPANY'S EQUITY

TOTAL EQUITY		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Share capital	1,156,217	1,156,217
Capital surplus	166,070,501	166,070,501
Other revenue reserves	29,514,702	24,707,653
Revaluation surplus	1,895,244	501,563
Retained earnings	0	3,445,938
Net profit for the period	4,289,965	0
Total equity	202,926,629	195,881,872

NET PROFIT OF THE COMPANY UPON RESTATEMENT OF EQUITY

NET PROFIT OF THE COMPANY UPON RESTATEMENT OF EQUITY	*in 000 SIT*
	31 Dec 2006
Net profit	8,651,076
Net profit using the euro (0.027 % growth)	8,599,209
Net profit using the cost of living index (2.8 % growth)	3,248,392

MOVEMENT OF REVALUATION SURPLUS

REVALUATION SURPLUS			*in 000 SIT*
	FUTURES CONTRACTS	*INTEREST SWAPS*	*TOTAL*
Opening balance as at 1 Jan 2006	501,563	0	501,563
Increase	4,220,974	9,275	4,230,249
Decrease	-2,871,650	0	-2,871,650
Increase of operating expenses	157,339	0	157,339
Decrease of operating expenses	-122,257	0	-122,257
Closing balance as at 31 Dec 2006	1,885,969	9,275	1,895,244

(11)
Provisions
1,677,170 thousand SIT

The payments made by venturers in 2006 in connection with the construction of the power plants on the lower Sava river in the amount of 4,290,932 thousand SIT were transferred from provisions to the item 'long-term operating liabilities'.

As at year-end 2006, provisions comprise:
- provisions for termination payments and jubilee benefits,
- provisions for contingent liabilities.

MOVEMENT OF PROVISIONS

PROVISIONS AND LONG-TERM ACCRUED COSTS AND DEFERRED REVENUES	*PROVISIONS FOR RETIREMENT AND JUBILEE BENEFITS*	*OTHER PROVISIONS*	*in 000 SIT* *TOTAL*
Value as at 1 Jan 2006	86,981	4,290,932	4,377,913
Formation, increase	15,186	1,581,624	1,596,810
Reversal	-6,621	0	-6,621
Transfers	0	-4,290,932	-4,290,932
Value as at 31 Dec 2006	95,546	1,581,624	1,677,170
Planned formation		4,192,874	4,192,874
Planned reversal		8,281,326	8,281,326

(12)
Long-term liabilities
23,074,461 thousand SIT

The Company's long-term liabilities include two long-term loans, as set out below:
- a long-term loan raised at the syndicate of Slovenian banks in 2003 for a period of 12 years and
- a long-term loan raised at a Slovenian bank in 2006 for a period of 5 years.

The principal due in 2007 is recorded among short-term liabilities to banks. Interest is accounted for on a monthly or quarterly basis and its undue portion payable in 2006 is recorded under short-term operating liabilities.

The loan raised in 2003 is in full due by October 2015. The interest rate changes with respect to the average yield of eleven-year bonds of the Republic of Slovenia; in 2007 it shall be adjusted to the amount of the valid EURIBOR rate plus a minimum margin. The loan is secured by ten blank bills of exchange.

The Company signed a contract on interest swaps for a loan in order to hedge the interest rate risk, effective 2 January 2007.

The long-term loan raised in 2006 will be repaid in full in 2011. Interest is charged at EURIBOR rate plus a minimum margin. The loan is secured by six blank bills of exchange.

Upon raising the loan, the Company also signed a contract on interest swaps, by which the risk of interest rate growth is lowered. The hedging is effective from 1 December 2006, due date is 1 December 2011. The estimated fair value of the interest swap as at 31 December 2006 in the amount of 9,275 thousand SIT is recorded under other short-term investments and revaluation surplus.

Long-term operating liabilities to group companies refer to payments made by venturers in connection with the joint venture. Due to their specific nature the payments are not secured.

Long-term operating liabilities are utilised after the start of operation of the individual power plants in the amount corresponding to the accumulated depreciation in the shares held by the individual venturers in the joint venture. Hence they were decreased by 107,968 thousand SIT in 2006.

As at year-end 2006, the venturers' investments in the power plants on the lower Sava river amounted to 22,200,980 thousand SIT.

LONG-TERM OPERATING LIABILITIES

PARTNERS IN JOINT VENTURE			*in 000 SIT*
	SHARE IN THE JOINT VENTURE	*31 Dec 2006*	*1 Jan 2006*
Dravske elektrarne Maribor d.o.o.	30.8%	6,770,036	1,995,729
Savske elektrarne Ljubljana d.o.o.	12.6%	2,769,560	816,434
Soške elektrarne Nova Gorica d.o.o.	2.8%	615,458	181,430
Termoelektrarna Brestanica d.o.o.	2.8%	615,458	181,430
Total long-term operating liabilities		10,770,512	3,175,023

LONG-TERM LIABILITIES AND THEIR MATURITY DATES

LONG-TERM LIABILITIES				*in 000 SIT*
		Maturity date		
	by 31 Dec 2009	*from 1 Jan 2010 to 31 Dec 2011*	*over 1 Jan 2012*	*TOTAL*
Long-term financial liabilities to banks	4,467,303	4,467,303	3,286,486	12,221,092
Long-term trade payables	82,857	0	0	82,857
Total	4,550,160	4,467,303	3,286,486	12,303,949

(13)
Short-term liabilities
32,293,619 thousand SIT

Short-term financial liabilities to banks refer to a portion of the principal of a long-term loan that is due in 2007.

Short-term liabilities to group companies refer to the supply of electric energy.

Short-term trade payables include short-term payables to suppliers of electric energy, electricity-related costs and short-term payables to suppliers in connection with the construction of the power plants on the lower Sava river.

Other short-term operating liabilities comprise income tax payables for 2006, payroll contributions for December and payroll tax, and interest payables on both long-term loans.

The Company settled all liabilities in due time.

SHORT-TERM FINANCIAL LIABILITIES

SHORT-TERM OPERATING LIABILITIES		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Short-term trade payables - domestic market	22,117,703	18,166,364
Short-term trade payables - foreign market	6,298,759	4,180,903
Short-term advances received	36	0
Other short-term payables on the account of others	5,765	1,583
Short-term payables to employees	81,966	68,049
Short-term payables to the state and other institutions	2,480,035	560,392
Short-term interest payable	30,020	35,806
Other short-term operating liabilities	104,706	2,024
Total	31,118,990	23,015,121

SHORT-TERM OPERATING LIABILITIES TO GROUP COMPANIES

GROUP COMPANIES	COUNTRY	31 Dec 2006	1 Jan 2006
			in 000 SIT
Dravske elektrarne Maribor d.o.o.	Slovenia	4,272,412	3,807,973
Savske elektrarne Ljubljana d.o.o.	Slovenia	346,706	336,893
Soške elektrarne Nova Gorica d.o.o.	Slovenia	807,513	466,379
Termoelektrarna Brestanica d.o.o.	Slovenia	626,228	937,175
Termoelektrarna Šoštanj d.o.o.	Slovenia	6,120,079	5,680,802
Premogovnik Velenje d.d.	Slovenia	2,118	2,377
HSE Invest	Slovenia	23,408	28,790
HSE Italia	Italy	1,869	1,466
HSE Hungary	Hungary	446,965	0
HSE Balkan Energy	Serbia	184,054	0
HSE Adria	Croatia	4,314	0
Other group companies	Slovenia	33,595	1,127
Total short-term operating liabilities to group companies		12,869,261	11,262,982

(14)
Accrued costs and deferred revenue
591,184 thousand SIT

SHORT-TERM ACCRUED COSTS AND DEFERRED REVENUES

	31 Dec 2006	1 Jan 2006
		in 000 SIT
Short-term accrued costs	380,352	357,061
Short-term deferred revenues	281	245
VAT on advances granted	210,551	6,204
Total short-term accrued costs and deferred revenues	591,184	363,510

4.8.2 INCOME STATEMENT

General

Information as to the basis for the preparation of the income statement, together with the specific accounting policies selected and applied in significant operations and transactions of the Company are introduced in disclosures of individual revenues and expenses.

The consolidated income statement has been prepared by applying Format I, defined under SAS 25.5.

The amount of expenses was influenced by methods or accounting policies applied and presented in disclosures of balance sheet items (depreciation, valuation of inventories). The methods and accounting policies have not changed compared to the previous financial year; however, the Company extended the useful lives of certain items of software recorded under Concessions, patents, licences, trademarks and similar rights.

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the income statement for 2005 are recorded according to SAS (2001) and presented under income statement items under SAS (2006).

Revenues
188,602,355 thousand SIT

Revenues from sale of electricity in Slovenia and abroad have a share of 99.94 % among net sales.

Revenues from services rendered mostly refer to services related to the sale of electric energy.

Capitalised own services represent services rendered in connection with the construction of the power plant on the Lower Sava river.

Revaluation operating revenues arose during the sale of property, plant and equipment and the reversal of impairment of trade receivables.

Financial revenue from shares and interests refer to dividends received.

Financial revenue from loans mostly represents interest on deposits.

Financial revenue from operating receivables represent gains on standardised futures held for trading, exchange gains from cash and operating receivables and profits from the sale of CO_2 emission coupons.

REVENUES

REVENUES	*in 000 SIT*	
	2006	**2005**
Operating revenues	188,232,564	146,107,927
Financial revenues	368,922	441,604
Other revenues	869	91,900
Total	188,602,355	146,641,431

OPERATING REVENUES

OPERATING REVENUES	2006	2005
		in 000 SIT
Revenues from sale of electric energy	188,083,150	146,039,685
Revenues from sale of services	108,225	28,237
Capitalised own services	37,797	36,409
Revaluation operating revenues	3,392	3,596
Total	188,232,564	146,107,927

GEOGRAPHICAL SEGMENTS

GEOGRAPHICAL SEGMENTS	2006	2005
		in 000 SIT
Domestic market	133,594,958	108,994,689
Foreign market	54,596,417	37,073,233
Total	188,191,375	146,067,922

Expenses
178,027,699 thousand SIT

The item of purchase cost of goods sold (97 % of total operating expenses) encompasses expenses for the purchase of electricity and related costs.

Costs of goods, materials and services, labour cost, administration and depreciation expenses, as well as other operating expenses represent less than a 3% share among total operating expenses.

The Company did not receive any claims for compensations or damages from its employees that based on legal provisions, the collective agreement or the Company's Articles of Association.

Financial expenses due to impairment and write-offs of investments represent the loss incurred through the sale of TDR - Metalurgija d.d.

Financial expenses for financial liabilities comprise interest paid on loans.

Financial expenses for operating liabilities include exchange losses from cash and operating liabilities.

EXPENSES

EXPENSES	2006	2005
		in 000 SIT
Operating expenses	176,190,291	139,085,654
Financial expenses	1,837,402	521,609
Other expenses	6	2
Total	178,027,699	139,607,265

OPERATING EXPENSES

OPERATING EXPENSES		*in 000 SIT*
	2006	**2005**
Purchase cost of goods sold	168,413,110	134,507,131
Direct costs of goods sold	2,637,736	2,109,811
Cost of material	56,664	41,942
Cost of services	1,126,091	747,824
Labour cost	1,204,319	1,083,304
Cost of amortisation / depreciation	354,071	207,276
Revaluation operating expenses	4,029	5,051
Other operating expenses	2,394,271	383,315
Total	176,190,291	139,085,654

Costs in terms of function

COSTS IN TERMS OF THEIR FUNCTION

		in 000 SIT
	2006	**2005**
Purchase cost of goods sold or production cost of quantities sold	173,315,354	136,885,285
Selling expenses	425,219	366,075
General administrative costs	2,411,921	1,797,885

Profit
10,574,656 thousand SIT

The Company concluded the financial year 2006 with a profit of 10,574,656 thousand SIT.

Net profit for the period
8,651,076 thousand SIT

Profit after current and deferred tax, representing the net profit for the period, was recorded in the amount of 8,651,076 thousand SIT.

Corporate income tax
2,365,858 thousand SIT

In accordance with provisions of the Corporate Income Tax Act, the Company's profit is taxed at 25% of the taxable base reported in the Company's tax return.

In 2006 the Company recorded 2.365.858 thousand SIT of liabilities for payment of corporate income tax.

Deferred taxes
442,278 thousand SIT

As at year-end, deferred tax assets amounted to 442,278 thousand SIT on account of the expenses qualifying for tax deduction which will be claimed in the future financial years, arising from:

- the formed provisions;
- the amortisation/depreciation has exceeded the capital allowance rates qualifying for tax deduction, and
- impairments of intangible assets.

The Company did not account for deferred tax liabilities in the reporting period.

OPERATING RESULT OF THE COMPANY

in 000 SIT

	2006	2005
Gross operating yield	188,232,564	146,107,927
Operating profit	12,042,273	7,022,273
Profit from ordinary activities	10,573,793	6,942,268
Profit from other activities	863	91,898
Total operating profit	10,574,656	7,034,166
Net profit for the period	8,651,076	7,034,166

4.8.3 CASH FLOW STATEMENT

General

The cash flow statement reveals changes in the balance of cash and cash equivalents over the financial year.

The item of cash comprises bank balances and call deposits.

The cash flow statement is prepared by using the indirect method (Format II - SAS 26.9).

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the cash flow statement for 2005 are recorded according to SAS (2001) and presented in items of the cash flow statement under SAS (2006).

In the cash flow for 2005, the funds provided by the venturers for financing the investment in the hydro power plant on the Lower Sava river in the amount of 3,175,023 thousand SIT were recorded as inflows from financing activities, despite the fact that these funds are categorised as long-term operating liabilities. Therefore the item was presented (in the 2005 comparable-data column) under cash flows from operating activities in the cash flow for 2006.

Data in the cash flow statement is obtained from the balance sheets for the current and previous year and the income statement for the current period.

In order for the inflows to be as close as possible to receipts, and outflows as close as possible to expenses, additional eliminations were made in the cash flow statement, as set out below:

- long-term investments: the partial advance payment made in 2005 for the acquisition of shares held by minority shareholders of Termoelektrarna Brestanica d.o.o. and Termoelektrarna Šoštanj d.o.o. in the amount of 5,851,886 thousand SIT;
- revaluation surplus: the cash inflows in association with standardised futures in the amount of 1,384,407 thousand SIT were recorded under inflows from operating activities.

CASH FLOWS

CASH FLOWS		*in 000 SIT*
	2006	**2005**
Cash flows from operating activities	16,370,829	8,447,482
Cash flows from investing activities	-13,484,595	-7,837,023
Cash flows from financing activities	-2,888,749	-366,472
Cash flow for the period	-2,515	243,987

4.8.4 STATEMENT OF CHANGES IN EQUITY

General

The statement of changes in equity encompasses all changes of equity components during the financial year.

The statement of changes in equity is prepared so that all components of equity are presented in form of a spreadsheet (Format I - SAS 27.2).

