BKS Bank d.d.
Annual report and financial statements for 2013.

Rastite s nama.

BKS Bank

CONTENT

Report by the President of the Management Board

On behalf of the Management Board of BKS Bank d.d. Rijeka, I wish to present the business results of the Bank achieved in the year 2013.

We must, unfortunately, determine that this was another year affected by the crisis, characterized with decline in overall business activity and numerous bankruptcies of Croatian companies and with increasing number of unemployment.

At the time of writing this report, the number of unemployed persons amounted to 375,000, or more than 20% of the working population.

It is clear and evident that the global crisis has affected Croatia harder than many other countries in the region, so that the recovery will be very slow and laborious.

In the real sector there is increasing number of less profitable companies, and the vast majority of companies that are facing difficulties use the institute of Prebanking settlement as last hope before going bankrupt.

In such circumstances, the banking business seems like a "walk through a minefield," that means that maximum caution and conservative approach to clients in order to preserve as much as healthy portfolio, is required.

The share of Non-Performing Loans already exceeds 27% of the total portfolio of placements to companies, and the assumption is that this percentage will significantly increase by the end of 2014 because additional provisions will be necessary to use for existing bad loans.

Of course, this situation has reflected to the profitability of the banking sector where the total profit of banks was reduced to over 50% compared to the year 2012, and more than half of banks will show a financial loss. In spite of this fact, the Croatian National Bank estimates that the banking sector remains stable, liquid and with capital adequacy sufficient to cover potential losses.

Our BKS Bank during 2013 has undertaken a number of measures in order to stabilize business activities, increase revenues and reduce overall costs; and particularly conservative approach to credit-guarantee business with clients has been conducted.

As a result of these measures, we have posted an operating result in amount of HRK 8.1 million, which is significantly higher than the one achieved in the year 2012 (HRK 1.1 million).

Unfortunately this was not sufficient to achieve an overall positive financial result because additional impairments and provisions against the client portfolio were recorded in the amount of HRK 17 million. This drove the bank to post a loss in the amount of HRK 8.7 million.

When we talk about the new provisions, we must point out that these relate mainly to the previously approved loans (except the loss of deposit upon bankruptcy of Centar banka d.d.), and are the result of further worsening of the financial position of clients and impairment of existing collaterals.

The Bank's business activities in the year 2014, will certainly greatly depend on the economic situation in the region. The good news is that in the year 2014, even international institutions estimate stopping of the GDP fall and the recovery in economic activity. The reality is, however, that the accumulated losses from prior periods will continue to remain a heavy burden of the Croatian economy, and it is quite clear that another difficult and uncertain business year awaits us.

Therefore, the BKS Bank's business policy will be consistent with the time in which we live, very cautious and conservative.

Report by the President of the Management Board (continued)

We plan to increase the overall Balance sheet and as well to increase the growth of loans to companies in the amount of approximately 10%, but the focus will still remain on reducing total operating costs.

As for the retail business, after the implementation of a number of new products and services, as well as organizational changes, we expect the effects and the increase in overall activity in this area, particularly the growth of primary sources (a vista and term deposits) and transaction accounts.

We firmly believe that in the year 2014 our business will be profitable. Additional strength for our optimism is the continued support and assistance provided by the owner, BKS Bank AG, Klagenfurt.

I would like to use this opportunity to thank all our clients and business partners for their confidence and support, and all the employees for their hard work and dedication during this challenging year.

Goran Rameša
President of the Management Board

Financial data from profit and loss account

During the course of financial year 2013 the Bank recorded a loss after taxes in amount of HRK 8.7 million.

In 2013 interest income amounted to HRK 51.5 million, which was HRK 0.6 million higher (1.1%) compared to the previous year. This modest increase in interest income was a result of the conservative growth of loans to customers due to market situation and decrease of average 3 month Euribor rate in 2013. Interest income from loans to customers contributed with 98% in the total recorded interest income.

Interest expenses for 2013 amounted to HRK 18.8 million. They consist of interest expenses for deposits from customers amounting to HRK 14.7 million (79%) and interest expenses for interbank loans of HRK 4.0 million. During 2013 corporate clients primarily kept term deposits in HRK and in HRK with FX clauses, while retail clients maintained term deposits in foreign currency.

Net income from fees amounted to HRK 3.7 million and was for HRK 0.2 million higher if compared to the previous year.

In 2013, total operating income amounted to HRK 38.3 million, while in 2012 operating income amounted to HRK 34 million, representing an increase of 12.6%.

Expenses arising from the increase of credit risk related provisions amounted to HRK 17.0 million.

In the current year the Bank has no obligation to pay income tax. Loss after tax amounts to HRK 8.7 million, while in 2012 loss after tax amounted to HRK 5.3 million.

Funds sources and obligatory reserve, liquidity and treasury

Sources of funds

The balance sheet total of BKS Bank d.d. Rijeka, reached in 2013 HRK 1,243,474 thousand, which represents an increase of 3.74% if compared with previous year.

The structure of total sources, has changed as follows: the share of borrowed (deposits and taken loans) funds increased from 82.53% to 83.90%, resulting in own funds (capital, profit and reserves) amounting to 16.10% of the total funds.

Within borrowed funds, the share of received deposits and other liabilities increased for 3.43 percentage points to 59.06%, while the secondary sources decreased from 42.37 to 38.51%. This decrease is consequence of repayment of a large loan received from Hrvatska banka za obnovu i razvoj, in December 2013.

The amount of total deposits compared to prior year has increased by HRK 66 million or 12.03%.

Deposits in HRK decreased by 2.08% to HRK 423 million and their share in the total deposit portfolio represents 68.40%.

Deposits in foreign currency increased to an amount of HRK 195 million. Corporate deposits dominate with 64.54%, while retail deposits make 35.46%.

Obligatory reserve, liquidity and treasury

The CNB Council reduced the reserve requirement calculation rate from 13.5% to 12% in order to boost the already high liquidity and enable banks to finance the economic recovery.

The reduced reserve requirement calculation rate were applied in December, with the result that total reserve requirements have decreased by approximately HRK 4.7 billion, down by HRK 3.9 billion and HRK 0.8 billion in the kuna and foreign exchange component respectively.

However, the decision requires banks to purchase three-year compulsory CNB bills for the total amount of the released reserve requirements. No interest is be charged on these bills and they are be non-transferrable, that is, banks are not be able to sell them to other persons, pledge them, etc., but they will be able to offer them, prior to maturity, at each months-end, for redemption to the central bank. The amount offered is to equal 50% of the increase in certain placements to domestic non-financial enterprises in the previous month.

Specifically, the first redemption of these bills was on 31 December 2013, in the amount of 50% of the increase in certain placements to domestic non-financial enterprises on 30 November relative to 31 October.

On the last day of December 2013 the Croatian National Bank announced the redemption of compulsory CNB bills in the amount of HRK 333.3 million.

BKS Bank d.d. Rijeka, also made the redemption of compulsory CNB bills in the amount of HRK 11 million.

Total calculated obligatory reserve in HRK has varied according to the amount of deposits in range from HRK 73 million in January up to HRK 69 million in December. Calculated obligatory reserve in foreign currencies have been lowest in December (EUR 1,422 thousand and USD 760 thousand), and highest in January (EUR 1,580 thousand and USD 826 thousand).

Funds sources and obligatory reserve, liquidity and treasury

Obligatory reserve, liquidity and treasury (Cont'd)

During the 2013, the Bank HRK liquidity oscillated from the periods of high liquidity to the periods of liquidity needs.

In periods of high liquidity, the Bank invested in liquidity reserves, particularly held in shares of investment funds denominated in HRK or linked to EUR and in Treasury Bills denominated in EUR, or linked to EUR, deposits within CNB and loans to other Croatian Banks.

Loans to other banks averaged to HRK 2 million daily, and the average amount invested in investment funds was averaging to HRK 42 million daily.

In 2012 the Bank held treasury bills in the average amount of HRK 1 million with the maturity of 91 days and with an interest rate of 0.8% p.a. for treasury bills lined to EUR and Treasury Bills in denominated in EUR with an interest of 5.25% p.a. in the amount EUR 2.5 million

Average interest rate, for placements on money market in HRK, during the 2016 did not significantly oscillate, and were ranging from 0.10 up to 1.50% p.a.

According to money market interest rate movements the weighted average rates for placed overnight deposits were in a range from 0.20% to 0.50% p.a. and the average rates for term deposits were in a range from 0.14 to 1.24% p.a.

In periods of higher placements to clients, the Bank has the ability to borrow funds from BKS AG under the Master loan agreement, under favourable conditions.

In 2013 the Bank has not withdrawn any new tranche from the Master loan agreement.
On the 31st December 2013, total funds withdrawn from BKS AG amounted to EUR 49.5 million.

Foreign currency liquidity was higher than the previous year, and it was maintained at a level in accordance with the Banks needs and applicable regulations.

During 2013 minimal ratio of receivables and liabilities in foreign currency was higher than minimum requirements. This percentage was between 20.87% and 25.84%

Funds in foreign currencies have been placed to other domestic and foreign banks as short term deposits (average EUR 11.36 million). Considering the fact that the interest rates on placed foreign currency deposits were lower than in the previous year the Bank has recorded a lower income than in 2012 (income amounted to EUR 14.13 thousand).

Operations with corporate clients

Bank's business activities also continued during 2013, in accordance with plans and development strategy, maintaining good relationship with existing clients and focusing on expansion/acquision of new clients, within a market segment of medium and large companies. Certain part of Bank's activities were also financing of state owned companies as well as regional governments and municipalities. Considering the condition of the economy and ongoing market crisis that has already been present for several years, goals and strategy remained unchanged and will not significantly alter in 2014.

Bank continues to operate at two locations, Rijeka and Zagreb. Majority of clients and credit portfolio relates to companies from these two regions. Expansion towards other markets, mostly region of Istria, Northern Croatia, Slavonia and Dalmatia is done from two mentioned locations, Rijeka and Zagreb. Given the state of the market, Banks strategy and intention to expand throughout Croatian market is currently on standby. Nature of corporate banking, customized, tailor-made service and development of IT sector allowed us also to establish business relationship with dislocated companies, covering the entire territory of Republic of Croatia.

Corporate department is organized through two regional centres/branches: Rijeka and Zagreb, under the authority of Head of corporate department. Each branch is organized in teams of 5 employees – Group leader, two corporate account managers and two associates for corporate banking (assistants).

Total corporate portfolio (Loans and discounted bills of exchange) on 31 December 2013 amounted in total HRK 774 million. Major share refers to loans to customers (short-term and long-term credit lines) amounting HRK 725 million or 93% of total corporate portfolio while the other part refers to discounted bills of exchange amounting HRK 49 million or 7% of total corporate portfolio. Total exposure of documentary business amounts HRK 54 million. The amount of approved, unused loans on 31 December 2013 is HRK 55 million.

Total portfolio (loans to corporate) during 2013 in relation to 2012 increased by 7.51%.

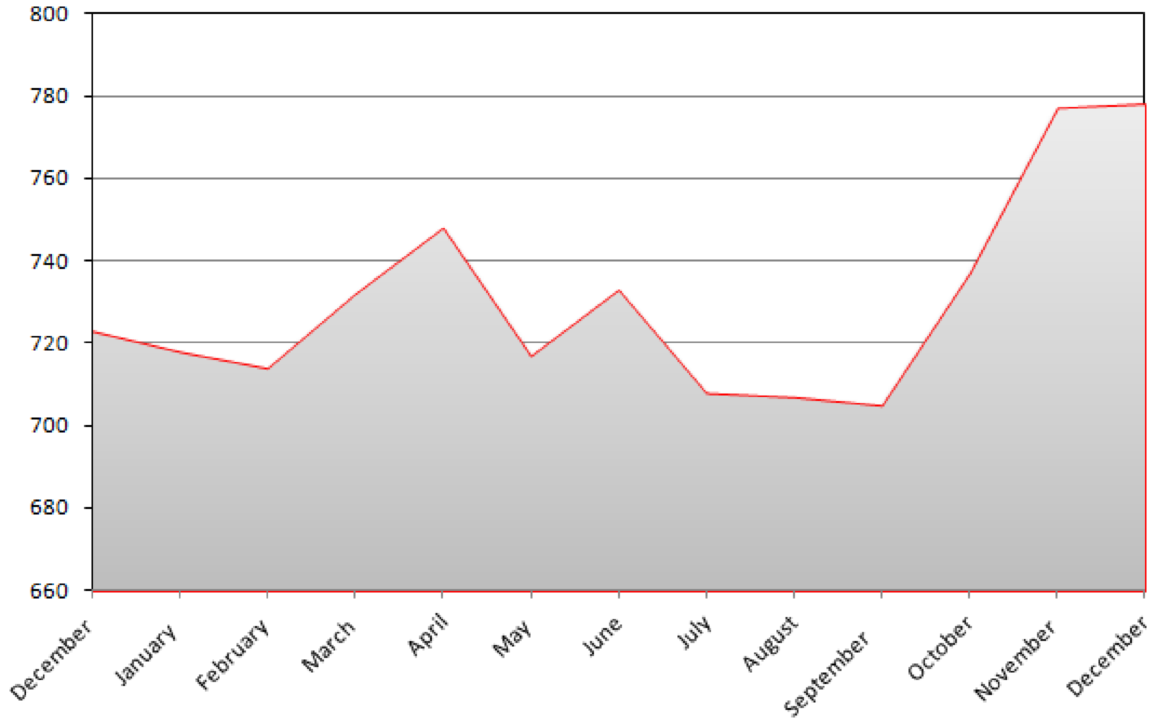
Growth of loan portfolio was recorded in Corporate Zagreb (+16.12%), while Corporate Rijeka recorded downfall (8.47%) compared to 31st Dec, 2012. Considering the portfolio of documentary business, regardless of the growth achieved in Corporate Zagreb, Rijeka still holds a dominant position (85%).

Out of total interest income in 2013, revenues from loans to corporate amounted 89.5%.

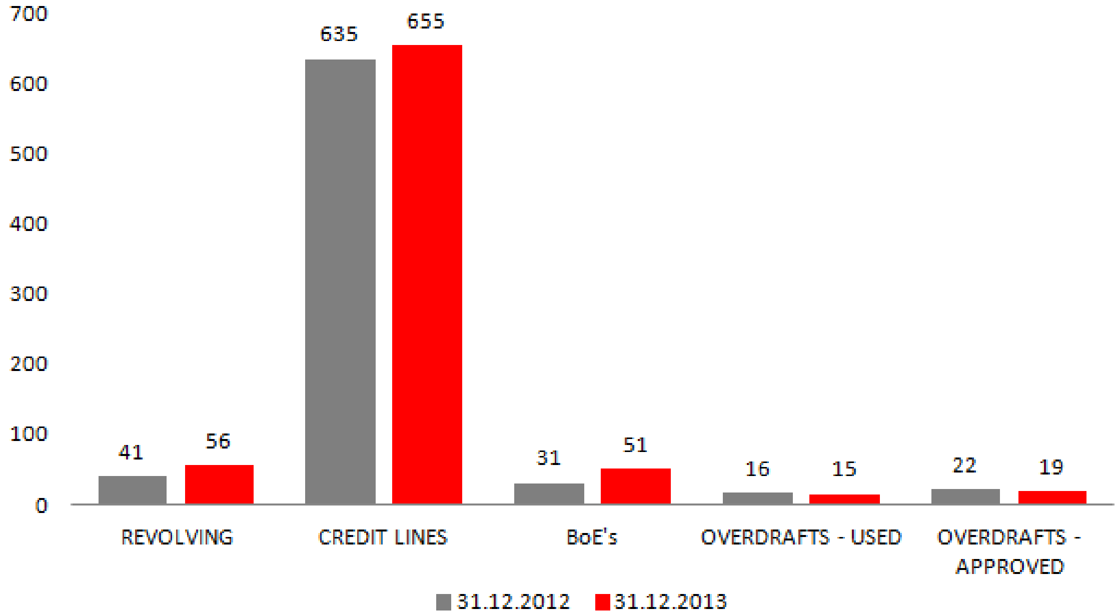
Total amount of deposits of corporate clients on 31 December 2013 amounted to 352 mil HRK. HRK 341 million refers to HRK deposits and deposits with currency clause and the remaining part are deposits denominated in foreign currencies.

Operations with corporate clients (continued)

Exposure in 2013 (HRK million)



Comparative exposure by products (HRK million)



Operations with corporate clients (continued)

Concentration of risk by economic sector in the portfolio of loans to customers may be presented as follows:

	in HRK thousand					in EUR thousand	
	2013	**%**	**2012**	**%**	**Index 2013/2012**	**2013**	**2012**
Trade and Commerce	213,470	26	228,977	30	93	27,950	30,346
Construction	228,114	28	214,530	28	106	29,867	28,431
Metallurgy	36,700	5	34,213	5	107	4,805	4,534
Transport, warehousing and public services	47,288	6	21,412	3	221	6,191	2,838
Energy	-	-	3,018	0	-	-	400
Shipbuilding	516	-	15,645	2	3	68	2,073
Services	143,745	18	149,643	20	96	18,821	19,832
Individuals and unincorporated businesses	82,627	10	70,425	9	117	10,818	9,333
Miscellaneous	54,879	7	22,077	3	249	7,185	2,926
Total	**807,339**	**100**	**759,941**	**100**	**106**	**105,705**	**100,713**

The analysis of exposures presented above shows that the largest proportion of exposures is recorded in the construction and trade industry.

Retail operations

During 2013 the Bank has intensified its orientation towards retail clients in terms of „personal banking“ which is defined within the retail strategy. The main focus is on the overall financial advisory of a client which is to be offered to all client segments. Consequently, the Retail department emphasized its development on a clear sales concept which was also communicated to the public by a media campaign called „Finally! A Bank where I am the king“.

One of the main preliminary steps towards intensified sales activities was the internal re-organisation of the Retail department, whereby all mid-/ back office activities were transferred to respective departments in order to achieve more autonomy for the sales activities.

Furthermore, high attention was also paid to additional educational programs for all retail employees with regard to product knowledge within qualitative financial advisory, internal product knowledge as well as a clearly defined sales advisory tool.

Additionally, internal and external sales monitoring tools were implemented in order to consequently follow and review market trends and internal sales activities.

Regarding new product development during 2013 the Bank focused on product implementations focusing on financial advisory – meaning a sales management tool which assists the retail sales staff for identifying client's needs within the product advisory phase and finally for the ultimate sales activity for the respective product.

Following the Bank's risk strategy a new loan product – insured consumer loan in cooperation with Croatia Osiguranje d.o.o. - was implemented.

Ongoing product adaptations were performed, Retail interest rates were adjusted following market trends, active retail involvement in adapting to new legislation topics or modifications of existing application system of the Bank were additional focus during 2013.

The result of all of the above measures and activities is a significant growth in the deposit and account business during 2013.

Number of retail clients by 31.12.2013 has reached 3,808, whereby during the year 514 new clients have been acquired. In 2012 the total number of retail clients was 3,491 with 241 new acquisitions.

