VIKTOR LENAC SHIPYARD GROUP
Consolidated Annual Financial Statements and Audit Report for 2011

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STATEMENT ON RESPONSIBILITY FOR FINANCIAL STATEMENTS

We acknowledge our responsibility for the preparation and presentation of the consolidated financial statements for the year 2011 in accordance with the International Financial Reporting Standards applied in the European Union and Croatia Law on Accounting to give a true and fair view of the financial position of Shipyard Viktor Lenac d.d. Rijeka and its subsidiary company (Group) as at December 31, 2011 and of the results of its operations for the year then ended.

We have made financial statements under the assumption that the Group shall continue doing its business for an indefinite period as reasonably expected, based on research conducted for, to have adequate funds to continue with its business in the foreseeable future.

We confirm, to the best of our knowledge and belief, the following representations:
- We acknowledge our responsibility for the implementation and consistent application of the appropriate accounting policies.
- We acknowledge our responsibility for giving reasonable and conservative estimates.
- We acknowledge our responsibility for the fair presentation of the financial statements in accordance with International Financial Reporting Standards and Republic of Croatia legal regulations, disclosure and interpretation of any significant deviation in the financial statements.
- We have produced the financial statements under the assumption of the continuity of business for an indefinite period of time, unless it is inappropriate to assume that the Group shall continue running its business activities.

We acknowledge our responsibility for keeping proper and accurate accounting records, which shall at any time reflect the financial status and business results of the Group with acceptable accuracy and precision as well as their compliance with the International Financial Reporting Standards and Republic of Croatia Law on Accounting (OG 109/07).

We, also, acknowledge our responsibility for taking care of the Group's assets and for undertaking reasonable measures for preventing and revealing embezzlements and other irregularities.

The financial statements have been approved as of 13 April 2012.

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board

Inženjerski biro-revizija d.o.o. Zadar
za reviziju financijskih izvještaja i pružanje usluga s područja računovodstva, poreznog savjetovanja, financijskih analiza i kontrola

23000 ZADAR, Poljana Plankit 1 Tel./Fax: 023/250-869

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF THE VIKTOR LENAC SHIPYARD GROUP

In the period from 19 October 2011 to 13 April 2012 we have audited the accompanying consolidated financial statements of the Viktor Lenac Shipyard Group, which comprise of the Consolidated Balance Sheet as at December 31, 2011, Consolidated Profit and Loss Account for the year 2011, including Comprehensive Income, Consolidated Cash Flow Statement and Consolidated Statement of Changes in Equity for the year then ended as well as supporting significant accounting policies and other explanatory notes to the financial statements. The consolidated financial statements are set out on pages 6 to 33.

Management's Responsibility for the Financial Statements

The Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the International Financial Reporting Standards as applied in the European Union. This responsibility includes: designing, implementing and maintaining of internal control relevant for preparation and fair presentation of financial statements that are free from material misstatements, whether due to error or fraud; selecting and applying of appropriate accounting policies as well as making of accounting estimates that are reasonable in the existing circumstances.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate 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 the 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.

Qualifications influencing auditor's opinion

1. As stated in the note no. 17 – Inventories, we are not able to confirm the value of inventories in its entirety considering that the value adjustment of inventories was not recorded analytically resulting in non-conformance between the analytical and synthetic records.

Opinion

In our opinion, the accompanying consolidated financial statements of the VIKTOR LENAC SHIPYARD GROUP which were the subject of our audit, exclusive of the effects from the item 1 (Qualifications) and other effects which could affect the financial statements, present fairly, in all material respects, the consolidated financial position as at December 31, 2011, consolidated financial performance, consolidated changes of equity and consolidated cash flows for the year 2010 in accordance with the International Financial Reporting Standards applicable in Republic of Croatia.

Issues not affecting auditor's opinion

1. Without any influence on our opinion we note to the note no.31 to the financial statements - Disputes, to the effect that their final outcome may not be established at the moment of drawing up this report either liabilities which might arise therefrom and which might be recorded in the financial statements.
2. Without any influence on our opinion we note the note no. 6 – Employee expenses.
3. We note to the note no.7 to the financial statements – Depreciation. The Company changed its depreciation policy and applied single rates of depreciation for the year 2011, resulting in a decrease in depreciation cost of approximately 14,500,00 Croatian Kuna.