Pursuant to Note 3 to the Introduction in SAS (2006), the opening balance data are disclosed upon translation as at 1 January 2006, as defined under provisions of Point 15 of the Introduction to the SAS (2006).

The transition to SAS (2006) resulted in a decrease of equity by 17,575,234 thousand SIT, in particular due to:

a) negative impact on retained loss in the amount of 71,145 thousand SIT,
b) elimination of the revaluation surplus referring to long-term financial investments amounting to 17,504.089 thousand SIT.

In addition, the general equity revaluation adjustment has been eliminated in the amount of 27 thousand SIT, as well as the increased capital surplus.

Movements to equity

The Company's equity recorded an increase in the reporting period by 12,881,325 thousand SIT, which is attributable mostly to:

a) net profit for the period amounting to 8,651,076 thousand SIT,
b) revaluation surplus referring to other financial instruments - futures contracts and interest rate swaps (4,230,249 thousand SIT).

Movements within equity

Part of the accumulated profit for 2005 in the amount of 517,083 thousand SIT was allocated among other revenue reserves based on a decision of the shareholders' meeting.

During the preparation of the financial statements for 2006, the net profit for the period was used for the coverage of retained loss in the amount of 71,145 thousand SIT.

Pursuant to a resolution by the Supervisory Board that was adopted upon a proposal by the Company's Managing Director, half of the net profit for 2006 in the amount of 4,289,966 thousand SIT was allocated to other revenue reserves.

Movements from equity

The Company's equity decreased by 5,836,568 thousand SIT in the reporting period, mostly due to:

a) distribution of part of the accumulated profit for 2005 to the founder in the amount of 3,000,000 thousand SIT,
b) revaluation surplus referring to other financial instruments - futures contracts in the amount of 2,836,568 thousand SIT.

Accumulated profit

Accumulated profit of 2006 is recorded at 4,289,965 thousand SIT and represents half of net profit for the period. The shareholders' meeting decides upon the distribution of the accumulated profit.

ACCUMULATED PROFIT

ACCUMULATED PROFIT		*in 000 SIT*
	2006	**2005**
Net profit for the period	8,651,076	7,034,166
Retained earnings or losses	-71,145	0
Reversal of revenue reserves	0	0
Allocation to revenue reserves pursuant to a resolution adopted by the Management (legal reserves, reserves for own shares and statutory reserves)	0	0
Allocation to revenues reserves pursuant to a resolution adopted by the Management and the Supervisory Board (other revenue reserves)	-4,289,966	-3,517,083
Accumulated profit for the period	4,289,965	3,517,083

4.8.5 OTHER DISCLOSURES

Remuneration of Management Board members and other employees with individual employment contracts

Remuneration of members of the Management Boards and other employees with individual contracts of employment include:

a) gross remunerations contained in the notice for income tax returns,
b) other fees,
c) premiums paid for additional pension insurance.

Remuneration of Supervisory Board members

Remuneration of Supervisory Board members represent attendance fees (gross) and travel expenses for carrying out tasks in the Supervisory Board and the audit commission.

In 2006 no advances, loans or guarantees were extended to these groups of persons.

Short-term operating liabilities include December wages and salaries for managers and employees with individual employment contracts, as well as attendance fees for Supervisory Board referring to December.

REMUNERATION OF INDIVIDUAL GROUPS OF PERSONS

GROUPS OF PERSONS		*in 000 SIT*
	2006	**2005**
Management Board members	27,918	98,035
Employees on individual contracts	293,679	269,973
Supervisory Board members	4,481	6,982

Costs of auditing and tax advisory

As for audit and tax advisory services, the Company had following costs (accounted not paid):

a) audit of annual reports of the Company and the Group (4,145 thousand SIT);
b) other audit-related services (33,507 thousand SIT);
c) tax advisory services (4,956 thousand SIT).

KPMG Slovenija d.o.o. as the statutory auditor carried out the audit of annual reports of the Company and the HSE Group, whereas other services were carried out by other audit and tax advisory companies.

Provisions of the Energy Act

With activating the Boštanj hydroelectric power plant in 2006, the Company carries out not only the activity of electric energy trading but also the activity of electric energy production.

Rules by which the Company separates the recording of assets and liabilities, as well as revenues and expenses in aforesaid activities, are following:

- business events and transactions are recorded within the related activity on the day of accrual,
- assets and liabilities are recorded separately for individual activity,
- revenues and expenses are recorded separately for individual activity.

BALANCE SHEET AS AT 31 DECEMBER 2006 BY COMPANY'S ACTIVITIES

ITEM				in 000 SIT
		TRADING	PRODUCTION	TOTAL
	ASSETS	236,265,346	24,297,717	260,563,063
A.	LONG-TERM ASSETS	201,565,840	22,254,986	223,820,826
I.	Intangible assets and long-term deferred costs and accrued revenues	1,356,234	0	1,356,234
1.	Concessions, patents, licences, trademarks and similar rights	1,356,234	0	1,356,234
II.	Property, plant and equipment	1,784,603	22,254,986	24,039,589
1.	Land and buildings	430,976	7,380,829	7,811,805
	b) Buildings	430,976	7,380,829	7,811,805
2.	Manufacturing plant and equipment	0	8,003,473	8,003,473
3.	Other plant and equipment	698,604	29,634	728,238
4.	Property, plant and equipment being acquired	655,023	6,841,050	7,496,073
	a) Property, plant and equipment in course of construction	655,023	5,320,211	5,975,234
	b) Advances for acquisition of property, plant and equipment	0	1,520,839	1,520,839
IV.	Long-term investments	197,934,832	0	197,934,832
1.	Long-term investments excluding loans	197,934,832	0	197,934,832
	a) Shares and interests in group companies	197,777,504	0	197,777,504
	b) Shares and interests in associates	130,328	0	130,328
	c) Other shares and interests	26,600	0	26,600
	d) Other long-term investments	400	0	400
V.	Long-term operating receivables	30,000	0	30,000
3.	Long-term operating receivables due from others	30,000	0	30,000
VI.	Deferred tax assets	460,171	0	460,171
B.	CURRENT ASSETS	34,424,678	2,038,918	36,463,596
II.	Inventories	785	0	785
1.	Material	462	0	462
4.	Advances for inventories	323	0	323
III.	Short-term investments	6,346,307	1,631,000	7,977,307
1.	Short-term investments excluding loans	1,247,698	0	1,247,698
	b) Other shares and interests	1,238,423	0	1,238,423
	c) Other short-term investments	9,275	0	9,275
2.	Short-term loans	5,098,609	1,631,000	6,729,609
	a) Short-term loans to group companies	734,609	0	734,609
	b) Short-term loans to others	4,364,000	1,631,000	5,995,000
IV.	Short-term operating receivables	27,077,230	406,476	27,483,706
1.	Short-term operating receivables due from group companies	460,047	91,450	551,497
2.	Short-term trade receivables	22,330,458	0	22,330,458
3.	Short-term operating receivables due from others	4,286,725	315,026	4,601,751
V.	Cash	1,000,356	1,442	1,001,798
C.	DEFERRED COSTS AND ACCRUED REVENUES	274,828	3,813	278,641
	OFF BALANCE SHEET ASSETS	45,538,565	7,253,452	52,792,017

Balance sheet as at 31 December 2006 by Company's activities (continuation)

ITEM				in 000 SIT
		TRADING	PRODUCTION	TOTAL
	LIABILITIES	**236,265,346**	**24,297,717**	**260,563,063**
A.	**EQUITY**	**191,442,226**	**11,484,403**	**202,926,629**
I.	Called-up capital	1,156,217	0	1,156,217
1.	Share capital	1,156,217	0	1,156,217
II.	Capital surplus	154,599,339	11,471,162	
III.	Revenue reserves	29,514,702	0	29,514,702
5.	Other revenue reserves	29,514,702	0	29,514,702
IV.	Revaluation surplus	1,895,244	0	1,895,244
V.	Retained profit	0	0	0
VI.	Net profit for the period	4,276,724	13,241	4,289,965
B.	**PROVISIONS AND LONG-TERM ACCRUED COSTS AND DEFERRED REVENUES**	**1,677,170**	**0**	**1,677,170**
1.	Provisions for pensions and similar liabilities	95,546	0	95,546
2.	Other provisions	1,581,624	0	1,581,624
C.	**LONG-TERM LIABILITIES**	**12,221,092**	**10,853,369**	**23,074,461**
I.	Long-term financial liabilities	12,221,092	0	12,221,092
2.	Long-term financial liabilities to banks	12,221,092	0	12,221,092
II.	Long-term operating liabilities	0	10,853,369	10,853,369
1.	Long-term operating liabilities to group companies	0	10,770,512	10,770,512
2.	Long-term trade payables	0	82,857	82,857
D.	**SHORT-TERM LIABILITIES**	**30,544,115**	**1,749,504**	**32,293,619**
II.	Short-term financial liabilities	1,174,629	0	1,174,629
2.	Short-term financial liabilities to banks	1,174,629	0	1,174,629
III.	Short-term operating liabilities	29,369,486	1,749,504	31,118,990
1.	Short-term operating liabilities to group companies	12,797,395	71,866	12,869,261
2.	Short-term trade payables	13,877,266	1,675,700	15,552,966
4.	Short-term operating liabilities from advances	0	36	36
5.	Other short-term operating liabilities	2,694,825	1,902	2,696,727
E.	**SHORT-TERM ACCRUED COSTS AND DEFERRED REVENUES**	**380,743**	**210,441**	**591,184**
	OFF BALANCE SHEET LIABILITIES	**45,538,565**	**7,253,452**	**52,792,017**

INCOME STATEMENT FOR 2006 BY COMPANY'S ACTIVITIES

ITEM				*in 000 SIT*
		TRADING	*PRODUCTION*	*TOTAL*
1.	Net sales	187,998,958	192,417	188,191,375
a)	Domestic market	133,402,541	192,417	133,594,958
b)	Foreign market	54,596,417	0	54,596,417
3.	Capitalised own products and/or services	37,797	0	37,797
4.	Other operating revenues (inclusive of revaluation operating revenues)	3,392	0	3,392
GROSS OPERATING YIELD		*188,040,147*	*192,417*	*188,232,564*
5.	Costs of goods, materials and services	172,180,953	52,648	172,233,601
a)	Cost of goods and materials sold and cost of materials used	171,106,544	966	171,107,510
b)	Cost of services	1,074,409	51,682	1,126,091
6.	Labour costs	1,204,319	0	1,204,319
a)	Payroll costs	831,592	0	831,592
b)	Social security costs	174,740	0	174,740
	- of which for pension insurance costs	110,578	0	110,578
c)	Other labour costs	197,987	0	197,987
7.	Write-downs in value	245,725	112,375	358,100
a)	Depreciation and amortisation expense	241,696	112,375	354,071
b)	Revaluation operating expenses associated with intangible assets and property, plant and equipment	3,690	0	3,690
c)	Revaluation operating expenses associated with current assets	339	0	339
8.	Other operating expenses	2,365,000	29,271	2,394,271
TOTAL OPERATING EXPENSES		*175,995,997*	*194,294*	*176,190,291*
OPERATING PROFIT OR LOSS		*12,044,150*	*-1,877*	*12,042,273*
9.	Financial revenue from shares	35,737	0	35,737
c)	Financial revenues from shares and interests in other companies	35,737	0	35,737
10.	Financial revenue from loans	224,530	15,118	239,648
a)	Financial revenue from loans to group companies	2,050	0	2,050
b)	Financial revenue from loans to others	222,480	15,118	237,598
11.	Financial revenue from operating receivables	93,537	0	93,537
a)	Financial revenue from operating receivables due from group companies	2	0	2
b)	Financial revenue from operating receivables due from others	93,535	0	93,535
TOTAL FINANCIAL REVENUES		*353,804*	*15,118*	*368,922*
12.	Financial expenses due to impairment and write-offs of investments	1,123,099	0	1,123,099
13.	Financial expenses for financial liabilities	672,087	0	672,087
a)	Financial expenses for loans received from group companies	114	0	114
b)	Financial expenses for loans received from banks	671,973	0	671,973

Income statement for 2006 by Company's activities (continuation)				
14.	Financial expenses for operating liabilities	42,216	0	42,216
a)	Financial expenses for operating liabilities due to group companies	39	0	39
b)	Financial expenses for trade payables and bills payable	4,010	0	4,010
c)	Financial expenses for other operating liabilities	38,167	0	38,167
TOTAL FINANCIAL EXPENSES		***1,837,402***	***0***	***1,837,402***
PROFIT FROM ORDINARY ACTIVITIES		***10,560,552***	***13,241***	***10,573,793***
15.	Other revenues	869	0	869
16.	Other expenses	6	0	6
PROFIT FROM EXTRAORDINARY ACTIVITIES		***863***	***0***	***863***
TOTAL OPERATING PROFIT		***10,561,415***	***13,241***	***10,574,656***
17.	Income tax	2,365,858	0	2,365,858
18.	Deferred taxes	-442,278	0	-442,278
19.	NET PROFIT FOR THE PERIOD	8,637,835	13,241	8,651,076

Partial division by acquisition

Long-term investments in the companies Savske elektrarne Ljubljana and Termoelektrarna Brestanica d.o.o. were included in the group of assets transferred to GEN energija as the acquiring company in the procedure of partial division by acquisition as at 31 December. Accordingly, the shareholders' equity was accounted for in the corresponding amount.

Balance sheet upon partial division

ITEM		***in 000 SIT***
		31 Dec 06
	ASSETS	***34,574,748***
A.	***LONG-TERM ASSETS***	***34,574,748***
IV.	Long-term investments	34,574,748
1.	Long-term investments excluding loans	34,574,748
	a) Shares and interests in group companies	34,574,748
LIABILITIES		***34,574,748***
A.	***EQUITY***	***31,574,185***
II.	Capital surplus	31,574,185
C.	***LONG-TERM LIABILITIES***	***2,824,059***
I.	Long-term financial liabilities	2,824,059
2.	Long-term financial liabilities to banks	2,824,059
D.	***SHORT-TERM LIABILITIES***	***176,504***
II.	Short-term financial liabilities	176,504
2.	Short-term financial liabilities to banks	176,504

4.9 ACCOUNTING RATIOS OF THE CONTROLLING COMPANY IN 000 SIT

Financial ratios of the Company for 2006 and 2005 are presented below[8].

EQUITY FINANCING RATE

	31 Dec 2006	1 Jan 2006
1. Liabilities	260,563,063	239,420,036
2. Equity	202,926,629	195,881,872
Equity financing rate = 2 / 1	77.88	81.82

In 2006 the Company financed its operations through own funds, as Company's equity has a 78 % share among total liabilities. Compared to the balance as at 1 January 2006, the equity financing rate decreased during the year due to the increase in operating liabilities, in particular liabilities due to venturers in association with the joint venture, and corporate income tax payables.