Retail operations (Cont'd)

Deposits

Retail deposits as of 31 December 2013 amount to HRK 265 million which represents an increase of 60% y-o-y. Detailed overview of the deposit business is shown in the table below:

in HRK million

DESCRIPTION	31.12.2013	31.12.2012
1. HRK DEPOSITS	**81.2**	**67.5**
- transaction accounts	3.8	2.3
- resident giro accounts	53.5	51.5
- non-resident giro accounts	0.6	0.6
- saving accounts in HRK	1.7	1.7
- term deposits in HRK	22.0	11.4
2. FOREIGN DEPOSITS	**184.1**	**97.2**
a) residents	137.8	71.1
- a vista	11.9	5.1
- term deposits	125.9	66.0
b) non-residents	46.2	26.1
- a vista	1.0	2.4
- term deposits	45.2	23.7
RETAIL DEPOSITS TOTAL (1+2)	**265.3**	**164.7**
DEPOSITS TOTAL	617,6	529,3
RETAIL DEPOSITS SHARE IN TOTAL DEPOSITS in %	42.9%	31.1%

From the above figures it is evident that the most significant growth was achieved in position of foreign deposits with domestic and foreign physical persons.

Loans

As of 31 December 2013 retail loans amounted to HRK 82.6 million which represents growth of HRK 12.5 million, or an increase of 18% when compared to 31 December 2012. This increase is mostly due to increase of loans to private persons and loans for buildings. However, due to the economic environment and financial crisis the budgeted loan volumes for 2013 were not reached.

Within total Bank's loan portfolio, retail loans participated with 9.6%.

Human resources

Business year 2013 is characterized by Croatian accession to the EU, which is in terms of harmonizing labour law regulations, and regulations related to the management and supervision of financial institutions, for the organizational units of human resource management in the banks, represented a considerable challenge.

The basic requirement to the credit institutions to have arrangements, strategies, processes and mechanisms to manage the risks to which they are exposed, including those that reflect and assume liability for bank's exposure to risks at the individual level, have been resulted in the adoption of new Remuneration policy, identifying individual employees whose professional activities have a material significant impact on the risk profile of the Bank and alignment of individual contracts of employment with the provisions of the new Policy.

In addition to the previously described changes, year 2013 is characterized by constant changes in economic and market environment. Acknowledging the fact that we operate in very dynamic circumstances, we try to adjust our organization and method of operations as well as profile, knowledge and competencies of employees to new conditions and demands of markets and customers, respecting the requirements of the legislator and the owner. According to that, during the year 2013 certain amendments to the internal organization and classification of job positions with associated personnel solutions have been made – the old department was disbanded and the new Credit risk management and back-office department was established, there have been some changes to the head positions and the new person to perform control function of compliance monitoring was appointed. Lower employee turnover during the year has been arisen from the very restrictive employment plan. Departures of employees (temporary, permanent) were used in a way to optimize the needs and retain all existing employees and, at the same time, increase the sales staff, what resulted with new employments only in the Retail department and a number of internal transfers and changes on work positions within or between departments.

Considering that the existing members of the Management Board mandate expires upon the expiry of the year 2013, the procedure on appointment of candidates for a new three-year mandate in the MB of the Bank, was conducted. The Supervisory Board again proposed the existing members (president and member), for whom, in the process of the appointment, in accordance with the new Policy of selection and assessment of the fulfilment of conditions for Supervisory and Management Board members and key function holders, the adequacy assessment procedure has been performed. At the end of the year 2013, the Croatian National Bank issued prior approval for membership in the Management Board of the proposed candidates for the next mandate. Also, all key functions holders have been included in the regular adequacy assessment procedure, while the same procedure, for the members of Supervisory Board, will be carried out in the coming year.

Continuous education and development of employees, even in the most challenging financial times, represent a significant investment for achieving future goals. During the year, many employees attended various external professional training, primarily for the most current areas such as risk management and risk control, innovations in the labour law and tax regulations, European standards for supervisory reporting, changes in payments system, etc. In accordance with the strategic goals and plans for year 2013, special attention was paid to the employees in direct work with retail clients, who throughout the year have been involved in a comprehensive program of 'in-house' training in sales and communication skills, organized in cooperation with our external long-time associates (Develor Ltd.).

Usually, the new heads of organizational units have been involved in developmental educational program in management skills.

The next time period sets before us new regulatory, organizational and personnel requirements and challenges, too, and we believe that we will meet them with equal success.

Human resources (continued)

Basic descriptive statistics about employees:

- On December 31, 2013 there were 62 employees (Management Board included) - 53 in headquarter in Rijeka and 9 in Branch office in Zagreb
- Gender: 45 female, 17 men
- Average age: 39,31
- Qualification structure

  MR = Master of science (4 – 6, 5%)
  VSS = University degree (44 – 71%)
  VŠS = Two-three years post secondary school degree; bacc (4 – 6,5%)
  SSS = Secondary school degree (10 - 16%)

- 60 employed under indefinite period work contract (open-ended work contract); 2 employed under fix-term contract (replacement for employees on maternity/parental leave)

Information technology

During 2013 the Bank has worked on the standardization of information technology to provide a faster response to technological change to which it is exposed on a daily basis. A number of improvements to the information systems have been made, including upgrade of internal control systems and introduction of new modules and improvements to the existing solutions thereby increasing automation of business processes and reducing the operational risk.

The Bank has conducted a number of tests and implementations of the Disaster Recovery and „Plan of Business continuity“ that enables to the Bank the continuity in providing services to its customers.

Great attention during 2013 was given to the analysis of the potential optimization of BKS Bank IT system and performing gap analysis with potential partners in the IT sector as the aim is to ensure a unified IT solution.

Bank corporate management report

Corporate management consists of a set of relations between the Management Board, the Supervisory Board, the managers, the shareholders and all other interested parties. It represents a structure in the framework where the company's goals are defined together with the ways of achieving them and of monitoring the results.

Responsible corporate management in BKS Bank d.d. is a prerequisite for the creation of durable values both for the shareholders and for all the others who are interested in the successful, safe and stable activity of the Bank accompanied by permanent maintenance and strengthening of confidence in the Bank.

As such, the Bank implements both the applicable external and internal regulations, and the rules of its parent company – BKS Bank AG, Klagenfurt, while ensuring that the latter are not contrary to the regulations in force in the Republic of Croatia, and it also monitors the alignment of its organizational structure, to be able to modify, i.e. adjust it promptly.

In addition to fulfilling the regulatory requirements, the Bank shall promote its corporate management by promoting the corporate culture and the awareness of the importance of the corporate management system.

The key principles of corporate management in the Bank are accomplished through:

(1) safeguarding of the shareholders' rights,
(2) establishment of an organizational structure that permits the setting of strategic goals and the affirmation of basic corporative values as well as an adequate infrastructure focused on their realization and monitoring. This is accomplished, among other things, through the monitoring of the business activities by the Supervisory Board and the functioning of the internal controls system.
(3) successful cooperation of the Supervisory Board and the Management Board of the Bank,
(4) setting up of a clear responsibility line within the Bank,
(5) Maintaining good and transparent relations and communication with all banking bodies, employees, management, shareholders, Bank clients and the general public.

The Bank's Management and Supervisory Boards are obliged to ensure the implementation of the corporate management's basic principles. The Bank implements the corporate management principles in the following way:

1. Shareholders and Bank General Meeting

1.1. Shareholders

Shareholders realize their voting right at the Bank General Meeting, and the right to participate goes to all subjects that have been registered as shareholders 15 days before the General Meeting is held.

Each share entitles its holder to one vote, to the dividends and other rights stemming from the law and the Bank Statute.

1.2. General Meeting

The Bank Management Board calls a General Meeting at least once a year.

Ordinary General Meeting shall be called by the Bank Management Board with no delay after the Supervisory Board has examined the annual financial reports, the Bank's Business Report and the draft decision on profit allocation.

Bank corporate management report (continued)

1.2. General Meeting (continued)

The General Meeting takes notice of the annual financial reports and the Management Board Report regarding the situation in the Bank, and in line with this passes the statement of release, approving the way in which the members of the Bank Management and Supervisory Boards managed the Bank business in the business year in question and also approving the decision on profit allocation.

In line with the law and the Bank Statute, the General Meeting decides on Statute amendments, share capital increases or reductions, appointment and release of the Supervisory Board members and the appointment of an auditor to audit the Bank's activities.

2. Cooperation between the Bank Management and Supervisory Boards

An efficient cooperation has been established between the Bank Management Board and the Supervisory Board. To this end the Management Board, with the approval of the Supervisory Board, adopts the basic business documents – business strategy, strategy and policy of risk taking and risk managing, the strategy and procedure of internal capital adequacy assessment, IT strategy as well as the budget (financial plan) for the current year. The Management Board reports regularly (through financial reports submitted on a quarterly and a yearly basis) to the Supervisory Board regarding the Bank’s activities and respective budget fulfilment.

In addition to the activities that, by law, need to be approved by the Bank Supervisory Board, the Management Board, in line with the Rule Book on Management Board (MB) Operations, must obtain approval also for the establishment of new companies and /or for the purchase or sale of shares, for the participation in other legal entities, for the acquisition and the sale of real estate, for the stipulation of contracts of lease of real estate, movables and equipment the duration of which exceeds one year if the annual rental fees exceed the amount of HRK 0.05 million, for investments of the single value exceeding HRK 0.3 million or of the total value in one year above HRK 1 million, for taking loans from a client or related group of clients if the value of one deal i.e. the total value exceeds the amount of HRK 10 million (except for money market and interbank market transactions), for the conclusion of deals causing the exposure towards a single client and the persons related to it in excess of the amounts foreseen by the Bank lending rules, for the definition of the Bank's business policy and strategy, for the definition of the Bank's financial plans, for passing of the Internal Audit Charter and of the annual internal audit program, giving of procuration, setting up or cessation of branches or subsidiaries, representative offices, etc.

An important element for a successful cooperation is the presentation of diligently prepared, true and timely reports to the Supervisory Board by the Bank Management Board, in written form – as a rule - on financial plans, risks management, operations that could have an impact on business profitability and Bank liquidity, on the course of business, especially the cash flow and the Bank Balance Sheet as well as on other principled issues of the business activity. At the same time, the Supervisory Board may require any information from the Bank Management Board regarding issues related to the Bank's activity, which have or could have a material impact on its position.

The good cooperation is manifested in the always open debate between the Bank Management Board and the Supervisory Board, as well as among the members in both these bodies.

3. Bank’s Management Board

The Management Board manages the Bank's activity on its own responsibility and represents the Bank before third parties. The Management Board shall act in the Bank's best interest and shall not be guided by personal interests, nor shall it ask or accept any type of benefit from third parties.

Bank corporate management report (continued)

3.1. Competence, structure and remuneration of the Management Board members

Managing the activity the Bank Management Board ensures in particular: that the Bank operates in line with risk management regulations; the Bank has established accurately determined, clear and consistent internal relations referring to responsibilities which provide a clear demarcation of powers and responsibilities as well as the prevention of conflict interest; the Bank monitors the risks it is exposed to in its activity; the Management Board reviews the adopted strategy and risk management policies and secures and maintains the adequate level of capital in terms of the risks the Bank is exposed to; ensures the functioning of the control functions and annually examines the adequacy of procedures and the effectiveness of control functions; the undisturbed performance of external and internal audit; that it conducts business and other books and business documentation, compiles accounting documents, assesses assets and liabilities realistically, draws up financial and other reports in line with accounting rules and standards; that it reports and informs the Croatian National Bank in line with the regulations and that it implements the measures set by the Central Bank.

The Bank Management Board consists of three members at the most. By law, the minimal number of members is two. One of the members has to be appointed President of the Management Board. Adequate diversity of the Management Board structure with respect to the number of members and the necessary professional knowledge, the capability and the experience of the members shall be determined by a Policy of selection and the fulfilment of conditions for Supervisory and Management Board members and key function holders. The members of the Management Board must fulfil all conditions prescribed by the law regulating operations of trading companies, all conditions prescribed by law and by-laws regulating operations of credit institutions as well as all conditions prescribed by the mentioned Policy.

All Management Board members manage the activity jointly while the single members manage specific business areas as defined by the Rule Book. If the Management Board consists of two members, decisions must be made unanimously. The Management Board members are in charge and responsible for specific business areas. The bank is jointly represented by at least two Management Board members or one member of the Management Board jointly with one authorized signatory.

The remuneration of the Management Board members consist of an agreed fixed pay and a variable portion (annual reward – bonus) amounting from 0 to a maximum corresponding to 25% of the individual annual basic pay. The amount of the annual reward- bonus is determined depending on the performance of the Management Board member and the Bank's performance in the previous financial year, in accordance with the provisions of the Remuneration Policy and Success measuring methodologies. The decision on the amount and period of payment of bonus-annual awards is passed by the Supervisory Board after determining of the audited financial statements and assessment of achieved goals by individual members of the Management Board by the competent committee of the Bank.

3.2. Conflict of interests

The regulations (internal and external) which regulate the conflict of interests are transparent and are followed in the Bank in the best possible way.
Pursuant to the mentioned regulations, and particularly the provisions of the Code of Professional Conduct, the Rule Book on MB Operations as well as the contracts on the managers' rights and obligations, Bank`s Management Board members:

(1) must not, without the consent of the Supervisory Board, participate in third parties or partnerships, either directly or indirectly,
(2) must not, either for their own or for some other's account, perform activities falling under the scope of the activity of the Bank (competition ban),
(3) may not be Supervisory Board members of a third company without the consent of the Supervisory Board,

Bank corporate management report (continued)

3.2. Conflict of interests (continued)

(4) are obliged to report to the Bank`s Supervisory Board any activity whereby a member of the Management Board or next of his kin of first degree acquires or sells - directly or indirectly shares or other securities issued by the Bank,
(5) are obliged to report to the Bank`s Supervisory Board a transaction by which a member of his closest family, directly or indirectly, individually or jointly acquire or release shares or business interests that exceed or fall below a qualified share. Shares or other securities issued by the Bank Likewise, Management Board members shall not use, either for their own or for the account of third parties any notions, information and business contacts, that they can obtain while carrying out their office of Management members.

Pursuant to statutory regulations, Bank lending to the Management Board members, to the members of their immediate family, to legal entities related to the Bank Management Board members – is subject to Supervisory Board approval.

In performing their duties Management Board members must not be guided by their personal interests, nor are they allowed to ask or accept any benefit and/or advantage, either for themselves or for any other party, nor to promise or grant any such benefit and/or advantage – on behalf and for account of the Bank - to these parties. Moreover, the Management Board is obliged to undertake all adequate and reasonable measures in order to ensure that the members of the Management Board and the Bank employees do not act contrary to the ban on divulgation and utilization of privileged information prescribed by the Securities Market Act.

3.3. Bank Management Board Committees

The Bank Management Board may establish various permanent or temporary bodies to assist it in the performance of its functions (e.g. ALCO Committee, etc.)

4. Bank's Supervisory Board

4.1. Competence, structure and remuneration of the Supervisory Board members

Once a year the Bank Supervisory Board submits to the Bank General meeting a report on its work and the work of the committees it has established.

The Bank Supervisory Board monitors the performance of the Bank's operations and in particular: appoints and recalls the members of the Management Board, convokes the General Meeting as required, gives the order to the auditor to examine the annual financial reports, participates in the definition of the annual financial reports, submits a written report on performed supervision to the General Meeting, represents the Bank before the Management Board, gives prior approval to the Management Board decisions when this is prescribed by law, the Statute or the Rule Book on MB Operations. In this way, the Supervisory Board directs the Bank' activity and supervises the business management actively.

In line with the Bank's Statute, the Supervisory Board may have at least three, five or seven members appointed by the Bank's General Meeting, but one of the Supervisory Board members must be independent one. Adequate diversity of the Supervisory Board structure with respect to the number of members and the necessary professional knowledge, the capability and the experience of the members shall be determined by a Policy of selection and the fulfilment of conditions for Supervisory and Management Board members and key function holders. The members of the Supervisory Board must fulfil all conditions prescribed by the law regulating operations of trading companies, all conditions prescribed by law and by-laws regulating operations of credit institutions as well as all conditions prescribed by the mentioned Policy. The Supervisory Board members appoint the president and his deputy among themselves.

Bank corporate management report (continued)

4.1. Competence, structure and remuneration of the Supervisory Board members (continued)

The Supervisory Board members may be granted a reward for their work in the Board. The decision in this respect is made by the General Meeting. General Assembly of the Bank has not adopted a decision on the right of the Supervisory Board members on remuneration for their work and therefore, until the general meeting determines otherwise, the Supervisory Board members do not receive any salary or other form of compensation for their work nor are entitled to participate in the profits of the Bank.

4. Bank's Supervisory Board

4.2. Conflict of interests

All the Bank Supervisory Board members are obliged to act in the Bank's best interest and in making decisions they cannot be guided by their own profit nor may they use their position in order to acquire some personal benefit.

The Supervisory Board members may not point out their membership in the Supervisory Board in public with the purpose of gaining any illicit, personal or professional benefit which may jeopardize the Bank's reputation or any other interest of the Bank. They are also compelled to report to the bank any operation whereby the member or any of their kin of first degree acquires or disposes of the shares or any other securities issued by the Bank, either directly or indirectly.

The Supervisory Board members shall inform the CNB about the appointment or termination of their office in management or supervisory boards of other legal entities, as well as about any deals based on which they or the members of their immediate family have, directly or indirectly, individually or jointly, acquired shares in the legal entity, based on which they have acquired or their shares have fallen below the qualified share.

4.3. Bank Supervisory Board Committees

For the purpose of quality preparations under the competence of the Bank Supervisory Board and the monitoring of the implementation of the decisions made and in order to increase the Supervisory Board's efficiency, the Audit Committee, the Personnel Committee and the Working Committee have been established to perform the monitoring within the scope of their competence and to make the decisions that fall under the competence of the Supervisory Board, prepare the draft decisions to be adopted at the Supervisory Board. The committees also report their activities to the Supervisory Board.

The Auditing Committee supervises the financial reporting; it monitors the efficiency of the system of internal control, audit and risk management systems; it supervises the financial reports' auditing, monitors the auditors' independence and gives recommendations to the Supervisory Board for the appointment of an independent auditor and performs other tasks in line with statutory regulations.
The Working Committee monitors all loans, assessments and other asset-related commercial activities (assets BKS Bank d.d.). Moreover the Committee is responsible for monitoring the Bank's overall activities that are subject to Supervisory Board approval.

The Personnel Committee monitors and deals with the relations between the Management Board and the Bank itself. Given the fact that the decision on appointment and revocation of the Management Board members as well as on the Bank's representation before the Management Board falls under the competence of the Supervisory Board, the Personnel Committee shall supervise and examine the relevant documentation to the extent of its powers, it will discuss the problems and the measures and prepare the draft decisions for the decisions to be adopted by the Supervisory Board.

Bank corporate management report (continued)

5. Internal control system

The internal control system is a system of processes and procedures set up to monitor the Bank's business efficiency, the reliability of its financial information and the compliance with the laws, regulations and good practice, all in order to protect the Bank's assets.