In Rijeka, 13 April 2012

"Inženjerski biro-revizija" d.o.o. Zadar

Certified auditor:	*President:*
Branimir Grgić	*Irena Dobrović, certified auditor*

CONSOLIDATED BALANCE SHEET

(As at 31 December 2011)

[redacted]

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board

CONSOLIDATED PROFIT AND LOSS ACCOUNT INCLUDING COMPREHENSIVE INCOME

(As at 31 December 2011)

[redacted]

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board

CONSOLIDATED CASH FLOW STATEMENT

(As at 31 December 2011)

[redacted]

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board

CONSOLIDATED STATEMENT ON CHANGES IN EQUITY

[redacted]

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board

Notes to Consolidated Financial Statements
(making an integral part of the consolidated financial statements)

1. GENERAL INFORMATION

The joint-stock company VIKTOR LENAC shipyard, Martinšćica bb, Rijeka (hereinafter referred to as „Mother company") has been registered under the company's registration number 040000358 in the register of the Commercial Court of Rijeka.

By the Rijeka Commercial Court's decision no. St-183/03 as of 8 December 2003, the Mother company was under bankruptcy proceedings, which terminated on 9 April 2008 by the decision of the Commercial Court of Rijeka after the implementation of the legally valid Bankruptcy plan.

The share capital of the Mother company amounts to 168,132,470 Croatian Kuna and is divided in:

- *15.988.060 non-materialized ordinary shares in name, each having a nominal value of 10 Croatian Kuna*
- *825.187 own shares, each having a nominal value of 10 Croatian Kuna*

According to the Notice on classification of legal entities by National classification of economic activities of the Central Bureau of Statistics in Zagreb, the Mother company has been classified under the subclass number 3011 – building of ships and floating vessels, having its tax number 03333710 and identification number 27531244647.

The Mother company's main activity is building, repair, conversion and other services relating to ships and other floating vessels. The Mother company has been registered for other activities such as steel constructions, trade, engineering and other various services.

On the day of 31 December 2011 the Mother company employed 581 employees.

The limited liability company VIKTOR - SERVISI Rijeka, Martinšćica bb, company's registration number 40040360 is an entity owned by the joint-stock company VIKTOR LENAC shipyard Rijeka, and shall, therefore, be included into the consolidation.
According to the Notice on classification of legal entities by National classification of economic activities of the Central Bureau of Statistics in Zagreb as of 13 February 2008, the subsidiary company has been classified under the subclass number 2811– production of engines and turbines exclusive of engines for aircrafts and motor vehicles, having its tax number 03767248 and identification number 06081251984.
The main activity of the subsidiary company is repair and maintenance of machines and devices. The share capital amounts to 254,000 Croatian Kuna.
On the day of 31 December 2011 the subsidiary company employed 17 employees.

The Viktor Lenac shipyard owns shares of minority interest in another company, which are not included into the consolidation.

Likewise, its subsidiary company also owns shares of minority interest in another company, which are not included into the consolidation.

The members of the Supervisory Board of the Mother company during 2011 and up to the moment of drawing up this report were:

Karlo Radolović	*Chairman*
Ive Mustać	*Member*
Anton Brajković	*Member*
Lenko Milin	*Member*
Goran Zemljić	*Member*

The Mother Company's Management Board is composed of three members:

Robert Škifić	*Chairman of the Board*
Sandra Uzelac	*Member of the Board*
Davor Lukeš	*Member of the Board*

The Mother Company had the following ownership structure as at 31 December 2011 :

	Shareholder	Number of shares	%
1	Tankerska Plovidba j.s.c. Zadar	8.138.460	48,40
2	Uljanik Shipyard j.s.c. Pula	3.904.063	23,22
3	Privredna Bank j.s.c. Zagreb / collective custody account	1.367.268	8,13
4	Croatian State Property Management Agency (AUDIO)	1.243.702	7,40
5	Shipyard Viktor Lenac j.s.c. Rijeka	825.187	4,90
6	Privredna Bank j.s.c. Zagreb	258.751	1,54
7	R.L.E. Ltd. Drniš	105.211	0,63
8	List Gmbh Austria	45.992	0,27
9	Jadranski pomorski servis j.s.c. Rijeka	35.874	0,21
10	Other	888.739	5,30
	Total	**16.813.247**	**100,00**

On the day of 13 April 2012, the Management Board of the Mother Company approved the Consolidated Financial Statements for their submitting to the Supervisory Board.