LONG-TERM FINANCING RATE

	31 Dec 2006	1 Jan 2006
1. Equity	202,926,629	195,881,872
2. Long-term liabilities	23,074,461	10,569,618
3. Provisions and long-term accrued expenses and deferred revenue	1,677,170	4,377,913
4. Total (1 + 2 + 3)	227,678,260	210,829,403
5. Liabilities	260,563,063	239,420,036
Long-term financing rate = 4 / 5	87.38	88.06

Out of Company's total liabilities 87 % are long-term and 13 % short-term. Compared to the balance as at 1 January 2006, the long-term financing rate has dropped by 0.7 percentage points, which mostly results from the increase in short-term trade payables.

OPERATING FIXED ASSETS RATE

	31 Dec 2006	1 Jan 2006
1. Property, plant and equipment	24,039,589	17,755,531
2. Intangible assets and long-term deferred costs and accrued revenue	1,356,234	471,925
3. Total long-term assets at carrying amount (1 + 2)	25,395,823	18,227,456
4. Assets	260,563,063	239,420,036
Operating fixed assets rate = 3 / 4	9.75	7.61

In 2006, property, plant and equipment and intangible assets and long-term deferred costs and accrued revenue accounted for 10 % of the total assets, which is understandable as most of the assets are long-term investments. Compared to 1 January 2006, operating fixed assets rate increased by 28 %, which is mostly due to new investments in the power plant on the Lower Sava river.

[8]Due to the transition to SAS (2006), the ratios for 2006 referring to the Balance Sheet were compared to the balances as at 1 January 2006.

LONG-TERM ASSETS RATE

	31 Dec 2006	1 Jan 2006
1. Property, plant and equipment	24,039,589	17,755,531
2. Intangible assets and long-term deferred costs and accrued revenue	1,356,234	471,925
3. Investment property	0	0
4. Long-term investments	197,934,832	187,158,569
5. Long-term operating receivables	30,000	30,000
6. Total (1 + 2 + 3 + 4 + 5)	223,360,655	205,416,025
7. Assets	260,563,063	239,420,036
Long-term assets rate = 6 / 7	85.72	85.80

Long-term assets rate refers to the share of long-term assets among total assets. In 2006, the ratio was established at 86 % of the total assets, the difference referred to current assets and deferred costs and accrued revenue. The long-term assets rate has remained nearly unchanged as at the year-end if compared to the balance as at 1 January 2006.

EQUITY TO OPERATING FIXED ASSETS

	31 Dec 2006	1 Jan 2006
1. Equity	202,926,629	195,881,872
2. Property, plant and equipment	24,039,589	17,755,531
3. Intangible assets and long-term deferred costs and accrued revenue	1,356,234	471,925
4. Total fixed assets at carrying amount (2 + 3)	25,395,823	18,227,456
Equity to operating fixed assets = 1/4	7.99	10.75

The ratio for 2006 shows that again, most of the Company's long-term assets and part of the operating current assets is financed by means of the owner's equity. The ratio was determined at 8, showing a decrease of 26 % compared to 1 January 2006, as due to investments the operating fixed assets increased far more than the equity.

IMMEDIATE SOLVENCY RATIO

	31 Dec 2006	1 Jan 2006
1. Cash	1,001,798	1,004,313
2. Short-term investments	7,977,307	7,487,134
3. Total liquid assets (1 + 2)	8,979,105	8,491,447
4. Short-term liabilities	32,293,619	28,227,123
Immediate solvency ratio = 3 / 4	0.28	0.30

The immediate solvency ratio is the relation between operating current assets and short-term liabilities. Although the ratio was set at 0.3 the Company has no solvency problems.

QUICK RATIO

	31 Dec 2006	1 Jan 2006
1. Cash	1,001,798	1,004,313
2. Short-term investments	7,977,307	7,487,134
3. Short-term receivables	27,483,706	25,436,281
4. Total (1 + 2 + 3)	36,462,811	33,927,728
5. Short-term liabilities	32,293,619	28,227,123
Quick ratio = 4 / 5	1.13	1.20

The quick ratio shows whether the Company finances short-term assets through short-term liabilities or also long-term. The ratio's value is higher by more than 1 % in 2006, indicating that part of short-term assets are financed by means of long-term liabilities. The ratio shows a decrease of 6 % over the figures recorded as at 1 January 2006, which is mostly due to higher short-term operating liabilities.

CURRENT RATIO

	31 Dec 2006	1 Jan 2006
1. Current assets	36,463,596	33,928,461
2. Short-term deferred costs and accrued revenue	278,641	57,657
3. Total (1 + 2)	36,742,237	33,986,118
4. Short-term liabilities	32,293,619	28,227,123
Current ratio = 3 / 4	1.14	1.20

The current ratio reflects the financing of short-term assets by means of short-term liabilities. Although the current ratio decreased by 1.1 percentage points in 2006, the Company records good solvency, as nearly all short-term assets are financed by short-term liabilities.

OPERATING EFFICIENCY RATE

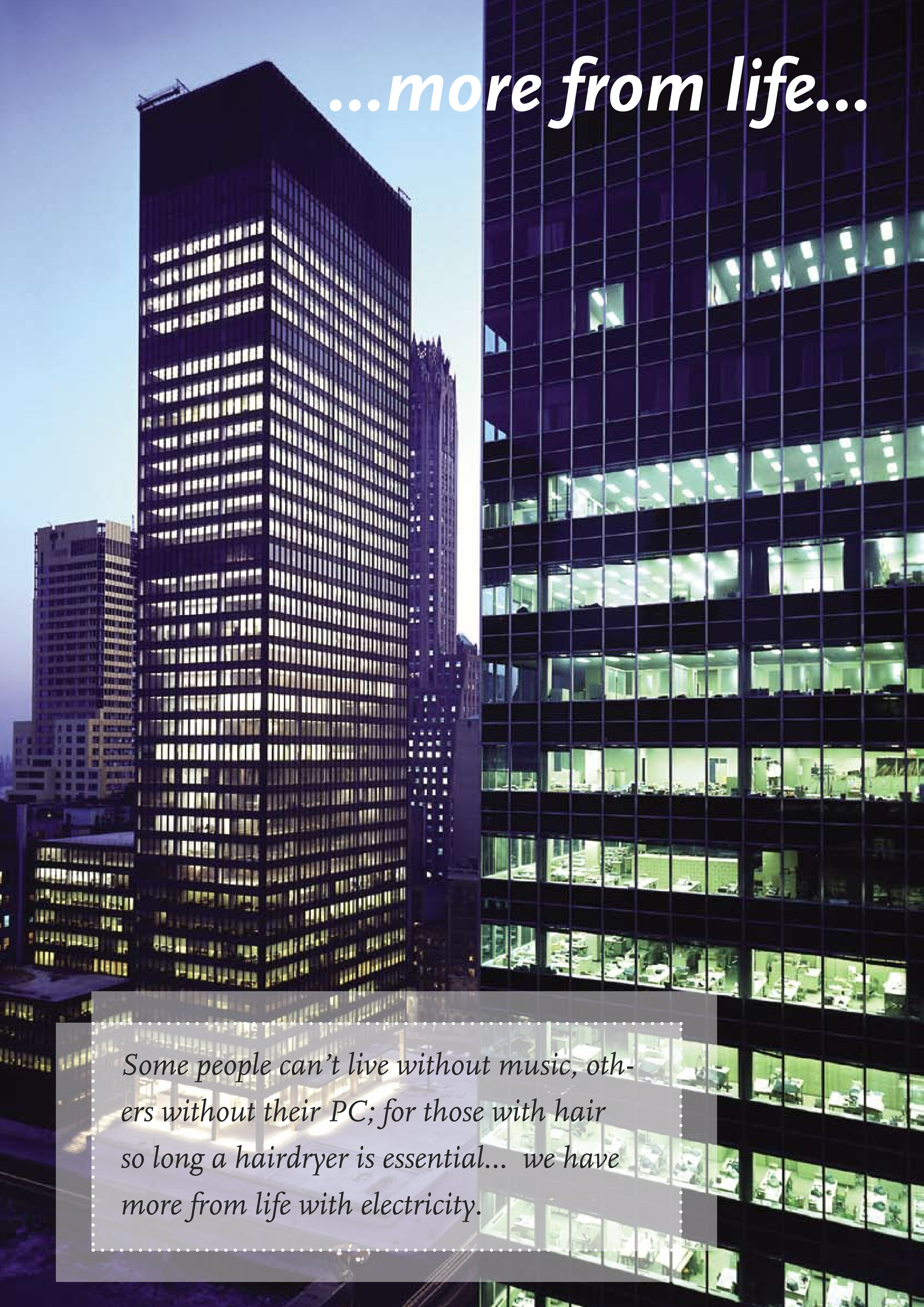
	2006	2005
1. Operating revenues	188,232,564	146,107,927
2. Costs of goods, materials and services	172,233,601	137,406,708
3. Labour costs	1,204,319	1,083,304
4. Write-downs in value	358,100	212,327
5. Other operating expenses	2,394,271	383,315
6. Total operating expenses (2 + 3 + 4 + 5)	176,190,291	139,085,654
Operating efficiency rate = 1 / 6	1.07	1.05

Operating revenues exceed operating expenses by 7 % in the reporting year. Compared to 2005, the operating efficiency rate increased by 2 %.

NET RETURN ON EQUITY RATIO

	2006	2005
1. Net profit for the period	8,651,076	7,034,166
2. Average capital	199,404,251	209,038,556
Net return on equity = 1 / 2	0.043	0.034

The net-return-on-equity ratio (ROE) indicates that the Company generated 4.3 SIT of net profit on 100 SIT of funded capital. Compared to 2005 the ratio increased by 29 %. Taking into account the Company's capital intensiveness the ratio's value is deemed as favourable.



...more from life...

Some people can't live without music, others without their PC; for those with hair so long a hairdryer is essential... we have more from life with electricity.

5

Financial Statements of the HSE Group

2006

5.1 GENERAL NOTES

Basis

Consolidated financial statements for 2006 have been prepared in accordance with provisions of the Companies Act (hereafter ZGD-1) and the Slovenian Accounting Standards 2006 (hereafter SAS 2006).

Financial statements have been prepared using the Slovene tolar (SIT) as the unit of currency, rounded to the nearest thousand.

A group of companies is an economic, yet not a legal entity, and as such not an independent holder of rights and liability. The consolidated financial statements are the financial statements of a group presented as those of a single company. The consolidated financial statements are prepared on the basis of the primary financial statements of the consolidated company, including the relevant consolidation adjustments (eliminations).

During the preparation of consolidated financial statements following qualitative characteristics have been taken into account:
- understandability,
- relevance,
- reliability and
- comparability.

Companies included in the consolidated financial statements

Prior to the consolidation of the HSE Group, the process of consolidation was applied for PV and TDR - Metalurgija. In accordance with consecutive methodology, consolidated financial statements are initially prepared by subsidiaries, and such statements are thereupon included in consolidated financial statements of the HSE Group.

The 2006 consolidated financial statements include also companies HSE Balkan Energy, HSE Hungary and HSE Adria as they have been founded in the respective financial year.

TDR - Metalurgija group is included in the consolidated financial statements for the last time as the Company HSE has sold its share in TDR - Metalurgija in December 2006. Hence, assets and liabilities of TDR - Metalurgija are recorded in the balance sheet only as at 1 January 2006 and no longer as at 31 December. Notwithstanding, TDR - Metalurgija is included in the consolidated income statement and the consolidated cash flow statement for 2006.

VALUE OF ELIMINATED ASSETS AND LIABILITIES OF SKUPINE TDR - Metalurgija GROUP

ITEM	*in 000 SIT*
	1 Jan 2006
Intangible assets and long-term deferred costs and accrued revenues	21,350
Property, plant and equipment	3,423,380
Inventories	1,376,079
Short-term investments	3,250
Short-term operating receivables	1,172,716
Cash	9,507
Deferred costs and accrued revenues	4,869
Provisions and accrued costs and deferred revenues	258,053
Long-term financial liabiliities	534,493
Long-term operating liabilities	21,992
Short-term financial liabilities	556,101
Short-term operating liabilities	877,703
Short-term accrued costs and deferred revenues	27,159
Off balance sheet items	1,234,373

COMPANIES INCLUDED IN THE CONSOLIDATED FINANCIAL STATEMENTS

Holding Slovenske elektrarne d.o.o.
Dravske elektrarne Maribor d.o.o.
Savske elektrarne Ljubljana d.o.o.
Soške elektrarne Nova Gorica d.o.o.
Termoelektrarna Brestanica d.o.o.
Termoelektrarna Šoštanj d.o.o.
Skupina Premogovnik Velenje
Skupina TDR - Metalurgija
HSE Invest d.o.o.
HSE Italia S.r.l.
HSE Balkan Energy d.o.o.
HSE Hungary Kft.
HSE Adria d.o.o.

Hereinafter the term »Group« refers to companies of the HSE Group that are listed above and included in the consolidated financial statements.

The financial year is considered the calendar year.

Companies excluded from the consolidated financial statements

The companies Sava and Elprom, in which Savske Elektrarne Ljubljana (SEL) and Soške Elektrarne Nova Gorica (SENG) hold a majority interest, are inactive and consequently not included in the consolidation on the level neither of controlling companies nor on the level of the Group. These two companies are not deemed to have a significant impact on the true and fair presentation of the Group's operations.

Dravske Elektrarne Maribor (DEM) has a 50% share in the company Eldom and irrespectively did not carry out the consolidation due to material insignificance. DEM has no controlling influence over the operations of Eldom.

Complete consolidation

The financial statements of individual Group companies have been incorporated into the consolidated financial statements on the basis of complete consolidation, which means that amounts are aggregated item by item, with related items of assets, liabilities, capital, revenues and expenses each represented as a cumulative sum. The following have also been eliminated in order that the Group is presented as if it were a single enterprise:

- controlling company's investments in subsidiaries and related controlling company's interests in equity of subsidiaries,
- investments and liabilities of Group companies,
- subsidiaries' intangible assets and long-term liabilities of the controlling company,
- intragroup receivables and liabilities,
- intragroup revenues and expenses.

The consolidated income statement encompasses the share of minority interests in the Group's operating profit or loss, while both the consolidated balance sheet as well as the consolidated statement of changes in equity, and equally present minority interests in the equity of the HSE Group.

Audit

Companies included in the consolidated financial statements have been audited, whereas for subsidiaries abroad the limited review procedures have been applied. The audit or limited reviews were for all respective companies carried out by KPMG Slovenija d.o.o., and all were issued an unqualified review.

Accounting policies

Accounting policies as well as the valuation rules were adjusted among the companies during the preparation of consolidated financial statements.

The valuation methods applied by the Group companies have not changed in 2006.

Transition to SAS (2006)

Group companies have prepared the financial statements in accordance with SAS (2006), whereas the same standards were applied also for the consolidated financial statements.