For this purpose an internal controls system has been established in the Bank as a system of procedures and processes for monitoring the efficiency of the Bank's operations, the reliability of financial reporting and adherence to statutory regulations and good business practice. This system is structured according to the size, type, scope and complexity of the business and in accordance with the Bank’s risk profile. This system is the subject of permanent upgrading and adjustment to the standards of the parent bank.

In addition to the members of the Bank Management Board and of the Supervisory Board, all employees and organizational units of the Bank take also part in the implementation of the mentioned control measures, integrated either directly or indirectly in the business processes.

The internal control system in the Bank functions through three mutually independent functions:

(1) the risks monitoring function,
(2) the compliance monitoring function; and
(3) the internal audit function.

Here we also need to add the activities linked to the prevention of both money laundering and the financing of terrorist activities.

A well-established internal controls system enables the Bank a timely monitoring and detection of any materially significant risk to which it may be exposed while performing its activity. The Bank develops an internal controls system adjusted to the standards of its parent Bank.

6. Transparent and timely reporting, external and internal communication

The responsibility for communicating with the public lies with the Management Board.

PR as well as the marketing functions are centralized at BKS Bank AG level, wherefrom, with the agreement of the Management Board, both public relations and internal communications get coordinated and managed. The Bank puts special emphasis on relations and communication with the clients, which are subject to provisions of the Code of Conduct, and the Ethics Code in Business, approved by the Croatian Chamber of Commerce, which has been accepted by the Bank.

The Bank's shareholders and the general public receive timely information through the mass media about the Bank's business, the financial results and the material facts that could have an impact on the Bank's structure and the value of its capital.

The Bank's financial statements are audited on a regular basis by a recognised auditing company that, in principle, belongs to the same auditing group as the company that audits the reports of the parent bank.

In line with the above mentioned, BKS Bank d.d. Rijeka hereby declares that a corporative structure has been established in the Bank, adequate to the business size, scope and structure and to the risks the Bank is exposed to, and that the Bank, considering its position within the BKS Bank AG Group as well as the environment in which it operates, is well organized and that business in 2013 was conducted adhering to the principles and guidelines of corporative management, which will continue to be followed in future as well.

Goran Rameša
President of the Management Board

General data

Bank Bodies	
General Meeting	**Chairman is elected among the Supervisory Board members**
Supervisory Board	**Herta Stockbauer, President** **Dieter Vinzenz Krassnitzer, Deputy President** **Josef Morak, member** **Harald Richard Brunner, member** **Ludwig - Hubert Ankele, member**
Management Board	**Goran Rameša, President** **Christian Peter Pettinger, member**

Address
Mljekarski trg 3, 51000 Rijeka, Hrvatska

SWIFT :
BFKKHR22

Web :
www.bks.hr

Giro account:
2488001-1011111116

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

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

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

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the Bank together with the annual financial statements for acceptance. If the Supervisory Board approves the annual financial statements they are deemed confirmed by the Management Board and Supervisory Board.

The financial statements set out on pages 24 to 86, as well as supplementary information prescribed by a decision of the Croatian National Bank on pages 87 to 93, which is not part of financial statements, were authorised by the Management Board on 5 March 2014 for issuance to the Supervisory Board and are signed below to signify this.

For and on behalf of BKS Bank d.d.:

Goran Rameša
President of the Management Board

Christian Peter Pettinger
Member of the Management Board

Independent Auditors' Report

Report on the Financial Statements

We have audited the accompanying financial statements ('the financial statements') of BKS Bank d.d. (the 'Bank') which comprise the statement of financial position as at 31 December 2013, and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information (as set out on pages 24 to 86).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with statutory accounting requirements for banks in Republic of Croatia, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Independent Auditor's Report (continued)

Opinion

In our opinion, the financial statements present fairly, in all material aspects, the financial position of the Bank as at 31 December 2013 and its financial performance and cash flows for the year then ended in accordance with statutory accounting requirements for banks in Republic of Croatia.

Other matters

The financial statements of the Bank as at and for the year ended 31 December 2012 were audited by another auditor who expressed an unmodified opinion on those statements on 5 March 2013.

Other legal and regulatory requirements

1) In accordance with the By-law on the Structure and Content of the Annual Financial Statements (National Gazette no 62/08) (hereinafter „the By-Law), the Bank's management has prepared forms which are presented on pages 87 to 93, and which contain a balance sheet as at 31 December 2013, profit and loss account, statement of changes in equity and cash flow statement for the year then ended together with notes on reconciliation of the forms to the primary financial statements of the Bank. This financial information is the responsibility of the Bank's management and is, pursuant to statutory accounting requirements for banks in Republic of Croatia, not a required part of the financial statements, but is required by the Bylaw. Our responsibility with respect to this financial information is to perform the procedures we consider appropriate to conclude whether this financial information have been properly derived from the audited financial statements. In our opinion, based on the procedures performed, the financial information presented in the forms has been properly derived, in all material respects, from the audited financial statements which were prepared in accordance with statutory accounting requirements for banks in Republic of Croatia as presented on pages 24 to 86 and are based on underlying accounting records of the Bank.

2) Management Board of the Bank has prepared Annual report as set out on pages 1 to 20. The Management Board is responsible for the preparation of the Annual report in accordance with the Croatian Accounting Law and for its accuracy. Our responsibility is to perform procedures we consider necessary to reach a conclusion on whether the Annual report is consistent with the audited financial statements. Our work as auditors was confined to checking the annual report with the aforementioned scope and did not include a review of any information other than that drawn from the audited accounting records of the Bank. In our opinion, the accounting information presented in the Annual report of the Bank for the year 2013 is in consistent, in all material respects, with the audited financial statements for that year which are presented on pages 24 to 86.

Ernst & Young d.o.o.
Zagreb, 5 March 2014

ERNST & YOUNG
d.o.o.
Zagreb, Radnička cesta 50

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER

(in thousands of HRK)	Note	2013	2012
Income statement			
Interest and similar income	4a	51,478	50,906
Interest expense and similar charges	4c	(18,815)	(22,155)
Net interest income		**32,663**	**28,751**
Fee and commission income	5a	5,158	5,067
Fee and commission expense	5b	(1,453)	(1,618)
Net fee and commission income		**3,705**	**3,449**
Net trading income from dealing in foreign currencies		819	1,087
Net income from investment securities	6	568	316
Other operating income	7	610	459
Operating income		**38,365**	**34,062**
Impairment losses on loans and advances to customers and banks	14b,13	(16,113)	(5,037)
Other impairment losses and provisions	8	(894)	(2,742)
Operating expenses	9	(30,237)	(31,834)
Loss before income tax		**(8,879)**	**(5,551)**
Income tax benefit	10a	168	217
Loss for the year after tax		**(8,711)**	**(5,334)**
Other comprehensive income		**-**	**-**
Total comprehensive income for the year		**(8,711)**	**(5,334)**

The accompanying accounting policies and other notes on pages 28 to 86 form an integral part of these financial statements.

STATEMENT OF FINANCIAL POSITION

FOR THE YEAR ENDED 31 DECEMBER

(in thousands of HRK)	Note	31 December 2013	31 December 2012
ASSETS			
Cash and cash equivalents	11	171,113	123,598
Obligatory reserve with the Croatian National Bank	12	84,393	95,009
Financial assets at fair value through profit or loss	15	42,780	45,772
Loans and advances to banks	13	79,813	103,363
Loans and advances to customers	14a	777,893	742,523
Available-for-sale financial assets	16	1,076	1,276
Held-to-maturity investments	17	49,269	48,693
Other assets	20	8,334	8,018
Property and equipment	18	21,921	23,208
Intangible assets	19	5,836	6,171
Deferred tax assets	10b	1,046	878
Total assets		**1,243,474**	**1,198,509**
LIABILITIES AND EQUITY			
LIABILITIES			
Deposits from banks	21	77	22,119
Deposits from customers	22	617,671	529,354
Borrowings	23	402,769	419,941
Provisions for liabilities and charges	24	2,899	2,534
Other liabilities	25	19,521	15,313
Total liabilities		**1,042,937**	**989,261**
EQUITY			
Issued share capital	26	200,000	200,000
Statutory reserve	27a	2,778	2,778
Retained (losses)/earnings	27b	(2,241)	6,470
Total equity		**200,537**	**209,248**
Total liabilities and equity		**1,243,474**	**1,198,509**

The accompanying accounting policies and other notes on pages 28 to 86 form an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

(in thousands of HRK)	**Issued share capital**	**Statutory reserve**	**Retained earnings /(losses carried forward)**	**Total**
Balance at 1 January 2012	**120,000**	**2,775**	**11,807**	**134,582**
Total comprehensive income for the year	-	-	(5,334)	(5,334)
Transfer to statutory reserve (Note 26a)	-	3	(3)	-
Increase in share capital	80,000	-	-	80,000
Balance at 31 December 2012	**200,000**	**2,778**	**6,470**	**209,248**
Balance at 1 January 2013	**200,000**	**2,778**	**6,470**	**209,248**
Total comprehensive income for the year	-	-	(8,711)	(8,711)
Balance at 31 December 2013	**200,000**	**2,778**	**(2,241)**	**200,537**

The accompanying accounting policies and other notes on pages 28 to 86 form an integral part of these financial statements.

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER

(in thousands of HRK)	Note	2013	2012
Cash flows from operating activities			
(Loss)for the year		**(8,711)**	**(5,334)**
Adjustments for:			
Depreciation and amortisation	*9*	4,329	4,975
Net foreign exchange loss from translation of monetary assets and liabilities	*7*	348	377
Impairment losses on loans and advances to customers	*14b*	16,113	5,037
Other impairment losses and provisions	*8*	894	2,742
Income tax benefit	*10a*	(168)	(217)
Cash flows from operating activities before changes in operating assets and liabilities		**12,805**	**7,580**
Changes in operating assets and liabilities:			
Net decrease/(increase) in obligatory reserve with the Croatian National Bank		10,616	(28,013)
Net decrease/(increase) in loans and advances to banks		19,740	(19,257)
Net decrease/(increase) in loans and advances to customers		(47,643)	(60,623)
Net decrease/(increase) in financial assets at fair value		2,992	(24,856)
Net (increase) in other assets		(644)	(180)
Net increase/(decrease) in deposits from banks		(22,042)	(6,144)
Net increase/(decrease) in deposits from customers		88,317	(20,416)
Net increase in other liabilities		3,822	2,557
Net cash outflow from operating activities before tax		**67,963**	**(149,352)**
Income tax paid		-	-
Net cash inflow/(outflow) from operating activities		**67,963**	**(149,352)**
Cash flows from investing activities			
Purchase of property and equipment		(165)	(510)
Purchase of intangible assets		(2,535)	(2,318)
Net increase in held-to-maturity investments		(576)	(6,673)
Net cash outflow from investing activities		**(3,276)**	**(9,501)**
Cash flows from financing activities			
Net (decrease)/increase in borrowings		(17,172)	73,937
Paid in share capital		-	80,000
Net cash (outflow)/inflow from financing activities		**(17,172)**	**153,937**
Net increase/(decrease) in cash and cash equivalents		**47,515**	**(4,916)**
Cash and cash equivalents at beginning of year		**123,598**	**128,514**
Cash and cash equivalents at end of year	11	**171,113**	**123,598**
Interest paid		*15,247*	*20,228*
Interest collected		*50,983*	*49,701*

The accompanying accounting policies and other notes on pages 28 to 86 form an integral part of these financial statements.

1. REPORTING ENTITY

BKS Bank d.d., Rijeka ("the Bank") is a joint stock company incorporated and domiciled in Croatia. The Bank was formerly known as Kvarner banka d.d. Rijeka. The registered office is at Mljekarski trg 3, in Rijeka. The Bank started its activities in April 1993 and its operations include receiving cash deposits, granting loans and making other placements. The Bank is focused on medium-sized companies and sole traders. The Bank is registered at the Commercial Court in Rijeka with authorised share capital in the amount of HRK 200,000 thousand.

2. BASIS OF PREPARATION

A) Accounting framework

The financial statements have been prepared in accordance with statutory accounting requirements for banks in Republic of Croatia.

Banking operations in Croatia are subject to the Credit Institutions Law, in accordance with which the Bank's financial reporting is regulated by the Croatian National Bank ("the CNB") which is the central monitoring institution of the banking system in Croatia. These financial statements have been prepared in accordance with these banking regulations.

The financial statements were approved by the Bank's Management Board on 5 March 2013 for approval by the Supervisory Board.

The principal accounting policies applied in the preparation of these financial statements are summarised below. Where specific accounting policies are aligned with accounting principles set out in International Financial Reporting Standards ("IFRS"), reference may be made to certain Standards in describing the accounting policies of the Bank; unless otherwise stated, these references are to Standards applicable at 31 December 2013. The accounting regulations based on which these financial statements have been prepared differ from IFRS both in terms of presentation and disclosures as well as in terms of recognition and measurement.

Attention is drawn to the following differences between the accounting regulations of the CNB and recognition and measurement requirements of IFRS:

- The CNB requires banks to recognise impairment losses, in income statement, on assets not identified as impaired (including sovereign risk assets) at prescribed rates (excluding assets carried at fair value). The Bank has made portfolio-based provisions of HRK 12,441 thousand (2012: HRK 10,437 thousand) carried in the balance sheet in compliance with these regulations, and has recognised a charge against income in respect of such provisions of HRK 2,004 thousand within the charge for impairment losses for the year (2012: charge of HRK 440 thousand). Although, in accordance with IFRS, such provisions should more properly be presented as an appropriation within equity, the Bank continues to recognise such provisions in the statement of comprehensive income as a substitute for existing but unidentified impairment losses calculated in accordance with the requirements of IFRS.
- A further difference between IFRS and the accounting regulations of the CNB relates to the determination of impairment losses by discounting the estimated cash flows of the impaired asset at the instrument's original effective interest rate. The Bank calculates impairment losses on individually significant items by estimating the future cash flows and discounting these estimated amounts at the instrument's original effective interest rate. The Bank generally recognises the amortisation of such discounts as a release of impairment allowance rather than as interest income. In certain cases, however, collections are recognised as interest income once impairment losses are fully reversed.
- Additionally the CNB prescribes minimum levels of impairment losses against certain specifically identified impaired exposures, which may be different from the impairment loss required to be recognised in accordance with IFRS.

2 BASIS OF PREPARATION (CONTINUED)

B) Basis of measurement

The financial statements are prepared on the fair value basis for financial assets at fair value through profit or loss and financial assets available for sale, except those financial assets available for sale for which a reliable measure of fair value is not available. Other financial assets and liabilities, and non-financial assets and liabilities, are stated at amortised or historical cost.

C) Use of estimates and judgements

In preparing the financial statements, management has made judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of commitments and contingencies at the balance sheet date, as well as amounts of income and expense for the period. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances and information available at the date of the preparation of the financial statements, the results of which form the basis for making judgements about the carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and any future periods affected.

Information about judgements made by management in the application of applicable standards that have significant effect on the financial statements and about estimates that have a significant risk of resulting in a material adjustment within the next financial year are included in Note 33.

D) Functional and presentation currency

The financial statements are presented in Croatian kuna (HRK), which is the Bank's functional and presentation currency. Amounts are rounded to the nearest thousand (unless otherwise stated). As at 31 December 2013 the exchange rates used for translation were HRK 5.5490 to USD 1 and HRK 7.6376 to EUR 1 (31 December 2012: HRK 5.7268 to USD 1 and HRK 7.5456 to EUR 1).

E) Financial crisis impact

The Bank places significant attention on the credit function in order to mitigate the risk of credit portfolio impairment. The impairment allowances and potential losses are regularly monitored.

Although the impact of the financial crisis cannot be predicted, the Bank has undertaken a number of activities focusing on the quality of the portfolio of its existing clients. This includes constant communication with clients and co-operation in terms of adjustment of terms and dynamics of payment, monitoring of the values of collateral obtained and obtaining of additional collateral from client and from the parent bank.

F) The accounting policies adopted are consistent with those of the previous financial year, except for the following standards and amendments to IFRS effective as of 1 January 2013:

- *IFRS 7 Financial Instruments: Disclosures (Amendment), effective January 1, 2013*
- *IFRS 13 Fair Value Measurement – effective January 1, 2013*
- *IFRS 1 First-time Adoption of International Financial Reporting Standards - Government Loans (Amendments) – effective January 1, 2013*
- *IFRS 1 First-Time Adoption of International Financial Reporting Standards (Amendment) - Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopters*
- *IAS 12 Income Taxes (Amendment) - Deferred Taxes: Recovery of Underlying Assets;*
- *IAS 19 Employee benefits (revised) – effective January 1, 2013*
- *IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine – effective January 1, 2013*

The adoption of the standards or interpretations is described below:

IFRS 7 Disclosures — Offsetting Financial Assets and Financial Liabilities — Amendments to IFRS 7

These amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognized financial instruments that are set off in accordance with IAS 32 Financial Instruments: Presentation. The disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are set off in accordance with IAS 32. These amendments did not have impact on the Bank's financial position or performance and are effective for annual periods beginning on or after 1 January 2013.

IFRS 13 Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Standard did not affect financial position and performance of the Bank but has affected the Banks's fair value disclosures. Standard is effective for annual periods beginning on or after 1 January 2013.

IFRS 1 Government Loans – Amendments to IFRS 1

These amendments require first-time adopters to apply the requirements of IAS 20 Accounting for Government Grants and Disclosure of Government Assistance, prospectively to government loans existing at the date of transition to IFRS. Entities may choose to apply the requirements of IFRS 9 (or IAS 39, as applicable) and IAS 20 to government loans retrospectively if the information needed to do so had been obtained at the time of initially accounting for that loan. The exception would give first-time adopters relief from retrospective measurement of government loans with a below-market rate of interest. The amendment is effective for annual periods on or after 1 January 2013. The amendment has no impact on the Bank.

IFRS 1 First-Time Adoption of International Financial Reporting Standards (Amendment) – Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopters

The IASB provided guidance on how an entity should resume presenting IFRS financial statements when its functional currency ceases to be subject to hyperinflation. The amendment shall be applied as from the commencement date of its first financial year starting on or after 1 January 2013. The amendment had no impact to the Banks's financial position or performance.

IAS 12 Income Taxes (Amendment) – Deferred Taxes: Recovery of Underlying Assets

The amendment clarified the determination of deferred tax on investment property measured at fair value and introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. It includes the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 should always be measured on a sale basis. The amendment shall be applied as from the commencement date of its first financial year starting on or after 1 January 2013 and there has been no effect on the Banks's financial position, performance or its disclosures.

IAS 19 Employee Benefits (Revised)

The IASB has issued numerous amendments to IAS 19. These range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording. The amendment is effective for annual periods beginning on or after 1 January 2013. There has been no impact on the Banks's financial position or results.

IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine

This interpretation applies to waste removal (stripping) costs incurred in surface mining activity, during the production phase of the mine. The interpretation addresses the accounting for the benefit from the stripping activity. The interpretation is effective for annual periods beginning on or after 1 January 2013. The new interpretation did not have an impact on the Bank.