2. BASIS FOR CONSOLIDATION, STATEMENT ON COMPLIANCE AND BASICS OF REPORTING SUMMARY OF BASIC ACCOUNTING POLICIES

a) *The Consolidated Financial Statements have been prepared in accordance with the law frame of the financial reporting applicable in the Republic of Croatia and International Financial Reporting Standards ("IFRS") applied in the European Union.*
The Consolidated Financial Statements have been prepared under the fundamental accounting assumption that effect of transaction is recognized when occurred and is recorded in the period to which the transaction refers, and under the assumption of the continuity of business for an indefinite period of time.

Accounting policies applied in the preparation of the 2010 financial statements have not changed compared with the previous year. The consolidated financial statements have been prepared by principle of historical cost, except for certain financial instruments recorded as per fair value.
The consolidated financial statements have been prepared in Croatian Kuna (HRK) as measuring or reporting currency.
According to the IFRS, all foreign currency receivables and liabilities as well as receivables and liabilities with foreign currency clause have been adjusted to the midpoint exchange rates of the Croatian National Bank as at 31st December 2011 as follows:

1 EUR = 7,530420 HRK (31.12. 2010: 1 EUR = 7,385173 HRK)
1 USD = 5,819940 HRK (31.12.2010: 1 USD = 5,568252 HRK)
1 NOK = 0,967672 HRK (31.12.2010: 1 NOK = 0,945072 HRK)
1 GBP = 8,986181 HRK (31.12.2010: 1 GBP = 8,608431 HRK)

Standards, interpretations and amendments issued by the International Accounting Standards Board ("IASB") and adopted by Croatia's Board, and are in force:

During the year, the Group adopted new and modified International Financial Reporting Standards and their interpretations. The application of modified IFRSs has not significantly influenced to the financial position and result of the Group and enabled data comparison. The adoption of modified standards did not affect the capital as at 1 January 2011.

- *Annual improvements to IFRSs issued in 2010: IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34 and IFRIC 13 (applied to periods starting with 1st January 2011 or later)*
- *Annual improvements to IFRSs issued in 2010: IAS 21, IAS 28, IAS 31, IAS 32 and IAS 39 Temporary Regulation Modifications (applied to periods starting with 1st January 2011 or later)*
- *Amendments to IAS 24 Related Party Disclosures (applied to periods starting with 1st January 2011 or later)*
- *IFRS 1 First-time Adoption of International Financial Reporting Standards – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (applied to periods starting with 1st January 2011 or later)*
- *IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interact project (applied to periods starting with 1st January 2011 or later)*
- *IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments project (applied to periods starting with 1st January 2011 or later)*

Standards, interpretations and amendments not in force:

On the date of approval of the financial statements, the following interpretations and standards, which were not in force as at 31 December 2011, were issued:

- *IFRS 9 Financial Instruments (new standard applied to periods starting with 1st January 2015 or later)*
- *IFRS 10 Consolidated Financial Statements (new standard applied to periods starting with 1st January 2013 or later)*
- *IFRS 11 Joint Arrangements (new standard applied to periods starting with 1st January 2013 or later)*
- *IFRS 12 Disclosure of Interests in Other Entities (new standard applied to periods starting with 1st January 2013 or later)*
- *IAS 27 and IAS 28 – modified to incorporate the consolidation exemptions (applied to periods starting with 1st January 2013 or later)*
- *IFRS 13 Fair Value Measurement (new standard applied to periods starting with 1st January 2013 or later)*
- *Modifications to IAS 1 Presentation of financial statements (applied to periods starting with 1st January 2012 or later)*
- *Modifications to IAS 19 Employee income (applied to periods starting with 1st January 2013 or later)*
- *IAS 32 Financial instruments: Presentation - Amendments to Offsetting* Financial Assets *and Financial Liabilities (applied to periods starting with 1st January 2014 or later)*
- *IFRS 1, First application of International Accounting Standards - Replacement of '*fixed dates*' for certain exceptions (applied to periods starting with 1st July 2011 or later)*
- *IFRS 1, First application of International Accounting Standards - Exemption for severe* hyperinflation *(applied to periods starting with 1st July 2011 or later)*
- *IFRS 7 Financial instruments: Disclosures (applied to periods starting with 1st July 2011 or later, or 1st January 2013 or later)*
- *IFRS 7 Financial instruments: Disclosures – Modifications to Disclosures for IFRS 9 First-time Adopters (applied to periods starting with 1st January 2015 or later)*
- *IAS 12 Income Taxes (revised) – Limited Exemption (applied to periods starting with 1st January 2012 or later)*

It is assumed by the Group's Management Board that all the above-mentioned interpretations and standards shall be applied in the Group's consolidated financial statements from the time when they shall be in force and that their adoption shall not have significant influence to consolidated financial statements in the period of first application.