Exchange rate and method of translation into domestic currency

Items in financial statements of individual Group companies that are denominated in foreign currencies are translated into local currency in the balance sheet and the income statement on the day of accrual, using the middle exchange rate of the Bank of Slovenia.

The balances of assets and liabilities in the balance sheets of individual Group companies expressed in a foreign currency have been translated at the middle exchange rate of the Bank of Slovenia as at 31 December 2006.

Exchange differences are recorded among financial revenues or financial expenses.

As for translating the financial statements of subsidiaries headquartered abroad for inclusion in the consolidated financial statements, following shall be applied:

- assets and liabilities are translated by applying the middle exchange rate of the Bank of Slovenia as of the balance sheet date,
- revenues and expenses are translated at the average middle exchange rate of the Bank of Slovenia for 2006 or for the period when the company was active (from establishment till the end of 2006),
- exchange differences are classified as a separate equity component - consolidated equity adjustments.

Intangible assets and long-term deferred costs and accrued revenues

Intangible assets are long-term assets enabling the performance of the Company's registered activities, whereas physically they do not exist.

Upon initial recognition intangible assets are valued at cost, which is inclusive of import and other non-refundable duties and costs that occur while preparing the asset for its intended use.

After recognition, intangible assets are carried at cost.

An item of intangible assets is amortised using the straight-line amortisation method (single-asset amortisation). Amortisation shall begin when the intangible asset is available for use.

In the bookkeeping records the cost as well as the accumulated depreciation is recorded separately for items of intangible assets, whereas in the balance sheet they are recorded at carrying amount i.e. as a difference between the cost and accumulated depreciation.

Long-term deferred costs and accrued revenues are initially recorded at cost and later written-off within the attributable costs.

Property, plant and equipment

Property, plant and equipment are long-term assets owned by the Group company and used for the performance of the registered activities.

An item of property, plant and equipment is initially recognised at cost comprising its purchase price, import duties and non-refundable purchase taxes, as well as directly attributable costs of bringing the asset to working condition for its intended use, in particular costs of transportation and installation. In one of the Group companies the purchase cost is increased by the amount of loan interest referring to the acquisition of an item of property, plant and equipment up till the date, when the asset was introduced for carrying out the activity.

Individual items of property, plant and equipment of great value with different useful lives are stated and accounted for separately at cost.

The cost does not include the costs incurred upon the dismantling and removing the items of property, plant and equipment.

Spare parts of higher value are accounted for under property, plant and equipment and depreciated over the useful life of the related asset.

The anticipated costs of regular inspections and repairs of property, plant and equipment are considered as parts of property, plant and equipment.

The cost model is applied for measurement of items of property, plant and equipment after initial recognition.

Grants and state aid provided in the acquisition of property, plant and equipment are not deducted from their cost but are instead included in the long-term accrued costs and deferred revenues and utilised in accordance with the accounted depreciation.

Property, plant and equipment intended for sale in the coming 12 months are recorded among short-term assets available for sale.

Subsequent expenditure on an item of property, plant and equipment increases its cost when it increases its future economic benefits in excess of the originally assessed future economic benefits. The subsequent expenditure enabling extension of the useful life of the asset initially reduces the accumulated depreciation.

Expenditure on repairs or maintenance of property, plant and equipment is made to restore or maintain the future economic benefits that an enterprise can expect from the originally assessed standard of performance of the asset. As such, it is usually recognised as an expense when incurred.

The difference between the net disposal proceeds and the carrying amount of an item of property, plant and equipment disposed of shall be recognised as revaluation operating revenue if the net disposal proceeds exceed the carrying amount, or as operating expenses if the carrying amount exceeds the net disposal proceeds.

An item of property, plant and equipment is depreciated using the straight-line depreciation method (single-asset amortisation). The depreciation of an item of property, plant and equipment begins on the first day of the following month after it has been available for use. Depreciation accounted for in the current year is recorded as operating expense of this financial year.

In the bookkeeping records the cost as well as the accumulated depreciation is recorded separately for items of property, plant and equipment, whereas in the balance sheet they are recorded at carrying amount i.e. as a difference between the cost and accumulated depreciation.

Long-term investments

Long-term investments are part of fixed assets that are made to earn returns and thus increase financial revenues. Group companies own them for more than a year.

Upon initial recognition, long-term investments are recorded at their initial cost, increased by the costs attributable directly to the investment.

Upon their recognition in the books of account, long-term investments are stated at their settlement date (payment date). After initial recognition, investments are carried at cost.

Group companies disclose long-term investments within the group of investments available for sale.

Deferred tax assets

Deferred tax assets represent the amount of accounted income tax from deducted temporary differences between operating expenses and deductible expenses for 2006.

Assets (disposal groups) held for sale

Assets (disposals groups) held for sale include assets for which we may reasonably believe that their carrying amount shall be settled with the sale of these assets in the next year and not by their further use.

Inventories

Inventories are part of current operating assets that shall be used while making products, rendering services or during their sale. Inventories comprise quantities held in store, in the process of completion and modification.

Group's inventories include also material, which includes also low-value assets with a useful life of 1 year and the value of not more than 500 EUR, products, work in progress and advances for inventories.

Material is initially recognised at cost comprising the purchase price, import duties and other non-refundable purchase taxes, and direct costs of purchase.

Inventories are revalued if the carrying amount exceeds their net realisable value. In such case, inventories are impaired whereas the value of impairment increases revaluation operating expenses in current assets.

Receivables

Receivables are the rights to claim the settlement of a debt, the payment for deliveries or rendered services and are part of the Group's current assets. Receivables are classified into long-term (due in more than 1 year) and short-term (due in less than 1 year).

An item of receivables should be recognised as an asset if it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise and if the cost of the asset can be measured reliably. Initially receivables of all categories are carried at amounts recorded in the relevant bookkeeping documents under the assumption that the amounts owed will also be collected.

In the consolidated financial statements advances paid are recorded under assets for which they were provided.

Allowances for receivables are formed if receivables are not repaid within a reasonable time; these allowances are recorded in the income statement and increase the revaluation operating expenses. Receivables are written-off when all legal remedies relating to their repayment are used.

Long-term receivables due in less than a year after the balance sheet date are recorded among short-term receivables.

Short-term investments

Short-term investments are that part of the Group's operating assets that in less than 1 year generate profits, which increase financial revenues.

Upon initial recognition, investments are recorded at their initial cost, increased by the costs attributable directly to the investment.

Upon their recognition in the books of account of Group companies, short-term investments are stated at their settlement date (payment date). After initial recognition, investments are carried at cost.

Group companies disclose short-term investments within the group of investments available for sale.

Short-term investments include also derivatives i.e. fair value of interest rate swaps, whereas interest on long-term loans is considered as a hedged item.

Short-term investments include also long-term investments that are due within the year after the balance sheet date.

Cash

Cash includes deposit money, i.e. cash deposited in accounts with a bank or another financial institution that can be used for payment purposes.

Short-term deferred costs and accrued revenues

Short-term deferred costs and accrued revenue include short-term deferred costs or short-term deferred expenses as well as short-term accrued revenue.

Short-term deferred costs or short-term deferred expenses are amounts incurred but not yet charged against the activities of the Group companies. Short-term accrued revenues are amounts included among revenues during the preparation of financial statements but not yet changed by Group companies.

Equity

Total equity is defined by the amounts invested by owners and the amounts generated during operation that belong to the owners.

Provisions and Long-term deferred costs and accrued revenues

Provisions are formed for obligations expected to arise from obligating past events in a period exceeding one year and whose amounts can reliably be estimated. They are formed when the obligation can reliably be measured.

Long-term deferred costs and accrued revenues comprise deferred revenue expected to cover estimated expenses in a period of more than one year. They also include government grants and donations for the acquisitions of property, plant and equipment, provided to cover the depreciation costs e.g. they are used up by recognising them as operating revenue.

Long-term liabilities

Long-term liabilities are recognised obligations associated with the financing of the Group companies' assets; they are classified as financial and operating liabilities. Long-term financial liabilities refer to liabilities due by lenders and trade payables to liabilities due by suppliers. Long-term liabilities refer to liabilities of the Group companies whose settlement is expected in a period of more than a year.

Upon initial recognition long-term liabilities are recorded at amounts paid and at a later stage decreased on the basis of repayments made. They are measured at cost.

Part of long-term liabilities that is due in less than 1 year after the balance sheet date, is recorded among short-term liabilities.

Short-term liabilities

Short-term liabilities are obligations that must be settled within a year. The Group records short-term financial and operating liabilities.

Short-term financial liabilities refer to liabilities due by lenders and short-term operating liabilities to trade payables.

Upon initial recognition short-term liabilities are recorded at amounts paid and at a later stage decreased on the basis of repayments made. They are measured at cost.

Short-term operating liabilities are initially valued on the basis of relevant documents that evidence the receipt of goods or service.

Part of long-term liabilities that is due in less than 1 year after the balance sheet date, is recorded among short-term liabilities.

Accrued costs and deferred revenues

Accrued cost and deferred revenue comprise short-term accrued costs and short-term deferred revenues.

Short-term accrued costs include costs that are recorded but have not yet occurred (not yet charged) although they refer to the period for which the financial statements have been prepared.

Short-term deferred revenues represent services already charged for but not yet rendered.

Revenues

Revenues are increases in economic benefits during the accounting period in form of increases of assets. They are recognised when it is probable that cash receipts will flow from them.

Operating revenues are sales revenues and other operating revenues associated with products and services.

Net sales include revenues generated from the sale of products or merchandise, material and services rendered during the accounting period. They should be recognised at selling prices stated in invoices or other documents, less discounts and rebates.

Changes in the value of inventories are the difference between the opening and closing balance of inventories.

Capitalised own services are products or services provided by the Group and recorded under intangible assets or property, plant and equipment.

Revaluation operating revenues are revenues recognised upon the disposal of property, plant and equipment and intangible assets, if their carrying amount is lower than selling price, as well as upon the elimination of impairment of trade receivables.

Financial revenues are revenues from investments that occur in connection with long-term and short-term investments, as well as long-term and short-term receivables. They include interest accounted, shares in profits of others and financial revenues from revaluation. They are recognised upon statements of accounts, irrespective of actual income associated with them.

Operating revenues from revaluation include profits on disposal of investments, taking into account the possible previous equity revaluation adjustment referring to the strengthening of these assets.

Other revenues comprise extraordinary items. They are recorded in actual amounts.

Expenses

Expenses are decreases in economic benefits during the accounting period in the form of decreases in assets or increases in liabilities. Expenses shall be recognised if decreases in economic benefits during the accounting period are associated with decreases in assets or increases in liabilities and such decreases can be measured reliably.

Operating expenses are equal to the calculated cost of the accounting period, increased by the cost held in the opening inventories of products and work in progress, and reduced by the cost held in the closing inventories of products and work in progress. Operating expenses include also the cost of goods sold. Operating expenses shall be recognised once costs are no longer held in inventories of products and work in progress or once merchandise has been sold.

Operating expenses comprise the purchase cost of goods sold, material costs, cost of services, labour cost and depreciation.

Revaluation operating expenses arise from the impairment of property, plant and equipment, intangible assets, inventories and operating receivables. They are recorded also in case of sale of aforesaid assets if the carrying amount exceeds the selling amount.

Financial expenses are arising on financing and investing. They include interest accounted and revaluation financial expenses. They are recognised upon statements of accounts, irrespective of actual payments associated with them.

Financial expenses include also exchange losses from receivables, investments and liabilities.

Revaluation financial expenses include losses on disposal of investments.

Other expenses include expenses that are neither operating nor financial. They are recorded at actual amounts.

5.2 AUDITOR'S REPORT

KPMG

Independent Auditor's Report

To the Shareholders of Holding Slovenske elektrarne d.o.o.

We have audited the accompanying consolidated financial statements of the Holding Slovenske elektrarne Group which comprise the consolidated balance sheet as at 31 December 2006, the consolidated income statement, the consolidated statement of changes in equity, the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

We also read the Management Report.

Management's responsibility for the financial statements

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

Auditor's responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Holding Slovenske elektrarne Group as at 31 December 2006, the result of its operations and its cash flows for the year then ended in accordance with the Slovenian Accounting Standards.

The Management Report is in conformity with the audited consolidated financial statements.

KPMG SLOVENIJA,
podjetje za revidiranje, d.o.o.

Marjan Mahnič, B.Sc.Ec.
Certified Auditor
Partner

Ljubljana, 30th March 2007

KPMG Slovenija, d.o.o.
1

5.3 CONSOLIDATED BALANCE SHEET

CONSOLIDATED BALANCE SHEET

ITEM		Note	31 Dec 2006	1 Jan 2006	31 Dec 2005
					in 000 SIT
	ASSETS		373,441,091	361,901,211	357,853,560
A.	***LONG-TERM ASSETS***		***301,919,231***	***294,665,481***	***294,595,506***
I.	Intangible assets and long-term deferred costs and accrued revenues	1	5,159,220	1,726,456	1,728,315
1.	Concessions, patents, licences, trademarks and similar rights		1,914,599	949,308	949,010
2.	Goodwill		2,475,000	0	0
4.	Long-term deferred development costs		158,995	124,432	124,432
5.	Other long-term deferred costs and accrued revenues		610,626	652,716	654,873
II.	Property, plant and equipment	2	293,328,048	289,777,092	290,431,512
1.	Land and buildings		144,956,471	139,585,249	140,426,111
	a) Land		10,934,069	11,585,258	11,585,258
	b) Buildings		134,022,402	127,999,991	128,840,853
2.	Manufacturing plant and equipment		119,812,185	118,658,892	118,658,892
3.	Other plant and equipment		2,136,695	1,889,817	1,889,817
4.	Property, plant and equipment being acquired		26,422,697	29,643,134	29,456,692
	a) Advances for acquisition of property, plant and equipment		21,015,194	26,389,786	26,389,786
	b) Property, plant and equipment in course of construction		5,407,503	3,253,348	3,066,906
IV.	Long-term investments	3	1,349,323	1,295,510	1,295,507
1.	Long-term investments excluding loans		1,241,863	1,166,504	1,166,501
	a) Shares and interests in group companies		6,038	6,038	6,038
	b) Shares and interests in associates		132,482	11,674	11,671
	c) Other shares and interests		548,860	677,584	677,584
	d) Other long-term investments		554,483	471,208	471,208
2.	Long-term loans		107,460	129,006	129,006
	b) Long-term loans to others		107,460	129,006	129,006
V.	Long-term operating receivables	6	937,281	1,140,173	1,140,172
2.	Long-term trade receivables		736,083	827,871	827,871
3.	Long-term operating receivables due from others		201,198	312,302	312,301
VI.	Deferred tax assets	4	1,145,359	726,250	0
B.	***CURRENT ASSETS***		***70,511,041***	***66,873,724***	***62,896,048***
I.	Assets (disposal groups) held for sale		50,458	4,084,464	107,338
II.	Inventories	5	7,058,011	8,367,982	8,367,978
1.	Material		4,774,340	5,054,112	5,054,112
2.	Work in progress		1,473	427,477	427,477
3.	Products and merchandise		2,143,259	2,858,000	2,858,000
4.	Advances for inventories		138,939	28,393	28,389
III.	Short-term investments	7	30,938,443	23,604,701	23,604,701
1.	Short-term investments excluding loans		694,521	745,529	745,529
	b) Other shares and interests		588,989	588,989	588,989
	c) Other short-term investments		105,532	156,540	156,540
2.	Short-term loans		30,243,922	22,859,172	22,859,172
	b) Short-term loans to others		30,243,922	22,859,172	22,859,172
IV.	Short-term operating receivables	6	31,039,705	29,256,269	29,255,723
2.	Short-term trade receivables		24,897,939	17,906,927	17,906,927
3.	Short-term operating receivables due from others		6,141,766	11,349,342	11,348,796
V.	Cash	8	1,424,424	1,560,308	1,560,308
C.	***DEFERRED COSTS AND ACCRUED REVENUES***	***9***	***1,010,819***	***362,006***	***362,006***
	OFF BALANCE SHEET ITEMS	10	73,298,859	39,633,622	39,633,622