Following standards become effective for annual periods beginning on or after January 1, 2013. The endorsement process within EU adopted the standards and decided that standards should be applied, at the latest, as from the commencement date of a financial year starting on or after January 1, 2014. It is expected that these new standards will have no significant impact on Bank's financial statements.

- *IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)*
- *IFRS 10 Consolidated Financial Statements, IAS 27 Separate Financial Statements*
- *IFRS 11 Joint Arrangements*
- *IFRS 12 Disclosure of Interests in Other Entities*

Standards endorsed by EU but not yet effective

IAS 32 Offsetting Financial Assets and Financial Liabilities — Amendments to IAS 32

These amendments clarify the meaning of "currently has a legally enforceable right to set-off". The amendments also clarify the application of the IAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. These amendments are not expected to impact the Banks's financial position or performance and become effective for annual periods beginning on or after 1 January 2014.

Investment Entities (Amendments to IFRS 10, IFRS 12, IAS 27 and IAS 28)

In October 2012 IASB issued the amendments that are effective for annual periods beginning on or after January 1, 2014. These amendments will apply to investments in subsidiaries, joint ventures and associates held by a reporting entity that meets the definition of an investment entity. An investment entity will account for its investments in subsidiaries, associates and joint ventures at fair value through profit or loss in accordance with IFRS 9 (or IAS 39, as appropriate), except for investments in subsidiaries, associates and joint ventures that provide services that relate only to the investment entity, which would be consolidated or accounted for using the equity method, respectively. An investment entity will measure its investment in another controlled investment entity at fair value. Non-investment entity parents of investment entities will not be permitted to retain the fair value accounting that the investment entity subsidiary applies to its controlled investees. For non-investment entities, the existing option in IAS 28, to measure investments in associates and joint ventures at fair value through profit or loss, will be retained. It is expected that there will be no significant impact on Bank's financial statements.

Recoverable Amount Disclosures for Non-Financial Assets – Amendments to IAS 36 Impairment

of Assets

These amendments remove the unintended consequences of IFRS 13 on the disclosures required under IAS 36. In addition, these amendments require disclosure of the recoverable amounts for the assets or CGUs for which impairment loss has been recognized or reversed during the period. These amendments are effective retrospectively for annual periods beginning on or after 1 January 2014 with earlier application permitted, provided IFRS 13 is also applied. The Bank has early adopted these amendments to IAS 36 in the current period since the amended/additional disclosures provide useful information as intended by the IASB, however, there are no effects on these financial statements.

Standards not yet endorsed by EU

The standards and interpretations that are issued, but not yet endorsed by EU, up to the date of issuance of the Banks's financial statements are disclosed below. The Bank intends to adopt these standards, if applicable, when they become effective.

IFRS 9 Financial Instruments: Classification and Measurement

IFRS 9, as issued, reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. Most of the requirements in IAS 39 for classification and measurement of financial liabilities and derecognition of financial assets and liabilities were carried forward unchanged to IFRS 9. The standard eliminates categories of financial instruments currently existing in IAS 39: available-for-sale and held-to-maturity. According to IFRS 9 all financial assets and liabilities are initially recognized at fair value plus transaction costs.

Hedge accounting

A new chapter on hedge accounting has been added to IFRS 9. This represents a major overhaul of hedge accounting and puts in place a new model that introduces significant improvements principally by aligning the accounting more closely with risk management. There are also improvements to the disclosures about hedge accounting and risk management.

The standard does not currently indicate the mandatory effective date. The IASB decided to defer the mandatory effective date of IFRS 9 until the date of the completed version of IFRS 9 is known. The standard has not yet been endorsed by EU. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Banks's financial assets, but will not have an impact on classification and measurements of financial liabilities. The Bank will quantify the effect in conjunction with the other phases, when the final standard including all phases is issued and endorsed by EU.

IFRIC 21 Levies

The interpretation is applicable to all levies other than outflows that are within the scope of other standards (e.g., IAS 12) and fines or other penalties for breaches of legislation. Levies are defined in the interpretation as outflows of resources embodying economic benefits imposed by government on entities in accordance with legislation. The interpretation clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. It also clarifies that a levy liability is accrued progressively only if the activity that triggers payment occurs over a period of time, in accordance with the relevant legislation. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability is recognized before the specified minimum threshold is reached. The interpretation does not address the accounting for the debit side of the transaction that arises from recognizing a liability to pay a levy. Entities look to other standards to decide whether the recognition of a liability to pay a levy would give rise to an asset or an expense under the relevant standards. The interpretation is effective for annual periods beginning on or after January 1, 2014. The new interpretation will have no impact on the Bank.

3 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies have been consistently applied to all periods presented in these financial statements.

3.1 Interest income and expense

Interest income and expense are recognised in the income statement as accrued for all interest-bearing financial instruments measured at amortised cost, using the effective interest rate method, i.e. the rate that discounts estimated future cash flows to net present value over the life of the underlying contract.

Interest income and expense also include fee and commission income and expense in respect of loans and advances to customers or borrowings from other banks, premium or discount amortisation, and other differences between the initial carrying amount of an interest-bearing financial instrument and its value at maturity, recognised on an effective interest basis.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the expected life of the financial instrument. The effective interest rate is the rate that discounts estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank does not consider future credit losses. The calculation includes all fees and percentage points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

3.2 Fee and commission income and expense

Fees and commissions mainly comprise fees related to domestic and foreign payments, the issue of guarantees and letters of credit and fees for credit risk analysis services, and are recognised in the income statement upon performance of the relevant service, unless they have been included in the effective interest calculation.

Loan commitment fees for loans that are likely to be drawn down are deferred and recognised as an adjustment to the effective interest rate on the loan. Commitment fees in relation to facilities where draw down is not probable are recognised over the term of the commitment. Other service fees are recognised based on the applicable service contracts.

3.3 Net trading income from dealing in foreign currencies

This category includes spreads earned from foreign exchange trading.

3.4 Net income from investment securities

This category includes gains and losses from disposals of available-for-sale financial assets and financial assets at fair value through profit or loss, and dividend income.

Dividend income on equity securities is credited to the income statement when the right to receive the dividend is established. There was no dividend income recognised in 2013 and 2012.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.5 Foreign currency translation

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

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security, and other changes in the carrying amount of the security. The translation differences are recognised in the income statement as part of the foreign exchange gains or losses on the revaluation of monetary assets and liabilities presented within operating expenses in the income statement.

3.6 Employee benefits

Defined pension contributions

The Bank has obligations for defined contributions to pension funds on a mandatory, contractual basis. The Bank has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due.

Provisions for retirement benefits and jubilee awards

In calculating provisions for retirement benefits and jubilee awards, the Bank discounts expected future cash outflows in respect of these liabilities using the discount rate which, in opinion of the Bank's management, best represents the time value of money.

3.7 Lease payments

Payments made by the Bank as lessee under operating leases are recognised in statement of comprehensive income on a straight-line basis over the term of the lease.

3.8 Financial instruments

Classification

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

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

A) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets which are classified as held for trading or on initial recognition designated by the Bank as at fair value through profit or loss. The Bank does not apply hedge accounting.

As stated above this category has two sub-categories: financial instruments held for trading, and those designated by management as at fair value through profit or loss at inception. Trading assets are those assets that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

The Bank designates financial assets at fair value through profit or loss when either:

- the assets are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise; or
- the asset contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Financial instruments at fair value through profit or loss include investments in investment fund units.

At the reporting date the Bank had no financial liabilities measured at fair value through profit or loss.

B) Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified in any of the other categories. Financial assets designated as available for sale are intended to be held for an indefinite period of time, but may be sold in response to needs for liquidity or changes in interest rates or foreign exchange rates. Available-for-sale financial assets include equity securities.

C) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the intention and ability to hold to maturity. These include Ministry of Finance treasury bills and corporate bills of exchange.

D) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money to a debtor with no intention of trading with the receivable and include loans and advances to banks, loans and advances to customers.

E) Other financial liabilities

Other financial liabilities comprise all financial liabilities of the Bank which are not held for trading or designated at fair value through profit or loss. After initial measurement all such Bank's financial liabilities are subsequently measured at amortised cost.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

Recognition and derecognition

Purchases and sales of financial instruments held to maturity, available for sale and financial assets at fair value through profit or loss are recognised on the settlement date, which is the date when the financial instrument is delivered to or transferred from the Bank. Loans and receivables and other financial liabilities are recognised when funds are disbursed to customers and when funds are received from lenders.

The Bank derecognises financial instruments (in full or part) when the rights to receive cash flows from the financial instrument have been realised, surrendered, expired or when the Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a ‘pass–through’ arrangement and has transferred substantially all the risks and rewards of the asset.

The Bank derecognises financial liabilities only when the financial liability ceases to exist, i.e. when it is discharged, cancelled or has expired. If the terms of a financial liability change, the Bank will cease recognising the liability and will immediately recognise a new financial liability, with new terms and conditions.

Initial and subsequent measurement

Financial assets and liabilities are recognised initially at their fair value plus, in the case of a financial asset or financial liability which is not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset or issuance of financial liability.

After initial recognition, the Bank measures financial assets at fair value through profit or loss and available-for-sale financial assets at their fair value, without any deduction for selling costs. Equity instruments classified as available for sale that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are stated at cost less impairment.

Loans and receivables and held-to-maturity investments and other financial liabilities are measured at amortised cost using the effective interest method.

Gains and losses

Gains and losses arising from a change in the fair value of the financial assets at fair value through profit or loss are recognised in the income statement.

Gains or losses arising from a change in the fair value of available-for-sale monetary assets are recognised directly in a fair value reserve within equity (other comprehensive income). Impairment losses, foreign exchange gains and losses, interest income and amortisation of premium or discount on available-for-sale monetary assets are recognised in the income statement. Foreign exchange differences on equity instruments are part of the fair value of these instruments and are recognised in a fair value reserve within equity (other comprehensive income).

Dividend income is recognised in the income statement. Upon sale or other derecognition of available-for-sale assets, any cumulative gains or losses on the instrument are transferred to the income statement.

Gains or losses arising from financial instruments carried at cost or amortised cost may also be recognised in the income statement when a financial instrument is derecognised or when its value is impaired.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

Fair value measurement principles

The fair values of quoted investments are based on current closing bid prices.

Impairment of financial assets

Impairment of financial assets identified as impaired

A) Financial assets carried at amortised cost

At each reporting date the Bank assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a “loss event”) and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about the following loss events:

I) significant financial difficulty of the borrower or issuer;
II) a breach of contract, such as a default or delinquency in interest or principal payments by a borrower;
III) the Bank granting to the borrower, for economic or legal reasons relating to the borrower’s financial difficulty, a concession that it would not otherwise consider;
IV) it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
V) the disappearance of an active market for the financial asset because of financial difficulties; or
VI) Observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows discounted at the financial asset’s original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan and receivable or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

Impairment of financial assets identified as impaired (continued)

Financial assets are tested for impairment on an individual basis. Those individually significant assets which are not impaired are included in the basis for collective impairment assessment.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Bank's rating process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be objectively linked to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

When a loan is uncollectible, it is written off against the related impairment allowance account. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised as a reversal of impairment losses in the income statement.

Renegotiated loans
Where possible, the bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

B) Financial assets carried at fair value

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity or debt investments classified as available for sale, a significant or prolonged decline in the fair value of the investment below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available for sale financial assets, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss, is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity securities are not subsequently reversed through the income statement, but all value increases until the final sales are recognised in equity.

If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss. Changes in impairment provisions attributable to the time value of money are reflected as a component of interest income. The Bank had no financial assets carried at fair value classified as available for sale at the balance sheet date.

C) Financial assets carried at cost

These include equity securities classified as available for sale for which there is no reliable fair value. The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. If such indication exists, impairment loss is recognised in income statement.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

Impairment of financial assets not identified as impaired

In addition to the above described impairment losses on financial assets identified as impaired, the Bank recognises impairment losses, in income, on all on- and off-balance-sheet credit risk exposures not identified as impaired using the rate of 1% in accordance with the specific accounting regulations of the Croatian National Bank.

Specific instruments

A) Debt securities

Debt securities are classified as held-to-maturity investments.

B) Loans and advances to banks

Loans and advances to banks are classified as loans and receivables.

C) Loans and advances to customers

Loans and advances to customers are classified as loans and receivables and are presented net of impairment allowances to reflect the estimated recoverable amounts.

D) Equity securities

Equity securities are classified as available for sale and are stated at cost, less impairment, in the absence of any reliable measure of fair value. There is no active market for these instruments.

E) Investments in investment funds

Investments in investment funds are classified as financial assets at fair value through profit or loss and are carried at current fair value. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable (i.e. similar) assets, liabilities or a group of assets and liabilities, such as a business

F) Cash and cash equivalents

Cash and cash equivalents as referred to in the cash flow statement comprises cash on hand, non–restricted current accounts with central banks and amounts due from banks available on demand or with an original maturity of three months or less.

G) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value, less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between proceeds (net of transaction costs) and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

H) Current accounts and deposits from banks and customers

Current accounts and deposits are classified as other liabilities and initially measured at fair value less transaction costs, and subsequently measured at amortised cost (using the effective interest method).

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.8 Financial instruments (continued)

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amounts are reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions, such as the Bank's trading activity.

3.9 Property and equipment

Property and equipment are tangible items that are held for use in the supply of services or for administrative purposes. Property and equipment are measured at cost less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Land and assets under development are not depreciated. Depreciation of all other tangible assets is recognised in income statement on a straight-line basis over their estimated useful lives as follows:

Buildings	40 years
IT equipment	4 years
Office furniture and other equipment	5-10 years

Depreciation methods and the assets' useful lives are reassessed, and adjusted if appropriate, at each reporting date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in the income statement.

3.10 Intangible assets

Intangible assets acquired by the Bank are measured at cost less accumulated amortisation and impairment losses.

Expenditure on development activities are capitalised if all of the requirements of International Accounting Standard 38 "*Intangible Assets*" are satisfied. Intangible assets are amortised on a straight-line basis over their estimated useful economic lives as follows:

Software	4 years
Leasehold improvements	5 years or during the lease period

The assets' useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.11. Assets acquired in lieu of uncollected receivables

The Bank regularly assesses the marketability of assets acquired in lieu of uncollected receivables and only marketable assets, the value of which can be measured reliably, are recognised as assets in the statement of financial position. The Bank's intention is mainly to sell such assets, however, in certain limited cases they may end up being used or rented out by the Bank if there is no demand for sale.

3.12 Income tax

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to other comprehensive income items, in which case it is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or non-current liabilities.

3.13 Impairment of property and equipment and intangible assets

Assets that have an indefinite useful life are not subject to amortisation and depreciation and are tested at least annually for impairment. At the balance sheet date the Bank did not have such assets. Assets that are subject to amortisation and depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets still not brought into use are reviewed at each reporting date. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount of property and equipment and intangible assets is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit.

Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.14 Provisions for liabilities and charges

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made, or as required by the law in the case of provisions for unidentified impairment of off-balance-sheet credit risk exposures, as previously referred to in Note 3.8 *"Financial instruments"*.

Provisions for liabilities and charges are maintained at the level which the Bank's management considers sufficient for absorption of incurred losses. The management determines the sufficiency of provisions on the basis of insight into specific items, current economic circumstances, risk characteristics of certain transaction categories, as well as other relevant factors.

Provisions are released only for items for which provisions are recognised at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

3.15 Issued share capital

Issued share capital represents the nominal value of paid-in ordinary shares classified as equity and is denominated in HRK.

Dividends are recognised as a liability in the period in which they are declared.

3.16 Retained earnings

Any profit or loss for the year is included in retained earnings. Appropriations from retained earnings such as dividends and transfers to other reserves are recognised when approved by shareholders.

3.17 Off-balance-sheet commitments and contingent liabilities

In the ordinary course of business, the Bank enters into credit-related commitments which are recorded in off-balance-sheet accounts and primarily comprise guarantees, letters of credit and undrawn loan commitments. Such financial commitments are recorded in the Bank's balance sheet if and when they become payable.

3.18 Managed funds for and on behalf of third parties

The Bank manages funds for and on behalf of corporate and retail customers. These amounts do not represent the Bank's assets and are excluded from the balance sheet. For the services rendered the Bank charges a fee.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

3.19 Changes in disclosures and restatements in financial statements

Certain balances included in the corresponding figures have been reclassified to conform to the current year presentation. Such reclassifications, in accordance with IAS 1.38, were carried out in order to enhance inter-period comparability of information and comprise the following changes. These change had only reclassification effect on the financial statements.

Position in 2012 financial statements	Reclassification to new position in 2013 financial statements	Balance in 2012 financial statements (in HRK thousand)	Change	2012 balance in financial statements for 2013 after reclassification
Other liabilities	Loans and advances to customers	17,852	(2,539)	15,313

NOTE 4 – NET INTEREST INCOME

	2013	2012
	(in thousands of HRK)	
a) Interest and similar income – analysis by source		
Companies	44,437	43,723
Individuals	4,570	3,719
State and public sector	1,392	2,029
Banks and other financial institutions	353	502
Other organisations	726	933
	51,478	**50,906**
b) Interest and similar income – analysis by product		
Loans and advance to customers	47,180	46,952
Debt securities and bills of exchange	3,945	3,452
Loans and advances to banks and other financial institutions	353	502
	51,478	**50,906**

	2013	2012
	(in thousands of HRK)	
c) Interest expense and similar charges – analysis by source		
Companies	8,561	11,009
Individuals	6,154	5,059
Banks	4,089	6,073
Other organisations	11	14
	18,815	**22,155**
d) Interest expense and similar charges – analysis by product		
Deposits from companies and other organisations	8,572	11,023
Deposits from individuals	6,154	5,059
Borrowings and deposits from banks	4,089	6,073
	18,815	**22,155**

NOTE 5 – NET FEE AND COMMISSION INCOME

	2013	2012
	(in thousands of HRK)	
a) Fee and commission income		
Domestic payment transactions	3,456	3,392
International payment transactions	616	713
Guarantees and letter of credits given	1,071	951
Other	15	11
	5,158	**5,067**
b) Fee and commission expense		
Domestic payment transactions	1,376	1,479
International payment transactions	77	78
Other	-	61
	1,453	**1,618**

NOTE 6 – NET INCOME FROM INVESTMENT SECURITIES

	2013	2012
	(in thousands of HRK)	
Realised gain on disposal of financial assets at fair value through profit or loss	568	316
	568	**316**

NOTE 7 – OTHER OPERATING INCOME

	2013	2012
	(in thousands of HRK)	
Recharged operating expenses to BKS AG	463	530
Net foreign exchange loss from translation of monetary assets and liabilities	(348)	(377)
Other income	495	306
	610	**459**

NOTE 8 – OTHER IMPAIRMENT LOSSES AND PROVISIONS

	2013	2012
	(in thousands of HRK)	
Increase/(release)in provisions for off-balance-sheet exposures (Note 24)	304	16
Increase in provisions for severance payments and jubilee awards (Note 24)	61	711
Impairment loss on other assets (Note 20)	329	1,915
Impairment loss on available for sale financial assets (Note 16)	200	100
	894	**2,742**

NOTE 9 – OPERATING EXPENSES

	2013	2012
	(in thousands of HRK)	
Personnel expenses	13,330	13,119
Professional services and material costs	3,855	4,405
Depreciation and amortisation	4,329	4,975
Software maintenance costs	4,219	4,100
Rent expenses	1,152	1,662
Administration and marketing expenses	1,347	1,499
Savings deposit insurance expenses	1,054	1,253
Other	951	821
	30,237	**31,834**

Personnel expenses include HRK 2,115 thousand (2012: HRK 2,103 thousand) of defined pension contributions payable into obligatory pension plans. Contributions are calculated as a percentage of employees’ gross salaries.