Key assumptions and estimates and uncertainty in preparing consolidated financial statements

In preparing consolidated financial statements, the Group's Management Board used estimates, judgements and assumptions which have influence to accounting value of assets and liabilities, disclosing of potential items on balance sheet date and disclosed revenues and expenses of the period then ended.

The estimates were used, without limitation, to the following items: calculation and period of depreciation and remaining value of the real-estate, plants, equipment and intangible assets, decrease in value, value adjustment of inventories and disputable claims, provisions for employees' salaries and wages, court disputes and warranty repairs. More details on accounting policies with respect to estimates can be found in other parts of this note as well as other notes of the financial statements.

The impact of future events cannot be anticipated with certainty. Accounting estimates, therefore, call for judgements. Judgements used in preparing consolidated financial statements are subject to changes due *to new events, new information, new experience or changes in business environment. Actual results may differ from such estimates.*

The basic accounting policies applied in the preparation of the consolidated financial statements for the year 2011 are as set forth below:

a) Revenues

/i/ Revenues are recognized on the day of delivery of goods and/or services, or invoicing date.

/ii/ Revenues from sales of goods and services are recognized if:
- *the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;*
- *the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;*
- *the amount of revenue can be measured reliably;*
- *it is probable that the economic benefits associated with the transaction will flow to the entity; and*
- *the costs incurred or to be incurred in respect of the transaction can be measured reliably.*

/iii/ Revenues from rendered services whose outcome of a transaction can be estimated reliably, shall be recognized by reference to the stage of completion of the transaction at the end of the reporting period. Revenues from rendered services are recognized if:
- *the amount of revenue can be measured reliably;*
- *it is probable that the economic benefits associated with the transaction will flow to the entity;*
- *the stage of completion of the transaction at the end of the reporting period can be measured reliably; and*
- *the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.*

When determining revenues from rendered services based on stage of completion of contracted activities at the end of the reporting period, revenues are recognized per specific contract, pursuant to stage of contract completion method, when it is highly possible to determine the percentage of completeness, clearly identify the occurred expenses and determine:
- *Total revenues, and*
- *Total expenses up to completion of the contract.*

When the outcome of a construction contract cannot be estimated reliably, revenues shall be recognized only to the extent of contract costs incurred that it is probable will be recoverable, and the contract costs shall be recognized as an expense in the period in which they are incurred.

Contract stage of completion is determined by total costs of material, work and other expenses that relate directly to the specific contract and occurred by the end of the reporting period, related to total evaluated expenses for each construction contract.
When it is probable that total contract costs will exceed total contract revenue, the expected loss shall be recognized as an expense immediately.

Government Grants are recognized as revenues in the period when related expenses will occur, if:
- *the terms of the grants have been met*
- *it is likely that the grants will be received.*

Financial revenues include interests on invested funds, positive exchange rate differences, revenues from dividends and other financing revenues.

Revenues from interests are recognized on a time proportional basis, with regards to the real income on the invested funds, pursuant to concluded contracts.

b) Expenses

The policy of expenses is recorded in such way that the periodic accountancy system determines expenses which are applicable to recognition in the calculation of current year result.

The recognition of expenses occurs if:

- a) *expenses result in decrease of funds or increase of liabilities that can be reliably measured;*
- b) *expenses have direct relation to occurred costs and revenues;*
- c) *when it is expected to achieve revenues in multiple reporting periods, recognition of expenses is performed by allocation on reporting periods;*
- d) *expense is immediately recognized in the reporting period when outflow does not achieve future economic benefit, and there are no conditions to be recognized as assets in the Balance Sheet;*
- e) *expense is immediately recognized in the reporting period upon appearance of liability, and there are no conditions to be recognized as an asset.*

Losses that can be identified as expenses are classified as expenses. In that case losses have to be related to occurring revenues. Losses are covered with revenues of the reporting period.
Financial expenses include expenses for interests against loans, discounts from sales of securities and receivables prior to their maturity, interests arising from delayed payments, negative exchange rate differences, losses from sales of shares and business portions, as well as other financing expenses.