CONSOLIDATED BALANCE SHEET (continuation)

ITEM					in 000 SIT
		Note	31 Dec 2006	1 Jan 2006	31 Dec 2005
	LIABILITIES		373,441,091	361,901,211	357,853,560
A.	***EQUITY***	11	***279,633,944***	***276,314,274***	***250,744,708***
I.	Called-up capital		1,156,217	1,156,217	1,156,217
1.	Share capital		1,156,217	1,156,217	1,156,217
II.	Capital surplus		166,070,501	166,070,501	166,070,501
III.	Revenue reserves		29,514,702	24,707,653	24,707,653
5.	Other revenue reserves		29,514,702	24,707,653	24,707,653
IV.	Revaluation surplus		2,038,793	2,992,398	501,563
V.	Retained profit		44,762,179	47,183,568	13,007,878
VI.	Net profit for the period		14,226,570	0	10,643,991
VII.	Consolidated capital adjustment		1,340	76	11
VIII.	Minority interests		21,863,642	34,203,861	34,656,894
B.	***PROVISIONS AND LONG-TERM ACCRUED COSTS AND DEFERRED REVENUES***	12	***13,750,162***	***12,868,686***	***34,577,721***
1.	Provisions for pensions and similar liabilities		3,194,132	3,417,682	0
2.	Other provisions		8,064,136	6,664,966	31,791,683
3.	Long-term accrued costs and deferred revenues		2,491,894	2,786,038	2,786,038
C.	***LONG-TERM LIABILITIES***	13	***35,606,202***	***31,522,943***	***31,522,943***
I.	Long-term financial liabilities		35,489,658	31,475,130	31,475,130
2.	Long-term financial liabilities to banks		35,489,570	31,467,466	31,467,466
4.	Other long-term financial liabilities		88	7,664	7,664
II.	Long-term operating liabilities		116,544	47,813	47,813
2.	Long-term trade payables		106,442	11,441	11,441
5.	Other long-term operating liabilities		10,102	36,372	36,372
D.	***SHORT-TERM LIABILITIES***	14	***42,654,318***	***40,277,531***	***40,277,531***
II.	Short-term financial liabilities		10,540,337	15,747,786	15,719,722
2.	Short-term financial liabilities to banks		10,424,222	15,709,373	15,709,373
4.	Other short-term financial liabilities		116,115	38,413	10,349
III.	Short-term operating liabilities		32,113,981	24,529,745	24,557,809
2.	Short-term trade payables		25,398,215	19,838,744	19,838,744
4.	Short-term operating liabilities from advances		121,434	24,736	24,736
5.	Other short-term operating liabilities		6,594,332	4,666,265	4,694,329
E.	***SHORT-TERM ACCRUED COSTS AND DEFERRED REVENUES***	15	***1,796,465***	***917,777***	***730,657***
	OFF BALANCE SHEET ITEMS	10	***73,298,859***	***39,633,622***	***39,633.622***

5.4 CONSOLIDATED INCOME STATEMENT

CONSOLIDATED INCOME STATEMENT

ITEM			in 000 SIT
		2006	2005
1.	Net sales	201,792,229	158,476,894
a)	Domestic market	139,562,987	114,006,930
b)	Foreign market	62,229,242	44,469,964
2.	Change in the value of inventories of products and work in progress	-505,528	1,558,026
3.	Capitalised own products and/or services	2,070,239	1,836,185
4.	Other operating revenues (inclusive revaluation operating revenues)	5,051,065	3,296,583
5.	Costs of goods, materials and services	127,276,636	94,589,095
a)	Cost of goods and materials sold and cost of materials used	115,067,076	82,499,097
b)	Cost of services	12,209,560	12,089,998
6.	Labour costs	30,909,902	30,752,661
a)	Payroll costs	21,528,490	21,132,681
b)	Social security costs	5,502,906	5,968,422
	- of which for pension insurance costs	3,850,511	3,775,056
c)	Other labour costs	3,878,506	3,651,558
7.	Write-downs in value	19,428,936	19,132,475
a)	Depreciation and amortisation expense	18,417,081	17,705,583
b)	Revaluation operating expenses associated with intangible assets and property, plant and equipment	936,882	737,318
c)	Revaluation operating expenses associated with current assets	74,973	689,574
8.	Other operating expenses	8,406,680	5,701,366
OPERATING PROFIT		***22,385,851***	***14,992,091***
9.	Financial revenue from shares	411,552	126,869
a)	Financial revenue from shares and interests in group companies	0	2,451
c)	Financial revenues from shares and interests in other companies	328,712	42,667
d)	Financial revenue from other investments	82,840	81,751
10.	Financial revenue from loans	999,913	1,021,561
b)	Financial revenue from loans to others	999,913	1,021,561
11.	Financial revenue from operating receivables	489,032	328,718
b)	Financial revenues from operating receivables due from others	489,032	328,718
12.	Financial expenses due to impairment and write-offs of investments	1,123,099	3
13.	Financial expenses for financial liabilities	2,061,431	1,902,535
b)	Financial expenses for loans received from banks	2,054,036	1,853,543
d)	Financial expenses for other financial liabilities	7,395	48,992
14.	Financial expenses for operating liabilities	89,982	96,944
b)	Financial expenses for trade payables and bills payable	25,555	5,399
c)	Financial expenses for other operating liabilities	64,427	91,545
PROFIT FROM ORDINARY ACTIVITIES		***21,011,836***	***14,469,757***
15.	Other revenues	297,573	435,766
16.	Other expenses	289,422	286,635
PROFIT FROM EXTRAORDINARY ACTIVITIES		***8,151***	***149,131***
TOTAL OPERATING PROFIT		***21,019,987***	***14,618,888***
17.	Income tax	2,831,477	204,184
18.	Deferred taxes	-419,084	0
19.	***NET PROFIT FOR THE PERIOD***	***18,607,594***	***14,414,704***
	Net profit for the period - majority interest	18,389,322	14,161,074
	Net profit for the period - minority interest	218,272	253,630

5.5 CONSOLIDATED CASH FLOW STATEMENT

CONSOLIDATED CASH FLOW STATEMENT

	ITEM	2006	2005
			in 000 SIT
	A. CASH FLOWS FROM OPERATING ACTIVITIES		
+	a) Items of income statement	40,101,793	31,417,230
	Operating revenue (except from revaluation) and financial revenue from operating receivables	205,193,503	160,836,350
	Operating expenses excluding depreciation or amortisation (except from revaluation) and financial expenses from operating liabilities	(164,654,667)	(129,215,100)
	Income taxes and other taxes not included in operating expenses	(437,043)	(204,020)
	b) Changes in net operating assets in balance sheet items (including accruals and deferrals, provisions and deferred tax assets and liabilities)	-2,622,004	-1,266,090
	Opening less closing operating receivables	(8,631,102)	(5,594,854)
	Opening less closing deferred costs and accrued revenues	(649,937)	(155,462)
	Opening less closing deferred tax assets	(421,430)	0
	Opening less closing assets (disposal group) held for sale	56,880	0
	Opening less closing inventories	(79,201)	(2,122,093)
	Closing less opening operating liabilities	5,546,107	6,216,745
	Closing less opening accrued costs and deferred revenues and provisions	1,556,679	389,574
=	Net cash from operating activities (a+b)	37,479,789	30,151,140
	B. CASH FLOWS FROM INVESTING ACTIVITIES		
+	a) Cash receipts from investing activities	246,325,582	220,462,977
	Interest and dividends received from investing activities	1,051,881	1,222,588
	Cash receipts from disposal of intangible assets	400,566	226,103
	Cash receipts from disposal of property, plant and equipment	773,043	120,707
	Cash receipts from disposal of long-term investments	358,019	513,844
	Cash receipts from disposal of short-term investments	243,742,073	218,379,735
-	b) Cash payments from investing activities	(278,632,755)	(243,607,950)
	Cash payments to acquire intangible assets	(1,181,624)	(1,316,935)
	Cash payments to acquire property, plant and equipment	(20,644,432)	(24,620,553)
	Cash payments to acquire long-term investments	(5,986,069)	(5,983,126)
	Cash payment to acquire short-term investments	(250,820,630)	(211,687,336)
=	c) Net cash from investing activities (a + b)	-32,307,173	-23,144,973
	C. CASH FLOWS FROM FINANCING ACTIVITIES		
+	a) Cash proceeds from financing activities	34,556,961	23,815,440
	Cash proceeds from increase in long-term financial liabilities	7,977,206	254,991
	Cash proceeds from increase in short-term financial liabilities	26,579,755	23,560,449
-	b) Cash payments from financing activities	(39,865,461)	(30,649,729)
	Interest paid on financing activities	(2,030,146)	(1,876,887)
	Cash repayments of long-term financial liabilities	(7,415,610)	(20,555,688)
	Cash repayments of short-term financial liabilities	(27,419,705)	(3,285,740)
	Dividends and other profit shares paid	(3,000,000)	(4,931,414)
=	c) Net cash from financing activities (a + b)	-5,308,500	-6,834,289
	D. CLOSING BALANCE OF CASH	1,424,424	1,560,308
+	x) Net cash inflow or outflow for the period	(135,884)	171,878
+	y) Opening balance of cash	1,560,308	1,388,430

5.5 CONSOLIDATED STATEMENT OF CHANGES IN EQUITY - FINANCIAL YEAR 2006

in 000 SIT

ITEM		Called-up capital: Share capital	Called-up capital: Uncalled capital	Capital surplus	Revenue reserves: Legal reserves	Revenue reserves: Reserves for own shares	Revenue reserves: Own shares and interests	Revenue reserves: Statutory reserves	Revenue reserves: Other revenue reserves
	Balance at 31 Dec 2005	1.156.217	0	166.070.501	0	0	0	0	24.707.653
	Changes due to transition to SAS (2006)	0	0	0	0	0	0	0	0
A.	***Opening balance***	***1.156.217***	***0***	***166.070.501***	***0***	***0***	***0***	***0***	***24.707.653***
B.	***Movements to equity***	***0***	***0***	***0***	***0***	***0***	***0***	***0***	***0***
d)	Net profit or loss for the period								
f)	Other increases in components in equity								
C.	***Movements within equity***	***0***	***0***	***0***	***0***	***0***	***0***	***0***	***4.807.049***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board								4.289.966
b)	Allocation of net profit to additional reserves based on a resolution of the shareholders' meeting								517.083
c)	Settlement of loss as a deduction component of equity								
f)	Other reallocation of components of equity								
D.	***Movements from equity***	***0***	***0***	***0***	***0***	***0***	***0***	***0***	***0***
a)	Payment of dividends								
b)	Redemption of equity								
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)								
e)	Other decreases in components of equity								
E.	***Closing balance for the period***	***1.156.217***	***0***	***166.070.501***	***0***	***0***	***0***	***0***	***29.514.702***

in 000 SIT

ITEM		Revaluation surplus	Retained earnings	Net profit for the period	Consolidated capital adjustment	Minority interest	TOTAL
	Balance at 31 Dec 2005	501.563	23.651.869	0	11	34.656.894	250.744.708
	Changes due to transition to SAS (2006)	2.490.835	23.531.699	0	65	(453.033)	25.569.566
A.	***Opening balance***	***2.992.398***	***47.183.568***	***0***	***76***	***34.203.861***	***276.314.274***
B.	***Movements to equity***	***4.371.595***	***0***	***18.389.322***	***1264***	***256.416***	***23.018.597***
d)	Net profit or loss for the period			18.389.322		218.272	18.607.594
f)	Other increases in components in equity	4.371.595			1.264	38.144	4.411.003
C.	***Movements within equity***	***(2.488.632)***	***2.042.694***	***(4.361.111)***			***0***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board			(4.289.966)			0
b)	Allocation of net profit to additional reserves based on a resolution of the shareholders' meeting		(517.083)				0
c)	Settlement of loss as a deduction component of equity		71.145	(71.145)			0
f)	Other reallocation of components of equity	(2.488.632)	2.488.632				0
D.	***Movements from equity***	***(2.836.568)***	***(4.464.083)***	***198.359***	***0***	***(12.596.635)***	***(19.698.927)***
a)	Payment of dividends		(3.000.000)				(3.000.000)
b)	Redemption of equity		(1.464.083)	198.359		(12.596.635)	(13.862.359)
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)	35.082					35.082
e)	Other decreases in components of equity	(2.871.650)					(2.871.650)
E.	***Closing balance for the period***	***2.038.793***	***44.762.179***	***14.226.570***	***1.340***	***21.863.642***	***279.633.944***

FINANCIAL YEAR 2005

ITEM		Called-up capital: Share capital	Called-up capital: Uncalled capital	Capital surplus	Revenue reserves: Legal reserves	Revenue reserves: Reserves for own shares	Revenue reserves: Statutory reserves	Revenue reserves: Other revenue reserves (in 000 SIT)
A.	***Opening balance***	***1.156.217***	***0***	***166.070.474***	***0***	***0***	***0***	***21.190.570***
B.	***Movements to equity***	***0***	***0***	***0***	***0***	***0***	***0***	***0***
d)	Net profit or loss for the period							
f)	Equity revaluation adjustment							
C.	***Movements within equity***	***0***	***0***	***0***	***0***	***0***	***0***	***3.517.083***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board							3.517.083
D.	***Premiki iz kapitala***	***0***	***0***	***0***	***0***	***0***	***0***	***0***
a)	Payment of dividends							
b)	Redemption of equity							
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)							
d)	Other decreases in components of equity							
E.	***Closing balance for the period***	***1.156.217***	***0***	***166.070.474***	***0***	***0***	***0***	***24.707.653***

ITEM		Net profit from previous periods	Net profit for the period	Equity revaluation adjustments: General equity revaluation adjustment	Equity revaluation adjustments: Specific equity revaluation adjustment	Consolidation equity adjustment	Equity of minority interest	TOTAL (in 000 SIT)
A.	***Opening balance***	***17.941.794***	***0***	***27***	***5.785***	***288***	***34.388.816***	***240.753.971***
B.	***Movements to equity***	***0***	***14.161.074***		***713.445***		***268.206***	***15.142.725***
d)	Net profit or loss for the period		14.161.074				253.630	14.414.704
f)	Equity revaluation adjustment				713.445		14.576	728.021
C.	***Movements within equity***	***0***	***(3.517.083)***		***0***			***0***
a)	Allocation of net profit as a component of equity based on a decision of the management and the supervisory board		(3.517.083)					0
D.	***Premiki iz kapitala***	***4.933.916***	***0***		***217.667***	***277***	***128***	***5.151.988***
a)	Payment of dividends	4.931.414						4.931.414
b)	Redemption of equity						38	38
d)	Transfer of specific equity revaluation adjustments (to operating revenue or expenses)	2.502			217.667			220.169
d)	Other decreases in components of equity					277	90	367
E.	***Closing balance for the period***	***13.007.878***	***10.643.991***	***27***	***501.563***	***11***	***34.656.894***	***250.744.708***

5.7 NOTES TO THE FINANCIAL STATEMENTS

5.7.1 CONSOLIDATED BALANCE SHEET

General

Information regarding the basis for preparation of the consolidated balance sheet and the specific accounting policies, selected and applied with significant transactions and other business transactions of the Group, are presented in disclosures of individual assets and liabilities.