During 2013, the Bank had 62 employees on average (2012: 62 employees).

NOTE 10 – INCOME TAX

a) Income tax recognised in the income statement

	2013	2012
	(in thousands of HRK)	
Current tax	-	-
Deferred tax	168	217
Income tax benefit	**168**	**217**

b) Movement in deferred tax asset

	2012	Charged to income statement	2013
		(in thousands of HRK)	
Deferred tax assets			
Provisions for severance payments and jubilee awards and unused holiday accrual	352	16	368
Deferred fee and interest income	526	152	678
Total deferred tax assets	**878**	**168**	**1.046**

	2011	Charged to income statement	2012
		(in thousands of HRK)	
Deferred tax assets			
Provisions for severance payments and jubilee awards and unused holiday accrual	210	142	352
Deferred fee and interest income	451	75	526
Total deferred tax assets	**661**	**217**	**878**

NOTE 10 – INCOME TAX (continued)

c) Reconciliation of the profit before tax and income tax expense

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

	2013	2012
	(in thousands of HRK)	
Profit before income tax	(8,879)	(5,551)
Income tax at 20% (2012: 20%)	(1,776)	(1,110)
Non-deductible expenses	802	851
Tax exempt income	(553)	(492)
Utilisation of tax losses	-	-
Income tax benefit	**(1,527)**	**(751)**
Effective income tax rate	-	-

d) Tax losses carried forward

A tax loss may be carried forward for five years subsequent to the year in which it was incurred by the Bank. The availability of tax losses available for offset against taxable income in future periods, calculated at the tax rate of 20% enacted at the reporting date, subject to review by Ministry of Finance, is as follows:

	2013	2012
	(in thousands of HRK)	
No more than 1 year	-	-
No more than 2 years	-	-
No more than 3 years	-	-
No more than 4 years	(751)	-
No more than 5 years	(1,527)	(751)
Total net tax losses carried forward not recognised as deferred tax asset	**(2,278)**	**(751)**

The deferred tax asset in respect of tax losses carried forward is not recognised as it is not known with sufficient degree of certainty whether there will be enough taxable base available in near future for the utilisation.

NOTE 11 – CASH AND CASH EQUIVALENTS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Cash in hand	6,373	5,160
Current accounts with other banks	101,392	95,878
Current accounts with the Croatian National Bank	63,348	22,560
	171,113	**123,598**

NOTE 12 – OBLIGATORY RESERVE WITH THE CROATIAN NATIONAL BANK

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Obligatory reserve		
- in kuna	69,315	79,070
- in foreign currency	15,078	15,939
	84,393	**95,009**

The CNB determines the requirement for banks to calculate an obligatory reserve, which is required to be deposited with the CNB and held in the form of other liquid receivables.

The obligatory reserve requirement as of 31 December 2013 amounted to 12% (in 2012: 13.5%) of kuna and foreign currency deposits, borrowings and issued debt securities.

As of 31 December 2013, the required rate of maintenance of the kuna obligatory reserve with the CNB amounted to 70% (2012: 70%), while the remaining 30% (2012: 30%) had to be held in the form of other liquid receivables. These ratios include the part of foreign currency obligatory reserve required to be held in HRK (see below).

At least 60% (2012: 60%) of the obligatory reserve calculated on foreign currency liabilities must be deposited with the CNB, while the remaining 40% (2012: 40%) (or less to the extent that the amount deposited with the CNB exceeds 60%) must be held in the form of other liquid receivables, after adjusting for the obligatory reserve requirement arising from foreign currency funds from non-residents and related parties (which is required to be held in full with the CNB). Since 14 January 2009, 75% of the obligatory reserve arising from foreign currency is required to be held in HRK and is added to the kuna part of the obligatory reserve.

NOTE 13 – LOANS AND ADVANCES TO BANKS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Domestic banks	4,218	21,115
Foreign banks	79,699	82,512
Impairment allowance	(4,104)	(264)
	79,813	**103,363**

The movements in impairment allowances for loans and advances to banks:

	2013	2012
	(in thousands of HRK)	
Balance at 1 January	**264**	**299**
Impairment losses	3,840	17
Reversal of impairment losses	-	(52)
Movement of impairment allowance recognised in income statement	***3,840***	***(35)***
Balance at 31 December	**4,104**	**264**

The increase in impairment allowance in the amount of HRK 3,840 thousand in 2013 relates to impairment loss on deposit held with bank that went into liquidation and which is recognized as loan loss provision

NOTE 14 – LOANS AND ADVANCES TO CUSTOMERS

a) Analysis by recipient

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Companies and similar organisations	724,696	689,845
Individuals and unincorporated businesses	82,643	70,096
Total loans	**807,339**	**759,941**
Portfolio based allowance for unidentified losses	(11,351)	(9,651)
Impairment allowance for identified losses	(18,095)	(7,767)
Total impairment allowance	**(29,446)**	**(17,418)**
	777,893	**742,523**
Total impairment allowance as a percentage of gross loans and advances to customers	3.65%	2.29%

b) Movements in impairment allowance for loans and advances to customers:

	2013	2012
	(in thousands of HRK)	
Balance at 1 January	**17,418**	**12,721**
Impairment losses	15,616	15,361
Reversal of impairment losses	(3,343)	(10,324)
Impairment losses on loans and advances to customers recognised in the income statement	**12,273**	**5,037**
Amounts written off	(245)	(340)
Balance at 31 December	**29,446**	**17,418**

NOTE 15 – FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Investments in investment funds, quoted	42,780	45,772
	42,780	**45,772**

NOTE 16 – AVAILABLE–FOR–SALE FINANCIAL ASSETS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Unlisted equity securities	2,083	2,083
Impairment allowance	(1.007)	(807)
	1,076	**1,276**

Movement in impairment allowance for available-for-sale investment securities:

	2013	2012
	(in thousands of HRK)	
Balance at 1 January	**807**	**707**
Charge for the year (note 8)	200	100
Balance at 31 December	**1,007**	**807**

NOTE 17 – HELD–TO–MATURITY INVESTMENTS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Unlisted		
Republic of Croatia Ministry of Finance treasury bills	-	18,268
Corporate bills of exchange	49,269	30,425
	49,269	**48,693**

NOTE 18 – PROPERTY AND EQUIPMENT

(in thousands of HRK)	**Buildings**	**IT equipment**	**Office furniture and other equipment**	**Other**	**Assets acquired but not brought into use**	**TOTAL**
Cost						
At 1 January 2013	**26,157**	**5,456**	**4,720**	**337**	**40**	**36,710**
Additions	-	159	6	-	-	165
Transfers from asset under construction	7	-	28	-	(28)	7
Disposals	-	(548)	(82)	-		(630)
At 31 December 2013	**26,164**	**5,067**	**4,672**	**337**	**12**	**36,252**
Accumulated depreciation and impairment losses						
At 1 January 2013	5,598	4,604	3,229	71	-	13,502
Charge for the year	653	352	447	7	-	1,459
Disposals	-	(548)	(82)	-	-	(630)
At 31 December 2013	**6,251**	**4,408**	**3,594**	**78**	**-**	**14,331**
Carrying value						
1 January 2013	**20,559**	**852**	**1,491**	**266**	**40**	**23,208**
31 December 2013	**19,913**	**659**	**1,078**	**259**	**12**	**21,921**
Cost						
At 1 January 2012	**25,055**	**5,150**	**4,705**	**337**	**1,465**	**36,712**
Additions	-	-	-	-	510	510
Transfers	1,102	814	19	-	(1,935)	-
Disposals	-	(508)	(4)	-	-	(512)
At 31 December 2012	**26,157**	**5,456**	**4,720**	**337**	**40**	**36,710**
Accumulated depreciation and impairment losses						
At 1 January 2012	**4,947**	**4,637**	**2,697**	**62**	**-**	**12,343**
Charge for the year	651	475	536	9	-	1,671
Disposals	-	(508)	(4)	-	-	(512)
At 31 December 2012	**5,598**	**4,604**	**3,229**	**71**	**-**	**13,502**
Carrying value						
1 January 2012	**20,108**	**513**	**2,008**	**275**	**1,465**	**24,369**
31 December 2012	**20,559**	**852**	**1,491**	**266**	**40**	**23,208**

Depreciation charge for the year is included within operating expenses in the income statement (Note 9).

NOTE 19 – INTANGIBLE ASSETS

(in thousands of HRK)	Software	Leasehold improvements	Assets acquired but not yet brought into use	TOTAL
Cost				
At 1 January 2013	**23,407**	**1,709**	**110**	**25,226**
Additions	1,262	-	1,273	2,535
Transfers	-	-	-	
At 31 December 2013	**24,669**	**1,709**	**1,383**	**27,761**
Accumulated amortisation and impairment losses				
At 1 January 2013	**17,769**	**1,286**	**-**	**19,055**
Charge for the year	2,557	313	-	**2,870**
At 31 December 2013	**20,326**	**1,599**	**-**	**21,925**
Carrying value				
1 January 2013	**5,638**	**423**	**110**	**6,171**
31 December 2013	**4,343**	**110**	**1,383**	**5,836**

Cost				
At 1 January 2012	**20,095**	**1,709**	**1,104**	**22,908**
Additions	-	-	2,318	2,318
Transfers	3,312	-	(3,312)	-
At 31 December 2012	**23,407**	**1,709**	**110**	**25,226**
Accumulated amortisation and impairment losses				
At 1 January 2012	**14,807**	**944**	**-**	**15,751**
Charge for the year	2,962	342	-	3,304
At 31 December 2012	**17,769**	**1,286**	**-**	**19,055**
Carrying value				
1 January 2012	**5,288**	**765**	**1,104**	**7,157**
31 December 2012	**5,638**	**423**	**110**	**6,171**

Amortisation charge for the year is included within operating expenses in the income statement (Note 9).

NOTE 20 – OTHER ASSETS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Accrued interest – not yet due	3,891	3,901
Accrued interest – due	6,039	5,534
Accrued fees	622	671
Receivable for commission for credit risk analysis	-	-
Property in lieu of uncollected receivables (real estates)	693	693
Other	863	664
	12,108	**11,463**
Impairment allowance against accrued interest	(3,514)	(3,181)
Impairment allowance against accrued fees	(260)	(264)
	(3,774)	**(3,445)**
	8,334	**8,018**

The movements in impairment allowances for other assets are as follows:

	2013	2012
	(in thousands of HRK)	
Balance at 1 January	**3,445**	**1,530**
Reversal of impairment losses	(404)	(1,650)
Impairment losses	733	3,565
Movement of impairment allowance recognised in income statement (note 8)	***329***	***1,915***
Balance at 31 December	**3,774**	**3,445**

Net movement of impairment allowance on other assets is recognised within “Other impairment losses and provisions” in the income statement (Note 8).

NOTE 21 – DEPOSITS FROM BANKS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Current accounts	77	214
Term deposits	-	21,905
	77	**22,119**

NOTE 22 – DEPOSITS FROM CUSTOMERS

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Companies and similar organisations		
- current accounts	67,513	65,504
- term deposits	284,783	299,113
Individuals and unincorporated businesses		
- current accounts and demand deposits	72,134	63,453
- term deposits	193,241	101,284
	617,671	**529,354**

NOTE 23 – BORROWINGS

In accordance with their terms, borrowings from the Croatian Bank for Reconstruction and Development ("HBOR") are used to fund loans to customers for eligible construction and development projects at preferential interest rates.

Borrowings from Croatian Bank for Reconstruction and Development

Currency	Principal '000	Maturity	Interest rate	31 December 2013	31 December 2012
HRK (EUR currency clause)	1,093	2013	2.00%	-	824
HRK (EUR currency clause)	1,590	2014	2.00%	2,429	4,799
HRK (EUR currency clause)	209	2014	2.00%	53	262
HRK (EUR currency clause)	805	2013	Euribor + 1.70%	-	217
HRK (EUR currency clause)	680	2017	Euribor + 1.70%	1,961	2,533
HRK (EUR currency clause)	41	2018	4.00%	-	173
HRK (EUR currency clause)	2,200	2023	Euribor + 1.89%	-	13,088
HRK (EUR currency clause)	300	2013	4.00%	-	242
HRK (EUR currency clause)	334	2018	2.75%	1,596	1,891
HRK (EUR currency clause)	276	2020	3.00%	1,422	1,613
HRK (EUR currency clause)	993	2020	3.00%	6,636	7,493
HRK (EUR currency clause)	275	2016	5.00%	1,446	1,949
HRK	12,058	2016	5.00%	6,531	9,546
HRK (EUR currency clause)	104	2016	3.00%	477	629
HRK (EUR currency clause)	239	2018	3.00%	1,819	1,174
HRK (EUR currency clause)	44	2019	2.00%	336	-
				24,706	**46,433**

Borrowings from foreign banks - BKS Bank AG Klagenfurt, Austria

Currency	Principal '000	Maturity	Interest rate		
EUR		2013	Euribor + 0.50%	-	173.549
EUR	32,661	2014	Euribor + 0.50%	248.223	116.957
EUR	11,000	2015	Euribor + 0.50%	84.014	83.002
EUR	6,000	2016	Euribor + 0.50%	45.826	-
				378.063	**373.508**
Total borrowings				**402.769**	**419.941**

The amount of undrawn borrowing facilities from BKS AG available on the balance sheet date 31 December 2013 is HRK 266,250 thousand. Maturity is not defined and the cancellation period is 5 days (if certain terms are fulfilled).

NOTE 24 – PROVISIONS FOR LIABILITIES AND CHARGES

(in thousands of HRK)	Portfolio based provision for off-balance sheet exposures	Provision for identified off-balance sheet exposures	Total provisions for off-balance sheet exposures	Provisions for severance payments and jubilee awards	Total
Balance at 1 January 2013	**787**	**-**	**787**	**1,747**	**2,534**
Net increase/(release) in income statement	304	-	304	61	365
Balance at 31 December 2013	**1,091**	**-**	**1,091**	**1,808**	**2,899**
Balance at 1 January 2012	**717**	**54**	**771**	**1,036**	**1,807**
Net increase/(release) in income statement	70	(54)	16	711	727
Balance at 31 December 2012	**787**	**-**	**787**	**1,747**	**2,534**

Net increase/decrease in provisions for liabilities and charges is recognised within "Other impairment losses and provisions" in the income statement (Note 8).

NOTE 25 – OTHER LIABILITIES

	31 December 2013	**31 December 2012**
	(in thousands of HRK)	
Interest payable – not yet due	13,150	9,631
Payments in advance by customers	2,465	1,476
Payables to suppliers	1,152	1,786
Accrued salary expenses	1,030	1,012
Interest payable – due	262	213
Items in transfer	192	108
Unused holiday accrual	177	156
Fees payable	113	104
Other liabilities	980	827
	19,521	**15,313**

NOTE 26 – ISSUED SHARE CAPITAL

	Total share capital
	(in thousands of HRK)
As at 1 January 2013	200,000
Increase in share capital	-
As at 31 December 2013	**200,000**

As at 31 December 2013 the registered, subscribed and fully paid capital comprises 2,000,000 ordinary shares (2012: 2,000,000) with a nominal value of HRK 100 each (2012: HRK 100).

The shareholder structure of the Bank is:

	At 31 December 2013		At 31 December 2012	
	Number of shares issued	%	Number of shares issued	%
BKS Bank AG, Klagenfurt	2,000,000	100.00	2,000,000	100.00
Total	2,000,000	100.00	2,000,000	100.00

Dividends

Dividends payable are recognised as a liability after having been ratified at the Annual General Meeting. During 2013 and 2012 there were no dividend payments.

NOTE 27 – OTHER RESERVES, FAIR VALUE RESERVE AND RETAINED EARNINGS

a) Statutory reserve

A statutory reserve has been created in accordance with Croatian law, which requires 5% of the profit for the year to be transferred to this reserve until it reaches 5% of issued share capital. The statutory reserve, in the amount of up to 5% of issued share capital, can be used for the coverage of current and prior year losses

b) Retained earnings

Retained earnings comprise accumulated net profits and net losses of prior years.

NOTE 28 – CONCENTRATION OF ASSETS AND LIABILITIES

The significant amount of assets and liabilities of the Bank are concentrated on amounts due from and to the Republic of Croatia and to related parties of Republic of Croatia, as follows:

	Note	31 December 2013	31 December 2012
		(in thousands of HRK)	
Current accounts with the Croatian National Bank	11	63,348	22,560
Obligatory reserve with the Croatian National Bank	12	84,393	95,009
Republic of Croatia Ministry of Finance treasury bills	17	-	18,268
Accrued interest and other assets		349	165
Decreased by:			
Borrowings from Croatian bank for reconstruction and development	23	(24,706)	(46,433)
Other liabilities		(570)	(502)
		122,814	**89,067**

As at 31 December 2013 total exposure towards the Republic of Croatia amounted to 9.88% of total assets (2012: 7.43%).

NOTE 29 – MANAGED FUNDS FOR AND ON BEHALF OF THIRD PARTIES

The Bank manages a number of loans on behalf of third parties in return for a fee. These assets are not the Bank's assets and are not recognised on the Bank's balance sheet.

Managed funds for and on behalf of third parties are as follows:

	31 December 2013	31 December 2012
	(in thousands of HRK)	
Assets		
Loans and advances to customers		
- individuals and unincorporated businesses	38	32
Interest receivable	8	1
	46	**33**
Liabilities		
Deposits from local government	38	32
Interest payable	8	1
	46	**33**

NOTE 30 – CONTINGENT LIABILITIES AND COMMITMENTS

Legal proceedings

As of 31 December 2013 there existed three legal proceedings outstanding against the Bank. in management opinion which was supported by external legal advice, no provision was recognised in financial statements.

Off-balance-sheet exposure

The following table indicates the contractual amounts of the Bank's off-balance-sheet financial instruments:

	31 December 2013	**31 December 2012**
	(in thousands of HRK)	
Guarantees and letters of credit	53,742	59,041
Commitments for facilities not withdrawn	55,312	27,363
	109,054	**86,404**

NOTE 31 – RELATED PARTY TRANSACTIONS

As at 31 December 2013 the sole shareholder of the Bank was Bank für Kaernten und Steiermark AG, Klagenfurt, Austria ("BKS Bank AG") who has multiple shareholders (there is no single majority shareholder with prevailing voting interest). The Bank considers that it has an immediate related party relationship with BKS Bank AG and its shareholders, subsidiaries and associates; the Supervisory and Management Board members and the Head of Corporate Department and the Zagreb Branch Director ("key management personnel"); close family members of key management personnel; and entities controlled, jointly controlled or significantly influenced by key management personnel and their close family members.