Financing expenses are recognized on time proportional basis, respectively in the period when they occurred. Negative exchange rate differences are not capitalized, but are included in the expenses of the period.

c) Financial result and profit tax

Profit/loss before taxation is determined in such way that the total accounting expenses are subtracted from total accounting revenues.

Profit tax liability (current tax) is determined pursuant to valid regulations of Law on Profit Tax.

d) Fixed intangible assets

Fixed intangible assets comprise of non-monetary assets that are identifiable without physical substance. Fixed intangible assets are recognized if they met the following conditions:

- a) *it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity,*
- b) *the cost of the asset can be measured reliably, and*
- c) *its single acquisition value exceeds 3,500 Croatian Kuna.*

If the criteria are not met, the costs are recorded as current period expenses.

After initial recognition, intangible asset is recorded based on its acquisition cost decreased for value adjustment (accumulated depreciation) and for accumulated losses from decrease.

Intangible assets are excluded from the Balance Sheet in case of disposal or if there are no expected future economic benefits from it. Gains or losses (difference between revenues from disposal and book value) arising from disposal or withdrawal of intangible assets are recognized as revenues or expenses of the current period.
Intangible assets are depreciated as every single item by linear method against the rate of 25% annually.

/i/ Depreciation is recorded from the first day of the following month after the fixed intangible asset has been activated. Depreciation for sold, given, or in any other way disposed or destroyed fixed intangible assets is recognized as expense up to the end of month when the assets were still in use.

e) Fixed tangible assets

Fixed tangible assets comprise of property, plants and equipment which the Group:
- *Owns and uses in business operations, administrative purposes or for rental to others;*
- *Acquires or builds with intention of continuous use;*
- *Does not sell through its basic operations and is expected that those assets will be in use for more than one period.*

Fixed tangible assets are recognized if following fulfilled:
- *it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity,*
- *the cost of the asset can be measured reliably,*
- *its single acquisition value exceeds 3,500 Croatian Kuna and useful period of life exceeds one year.*

Except, if the single value of the asset does not exceed 3,500 Croatian Kuna and it is undoubtedly evaluated that its useful period of life exceeds one year, it is considered as fixed tangible asset and is completely written-off as expense of the current period. Fixed tangible assets that do not exceed value of 3,500 Croatian Kuna nor its useful period of life exceeds one year are recorded as inventory and therefore are completely written-off upon activation.
Upon acquisition, fixed tangible assets are recorded in the business books at acquisition value.
Goods and services made internally and included in use as fixed tangible assets are recorded at their production value, under condition that the production value does not exceed net market value. Production value does not include internal profits, unusual values of waste material, work and other assets.
The production cost is determined pursuant to IAS 2 – Inventories. Additional costs are included in the book value of the assets or, if needed, are recognized as separate assets only if the company expects to have future economic benefits of that assets, or if their expense can be reliably measured.

After initial recognition, property, plant and equipment are recorded based on their acquisition cost decreased for accumulated depreciation and accumulated losses from decrease. Basis for depreciation is acquisition value (gross book value) of the single asset.

Plants and equipment are withdrawn from use and are disposed when there are no expected economic benefits from them or market values.
If while in use a fixed tangible asset has been damaged or withdrawn from active use, the asset is depreciated up to the end of month when it was withdrawn from active use.
If its net book value exceeds its sale value, the difference is recorded as expense upon sale (net principle recording). In case its sale value exceeds its book value, the difference is recorded as revenue of the current period (net principle recording).

/i/ *Depreciation is charged for each single asset, against linear method at rates suitable for disposal of acquisition value through its evaluated useful period of life. Land and assets under construction are not depreciated.*
Rates applied for depreciation are as follows:

- buildings	*2,5-10%*
- ships and docks	*2,5-5%*
- cranes and plants	*6,67-10%*
- production equipment	*10-12%*
- transportation vehicles	*20%*
- office computer and related equipment	*10-20%*

The Group evaluates useful life of fixed tangible assets on a regular basis and based on the Management's decisions uses legally recognized accelerated depreciation rates.
Depreciation and recognition of expense starts from the first day of the month followed by activation of the fixed tangible asset.
Depreciation for sold, given, or in any other way disposed or destroyed fixed tangible assets is recognized as expense up to the end of month when the assets were still in use.
Fixed assets are recorded in the Balance Sheet even if they are completely written-off, up to sale, gift, or disposal of any kind.