As for the transition to the SAS (2006) following changes have been disclosed:

- formation of provisions for jubilee benefits and termination benefits termination in the amount of 3,417,682 thousand SIT and charged against retained profit or loss,
- formation of deferred taxes in the amount of 726,250 thousand SIT due to the formation of provisions for jubilee and termination benefits,
- formation of provisions for closing the Škale cave in the amount of 3,034,924 thousand SIT and charged against retained profit or loss,
- transfer of part of badwill amounting to 28,108,568 thousand SIT and recorded in the consolidated balance sheet of 2005 among retained profit or loss,
- transfer of part of the badwill amounting to 53,073 thousand SIT and recorded in the consolidated balance sheet of 2005 among revaluation surplus,
- transfer of part of intangible assets in the amount of 5,031,675 thousand SIT to property, plant and equipment,
- transfer of part of property, plant and equipment in the amount of 4,084,464 thousand SIT to current assets held for sale,
- elimination of long-term differed costs of operation in the amount of 1,987 thousand SIT,
- transfer of VAT in the amount of 187,120 thousand SIT from advances for property, plant and equipment, inventories and other operating receivables to accrued costs and deferred revenues.

The Group has not additional information whose disclosure in the consolidated balance sheet is not obligatory though are considered to be significant for a true and fair presentation of the Group's operations.

Assets and liabilities are recorded at fair value or at initial cost if the fair value of assets or liabilities cannot be defined.

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the consolidated balance sheet for 2005 are recorded in two columns, namely:

- under SAS (2001) and in items of the consolidated balance sheet under SAS (2006),
- under restated amounts as at 1 January 2006 in compliance with Point 15 of the Introduction to the SAS (2006).

(1) Intangible assets and long-term deferred costs and accrued revenues 5,159,220 thousand SIT

Intangible assets are amortised over their useful lives and the rates of amortisation range from 5 to 50 % p.a.

The Group conducted no impairment of intangible assets during the reporting period.

Concessions, patents, licences, trade marks and similar rights were eliminated during the consolidation process in the amount of 10,770,512 thousand SIT.

Goodwill was formed in the amount of 2,475,000 thousand SIT as a result of the purchase cost exceeding the book value of the long-term investment made in the subsidiary that was acquired in 2006.

COST AND ACCUMULATED AMORTISATION OF INTANGIBLE ASSETS AND LONG-TERM DEFERRED COSTS AND ACCRUED REVENUES

BALANCE AS AT 31 Dec 2006	CONCESSIONS, PATENTS, LICENCES TRADEMARKS AND SIMILAR RIGHTS	GOODWILL	LONG-TERM DEFERRED DEVELOPMENT COSTS	OTHER LONG-TERM DEFERRED COSTS AND ACCRUED REVENUES	TOTAL (in 000 SIT)
Cost	2,730,422	2,475,000	158,995	610,626	5,975,043
Accumulated amortisation	815,823	0	0	0	815,823
Book value	1,914,599	2,475,000	158,995	610,626	5,159,220

MOVEMENT OF INTANGIBLE ASSETS AND LONG-TERM DEFERRED COSTS AND ACCRUED REVENUES

INTANGIBLE ASSETS	CONCESSIONS, PATENTS, LICENCES TRADEMARKS AND SIMILAR RIGHTS	GOODWILL	LONG-TERM DEFERRED DEVELOPMENT COSTS	OTHER LONG-TERM DEFERRED COSTS AND ACCRUED REVENUES	TOTAL (v 000 SIT)
Carrying amount as at 1Jan 2006	949,308	0	124,432	652,716	1,726,456
Additions	1,743,267	2,475,000	62,377	81,233	4,361,877
Transfers	-428,390	0	-27,814	-123,323	-579,527
Decrease	160,371	0	0	0	0
Revaluation	-325,285	0	0	0	-325,285
Amortisation	-184,672	0	0	0	-184,672
Book value as at 31 Dec 2006	1,914,599	2,475,000	158,995	610,626	5,159,220

(2)
Property, plant and equipment
293,328,048 thousand SIT

In 2006, no impairment of property, plant and equipment was carried out.

Group companies record no property, plant and equipment under finance lease or mortgage.

COST AND ACCUMULATED DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

BALANCE AS AT 31 Dec 2006	LAND	BUILDINGS	MANUFACTURING PLANT AND EQUIPMENT	OTHER PLANT AND EQUIPMENT	PROPERTY, PLANT AND EQUIPMENT IN COURSE OF CONSTRUCTION	ADVANCES FOR PROPERTY, PLANT AND EQUIPMENT	TOTAL (in 000 SIT)
Cost	10,934,069	293,032,241	437,185,667	8,273,831	21,015,194	5,407,503	775,848,505
Accumulated depreciation	0	159,009,839	317,373,482	6,137,136	0	0	482,520,457
Book value	10,934,069	134,022,402	119,812,185	2,136,695	21,015,194	5,407,503	293,328,048

MOVEMENT OF PROPERTY, PLANT AND EQUIPMENT

PROPERTY, PLANT AND EQUIPMENT	LAND	BUILDINGS	MANUFACTURING PLANT AND EQUIPMENT	OTHER PLANT AND EQUIPMENT	PROPERTY, PLANT AND EQUIPMENT IN COURSE OF CONSTRUCTION	ADVANCES FOR PROPERTY, PLANT AND EQUIPMENT	TOTAL (in 000 SIT)
Carrying amount as at 1 Jan 2006	11,585,258	127,999,991	118,658,892	1,889,817	26,389,786	3,253,348	289,777,092
Additions	66,457	12,832,644	15,265,125	688,314	19,780,059	3,616,283	52,248,882
Disposals	-822,606	-1,984,094	-1,333,206	-144,130	-7,229,458		-11,513,494
Transfers	104,960	92,351	-198,340	195,562	-17,925,193	-1,462,128	-19,192,788
Depreciation	0	-4,918,490	-12,580,286	-1,492,868	0	0	-17,991,644
Book value as at 31 Dec 06	10,934,069	134,022,402	119,812,185	2,136,695	21,015,194	5,407,503	293,328,048

(3)
Long-term investments
1,349,323 thousand SIT

In the process of consolidation 197,785,096 thousand SIT of long-term investments in Group companies were eliminated.

COST AND VALUE ADJUSTMENT OF LONG-TERM INVESTMENTS EXCEPT OF LOANS

BALANCE AS AT 31 Dec 2006	SHARES AND INTERESTS IN GROUP COMPANIES	SHARES AND INTERESTS IN ASSOCIATES	SHARES AND INTERESTS IN ASSOCIATES	OTHER SHARES AND INTERESTS	in 000 SIT TOTAL
Cost	6,038	132,482	549,044	554,483	1,242,047
Value adjustment	0	0	184	0	184
Book value	6,038	132,482	548,860	554,483	1,241,863

MOVEMENT OF LONG-TERM INVESTMENTS EXCEPT OF LOANS

LONG-TERM INVESTMENTS	SHARES AND INTERESTS IN GROUP COMPANIES	SHARES AND INTERESTS IN ASSOCIATES	SHARES AND INTERESTS IN ASSOCIATES	OTHER SHARES AND INTERESTS	in 000 SIT TOTAL
Carrying amount as at 1 Jan 2006	6,038	11,674	677,584	471,208	1,166,504
Additions	0	129,929	246	125,856	256,031
Transfers, disposals	0	-9,121	-128,970	-42,581	-180,672
Book value as at 31 Dec 2006	6,038	132,482	548,860	554,483	1,241,863

(4)
Deferred tax assets
1,145,359 thousand SIT

During the transition to SAS (2006) all Group companies, which formed provisions for jubilee and termination benefits, took account also of deferred tax assets.

In 2006, subsidiaries have not formed additional deferred tax assets from other items; they have, however, suitably restated the recorded liability due to the utilisation and formation of said provisions.

No deferred tax assets were established by the Group companies in the reporting period.

MOVEMENT OF DEFERRED TAX ASSETS

ITEM				*in 000 SIT*
	Balance as at 1 Jan 2006	*Increase (formation)*	*Utilisation, reversal*	*Balance as at 31 Dec 2006*
Deferred tax assets	726,250	517,147	98,038	1,145,359
Total	726,250	517,147	98,038	1,145,359

(5) Inventories 7,058,011 thousand SIT

As for the inventories of material, the biggest amount refers to inventories of maintenance material, low-value spare parts and heating oil. Inventories of products mostly refer to coal.

(6) Receivables 31,976,986 thousand SIT

Long-term trade receivables are not secured.

Most of short-term trade receivables are secured, whereas the remaining part is not due to their nature.

17,900,803 thousand SIT of short-term intragroup receivables were eliminated in the process of consolidation.

LONG-TERM OPERATING RECEIVABLES IN TERMS OF MATURITY

LONG-TERM OPERATING RECEIVABLES				*in 000 SIT*
			Maturity	*TOTAL*
	up to 3 years	*from 3 to 5 years*	*over 5 years*	
Trade receivables	92,010	184,020	460,053	736,083
Receivables due by others	122,235	29,069	49,894	201,198
Total	214,245	213,089	509,947	937,281

SHORT-TERM OPERATING RECEIVABLES IN TERMS OF MATURITY

SHORT-TERM OPERATING RECEIVABLES							*in 000 SIT*
	Classification in terms of maturity						
	undue	*due of up to 3 months*	*due from 3 to 6 months*	*due from 6 to 9 months*	*due from 9 to 12 months*	*due over 1 year*	*TOTAL*
Trade receivables	24,698,443	206,865	601	1,200	9	2,628	24,909,746
Receivables due by others	6,141,766	0	0	0	0	418	6,142,184
Total	30,840,209	206,865	601	1,200	9	3,046	31,051,930

(7)
Short-term investments
30,938,443 thousand SIT

Most of Group's short-term investments refer to deposits in Slovenia's major banks, hence the exposure to risks is minimum.

Intragroup short-term investments in the amount of 1,409,543 thousand SIT were eliminated in the process of consolidation.

SHORT-TERM INVESTMENTS

SHORT-TERM INVESTMENTS		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Deposits with banks	30,072,202	22,730,020
Investments in equity securities	588,989	588,989
Short-term loans to associates	12,000	88,050
Short-term-term loans to others	159,720	24,797
Other short-term investments	105,532	172,845
Total	30,938,443	23,604,701

(8)
Cash
1,424,424 thousand SIT

The item of cash includes cash in hand, bank balances and money at call.

(9)
Deferred costs and accrued revenues
1,010,819 thousand SIT

Most of deferred costs and accrued revenues refer to short-term deferred costs (accrued costs of energy, concessions paid in advance, insurance premiums and maintenance costs, etc.).

(10)
Off balance sheet items
73,298,859 thousand SIT

Off balance sheet items encompass granted and received instruments for insurance of payments (bank guarantees, insurance policies), granted guarantees, received damages and the value of futures contracts.

(11)
Equity
279,633,944 thousand SIT

Share capital of the Group represents the share capital of the parent company; it remained unchanged in 2006.

Capital surplus recorded an increase by 27 thousand SIT due to the transfer of the general equity revaluation adjustment of the parent company during the transition to SAS (2006).

Other revenue reserves have increased in the reporting period by:

- 517,083 thousand SIT based on the resolution adopted by the shareholders' meeting of the parent company (part of accumulated profit of 2005) and
- 4,289,966 thousand SIT based on the resolution adopted by the supervisory board of the parent company following a proposal of the Managing Director (half of the parent company's net profit in 2006).

Retained earnings in the amount of 44,762,179 thousand SIT represents the parent company's share in retained profits of subsidiaries and the badwill relating to the difference between parent company's long-term investments and subsidiaries' equity.

Net profit for the period in the amount of 14,226,570 thousand SIT consists of the accumulated profit of the parent company (4,289,965 thousand SIT), profits and losses of subsidiaries in 2006 (6,957,980 thousand SIT) belonging to the parent company, and the utilisation of badwill (2,978,625 thousand SIT) and other impacts on the consolidated operating profit.

Revaluation surplus of 2,038,793 thousand SIT is formed in the parent company in the amount of 1,895,244 thousand SIT and in the consolidation procedure in the amount of 143,549 thousand SIT, representing the parent company's share in the formation of revaluation surpluses in subsidiaries.

Consolidated capital adjustment recorded at 1,340 thousand SIT represents exchange differences that occurred during the translation of balance sheet items and income statement items of subsidiaries located abroad.

Minority interests decreased in 2006 by 12,793,252 thousand SIT and thus amount to 21,863,642 thousand SIT.

Equity of subsidiaries was eliminated during the process of consolidation in the amount of 195,717,873 thousand SIT.

GROUP'S EQUITY

TOTAL EQUITY		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Share capital	1,156,217	1,156,217
Capital surplus	166,070,501	166,070,501
Other revenue reserves	29,514,702	24,707,653
Revaluation surplus	2,038,793	2,992,398
Retained earnings	44,762,179	47,183,568
Net profit for the period	14,226,570	0
Consolidation equity adjustment	1,340	76
Minority interests	21,863,642	34,203,861
Total	279,633,944	276,314,274

NET PROFIT OF THE GROUP UPON RESTATEMENT OF EQUITY

NET PROFIT OF THE GROUP UPON RESTATEMENT OF EQUITY	*in 000 SIT*
	2006
Net profit	18,389,322
Net profit using the euro (0.027 % growth)	18,325,451
Net profit using the cost of living index (2.8 % growth)	11,735,237

(12) Provisions and long-term accrued and deferred revenues 13,750,162 thousand SIT

In 2006, all Group companies additionally formed and utilised provisions formed for jubilee and retirement benefits.