The Bank enters into a number of transactions with related parties in the normal course of business.

Parent bank

The Bank obtains borrowings and deposits and also places deposits and holds current accounts with the parent bank. As of 31 December 2013 the Bank had borrowings from the parent bank in the amount of HRK 378,063 thousand (2012: HRK 373,508 thousand) and deposits from the parent bank in the amount of HRK 77 thousand (2012: HRK 22,119 thousand). Total interest payable to the parent bank as at 31 December 2013 amounts to HRK 430 thousand (2012: HRK 416 thousand). During 2013, the Bank recorded HRK 2,786 thousand (2012: HRK 4,334 thousand) of interest expense, fee expenses in the amount of HRK 79 thousand (2012: HRK 61 thousand) and net foreign exchange loss in the amount of HRK 4,587 thousand (2012: HRK 1,388 thousand) in respect of borrowings and deposits received from the parent bank.

In addition, as of 31 December 2013 the Bank held current accounts in the amount of HRK 29,063 thousand (2012: HRK 13,865 thousand). Total interest receivable from the parent bank as at 31 December 2013 amounts to HRK 11 thousand (2012: HRK 11 thousand) and total interest income in 2013 amounted to HRK 0 thousand (2012: HRK 79 thousand).

In 2011 the Bank provided credit analysis services to the parent bank. During 2011 the Bank earned HRK 2,334 thousand from fee income for credit analysis services of which HRK 1,739 thousand was receivable as at 31 December 2011. In 2012 and 2013 the Bank provided no such services.

In addition, the Bank recognised other income of HRK 445 thousand (2012: HRK 555 thousand), of which HRK 35 thousand (2012: HRK 56 thousand) was receivable as at 31 December 2013, and other expense of HRK 448 thousand (2012: HRK 805 thousand).

Related companies

BKS Leasing Croatia d.o.o. is a related company which has deposits with the Bank in the amount of HRK 159,052 thousand as of 31 December 2013 (2012: HRK 112,894 thousand) upon which the Bank incurred interest payable in the amount of HRK 6,207 thousand (2012: HRK 3,119 thousand). In 2013 the Bank recorded interest expense in the amount of HRK 3,252 thousand (2012: HRK 3,065 thousand) in relation to deposits placed by BKS Leasing Croatia d.o.o., and other expense of HRK 78 thousand (2012: HRK 77 thousand).

NOTE 31 – RELATED PARTY TRANSACTIONS (continued)

Key management personnel

In 2013, the total remuneration of the Management Board was HRK 1,510 thousand (2012: HRK 1,467 thousand) and of other key management personnel was HRK 1,040 thousand (2012: HRK 1,007 thousand) and consisted of short-term benefits only. Out of these benefits, in 2013, the Bank made pension contributions into obligatory pension funds for Management Board in the amount of HRK 227 thousand (2012: HRK 240 thousand) and to other key management in the amount of HRK 192 thousand (2012: HRK 192 thousand). As of the date of approval of these financial statements by the Management Board, no management bonuses were accrued for.

The Bank has granted loans to key management personnel in the amount of HRK 1,274 thousand (2012: HRK 1,360 thousand) as at 31 December 2013. As a result, during 2013 the Bank recorded interest income in the amount of HRK 64 thousand (2012: HRK 52 thousand).

The Bank also has deposits from key management personnel in the amount of HRK 2,379 thousand (2012: HRK 2,710 thousand) as at 31 December 2013 on which it has recorded interest expense in the amount of HRK 116 thousand during 2013 (2012: HRK 72 thousand).

Companies under the significant influence of key management personnel and their close family members and Supervisory Board members

Mr Goran Rameša, President of the Management Board, is also the President of the Supervisory Board of the company Rapska plovidba d.d., Rab, which the Bank considers to be a related party. The Bank has granted loans to Rapska plovidba d.d., Rab in the amount of HRK 10,128 thousand (2012: HRK 11,549 thousand) and has recorded interest income in the amount of HRK 616 thousand during 2013 (2012: HRK 737 thousand). The Bank also has deposits from Rapska plovidba d.d. in the amount of HRK 89 thousand (2012: HRK 34 thousand) and as a result has recorded interest expense in the amount of HRK 7 thousand (2012: HRK 1 thousand).

Other companies under the significant influence of key management personnel are Konto d.o.o. and Darin d.o.o. The Bank has deposits from Konto d.o.o. and Darin d.o.o. The Bank also provides payment transaction services to these companies.

No fees to Supervisory Board members were paid during 2013 and 2012.

NOTE 31 – RELATED PARTY TRANSACTIONS (continued)

Key transactions with immediate related parties and related amounts arising from transactions with immediate related parties were as follows:

2013	Assets HRK'000	Liabilities HRK'000	Income HRK'000	Expense HRK'000
Key shareholder	29.110	378,570	445	7,901
BKS Bank AG, Klagenfurt				
Other related companies				
BKS Leasing Croatia d.o.o.	9	165,260	92	5,154
Key management personnel				
Management Board				
Short-term benefits (bonuses, salaries and fees)	-	118	-	1,510
Loans and deposits	-	2,297	1	114
Other key management personnel				
Short-term benefits (bonuses, salaries and fees)	-	86	-	1,040
Loans and deposits	1,274	82	63	2
Companies under the significant influence of key management personnel and their close family members and Supervisory Board members				
Rapska plovidba d.d., Rab	10,218	89	616	7
Other	-	178	5	1
Total	**40,611**	**546,680**	**1,222**	**15,729**

2012	Assets HRK'000	Liabilities HRK'000	Income HRK'000	Expense HRK'000
Key shareholder	13,932	396,043	634	6,588
BKS Bank AG, Klagenfurt				
Other related companies				
BKS Leasing Croatia d.o.o.	9	116,013	97	3,176
Key management personnel				
Management Board				
Short-term benefits (bonuses, salaries and fees)	-	113	-	1,467
Loans and deposits	21	2,681	1	72
Other key management personnel				
Short-term benefits (bonuses, salaries and fees)	-	81	-	1,007
Loans and deposits	1,339	29	52	-
Companies under the significant influence of key management personnel and their close family members and Supervisory Board members				
Rapska plovidba d.d., Rab	11,549	34	737	1
Other	-	270	5	1
Total	**26,850**	**515,264**	**1,526**	**12,312**

NOTE 32– FINANCIAL RISK MANAGEMENT

This section provides details of the Bank's exposure to risks and describes the methods used by management to identify, measure and manage risks in order to safeguard capital. The most important types of financial risks to which the Bank is exposed are credit risk, liquidity risk, market risk and operational risk. Market risk includes currency risk, interest rate risk and price risk.

An integrated system of risk management is being established by introducing a set of policies and procedures, determining the limits of risk levels acceptable to the Bank and monitoring their implementation. Methodologies and models for managing operational risk are being developed.

a) Credit risk

The Bank is subject to credit risk through its lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties.

The risk that counterparties to financial instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Bank deals with counterparties of good credit standing, and when appropriate, obtain collateral.

In addition to the carrying amounts of the assets in the statement of financial position, the Bank is exposed to off-balance-sheet credit risk through commitments to extend credit and guarantees issued (refer to Note 30).

Exposure to credit risk is managed in accordance with the Bank's policies. Credit exposures to portfolios and individual client/group exposures are reviewed on a regular basis taking into account set limits. Any proposed substantial increases in credit exposure are reviewed by an appropriate decision-making level. The Management Board is regularly informed of all significant changes in quantity and quality of the portfolio, including proposed impairment losses. Credit risk assessment is continuously monitored and reported, thus enabling the early identification of impairment in the credit portfolio. The Management Board believes that the Bank continually applies prudent methods in the process of credit risk assessment.

A significant part of credit risk exposures is secured with collateral in the form of cash, guarantees, mortgages and other forms of security.

Geographic concentrations of assets, liabilities and off balance sheet items

	31 December 2013			**31 December 2012**		
(in thousands of HRK)	**Assets**	**Liabilities**	**Off balance sheet items**	**Assets**	**Liabilities**	**Off balance sheet items**
Croatia	1,071,616	617,078	109,054	1,043,357	564,962	86,404
European Union	171,858	423,303	-	155,152	422,109	-
Other	-	2,556	-	-	2,190	-
	1,243,474	**1,042,937**	**109,054**	**1,198,509**	**989,261**	**86,404**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

a) Credit risk (continued)

Industry segmentation of loans and advances:

(in thousands of HRK)	**31 December 2013**	**%**	**31 December 2012**	**%**
Gross balances before impairment allowances				
Trade and commerce	213,470	26	229,231	30
Construction	228,114	28	214,535	28
Metallurgy	36,700	5	34,209	5
Transport, warehousing and public services	47,288	6	21,420	3
Energy	-	-	3,018	0
Shipbuilding	516	0	15,692	2
Services	143,745	18	149,641	20
Individuals and unincorporated businesses	82,627	10	70,102	9
Miscellaneous	54,879	7	22,093	3
	807,339	**100**	**759,941**	**100**

The following table shows maximum exposure to credit risk relating to balance sheet assets and off-balance sheets items

(in thousands of HRK)	**Note**	**31 December 2013**	**31 December 2012**
ASSETS			
Current accounts with CNB and other banks	11	164,740	118,438
Obligatory reserve with the Croatian National Bank	12	84,393	95,009
Loans and advances to banks	13	79,813	103,363
Loans and advances to customers	14a	777,893	742.523
Financial assets at fair value through profit or loss	15	42,780	45,772
Held-to-maturity investments	17	49,269	48,693
Accrued interest and fees, net	20	6,778	6,661
Total credit risk exposed assets		**1,205,666**	**1,160,459**
OFF-BALANCE SHEET			
Guarantees and letters of credit	30	53,742	59,041
Commitments for facilities not withdrawn	30	55,312	27,363
		109,054	**86,404**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

a) Credit risk (continued)

The above table represents the maximum direct credit risk exposure of the Bank as at 31 December 2013 and 31 December 2012, without taking into account of any collateral held or other credit enhancements attached or exposure to investment funds investing in debt instruments. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the balance sheet.

Total collaterals available to reduce the credit risk as at 31 December 2013 and 31 December 2012:

(in HRK thousands)	**31 December 2013**	**31 December 2012**
Real estates	23,167	23,167
Deposits	103,423	125,340
Shares	15,691	13,638
Guarantees	1,919,173	1,680,285
Other	1,957	1,957
Total	**2,063,411**	**1,844,387**

Impairment losses

(in thousands of HRK)	**31 December 2013**		**31 December 2012**	
CNB rating	**Loans**	**Impairment allowance for identified losses**	**Loans**	**Impairment allowance for identified losses**
A	749,686	-	676.114	-
B	51,134	11,576	81,842	5,782
C	6,519	6,519	1,985	1,985
	807,339	**18,095**	**759.941**	**7,767**

The rate of impairment allowance on the non-performing loan portfolio (CNB Ratings B and C) is 31.39% (2012: 9.27%).

Total impairment allowance for loans and receivables is HRK 29,446 thousand (2012: HRK 17,418 thousand) of which HRK 18,095 thousand (2012: HRK 7,767 thousand), disclosed in the table above, represents specific impairment allowance and the remaining amount of HRK 11,351 thousand (2012: HRK 9,651 thousand) represents the general provision calculated on a portfolio basis for on-balance sheet exposures. The analysis by performance of loans and advances to customers net of specific impairment allowances is as follows:

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

a) Credit risk (continued)

Loans and advances to individuals and unincorporated business	**31 December 2013**	**31 December 2012**
	(in thousands of HRK)	
Gross		
Not due and not impaired	80,330	67.353
Not due and impaired	239	302
Due but not impaired	131	493
Due and impaired	1,943	1,948
	82,643	70.096
Impairment allowance for identified losses	(908)	(913)
Net loans and advances to individuals and unincorporated business	**81,735**	**69,183**

Loans and advances to companies	**31 December 2013**	**31 December 2012**
	(in thousands of HRK)	
Gross		
Not due and not impaired	659,467	578,652
Not due and impaired	11,377	23,179
Due but not impaired	9,758	29,616
Due and impaired	44,094	58,398
	724,696	689,845
Impairment allowance for identified losses	(17,187)	(6,854)
Net loans and advances to companies	**707,509**	**682,991**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

a) Credit risk (continued)

The table below represents the aging structure of past due but not impaired loans:

	Less than 1 month	1 to 3 months	3-12 months	> 12 months	Total
31 December 2013					
Companies	5,206	3,360	1,192	-	9,758
Individuals	110	20	1	-	131
Total	**5,316**	**3,380**	**1,193**	**-**	**9,889**
31 December 2012					
Companies	27,308	1,771	537	-	29,616
Individuals	110	383	-	-	493
Total	**27,418**	**2,154**	**537**	**-**	**30,109**

b) Liquidity risk

Liquidity risk arises in the general funding of the Bank’s activities and in the management of positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate timeframe. The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs and guarantees and other cash settled calls. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Management Board sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand. The Bank manages liquidity reserves daily, ensuring also accomplishment of all customer needs.

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

b) Liquidity risk (continued)

The table below analyses assets and liabilities of the Bank into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date, except for the obligatory reserve which is presented as maturing within one month. In addition, financial assets at fair value through profit or loss are presented as maturing within one month, and available-for-sale financial assets are presented as maturing in over 3 years.

(in thousands of HRK)	**Up to 1 month**	**1-3 months**	**3-12 months**	**1 - 3 years**	**Over 3 years**	**Total**
As at 31 December 2013						
ASSETS						
Cash and cash equivalents	171,113	-	-	-	-	171,113
Obligatory reserve with CNB	84,393	-	-	-	-	84,393
Loans and advances to banks	60,337	19,476	-	-	-	79,813
Loans and advances to customers	102,926	35,866	182,328	122,419	334,354	777,893
Financial assets at fair value through profit or loss	42,780	-	-	-	-	42,780
Available-for-sale financial assets	-	-	-	-	1,076	1,076
Held-to-maturity investments	4,473	770	41,924	2,102	-	49,269
Property and equipment	-	-	-	-	21,921	21,921
Intangible assets	-	-	-	-	5,836	5,836
Deferred tax assets	-	-	-	1,046	-	1,046
Other assets	7,612	244	478	-	-	8,334
Total assets	**473,634**	**56,356**	**224,730**	**125,567**	**363,187**	**1,243,474**
LIABILITIES AND EQUITY						
Deposits from banks	77	-	-	-	-	77
Deposits from customers	157,736	77,888	255,290	40,039	86,718	617,671
Borrowings	559	27,761	228,634	139,762	5,999	402,715
Provisions for liabilities and charges	-	1,091	-	-	1,807	2,898
Other liabilities	7,238	4,120	6,866	709	642	19,575
Total equity	-	-	-	-	200,538	200,538
Total liabilities and equity	**165,610**	**110,860**	**490,790**	**180,510**	**295,704**	**1,243,474**
Net liquidity gap	**308,024**	**(54,504)**	**(266,060)**	**(54,943)**	**67,483**	**-**

NOTE 32 – FINANCIAL RISK MANAGEMENT (continued)

b) Liquidity risk (continued)

(in thousands of HRK)	**Up to 1 month**	**1-3 months**	**3-12 months**	**1 - 3 years**	**Over 3 years**	**Total**
As at 31 December 2012						
ASSETS						
Cash and cash equivalents	123,598	-	-	-	-	123,598
Obligatory reserve with CNB	95,009	-	-	-	-	95,009
Loans and advances to banks	90,993	7,923	2,288	2,159	-	103,363
Loans and advances to customers	129,664	46,909	246,609	104,829	214,512	742,523
Financial assets at fair value through profit or loss	45,772	-	-	-	-	45,772
Available-for-sale financial assets	-	-	-	-	1,276	1,276
Held-to-maturity investments	4,137	473	44,083	-	-	48,693
Property and equipment	-	-	-	-	23,208	23,208
Intangible assets	-	-	-	-	6,171	6,171
Deferred tax assets	-	-	-	878	-	878
Other assets	6,800	294	914	10	-	8,018
Total assets	**495,973**	**55,599**	**293,894**	**107,876**	**245,167**	**1,198,509**
LIABILITIES AND EQUITY						
Deposits from banks	214	-	21,905	-	-	22,119
Deposits from customers	158,758	97,949	221,595	9,231	41,821	529,354
Borrowings	991	24,168	159,335	216,757	18,690	419,941
Provisions for liabilities and charges	-	787	-	-	1,747	2,534
Other liabilities	7,525	3,083	3,800	698	207	15,313
Total equity	-	-	-	-	209,248	209,248
Total liabilities and equity	**167,488**	**125,987**	**406,635**	**226,686**	**271,713**	**1,198,509**
Net liquidity gap	**328,488**	**(70,388)**	**(112,741)**	**(118,813)**	**(26,546)**	**-**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

b) Liquidity risk (continued)

Analysis of the financial liabilities

The table below presents the maturity structure of the undiscounted liabilities taking into account the earliest possible repayment date. The Bank's financial liabilities without contracted maturity are treated as on demand liabilities.

31 December 2013

(in HRK thousand)	**Less than 1 month**	**1 to 3 months**	**3-12 months**	**1 to 3 years**	**More than 3 years**	**Total**
Financial liabilities						
Deposits from credit institutions	77	-	-	-	-	77
Deposits from customers	158,801	82,365	268,395	47,618	101,705	658,884
Borrowings	761	28,043	231,312	143,024	6,528	409,668
Total financial liabilities	159,639	110,408	499,707	190,642	108,233	1,068,629

31 December 2012

(in HRK thousand)	**Less than 1 month**	**1 to 3 months**	**3-12 months**	**1 to 3 years**	**More than 3 years**	**Total**
Financial liabilities						
Deposits from credit institutions	214	-	22,055	-	-	22,269
Deposits from customers	160,848	101,625	229,632	10,308	56,176	558,589
Borrowings	1,165	24,467	161,243	221,381	20,143	428,399
Total financial liabilities	162,227	126,092	412,93	231,689	76,319	1,009,257

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

b) Liquidity risk (continued)

The contractual maturity structure of the Bank's contingent liabilities and commitments

	Less than 1 month	1 to 3 months	3-12 months	1 to 3 years	More than 3 years	Total
31 December 2013						
Guarantees	9,091	12,323	23,363	7,009	1,650	53,436
Letters of credit	-	306	-	-	-	306
Revolving loans	11,033	-	-	-	-	11,033
Other frame loans	44,279	-	-	-	-	44,279
Total 2013	**64,403**	**12,629**	**23,363**	**7,009**	**1,650**	**109,054**
31 December 2012						
Guarantees	5,666	7,447	33,155	12,590	183	59,041
Letters of credit	-	-	-	-	-	-
Revolving loans	17,992	-	-	-	-	17,992
Other frame loans	9,371	-	-	-	-	9,371
Total 2012	**33,029**	**7,447**	**33,155**	**12,590**	**183**	**86,404**

NOTE 32 – FINANCIAL RISK MANAGEMENT (continued)

c) Currency risk

The Bank is exposed to currency risk through transactions in foreign currencies. Foreign currency exposure arises from credit, deposit-taking, investment and trading activities. It is monitored regularly, in accordance with legislation and internally set limits, for each currency and for the total balance sheet denominated in or linked to foreign currency.