f) Long-term financial assets

Long-term financial assets represent investment of cash, property and rights for generating revenues, whose benefits are expected in periods longer than one year.
Accounting policy and procedures differ depending whether the investments occurred from:

- *Investments in participation at others up to 20% of voting power;*
- *Investment into associated companies (portion 20% - 50%);*
- *Investments into dependent companies (portion exceeds 50%);*
- *Investments through business relations with partners in market.*

Initial investment in associated and dependent companies is recorded at acquisition cost increased for transaction expenses. On the financial statements date these investments are recorded depending on the portion in these associated companies.

g) Inventories

Inventories of raw and other material are valued according to their acquisition value (average weighted price principle) or their net market value, depending on which one is lower.

Reduction of inventory value is performed by charging expenses of the current period based on evaluation made by professional services on damage, deterioration of inventory and in case when recoverable value (value that can be realized by sale or use of those inventories) is lower than acquisition cost.
If the professional services evaluate that use of certain inventories in future contracts is doubtful, respectively that some products on stock are not spendable, the company performs write-off of inventories, which is recorded as expense of the current period. When and if there are no circumstances that caused the prior reduction of value, respectively write-off of inventories, the value of inventories should be increased up to the acquisition cost, meaning up to value that can be realized and expended in regular production.

Small inventory and tools are being written-off completely upon activation.

Inventories that are damaged upon manipulation and storage, as well as inventories that lose their usage value are being written-off and charge operating expenses through inventory taking or by special committees with permission granted by a responsible person, up to the written-off values prescribed by Leakage, Breakage and Damage Act and with permission of Tax Department.

If the Mother company up to the reporting period does not conclude the initiated contract, it records the value of inventories for production in progress as of the end of the period.

The value of production in progress is recorded at actual costs that can be related to a specific contract.

The actual costs comprise of direct and indirect costs of production which occurred by the end of the reporting period:

- *Variable and fixed direct costs of production that can be directly related to the specific contract on a reasonable basis, such as costs of built in material, direct work and services of others directly involved in rendering services*
- *Variable and fixed general costs of production that are being allocated by a key to specific contracts, respectively in proportion to direct costs, meaning that are being assigned to the value of inventories for production in progress based on normal capacity (normal realized capacity in regular circumstances of operations through a certain period of time).*

The total amount of recorded costs of production in progress decrease expenses of the period, respectively are recognized as expenses of the period at the same time as revenues are being recognized upon completion of works and delivery of the total project.

Cost i.e. value of inventories for production in progress does not include profit or general operation expenses and administrative expenses which cannot be related to rendering of services, but charge expenses of the period when they occurred.

h) Receivables

Trade receivables, receivables from state, employees and other legal and private persons are recorded in the business books based on valid documentation of their occurrence and data on their value.

Trade receivables from customers in abroad shown in foreign exchange currencies are recorded in Croatian currency, calculated based on mean exchange rate of Croatian National Bank as of the date of recording the receivable.
Upon collection of receivable, the differences that occur due to exchange rate are recorded as revenues or expenses of the Group.
Open balances of trade receivables from customers in abroad as of the Balance Sheet date are set at mean exchange rate of Croatian National Bank and the exchange rate differences are recorded as revenues or expenses.
Increase of receivables for interests is based on the contract and calculations of the legal interest rates as prescribed by law.
Value adjustment of receivables is performed based on evaluation that the receivable has not been collected when due, i.e. that it is uncollectible and claimed on court. The Decision on value adjustment of receivables is made by the Management.
Value adjustment of receivables is recorded in the Profit and Loss Account of the Group.

i) Short-term financial assets

Short-term financial assets comprise of investment of cash, property, rights and granted merchandize loans for generating revenues, whose benefits are expected to arise within one year.
Short-term financial investments within one year are recorded in the business books at investment cost. The value is determined for each investment.
Value adjustment of short-term assets is performed based on evaluation that the investment is high risk or it is claimed on court. The Decision is made by the Mother company's Management Board.