The item of provisions include provisions formed and utilised in compliance with the legislation on organisations for disabled person, provisions for contractual liabilities, provisions relating to the closure of the Škale cave that were also utilised in 2006, and provisions for unsettled compensation claims during the transfer of contracts on easement (rights of use).

Long-term accrued and deferred costs include provisions from government grants received for acquisition of fixed assets, which were utilised in 2006 for the accounted depreciation. This Group comprises also provisions referring to CO_2 emission coupons received.

MOVEMENT OF PROVISIONS AND LONG-TERM ACCRUED COSTS AND DEFERRED REVENUES

ITEM						*in 000 SIT*
	BALANCE as at 1 Jan 2006	*INCREASE (FORMATION)*	*UTILISATION, REVERSAL*	*BALANCE as at 31 Dec 2006*	*PLANNED FORMATION*	*PLANNED UTILISATION*
Long-term provisions for retirement and jubilee benefits	3,417,682	341,255	564,805	3,194,132	0	0
Other long-term provisions	6,664,966	2,993,886	1,594,716	8,064,136	1,350,000	666,000
Long-term accrued and deferred revenues	2,786,038	15,707	309,851	2,491,894	15,000	230,836
Total	12,868,686	3,350,848	2,469,372	13,750,162	1,365,000	896,836

(13) Long-term liabilities 35,606,202 thousand SIT

Most of the Group's long-term liabilities consist of long-term bank loans secured by bills, acceptance orders, guarantees, receivables or warranties issued by the Republic of Slovenia.

Loans were taken from Slovenian and foreign banks, and interest rates range depending on the type of loan, maturity period and occasion of borrowing. These also include loans that shall fall due for payment in more than five years and not later than by 2015. Long-term liabilities are introduced in greater detail in annual reports of individual Group companies.

Contracts on interest rate swaps are concluded for part of long-term liabilities of the Group by which the risk of interest rate growth is lowered.

All long-term liabilities are settled within contractual deadlines.

In the process of consolidation, intragroup long-term operating liabilities were eliminated in the amount of 10,770,512 thousand SIT.

LONG-TERM LIABILITIES

LONG-TERM LIABILITIES		*in 000 SIT*
	31 Dec 2006	*1 Jan 2006*
Long-term financial liabilities to banks	35,489,570	31,467,466
Long-term financial liabilities to others	88	7,664
Long-term trade payables	106,442	11,441
Long-term operating liabilities to others	10,102	36,372
Total	35,606,202	31,522,943

LONG-TERM LIABILITIES AND THEIR MATURITY DATES

LONG-TERM LIABILITIES				*in 000 SIT*
	MATURITY DATE			
	FROM 1 TO 3 YEARS	*FROM 3 TO 5 YEARS*	*OVER 5 YEARS*	*TOTAL*
Long-term financial liabilities to banks	14,301,156	8,950,623	12,237,791	35,489,570
Long-term financial liabilities to others	88	0	0	88
Long-term trade payables	106,442	0	0	106,442
Long-term operating liabilities to others	5,433	2,849	1,820	10,102
Total	14,413,119	8,953,472	12,239,611	35,606,202

(14) Short-term liabilities 42,654,318 thousand SIT

All short-term financial liabilities are undue.

Short-term financial liabilities are secured by bills, acceptance orders, guarantees, receivables or warranties issued by the Republic of Slovenia.

Short-term financial liabilities are introduced in greater detail in the annual reports of the individual subsidiaries.

Carrying amounts of short-term liabilities of significant value equal their fair value.

762,073 thousand SIT of short-term intragroup financial liabilities and 17,901,010 thousand SIT of short-term intragroup operating liabilities have been eliminated during the process of consolidation.

SHORT-TERM LIABILITIES

SHORT-TERM LIABILITIES		***in 000 SIT***
	31 Dec 2006	***1 Jan 2006***
Short-term financial liabilities to banks	10,424,222	15,709,373
Short-term financial liabilities to others	116,115	38,413
Short-term trade payables	25,396,046	19,838,744
Short-term operating liabilities to associates	2,169	0
Short-term operating liabilities from advances	121,434	24,736
Short-term operating liabilities to others	6,594,332	4,666,265
Total	42,654,318	40,277,531

SHORT-TERM FINANCIAL LIABILITIES AND THEIR MATURITY DATES

SHORT-TERM OPERATING LIABILITIES	***CLASSIFICATION BY MATURITY***						***in 000 SIT***
	UNDUE	***OVERDUE FOR LESS THAN 3 MONTHS***	***OVERDUE FROM 3 TO 6 MONTHS***	***OVERDUE FROM 6 TO 9 MONTHS***	***OVERDUE FROM 9 TO 12 MONTHS***	***OVERDUE FOR MORE THAN 1 YEAR***	***TOTAL***
Short-term trade payables	25,389,549	8,666	0	0	0	0	25,398,215
Short-term liabilities from advances	121,434	0	0	0	0	0	121,434
Other short-term liabilities	6,594,332	0	0	0	0	0	6,594,332
Total	32,105,315	8,666	0	0	0	0	32,113,981

(15)
Accrued costs and deferred revenues
1,796,465 thousand SIT

Most of accrued costs and deferred revenues refer to accrued costs for dependent costs of electricity, VAT and for advances granted.

During the process of consolidation, accrued costs and expenses formed in connection with CO_2 emission coupons were eliminated in the amount of 239,496 thousand SIT, as the revenue for the Group shall occur in 2007.

MOVEMENT OF ACCRUED COSTS AND DEFERRED REVENUES

ITEM				in 000 SIT
	BALANCE as at 1 Jan 2006	INCREASE (FORMATION)	UTILISATION	BALANCE AS AT 31 Dec 2006
Short-term accrued revenues	906,445	1,251,035	364,599	1,792,881
Short-term deferred revenues	11,332	43	7,791	3,584
Total	917,777	1,251,078	372,390	1,796,465

5.7.2 CONSOLIDATED INCOME STATEMENT

General

Information as to the basis for the preparation of the consolidated income statement, together with the specific accounting policies selected and applied in significant operations and transactions of the Group are introduced in disclosures of individual revenues and expenses.

The consolidated income statement has been prepared by applying Format I, defined under SAS 25.

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the consolidated income statement for 2005 are recorded according to SAS (2001) and presented under income statement items under SAS (2006).

Revenues
210,606,075 thousand SIT

Revenues are classified into operating, financial and other revenues.

REVENUES

REVENUES		in 000 SIT
	2006	2005
Operating revenues	208,408,005	165,167,688
Financial revenues	1,900,497	1,477,148
Other revenues	297,573	435,766
Total	210,606,075	167,080,602

Operating revenues
208,408,005 thousand SIT

Most of the net sales refer to revenues generated by the parent company through the sale of electricity.

The value of capitalised own products and/or services increased by 1,357,260 thousand SIT in the process of consolidation; the increase represents the sale of property, plant and equipment within the Group.

Other operating revenues increased by 2,738,385 thousand SIT during the consolidation process and represents mostly badwill relating to the long-term investment acquired in 2006, whose book value exceeds the purchase cost.

Intragroup net sales amounting to 100,157,643 thousand SIT and other intragroup operating revenues in the amount of 406,750 thousand SIT were eliminated during the consolidation.

Financial revenues
1,900,497 thousand SIT

Financial revenues mostly represent interest on deposits and dividends received.

Intragroup financial revenues amounting to 6,414 thousand SIT were eliminated during the process of consolidation.

Other revenues
297,573 thousand SIT

Other revenues include damages and government grants received.

Segments

Group's net sales are classified in terms of two geographical segments.

GEOGRAPHICAL SEGMENTS

NET SALES BY GEOGRAPHICAL SEGMENT		*in 000 SIT*
	2006	**2005**
Domestic market	139,562,987	114,006,930
Foreign market	62,229,242	44,469,964
Total	201,792,229	158,476,894

Group's net sales are also classified in terms of two business segments.

BUSINESS SEGMENTS

NET SALES BY BUSINESS SEGMENT		*in 000 SIT*
	2006	**2005**
Electrical energy	186,725,723	145,344,727
Other	15,066,506	13,132,167
Total	201,792,229	158,476,894

Expenses
189,586,088 thousand SIT

Expenses are classified into operating, financial and other expenses.

EXPENSES

EXPENSES		*in 000 SIT*
	2006	*2005*
Operating expenses	186,022,154	150,175,597
Financial expenses	3,274,512	1,999,482
Other expenses	289,422	286,635
Total	189,586,088	152,461,714

Operating expenses
182,022,154 thousand SIT

The cost of goods sold refers predominantly to the purchase of electricity held for sale.

Costs of material represent mostly costs of energy, fuel, material for each individual type of production, and spare parts.

Costs of goods and material sold were eliminated during consolidation in the amount of 98,826,283 thousand SIT.

Major part of cost of services refer to production, maintenance, transport and insurance premiums.

Costs of services amounting to 349,249 thousand SIT were eliminated during consolidation.

Labour costs comprise salaries and wages, social insurance contributions, additional pension insurance and other labour cost (meal allowance, commuting allowance, vacation bonus, jubilee benefits, termination benefits, financial support, etc.). Other labour cost includes also tax on wages and salaries.

Most of the write-downs in value refer to amortisation of intangible assets and depreciation of property, plant and equipment.

Major part of revaluation operating expenses associated with intangible assets and property, plant and equipment represents the write-off of technically inefficient and obsolete assets.

The Group companies apply the straight-line of amortisation/depreciation for intangible assets and property, plant and equipment. Assets are amortised individually taking into account the anticipated useful lives.

The depreciation of property, plant and equipment acquired through government grants is accounted for separately, hence long-term accrued costs and deferred expenses are utilised in the relevant amount and revenues are recorded.

RATES OF AMORTISATION / DEPRECIATION APPLIED WITH INTANGIBLE FIXED ASSETS AND PROPERTY, PLANT AND EQUIPMENT

	in 000 SIT
	2006
Buildings	1 - 13 %
Manufacturing plant and equipment	1.7 - 25 %
Other equipment	3.35 - 33.3 %
Computer equipment	33.33 - 50 %
Intangible assets	5 - 50 %

The Group applies similar rates of depreciation for tangible fixed assets of the same kind. As for the manufacturing plant and equipment, individual subsidiaries apply depreciation rates that are suitable for the activity carried out.

Other operating costs comprise the concession-related contribution, contributions for the building land, real property tax, water consumption cost, environmental levy, formation of provisions, scholarships and donations.

Other intragroup operating costs were eliminated in the amount of 267,612 thousand SIT during the process of consolidation.

Financial expenses
3,274,512 thousand SIT

Most of financial expenses refer to interest of long-term and short-term loans extended to Group companies as well as to loss that was incurred through the sale of TRD - Metalurgija.

10,643 thousand SIT of financial expenses were eliminated during consolidation.

Other expenses
289,422 thousand SIT

Other expenses comprise mainly damages.

Costs in terms of function

COSTS IN TERMS OF THEIR FUNCTION

		in 000 SIT
	2006	*2005*
Purchase cost of goods sold or production cost of quantities sold	165,820,661	129,863,748
Selling expenses	2,928,637	3,028,434
General administrative costs	15,708,145	13,886,624

Corporate income tax
2,831,477 thousand SIT

The corporate income tax is calculated by taking into account prescribed tax regimes and rates in countries, in which the Group companies are located. All Group companies are subject to this tax.

In 2006 three of the Group companies, the Group, as well as all companies located abroad were liable for the payment of the corporate income tax, whereas the remaining companies were not subject to this tax due to the utilisation of tax benefits for covering retained losses.

Deferred taxes
- 419,084 thousand SIT

All Group companies that have formed provisions for jubilee and termination benefits, have accounted also for related deferred taxes in 2006 and recorded either as deferred tax income or deferred tax expenses

Net profit
18,607,594 thousand SIT

The item of net profit includes the net profit of the controlling company (8,651,076 thousand SIT), the Group companies' share in subsidiaries' net profit (6,759,621 thousand SIT), the net profit referring to the utilisation of badwill and other impacts on the consolidated income statement (2,978,625 thousand SIT), and net profit of the minority interest (218,272 thousand SIT).

OPERATING PROFIT OF THE GROUP

		in 000 SIT
	2006	**2005**
Gross operating yield	208,408,005	165,167,688
Operating profit	22,385,851	14,992,091
Operating profit from ordinary activities	21,011,836	14,469,757
Operating profit from other activities	8,151	149,131
Total operating profit	21,019,987	14,618,888
Net profit for the period	18,607,594	14,414,704
- of which majority interest	18,389,322	14,161,074
- of which minority interest	218,272	253,630

5.7.3 CONSOLIDATED CASH FLOW STATEMENT

General

The consolidated cash flow statement reveals changes in the balance of cash and cash equivalents over the financial year.

The item of cash comprises cash in hand, bank balances and call deposits.

The consolidated cash flow statement is prepared by using the indirect method (Format II - SAS 26.9).

Pursuant to Note 3 in the Introduction to SAS (2006), the comparable data in the consolidated cash flow statement for 2005 are recorded according to SAS (2001) and presented in items of the consolidated cash flow statement under SAS (2006).

The data in the consolidated cash flow statement are obtained from the consolidated cash flow statements of Group companies, by taking into account also elimination during the consolidation procedure.

CASH FLOWS

		in 000 SIT
	2006	**2005**
Cash flows from operating activities	37,479,789	30,151,140
Cash flows from investing activities	-32,307,173	-23,144,973
Cash flows from financing activities	-5,308,500	-6,834,289
Cash flow for the period	-135,884	171,878

5.7.4 CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

General
The consolidated statement of changes in equity encompasses all changes of equity components during the financial year.

Method
The consolidated statement o changes in equity is prepared in compliance with Format I as defined under SAS 27.2.

Accumulated profit is not established at the Group level.

Pursuant to Note 3 to the Introduction in SAS (2006), the opening balance data are disclosed upon translation as at 1 January 2006, as defined under provisions of Point 15 of the Introduction to the SAS (2006).