The Bank manages its currency risk by setting principles and limits for foreign currency exposures and monitoring against these limits. The Bank directs its business activities towards trying to minimise the gap between assets and liabilities denominated in or linked to foreign currency, and maintaining the daily business activities within daily potential loss limits.

In measuring foreign currency exposure, the Bank relies on regulations prescribed by the CNB. In calculating the capital requirement for currency risk the standard method has been used in accordance with the CNB regulation on capital adequacy.

Due to the insignificant difference between financial assets and financial liabilities denominated and linked to EUR the sensitivity of change in HRK/EUR is not significant at the end of 2013 and 2012.

NOTE 32 – FINANCIAL RISK MANAGEMENT (continued)

c) Currency risk (continued)

Assets and liabilities are analysed by currency as follows:

(in thousands of HRK)	**EUR**	**EUR linked**	**USD**	**Other currencies**	**HRK**	**Total**
As at 31 December 2013						
ASSETS						
Cash and cash equivalents	100,472	-	2,745	1,603	66,293	171,113
Obligatory reserve with CNB	10,861	-	4,217	-	69,315	84,393
Loans and advances to banks	79,813	-	-	-	-	79,813
Loans and advances to customers	45,377	593,358	-	-	139,158	777,893
Financial assets at fair value through profit or loss	-	-	-	-	42,780	42,780
Available-for-sale financial assets	12	-	-	-	1,064	1,076
Held-to-maturity investments	-	-	-	-	49,269	49,269
Property and equipment	-	-	-	-	21,921	21,921
Intangible assets	-	-	-	-	5,836	5,836
Deferred tax assets	-	-	-	-	1,046	1,046
Other assets	451	3.442	1	-	4,440	8,334
Total assets	**236,986**	**596,800**	**6,963**	**1,603**	**401,122**	**1,243,474**
LIABILITIES AND EQUITY						
Deposits from banks	-	-	-	-	77	77
Deposits from customers	186,895	237.523	6.838	1.481	184,934	617,671
Borrowings	378,063	18.130	-	-	6.522	402,715
Provisions for liabilities and charges	-	-	-	-	2.898	2,898
Other liabilities	3,262	6.728	141	1	9.443	19,575
Total equity	-	-	-	-	200.538	200,538
Total liabilities and equity	**568,220**	**262,381**	**6,979**	**1,482**	**404,412**	**1,243,474**
Net foreign exchange position	**(331,234)**	**334,419**	**(16)**	**121**	**(3,290)**	**-**

NOTE 32 – FINANCIAL RISK MANAGEMENT (continued)

c) Currency risk (continued)

(in thousands of HRK)	EUR	EUR linked	USD	Other currencies	HRK	Total
As at 31 December 2012						
ASSETS						
Cash and cash equivalents	93,943	-	2,589	1,761	25,305	123,598
Obligatory reserve with CNB	11,530	-	4,409	-	79,070	95,009
Loans and advances to banks	89,416	-	-	-	13,947	103,363
Loans and advances to customers	-	555,053	-	-	187,470	742,523
Financial assets at fair value through profit or loss	-	19,230	-	-	26,542	45,772
Available-for-sale financial assets	12	-	-	-	1,264	1,276
Held-to-maturity investments	18,268	-	-	-	30,425	48,693
Property and equipment	-	-	-	-	23,208	23,208
Intangible assets	-	-	-	-	6,171	6,171
Deferred tax assets	-	-	-	-	878	878
Other assets	67	3,167	-	-	4,784	8,018
Total assets	**213,236**	**577,450**	**6,998**	**1,761**	**399,064**	**1,198,509**
LIABILITIES AND EQUITY						
Deposits from banks	21,905	-	-	-	214	22,119
Deposits from customers	132,712	229,341	6,821	1,327	159,153	529,354
Borrowings	373,508	36,888	-	-	9,545	419,941
Provisions for liabilities and charges	-	-	-	-	2,534	2,534
Other liabilities	3,112	4,038	133	2	8,028	15,313
Total equity	-	-	-	-	209,248	209,248
Total liabilities and equity	531,237	270,267	6,954	1,329	388,722	1,198,509
Net foreign exchange position	**(318,001)**	**307,183**	**44**	**432**	**10,342**	**-**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

d) Interest rate risk

In the course of its business operations, the Bank is exposed to interest rate risk to the extent to which its interest-earning assets and interest-bearing liabilities mature or their interest rates change at various times and in various amounts. In the case of floating rate assets and liabilities the Bank is also exposed to basis risk, which is the difference in re-pricing characteristics of the various floating rate indices, and different types of interest. Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with the Bank's business strategies.

The majority of loans to and receivables from companies and individuals and deposits from companies and individuals are at variable interest rates.

Sensitivity is calculated for significant financial assets (loans and advances to customers) and financial liabilities (deposits and from customers and borrowings) which bear variable interest rates at year end. No sensitivity was calculated for held-to-maturity investments since they bear interest at a fixed rate and are carried at amortised cost.

Sensitivity is calculated to reflect possible changes of average interest's rate applicable on underlying financial assets and financial liabilities. Should the average interest rate on interest-earning assets and interest bearing liabilities increase/decrease by 1 percentage point with all other variables held constant, the Bank's after tax profit for the year would be HRK 1,084 thousand (2012: HRK 227 thousand) lower/higher.

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

d) Interest rate risk (continued)

The table below summarises the Bank's exposure to interest rate risks. The tables are management's estimate of the interest rate risk for the Bank as of 31 December 2013 and 31 December 2012 and are not necessarily indicative of the positions at other times but provide some indication of the sensitivities of the Bank's earnings to movements in interest rates. Earnings will also be affected by the currency of the assets and liabilities and equity. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual re-pricing or maturity dates:

(in thousands of HRK)	Up to 1 month	1-3 months	3-12 months	1 -3 years	Over 3 years	Non-interest bearing	Total	Fixed interest
As at 31 December 2013								
ASSETS								
Cash and cash equivalents	4,397	-	-	-	-	166,716	171,113	-
Obligatory reserve with CNB	-	-	-	-	-	84,393	84,393	-
Loans and advances to banks	60,337	19,476	-	-	-	-	79,813	79,813
Loans and advances to customers	725,551	115	1,036	579	50,612	-	777,893	59,153
Financial assets at fair value through profit or loss	-	-	-	-	-	42,780	42,780	-
Available-for-sale financial assets	-	-	-	-	-	1,076	1,376	-
Held-to-maturity investments	4,473	770	41,924	2,102	-	-	49,269	49,269
Property and equipment	-	-	-	-	-	21,921	21,921	-
Intangible assets	-	-	-	-	-	5,836	5,836	-
Deferred tax assets	-	-	-	-	-	1,046	1,046	-
Other assets	-	-	-	-	-	8,334	8,334	-
Total assets	**794,758**	**20,361**	**42,960**	**2,681**	**50,612**	**332,102**	**1,243,474**	**188,235**
LIABILITIES AND EQUITY								
Deposits from banks	77	-	-	-	-	-	77	-
Deposits from customers	363,470	30,916	128,592	38,412	55,556	725	617,671	454,960
Borrowings	402,715	-	-	-	-	-	402,715	-
Provisions for liabilities and charges	-	-	-	-	-	2,898	2,898	-
Other liabilities	-	-	-	-	-	19,575	19,575	-
Total equity	-	-	-	-	-	200,538	200,538	-
Total liabilities and equity	**766,262**	**30,916**	**128,592**	**38,412**	**55,556**	**223,736**	**1,243,474**	**454,960**
Interest sensitivity gap	**28,496**	**(10,555)**	**(85,632)**	**(35,731)**	**(4,944)**	**108,366**	**-**	**(266,725)**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

d) Interest rate risk (continued)

(in thousands of HRK)	**Up to 1 month**	**1-3 months**	**3-12 months**	**1 -3 years**	**Over 3 years**	**Non-interest bearing**	**Total**	**Fixed interest**
As at 31 December 2012								
ASSETS								
Cash and cash equivalents	52,285	-	-	-	-	71,313	123,598	-
Obligatory reserve with CNB	-	-	-	-	-	95,009	95,009	-
Loans and advances to banks	95,440	7,923	-	-	-	-	103,363	89,416
Loans and advances to customers	693,355	148	49,617	813	1,129	-	742,523	62,349
Financial assets at fair value through profit or loss	-	-	-	-	-	45,772	45,772	-
Available-for-sale financial assets	-	-	-	-	-	1,276	1,276	-
Held-to-maturity investments	4,137	473	44,083	-	-	-	48,693	48,693
Property and equipment	-	-	-	-	-	23,208	23,208	-
Intangible assets	-	-	-	-	-	6,171	6,171	-
Deferred tax assets	-	-	-	-	-	878	878	-
Other assets	-	-	-	-	-	8,018	8,018	-
Total assets	**842,678**	**8,544**	**93,700**	**813**	**1,129**	**251,645**	**1,198,509**	**200,458**

(in thousands of HRK)	**Up to 1 month**	**1-3 months**	**3-12 months**	**1 -3 years**	**Over 3 years**	**Non-interest bearing**	**Total**	**Fixed interest**
LIABILITIES AND EQUITY								
Deposits from banks	22,119	-	-	-		-	22,119	-
Deposits from customers	461,393	11,914	52,599	577	990	1,881	529,354	67,647
Borrowings	419,941	-	-	-	-	-	419,941	-
Provisions for liabilities and charges	-	-	-	-	-	2,534	2,534	-
Other liabilities	-	-	-	-	-	15,313	15,313	-
Total equity	-	-	-	-	-	209,248	209,248	-
Total liabilities and equity	**903,453**	**11,914**	**52,599**	**577**	**990**	**228,976**	**1,198,509**	**67,647**
Interest sensitivity gap	**(60,775)**	**(3,370)**	**41,101**	**236**	**139**	**22,669**	**-**	**132,811**

NOTE 32– FINANCIAL RISK MANAGEMENT (continued)

e) Price risk

Price risk is the possibility that prices will fluctuate, affecting the fair value of investments and other instruments that derive their value from a particular investment. The primary exposure to price risk arises from the Bank’s holding of investments in units in investment funds.

Should the prices of investment funds at 31 December 2013 increase/decrease by 5% with all other variables held constant, the Bank’s after tax profit for the year would be HRK 2,139 thousand (2012: HRK 2,288 thousand) higher/lower.

f) Operational risk

Operational risk is the possibility of financial loss due to errors, breaches, terminations or damages caused by internal processes, employees of the Bank, systems as well as by events caused by external factors. Operational risk is defined as legal and compliance risk but not strategic and reputational risk.

The Bank is exposed to operational risk in all segments of its activities. The Bank seeks to manage its operational risk in accordance with defined principles, with the final purpose being to mitigate or avoid operational risk. Methodologies and models for managing operational risk are being developed.

g) Capital adequacy

The amount of capital allocated by individual activity is based primarily on regulatory requirements. The procedure of capital allocation for specific activities is performed independently from responsible personnel for certain activities.

The rate of capital adequacy is calculated as the ratio between guarantee capital and the sum of credit-risk-weighted assets, exposure to market risks (currency risk) and operational risk and the estimated exposure of the open foreign exchange position to currency risk.

Regulatory capital and capital adequacy ratio according to CNB requirements (as of the date of issuance of these financial statements information on	**31 December 2013**	**31 December 2012**
	(in thousands of HRK)	
GUARANTEE CAPITAL		
Ordinary share capital and reserves	200,427	208,825
Supplementary capital	-	-
Deductions	(1,293)	(1,360)
Total guarantee capital	**199,134**	**207,465**
Risk weighted assets (unaudited)		
Credit-risk-weighted assets and other risk exposures	928,016	935,899
CREDIT- RISK- WEIGHTED ASSETS AND OTHER RISK EXPOSURES	**928,016**	**935,899**
Capital adequacy ratio	**21.46%**	**22.17%**

NOTE 33 – ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Bank makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly evaluated, and are based on historical experience and other factors such as the expected flow of future events that can be rationally assumed in existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Bank's credit risk portfolio represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a possible material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

a) Impairment losses on loans and advances to customers

The Bank monitors the creditworthiness of its customers on an ongoing basis. In accordance with regulations, the need for impairment of the Bank's on- and off-balance-sheet credit risk exposure is assessed at least quarterly. Impairment losses are made mainly against the carrying value of loans and advances to corporate and retail customers (summarised in Note 14b), and as provisions arising from off-balance-sheet risk exposure to customers, mainly in the form of undrawn lending commitments, guarantees and letters of credit (summarised in Note 24). Impairment losses are also considered for credit risk exposures to banks, and for other assets not carried at fair value, where the primary risk of impairment is not credit risk.

A summary of impairment allowances on exposures to customers is presented below:

	Note	31 December 2013	31 December 2012
		(in thousands of HRK)	
Impairment allowance on loans and advances to customers	14b	29,446	17,418
Provisions for off-balance-sheet exposures	24	1,091	787
		30,537	**18,205**

Financial assets carried at amortised cost

The Bank first assesses whether objective evidence of impairment exists. However, assets assessed individually as unimpaired are then included in groups of assets with similar credit risk characteristics. These portfolios are then assessed collectively for impairment.

The Bank estimates impairment losses in cases where it judges that the observable data indicates the likelihood of a measurable decrease in the estimated future cash flows of the asset or portfolio of assets. Such evidence includes delinquency in payments or other indications of financial difficulty of borrowers and adverse changes in the economic conditions in which borrowers operate or in the value or enforceability of security, where these changes can be correlated with defaults.

NOTE 33 – ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)

The Bank takes into consideration the combined effect of several events when assessing impairment and uses its experienced judgment in cases where the observable data required to estimate impairment is limited. In estimating impairment losses on items individually or collectively assessed as impaired, the Bank also has regard to the ranges of specific impairment loss rates prescribed by the CNB.

The Bank has recognised an impairment allowance calculated on a portfolio basis in accordance with the range of impairment loss rates of 1% prescribed by the CNB to be calculated on all credit risk exposures except those carried at fair value through profit or loss, including off-balance-sheet amounts (including undrawn lending commitments) and sovereign risk. Amounts assessed as impaired are excluded from this calculation.

b) Impairment of available-for-sale equity investments

The Bank determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. The impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows.

c) Held-to-maturity investments

The Bank follows the guidance of IAS 39 on classifying non derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgement. In making this judgement, the Bank evaluates its intention and ability to hold such investments to maturity.

d) Taxation

The Bank provides for tax liabilities in accordance with the tax laws of the Republic of Croatia. Tax returns are subject to the approval of the tax authorities who are entitled to carry out subsequent inspections of taxpayers' records.

NOTE 33 – ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)

e) Regulatory requirements

CNB is entitled to carry out regulatory inspections of the Bank's operations and to request changes to the carrying values of assets and liabilities, in accordance with the underlying regulations.

f) Litigation and claims

The Bank performs individual assessment of all court cases. The initial assessment is made by the Bank's Legal Department. The Bank is a defendant in two smaller lawsuits of immaterial value that have arisen in the course of the Bank's ordinary business. Management is of the opinion that the final outcome of these court cases will be in the Bank's favour, therefore no provision has been made.

NOTE 34 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value represents the amount at which an asset could be exchanged or a liability settled on an arm's length basis.

Financial assets at fair value through profit or loss are measured at their current fair value.

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: quoted price (unadjusted) in an active market;
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the financial assets, either directly (for example prices) or indirectly (for example derived from prices);
- Level 3: inputs for assets are not based on observable market data (for example valuation techniques using significant unobservable inputs).

	Level 1	Level 2	Level 3	Total
31 December 2013				
Financial assets at fair value through profit or loss				
Investment funds	42,780	-	-	**42,780**
31 December 2012				
Financial assets at fair value through profit or loss				
Investment funds	45,772	-	-	**45,772**

NOTE 34 – FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

During 2013 and 2012 there have been no transfers of assets between Level 1 and Level 2 of the fair value hierarchy and there have been no any transfers to or from Level 3

Financial assets available for sale are measured at cost less impairment. Loans and receivables and held-to-maturity assets are measured at amortised cost less impairment.

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments which are not already recorded at fair value in the financial statements:

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that have a short term maturity it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates for similar financial instruments.

Loans and advances

The carrying value of loans with variable interest rate approximates their fair value. It is not practicable to calculate the fair value of the Bank’s portfolio of fixed rate loans. However, as the Bank has a limited portfolio of loans and advances with both fixed rate and longer term maturity, management believes that the fair value of loans and advances is not significantly different from their carrying value at the balance sheet date, not taking into account general provisions as required by the CNB and expected future losses.

Bank and customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values. The carrying value of the Bank’s deposits which are given with variable rate, being market rate, approximates their fair value. It is not practicable to calculate the fair value of deposits with fixed interest rates, however, since these deposits are with short term maturity the Bank believes that their fair value is not significantly different to their carrying value.

Borrowings

Most of the Bank’s long-term debt has no quoted market prices. It is not practicable for the Bank to estimate the fair value of this debt.

NOTE 35 – OPERATING LEASES

The Bank leases offices for business purposes under operating leases. The lease is cancellable, runs for an initial period of five years and does not include contingent rental expenses.

During 2013, the Bank recognised HRK 1,152 thousand as an expense in the income statement in respect of operating leases (2012: HRK 1,662 thousand) (Note 9).