Changes in consolidated financial statements of the Group companies due to the transition to SAS (2006) had an impact on following equity items:

a. increase of the retained profit or loss of the Group amounting to 23,531,699 thousand SIT, namely:
   - decrease in Group's retained profit or loss due to losses that occurred with the opening of Group companies (4,576,869 thousand SIT), and
   - transfer of badwill from provisions in the amount of 28,108,568 thousand SIT.

b. increase in revaluation surplus in the amount of 2,490,835 thousand SIT, namely:
   - transfer of badwill from provisions in the amount of 53,073 thousand SIT, and
   - increase in revaluation surplus amounting to 2,437,762 thousand SIT.

c. Increase of consolidated capital adjustment in the amount of 65 thousand SIT due to the elimination of exchange differences as regards the investment made in a company abroad.

d. decrease of minority interests in the amount of 453,033 thousand SIT, namely:
- decrease in retained profit or loss of minority interests due to losses that occurred with the opening of the group companies in the amount o 1,151,535 thousand SIT in
- increase of revaluation surplus by 698,502 thousand SIT.

In 2006, the item of equity recorded an increase of 3,319,670 thousand SIT.

Movements to equity

In 2006, movements to equity were recorded at 23,018,597 thousand SIT.

Equity of the Group (exclusive of minority interests) increased by 22,762,181 thousand SIT, namely:

- by the amount of the Group's profit (18,389,322 thousand SIT)
- by the amount of the consolidated capital adjustment (1,264 thousand SIT) as a result of adjusting investments in equity of subsidiaries abroad, and
- by the amount of the revaluation surplus (4,371,595 thousand SIT), of which 4,230,249 thousand SIT is recorded by the controlling company while the amount of 141,346 thousand SIT refers to the controlling company's share in the revaluation surplus formed in subsidiaries.

Equity of minority interests recorded an increase of 256,416 thousand SIT, based on:

- the Group's net profit amounting to 218,272 thousand SIT, and
- the revaluation surplus formed in Group companies and amounting to 38,144 thousand SIT.

Movements within equity

Movements within equity amounting to 7,366,826 thousand SIT comprise:

- appropriation of half of the controlling company's profit from 2006 among other revenue reserves pursuant to a resolution by the Supervisory Board that was adopted upon a proposal by the controlling company's Managing Director (4,289,966 thousand SIT),
- coverage of the controlling company's loss based on the net profit for 2006 in the amount of 71,145 thousand SIT referring to the transition to SAS (2006),
- allocation of half of the controlling company's accumulated profit of 2005 (517,083 thousand SIT) to other revenue reserves according to the resolution of the shareholders' meeting, and
- coverage of retained Group companies' loss based on the revaluation surplus in the amount of 2,488,632 thousand SIT.

Movements from equity

Movements from equity were recorded at 19,698,927 thousand SIT.

Decrease of Group's equity (exclusive of minority interests) in the amount of 7,102,292 thousand SIT consists of:

- distribution of part of the controlling company's accumulated profit of 2005 in the amount of 3,000,000 thousand SIT,
- decrease of revaluation surplus in connection with derivatives (2,836,568 thousand SIT),
- decrease in retained profit or loss due to the sale of TDR - Metalurgija (1,464,083 thousand SIT), and
- increase in the operating profit due to the sale of TDR - Metalurgija amounting to 198,359 thousand SIT and representing the controlling company's share in the loss of TDR for 2006.

Decrease in equity of minority interests amounting to 12,596,635 thousand SIT consists of:

- 830,544 thousand SIT referring to the sale of a share in TDR - Metalurgija,
- 11,766,091 thousand SIT referring to the sale of shares in other subsidiaries.

5.7.5 OTHER DISCLOSURES

Remuneration of Management Board members and other employees with individual employment contracts

Remuneration of members of the Management Boards and other employees with individual contracts of employment include:

- gross remunerations contained in the notice for income tax returns,
- premiums paid for additional pension insurance, and,
- other fees.

Remuneration of Supervisory Board members

Remuneration of Supervisory Board members represent:

- attendance fees (gross) and travel expenses.

Upon a resolution adopted by the Shareholders' Meeting in 2005 members of Management Boards and other employees on individual contracts of employment, as well as members of the group's Supervisory Boards did in not participate in the net profits nor were they approved any advances, loans or guarantees by group companies.

For these same groups of individuals, remunerations and payables pertaining to housing loans approved prior to 2002, as well as reimbursements of expenses such as (vehicle) fuel and motorway tolls, are shown in the tables below.

Loan receivables decreased in the reporting period by the repaid amount of 526 thousand SIT. The loan has a foreign currency clause and does not bore interest.

In 2006, loans referring to the Housing Act are no longer disclosed among receivables from loans but are included among other operating receivables, hence the comparable data for 2005 are also presented in the schedule.

REMUNERATION OF INDIVIDUAL GROUPS OF PERSONS

GROUPS OF PERSONS	in 000 SIT	
	2006	2005
Members of Management Boards	256,649	304,737
Employees on individual contracts	841,325	864,791
Members of Supervisory Boards	19,212	15,519

PAYABLES ON LOANS GRANTED TO INDIVIDUAL GROUPS OF PERSONS

GROUPS OF PERSONS	in 000 SIT		
	31 Dec 2006	1 Jan 2006*	31 Dec 2005
Members of Management Boards	0	0	0
Employees on individual contracts	2,199	2,725	12,359
Members of Supervisory Boards	0	0	1,083

*Balance of loans exclusive of loans under the Housing Act (Official Journal of RS no 18/91)

OPERATING RECEIVABLES DUE BY INDIVIDUAL GROUPS OF PERSONS

GROUPS OF PERSONS	in 000 SIT	
	31 Dec 2006	31 Dec 2005
Members of Management Boards	21	0
Owners	0	0
Members of Supervisory Boards	0	0

Costs of auditing and tax advisory

As for audit and tax advisory services, the HSE Group had following costs (accounted not paid):

a) audit of annual reports of HSE Group companies (36,725 thousand SIT),
b) other audit-related services (34,617 thousand SIT),
c) tax advisory services (17,724 thousand SIT).

KPMG Slovenija d.o.o. as the statutory auditor carried out the audit of annual reports of the HSE Group, whereas other services were carried out by other audit and tax advisory companies.

5.8 FINANCIAL RATIOS OF THE HSE GROUP IN THOUSAND SIT

Financial ratios of the HSE Group for 2006 and 2005[9].

EQUITY FINANCING RATE

	31 Dec 2006	1 Jan 2006
1. Liabilities	373,441,091	361,901,211
2. Equity	279,633,944	276,314,274
Equity financing rate = 2 / 1	74.88	76.35

In 2006 the Group financed its operations through own funds, as equity has a 75% share among total liabilities, indicating that the Group bears no financial risk. Compared to the balance as at 1 January 2006, the equity financing rate decreased during the year by 2% due to the increase in short-term operating liabilities, in particular trade payables.

LONG-TERM FINANCING RATE

	31 Dec 2006	1 Jan 2006
1. Equity	279,633,944	276,314,274
2. Long-term liabilities	35,606,202	31,522,943
3. Provisions and long-term accrued expenses and deferred revenue	13,750,162	12,868,686
4. Total (1 + 2 + 3)	328,990,308	320,705,903
5. Liabilities	373,441,091	361,901,211
Long-term financing rate = 4 / 5	88.10	88.62

The Group financed its operations through own assets, of which 88 % are long-term and 12 % short-term. Compared to the balance as at 1 January 2006, the long-term financing rate has dropped.

OPERATING FIXED ASSETS RATE

	31 Dec 2006	1 Jan 2006
1. Property, plant and equipment	293,328,048	289,777,092
2. Intangible assets and long-term deferred costs and accrued revenue	5,159,220	1,726,456
3. Total long-term assets at carrying amount (1 + 2)	298,487,268	291,503,548
4. Assets	373,441,091	361,901,211
Operating fixed assets rate = 3 / 4	79.93	80.55

In 2006, property, plant and equipment and intangible assets and long-term deferred costs and accrued revenue accounted for 80 % of the total assets. Compared to 1 January 2006, the operating fixed assets rate dropped by 0.6 percentage point.

[9] As for the transition to the new SAS (2006), the ratios for 2006 referring to the balance sheet were compared with the balance as at 1 January 2006.

LONG-TERM ASSETS RATE

	31 Dec 2006	1 Jan 2006
1. Property, plant and equipment	293,328,048	289,777,092
2. Intangible assets and long-term deferred costs and accrued revenue	5,159,220	1,726,456
3. Investment property	0	0
4. Long-term investments	1,349,323	1,295,510
5. Long-term operating receivables	937,281	1,140,173
6. Total (1 + 2 + 3 + 4 + 5)	300,773,872	293,939,231
7. Assets	373,441,091	361,901,211
Long-term assets rate = 6 / 7	80.54	81.22

Long-term assets rate refers to the share of long-term assets among total assets. In 2006, the ratio was established at 81 % of the total assets, the difference referred to current assets and deferred costs and accrued revenue. The long-term assets rate has remained nearly unchanged as at the year-end if compared to the balance as at 1 January 2006, which is mostly due to the increase in Group's short-term investments (e.g. deposits of companies with major Slovenia's banks).

EQUITY TO OPERATING FIXED ASSETS

	31 Dec 2006	1 Jan 2006
1. Equity	279,633,944	276,314,274
2. Property, plant and equipment	293,328,048	289,777,092
3. Intangible assets and long-term deferred costs and accrued revenue	5,159,220	1,726,456
4. Total fixed assets at carrying amount (2 + 3)	298,487,268	291,503,548
Equity to operating fixed assets = 1/4	0.94	0.95

The ratio refers to the relation between equity and fixed operating assets. In 2006, the ratio was determined at 0.9, showing the Group's most non-liquid assets were financed through equity.

IMMEDIATE SOLVENCY RATIO

	31 Dec 2006	1 Jan 2006
1. Cash	1,424,424	1,560,308
2. Short-term investments	30,938,443	23,604,701
3. Total liquid assets (1 + 2)	32,362,867	25,165,009
4. Short-term liabilities	42,654,318	40,277,531
Immediate solvency ratio = 3 / 4	0.76	0.62

The immediate solvency ratio is the relation between operating current assets and short-term liabilities. In 2006 the ratio was set at 0.8 and indicates an increase compared to 1 January 2006. It is a result of higher short-term investments or deposits mentioned.

QUICK RATIO

	31 Dec 2006	1 Jan 2006
1. Cash	1,424,424	1,560,308
2. Short-term investments	30,938,443	23,604,701
3. Short-term receivables	31,039,705	29,256,269
4. Total (1 + 2 + 3)	63,402,572	54,421,278
5. Short-term liabilities	42,654,318	40,277,531
Quick ratio = 4 / 5	1.49	1.35

The quick ratio shows whether the Group finances short-term assets through short-term liabilities or also long-term. The ratio's value is was recorded at 1.5 meaning that in addition to inventories also other short-term assets are financed. The ratio shows an increase of 10 % over the figures recorded as at 1 January 2006.

CURRENT RATIO

	31 Dec 2006	1 Jan 2006
1. Current assets	70,511,041	66,873,724
2. Short-term deferred costs and accrued revenue	1,010,819	362,006
3. Total (1 + 2)	71,521,860	67,235,730
4. Short-term liabilities	42,654,318	40,277,531
Current ratio = 3 / 4	1.68	1.67

The current ratio reflects the financing of short-term assets by means of short-term liabilities. The Group records good solvency as the ratio was 1.7 in the reporting period.

OPERATING EFFICIENCY RATE

	2006	2005
1. Operating revenues	208,408,005	165,167,688
2. Costs of goods, materials and services	127,276,636	94,589,095
3. Labour costs	30,909,902	30,752,661
4. Write-downs in value	19,428,936	19,132,475
5. Other operating expenses	8,406,680	5,701,366
6. Total operating expenses (2 + 3 + 4 + 5)	186,022,154	150,175,597
Operating efficiency rate = 1 / 6	1.12	1.10

Operating revenues exceed operating expenses by 12 % in the reporting year. Compared to 2005, the operating efficiency rate increased by 2 %.

NET RETURN ON EQUITY RATIO

	2006	2005
1. Net profit for the period	18,607,594	14,414,704
2. Average capital	277,974,109	245,749,340
Net return on equity = 1 / 2	0.067	0.059

In 2006, the net-return-on-equity ratio (ROE) was recorded at 6.7 % indicating that the Group generated 6.7 SIT of net profit on 100 SIT of funded capital. Compared to 2005 the ratio increased by 14% mostly due to Group's higher profit.

...charging batteries...

After a busy day at work, we like to walk, talk and pore over the brightly lit shop windows. It is our way to relax, to wind down and charge the batteries for a new day.

6

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2006

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GLOSSARY OF ACRONYMS

GDP	Gross domestic product
CM	Centre of managing
ČHE	Pumped storage plant
DEM	Dravske elektrarne Maribor d.o.o.
DLN	National spatial plan
E - OVE	Energy from renewable sources
EE	Electrical energy
EECS	Energy Efficiency Certificate System
EES	Electric energetic system
EEX	European Energy Exchange
EFET	European Federation of Energy Traders
EIB	European Investment Bank
ELES	Elektro – Slovenija d.o.o.
EPRS	Elektroprivreda Republike Srbske
ERM2	Exchange rate mechanism
EU	European Union
EUR	Euro
EURIBOR	Euro Interbank Offered Rate
GEN	GEN energija d.o.o.
GZS	Slovenia's Chamber of Economics
HE	Hydroelectric power plant
HEP	Hrvatska elektroprivreda
HSE	Holding Slovenske elektrarne d.o.o.
IP	Invest program
ISO	The International Organization for Standardization
mHE	Small hydroelectric power plant
NAP	National allocation plan
NEK	Nuklearna elektrarna Krško d.o.o.
NEP	National energy programme
NS	Supervisory Board
ODOS	Electronic document system

OHSAS	Occupational Health and Safety Standard
OVE	Renewable sources of energy
Pol	Confirmation of the source
PPE	Gas-fired thermal power plant
PZI	Implementation project
PV	Premogovnik Velenje d.d.
RECS	Renewable Energy Certificate System
R & R	Research and development
RS	Republic of Slovenia
RTP	Transformation station
SCADA	Supervisory Control And Data Acquisition
SČG	Serbia and Montenegro
SDE	Energy Union of Slovenia
SEL	Savske elektrarne Ljubljana d.o.o.
SENG	Soške elektrarne Nova Gorica d.o.o.
SKEP	Economic Outlook and Policy Services
SOPO	System operator of the transmission network
SPESS	Slovenia's Union of Energy Raw Material Recovery
SAS	Slovenian Accounting Standards
SURS	Statistical Office of the RS
TDR - Metalurgija	Tovarna dušika Ruše - Metalurgija d.d.
TE	Thermal power plant
TEB	Termoelektrarna Brestanica d.o.o.
TEŠ	Termoelektrarna Šoštanj d.o.o.
TET	Termoelektrarna Trbovlje d.o.o.
TrUD	Sustainable water management on the Drava river
TK	Telecommunications
UCTE	Union for the Co-ordination of Transmission of Electricity
ZGD - 1	Companies Act
ZSSS	Federation of Free Unions of Slovenia

Annual Report 2006 is published in compliance with the provisions of the Companies Act.
The Slovenian version of this Annual Report is authoritative.