Schedules prepared in accordance with CNB decision

a) Balance sheet

Assets	31 December 2013	31 December 2012
		(in thousands of HRK)
1. Cash and deposits with CNB		
1.1. Cash	6,373	5,160
1.2. Accounts and deposits with CNB	147,741	117,569
2. Deposits with banks	181,206	185,294
3. Treasury bills of Ministry of finance and Treasury bills of CNB	-	-
4. Securities and other financial instruments classified as held for trading	-	-
5. Securities and other financial instruments classified as available for sale	1,076	1,276
6. Securities and other financial instruments classified as held to maturity	49,269	48,693
7. Securities and other financial instruments not actively traded but measured at fair value through profit or loss	42,780	45,772
8. Derivative financial assets	-	-
9. Loans and advances to banks	-	13,947
10. Loans and advances to customers	777.893	742,523
11. Investments in subsidiaries. associates and joint ventures	-	-
12. Foreclosed assets	693	693
13. Property and equipment (net of depreciation)	21,920	23,208
14. Interest, fees and other assets	14,523	14,374
Total assets	**1,243,474**	**1,198,509**

Schedules prepared in accordance with CNB decision (continued)

a) Balance sheet (continued)

Liabilities and equity	31 December 2013	31 December 2012
	(in thousands of HRK)	
1. Borrowings from financial institutions		
1.1. Short term borrowings	106,927	105,639
1.2. Long term borrowings	295,788	314,302
2. Deposits		
2.1. Deposits on gyro and current accounts	118,814	114,364
2.2. Savings deposits	20,853	14,808
2.3. Term deposits	478,024	422,301
3. Other borrowings		-
3.1. Short term borrowings	-	-
3.2. Long term borrowings	-	-
4. Derivative and other trading financial liabilities not actively traded		-
5. Issued debt securities	-	-
5.1. Short term issued debt securities		-
5.2. Long term issued debt securities	-	-
6. Issued subordinated instruments	-	-
7. Issued hybrid instruments	-	-
8. Interest. fees and other liabilities	22,531	17,847
Total liabilities	**1,042,937**	**989,261**
Equity		
1. Share capital	200,000	200,000
2. Profit/(Loss) for the year	(8,711)	(5,334)
3. Retained earnings	6,470	11,804
4. Legal reserves	2,778	2,778
5. Statutory and other equity reserves	-	-
6. Unrealised gain/(loss) on fair value measurement of available-for-sale financial assets	-	-
Total equity	**200,537**	**209,248**
Total liabilities and equity	**1,243,474**	**1,198,509**

Schedules prepared in accordance with CNB decision (continued)

b) Income statement for the year ended 31 December

	2013	**2012**
	(in thousands of HRK)	
1. Interest income	51,473	50,906
2. (Interest expense)	(19,502)	(23,396)
3. Net interest income	**31,971**	**27,510**
4. Fee and commission income	5,160	5,067
5. (Fee and commission expense)	(1,453)	(1,618)
6. Net fee and commission income	**3,707**	**3,449**
	-	
7. Gain/(Loss) from investments in subsidiaries. associates and joint ventures	-	-
8. Gain/(Loss) from trading activities	819	1,087
9. Gain/(Loss) from embedded derivatives	-	-
10. Gain/(Loss) from assets not actively traded but measured as at fair value through profit or loss	568	316
11. Gain/(Loss) from financial assets classified as available for sale	-	-
12. Gain/(Loss) from financial assets classified as held to maturity	-	-
13. Gain/(Loss) arising from hedging transactions	-	-
14. Income from investments in subsidiaries. associates and joint ventures	-	-
15. Income from other equity investments	-	-
16. Gain/(Loss) from foreign exchange differences	(238)	(389)
17. Other income	958	836
18. Other expenses	-	-
19. General administrative expenses and depreciation	(29,665)	(30,581)
20. Net income from business activities before impairment losses and provisions	**8,120**	**2,228**
21. Impairment losses and provisions	(16,999)	(7,779)
22. Profit/(Loss) before tax	**(8,879)**	**(5,551)**
23. Income tax	168	217
24. Profit/(Loss) for the year	**(8,711)**	**(5,334)**

Schedules prepared in accordance with CNB decision (continued)

c) Cash flow statement for the year ended 31 December

	2013	2012
	(in thousands of HRK)	
Operating activities		
1.1. (Loss)/Profit before taxation	(8,879)	(5,551)
1.2. Impairment losses and provisions	17,007	7,779
1.3. Depreciation and amortisation	4,329	4,975
1.4. Net unrealised (gain)/loss from financial assets classified as fair value through profit or loss	-	-
1.5. (Gain)/loss from disposal of tangible assets	-	-
1.6. Other (gains)/losses	348	377
1. Cash flows from operating activities before changes in operating assets (1.1. to 1.6.)	**12,805**	**7,580**
2.1. Deposits with CNB	10,616	(28,013)
2.2. Treasury bills of Ministry of finance and treasury bills of CNB	-	-
2.3. Deposits with banks and loans and advances to financial institutions	19,740	(19,841)
2.4. Loans and advances to customers	(47,643)	(62,154)
2.5. Securities and other financial instruments classified as held for trading	-	-
2.6. Securities and other financial instruments classified as available for sale	-	-
2.7. Securities and other financial instruments not actively traded but measured at fair value through profit or loss	2,992	(24,772)
2.8. Other operating assets	(644)	(178)
2. Net (increase)/decrease of operating assets (2.1 to 2.8.)	**(14,939)**	**(134,958)**
Increase/(decrease) of operating liabilities		
3.1. A vista deposits	10,553	(71,184)
3.2. Savings and term deposits	55,722	45,195
3.3. Derivative financial liabilities and other trading liabilities		-
3.4. Other liabilities	3,822	2,166
3. Net increase/(decrease) of operating liabilities (3.1. to 3.4.)	**70,097**	**(23,823)**
4. Net cash flow from operating activities before tax (1+2+3)	67,963	(151,201)
5. Income tax paid		
6. Net inflow/(outflow) of cash from operating activities (4-5)	**67,963**	**(151,201)**
Investment activities		
7.1. Proceeds from disposal/(consideration paid) of/for tangible and intangible assets	(2,700)	(2,827)
7.2. Proceeds from disposal/(consideration paid) of/for investments in subsidiaries. associates and joint ventures	-	-
7.3. Proceeds from disposal/(consideration paid) of/for financial assets and other financial instruments classified as held to maturity	(576)	(6,481)
7.4. Dividends received	-	-
7.5. Other inflow/(outflow) from investment activities		-
7. Net cash flow from investment activities (7.1. to 7.5)	**(3,276)**	**(9,308)**

Schedules prepared in accordance with CNB decision (continued)

c) Cash flow statement for the year ended 31 December (continued)

Financing activities		
8.1. Net increase/(decrease) of borrowings	(17,172)	75,593
8.2. Net increase/(decrease) of issued debt securities	-	-
8.3. Net increase/(decrease) of subordinated and hybrid instruments	-	-
8.4. Inflow from share capital issue	-	80,000
8.5. (Dividend paid)	-	-
8.6. Other inflow/(outflow) from financing activities	-	-
8. Net cash flow from financing activities (8.1. to 8.6.)	**(17,172)**	**155,593**
9. Net increase/(decrease) of cash and cash equivalents (6+7+8)	**47,515**	**(4,916)**
10. Effect of foreign exchange differences on cash and cash equivalents	-	-
11. Net increase/(decrease) of cash and cash equivalents (9+10)	**47,515**	**(4,916)**
12. Cash and cash equivalents at the beginning of the year	**123,598**	**128,514**
13. Cash and cash equivalents at the end of the year	**171,113**	**123,598**

Schedules prepared in accordance with CNB decision (continued)

d) Statement of changes in equity

	In thousands of HRK	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (losses)	Profit/ (Loss) for the year	Unrealised loss/gain on measurement of financial assets available for sale	Minority interest	Total
1,	**Balance at 1 January 2012**	**120,000**	**-**	**2,775**	**11,807**	**-**	**-**	**-**	**134,582**
2,	Change of accounting policies and correction of errors	-	-	-	-	-	-	-	-
3,	**Restatement of balance at 1 January of current year (1+2)**	**120,000**	**-**	**2,775**	**11,807**	**-**	**-**	**-**	**134,582**
4,	Disposal of financial assets available for sale	-	-	-	-	-	-	-	-
5,	Change of fair value of available for sale portfolio	-	-	-	-	-	-	-	-
6,	Tax on items directly recognised in equity	-	-	-	-	-	-	-	-
7,	Other gains and losses directly recognised in equity	-	-	-	-	-	-	-	-
8,	**Net gains/losses recognised directly in equity (4+5+6+7)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
9,	Profit/(loss) for the year	-	-	-	-	**(5,334)**	-	-	(5,334)
10,	**Total recognised income and expenses for the year (8+9)**	**-**	**-**	**-**	**-**	**(5,334)**	**-**	**-**	**(5,334)**
11,	Increase/decrease of share capital	80,000	-	-	-	-	-	-	80,000
12,	Increase/decrease of treasury shares	-	-	-	-	-	-	-	-
13,	Other changes	-	-	-	-	-	-	-	-
14,	Transfers to reserves	-	-	3	(3)	-	-	-	-
15,	Payment of dividends	-	-	-	-	-	-	-	-
16,	**Profit distribution (14+15)**	**-**	**-**	**3**	**(3)**	**-**	**-**	**-**	**-**
17,	**Balance at 31 December 2012 (3+10+11+12+13+16)**	**200,000**	**-**	**2,778**	**11,804**	**(5,334)**	**-**	**-**	**209,248**

Schedules prepared in accordance with CNB decision (continued)

d) Statement of changes in equity

	In thousands of HRK	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (losses)	Profit/ (Loss) for the year	Unrealised loss/gain on measurement of financial assets available for sale	Minority interest	Total
1,	**Balance at 1 January 2013**	**200,000**	**-**	**2,778**	**6,470**	**-**	**-**	**-**	**209,248**
2,	Change of accounting policies and correction of errors	-	-	-	-	-	-	-	-
3,	**Restatement of balance at 1 January of current year (1+2)**	**200,000**	**-**	**2,778**	**6,470**	**-**	**-**	**-**	**209,248**
4,	Disposal of financial assets available for sale	-	-	-	-	-	-	-	-
5,	Change of fair value of available for sale portfolio	-	-	-	-	-	-	-	-
6,	Tax on items directly recognised in equity	-	-	-	-	-	-	-	-
7,	Other gains and losses directly recognised in equity	-	-	-	-	-	-	-	-
8,	**Net gains/losses recognised directly in equity (4+5+6+7)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
9,	Profit/(loss) for the year	-	-	-	-	(8,711)	-	-	**(8,711)**
10,	**Total recognised income and expenses for the year (8+9)**	**-**	**-**	**-**	**-**	**(8,711)**	**-**	**-**	**(8,711)**
11,	Increase/decrease of share capital	-	-	-	-	-	-	-	-
12,	Increase/decrease of treasury shares	-	-	-	-	-	-	-	-
13,	Other changes	-	-	-	-	-	-	-	-
14,	Transfers to reserves	-	-	-	-	-	-	-	-
15,	Payment of dividends	-	-	-	-	-	-	-	-
16,	**Profit distribution (14+15)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
17,	**Balance at 31 December 2013 (3+10+11+12+13+16)**	**200,000**	**-**	**2,778**	**6,470**	**(8,711)**	**-**	**-**	**200,537**

BKS Bank d.d., RIJEKA

Supplementary information prescribed by a decision of the Croatian National Bank

Reconciliation between financial statements and schedules per decision of CNB – Balance sheet (assets) as at 31 December 2013

Financial statements	Total	Current accounts CNB	Current accounts with other banks	Foreclosed assets	Loans and advances to customers	PPE	Intangible assets	Other assets	Deferred tax assets	Total	CNB prescribed schedules
	HRK '000	1	2	4	5	6	7	8	9	HRK '000	
											1. Cash and deposits with CNB
Cash reserves	171.113	(63.348)	(101.392)	-	-	-	-	-	-	**6.373**	1.1 Cash
Obligatory reserve with the Croatian National Bank	84.393	63.348	-	-	-	-	-	-	-	**147.741**	1.2. Accounts and deposits with CNB
Loans and advances to banks	79.813	-	101.392	-	-	-	-	-	-	**181.206**	2. Deposits with banks
										-	
	-	-	-	-	-	-	-	-	-	**-**	3.Treasury bills of Ministry of finance and Treasury bills of CNB
	-	-	-	-	-	-	-	-	-	**-**	
Loans and advances to customers	777.893	-	-	-	(777.893)	-	-	-	-		4.Securities and other financial instruments classified as held for trading
Available for sale financial assets	1.076	-	-	-	-	-	-	-	-	**1.076**	5.Securities and other financial instruments classified as available for sale
Held to maturity investments	49.269	-	-	-	-	-	-	-	-	**49.269**	6.Securities and other financial instruments classified as held to maturity
Financial assets at fair value through profit or loss	42.780	-	-	-	-	-	-	-	-	**42.780**	7.Securities and other financial instruments not actively traded but measured at fair value through profit or loss
		-	-	-	-	-	-	-	-	**-**	8. Derivative financial assets
		-	-	-	-	-	-	-	-		
		-	-	-	-	-	-	-	-	**-**	9.Loans and advances to banks
		-	-	-	-	-	-	-	-		
		-	-	-	777.893	-	-	-	-	**777.893**	10.Loans and advances to customers
		-	-	-	-	-	-	-	-	**-**	
		-	-	-	-	-	-	-	-	**-**	11. Investments in subsidiaries, associates and joint ventures
		-	-	-	-	-	-	-	-	**-**	
				693						**693**	12. Foreclosed assets
		-	-	-	-	-	-	-	-	**-**	
						21.921	-	-	-	**21.920**	13. Property and equipment (net of depreciation)
		-	-	-	-	-	-	-	-	**-**	
							5.836	7.641	1.046	**14.523**	14. Interest, fees and other assets
Property and equipment	21.921	-	-	-	-	(21.921)	-	-	-	**-**	
Intangible assets	5.836	-	-	-	-	-	(5.836)	-	-	**-**	
Deferred tax assets	1.046	-	-	-	-	-	-	-	(1.046)	**-**	
Other assets	8.334	-	-	(693)	-	-	-	(7.641)	-	**-**	
				-	-	-	-	-	-		
Total assets	**1.243.474**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1.243.474**	**Total assets**

Supplementary information prescribed by a decision of the Croatian National Bank

Reconciliation between financial statements and schedules per decision of CNB - Balance sheet (liabilities and equity) as at 31 December 2013

Financial statements	Total	Deposits from banks	Deposits from customers	Interest, fees and other liabilities	Fee deferral	Other liabilities	Total	CNB prescribed schedules
LIABILITIES	**HRK '000**	**1**	**2**	**3**	**4**		**HRK '000**	
Borrowings	**402.769**	-	-	-	(54)	-	**402.715**	**1. Borrowings from financial institutions**
							106.927	1.1. Short term borrowings
							295.788	1.2. Long term borrowings
Deposits from banks	77	(77)	-	-	-	-	-	
Deposits from customers	617.671	-	(617.671)	-	-	-	-	
	-	77	617.671	-	-	(57)	**617.691**	**2. Deposits**
	-	-	-	-	-	-	118.814	2.1. Deposits on gyro and current accounts
	-	-	-	-	-	-	20.853	2.2. Savings deposits
	-	-	-	-	-	-	478.024	2.3. Term deposits
	-	-	-	-	-	-	-	**3. Other borrowings**
	-	-	-	-	-	-	-	3.1. Short term borrowings
	-	-	-	-	-	-	-	3.2. Long term borrowings
	-	-	-	-	-	-	-	4. Derivative and other financial liabilities not actively traded
	-	-	-	-	-	-	-	**5. Issued debt securities**
	-	-	-	-	-	-	-	5.1. Short term issued debt securities
	-	-	-	-	-	-	-	5.2. Long term issued debt securities
Provisios for liabilities and charges	2.899	-	-	(2.899)	-	-	-	6. Issued subordinated instruments
		-	-	-	-	-	-	7. Issued hybrid instruments
Other liabilities	19.521			2.899	54	57	22.531	8. Interest, fees and other liabilities
Total liabilities	**1.042.937**	**-**	**-**	**-**	**-**	**-**	**1.042.937**	**Total liabilities**

Financial statements	Total	Statutory reserve	Profit for the year	Retained earnings	Total	CNB prescribed schedules
EQUITY AND RESERVES	**HRK '000**	**1**	**2**	**3**	**HRK '000**	
Issues share capital	200.000				**200.000**	1. Share capital
			(8.711)		**(8.711)**	2. Profit/(loss) for the year
Statutory reserve	2.778	(2.778)		6.470	**6.470**	3. Retained earnings (losses)
		2.778			**2.778**	4. Legal reserves
Reserve for general banking risks	-	-	-	-	**-**	5. Statutory and other equity reserves
	-	-	-	-	**-**	6. Unrealised gain/(loss) on fair value measurment of available-for-sale financial assets
Retained earnings	(2.241)		8.711	(6.470)	**-**	
Total equity and reserves	**200.537**		**-**	**-**	**200.537**	**Total equity and reserves**

BKS Bank d.d., RIJEKA

Supplementary information prescribed by a decision of the Croatian National Bank

Reconciliation between financial statements and schedules per decision of CNB – Income statement for the year ended 31 December 2013

Financial statements	Total	Gain on disposal of financial assets not actively traded	Movement in provision for off balance sheet exposure, severance payments and jubilee awards, interests and fees	Foreign currencies exchange differences	Impairment losses on loans and advances to customers	Savings deposits insurance	Transfer of administration costs	Other transfer of costs	Total	CNB prescribed schedules
	HRK '000	1	2	3	4	5	6		HRK '000	
Interest and similar income	51.478	-	-	-	-	-	-	(5)	51.473	1 Interest income
Interest expense and similar charges	(18.815)	-	-	91	-	(1.054)	-	276	(19.502)	2 (Interest expense)
Net interest income	**32.663**	-	-	-	-	-	-	-	**31.971**	**3 Net interest income**
Fee and commission income	5.158	-	-	-	-	-	-	2	5.160	4 Fee and commission income
Fee and commission expense	(1.453)	-	-	-	-	-	-	-	(1.453)	5 (Fee and commission expense)
Net fee and commission income	**3.705**	-	-	-	-	-	-	-	**3.707**	**6 Net fee and commission income**
										7 Gain/(Loss) from investments in subsidiaries, associates and joint ventures
Net trading income from dealing in foreign currencies	819	-	-	-	-	-	-	-	819	8 Gain/(Loss) from trading activities
		-	-	-	-	-	-	-	-	9 Gain/(Loss) from embedded derivatives
		568	-	-	-	-	-	-	568	10 Gain/(Loss) from assets not actively traded but measured at fair value through profit or loss
		-	-	-	-	-	-	-	-	11 Gain/(Loss) from financial assets classified as available for sale
		-	-	-	-	-	-	-	-	12 Gain/(Loss) from financial assets classified as held to maturity
		-	-	-	-	-	-	-	-	13 Gain/(Loss) arising from hedging transactions
		-	-	-	-	-	-	-	-	14 Income from investments in subsidiaries, associates and joint ventures
		-	-	-	-	-	-	-	-	15 Income from other equity investments
		-	-	(439)	-	-	-	201	(238)	16 Gain/(Loss) from foreign exchange differences
Net income from investment securities	568	(568)	-	-	-	-	-	-	-	
Other operating income	610	-	-	348	-	-	-	-	958	17 Other income
Operating income	**38.365**	-	-	-	-	-	-	-		
									-	18 Other expenses
	-	-	-	-	-	-	(29.183)	(482)	(29.665)	19 General administrative expenses and depreciation
	-	-	-	-	-	-	-			
	-	-	-	-	-	-	**-**	**-**	**8.120**	**20 Net income from business activities before impairment losses and provisions**
	-	-	(894)	-	(16.113)	-	-	8	(16.999)	21 Impairment losses and provisions
Impairment losses on loans and advances to customers	(16.113)	-	-	-	16.113	-	-	-	-	
Other impairment lossed and provisions	(894)	-	894	-	-	-	-	-	-	
Operating expenses	(30.237)	-	-	-	-	1.054	29.183	-	-	
Profit before income tax	**(8.879)**	-	-	-	-			**-**	**(8.879)**	**22 Profit/(Loss) before tax**
Income tax benefit/(expense)	168	-	-	-	-	-	-	-	168	23 Income tax
Profit for the year	**(8.711)**	-	-	-	-	**-**	**-**	**-**	**(8.711)**	**24 Profit/(Loss) for the year**