j) Cash and cash equivalents

Cash and cash equivalents include cash in banks, in register and short-term deposits at banks with contracted maturity of up to 3 months. The balance of the cash in bank is recorded at nominal value in Croatian currency. Foreign exchange funds in bank and register is set at mean exchange rate of Croatian National Bank.
Exchange rate differences arising from setting foreign exchange funds to mean exchange rate of Croatian National Bank are recorded as revenues / expenses of the current period.

k) Deferred costs and accrued revenues

Outflows that covered expenses referring to future periods are recorded according to the amounts specified in valid documentation supporting the business event.
Discrepancy of the calculation period of deferred costs at the end of the year creates a balance which is transferred into the following period as a Balance Sheet position.
Realized revenues that do not meet the criteria to be recorded as receivables, are recorded in the calculated amount specified in the valid documentation supporting the business event, and are being transferred as a Balance Sheet position to the following period in which they are carried over to the receivables once they meet the criteria.

l) Equity

Equity is own source for financing assets and is expressed pursuant to articles of International Financial Reporting Standards as remaining of the assets after deduction of all liabilities. Subscribed capital is recorded in the amount that is subscribed in the court registry upon establishment, i.e. change of subscribed value of capital in the commercial registry.Policy of recording reserves depends on their shape and policy of the Group (legal, statutory and similar).

m) Provisions

Provisions should be recognized when an entity has a present obligation (legal or constructive) as a result of a past event or it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at balance sheet date and adjusted to the latest best evaluations.
Provisions arising from contracts, such as provisions for severance wages, provisions for expenses in guaranty periods, and provisions for expenses arising from initiated court claims are also recognized as an expense of the period for risk provisions based on legal and other regulations.

n) Long-term liabilities

Long-term liabilities are recorded in the business books in the amounts specified in valid documentation or contract supporting the event. Long-term liabilities refer to liabilities with maturity exceeding 12 months starting from the date of financial statements. Classification of the long-term and short-term liabilities is performed on each day of the Balance Sheet.

o) Short-term liabilities

Short-term liabilities are recorded in the business books in the amount specified in valid documentation or contract supporting the event. Short-term liabilities refer to liabilities with maturity less than 12 months. Classification of the long-term and short-term liabilities is performed on each day of the Balance Sheet.
Short-term liabilities recorded in foreign exchange funds and those with currency clause are being set at mean exchange rate of the Croatian National Bank in Croatian currency.
Upon settlement of these liabilities, the differences that occur as exchange rate differences are recorded as revenues or expenses of the company.
Open balances of liabilities shown in the foreign exchange currencies are being set at mean exchange rate of Croatian National Bank as of the Balance Sheet Date and exchange rate differences that occurred are recorded as revenues or expenses of the company.

Rental costs are recorded as expense of the period when they occurred.

p) Accrued costs and deferred revenues

Expenses that occurred in the current period for which the company did not receive invoices or has incomplete documentation for their booking, but it is possible to determine their amount (for example rental costs, audit fees based on contract) are recorded in the Balance Sheet as accrued costs, since the liability will be recorded in the future period.

Realized expenses which do not meet the criteria to be recorded as liabilities, are recorded at the amount specified in the documentation which anticipated the business event and are transferred as a Balance Sheet position in the following period in which they are carried over to liabilities once they meet the criteria.
Collected revenues that do not meet the criteria to be recognized in the current period are deferred for future periods.

3. REVENUES FROM SALES

in HRK

	31.12.2011	31.12.2010
Revenues from rendered services on domestic market	44.787.880	39.146.992
Revenues from rendered services on foreign market	290.641.142	261.940.095
Total	**335.429.022**	**301.087.087**

Revenues from rendered services classified by type of service rendered:

in HRK

	Domestic market	Foreign market	Total
Shiprepair	32.608.321	241.607.928	274.216.249
Conversions	10.332.097	48.247.382	58.579.479
Other	1.847.462	785.832	2.633.294
Total	**44.787.880**	**290.641.142**	**335.429.022**

4. OTHER REVENUES

in HRK

	31.12.2011	31.12.2010
Revenues from sales of material	6.458.990	7.028.717
Rentals (non-associates)	856.335	959.337
Revenues from withdrawal of long-term reserves	2.806.609	10.252.170
Revenues from Government grants	78.000	26.200
Revenues of written-off liabilities	651.289	414.298
Collection of damage claims from insurance	292.495	151.084
Revenues from sales of buildings, plants and equipment	39.062	18.428
Other revenues	2.158.765	2.507.626
Total	**13.341.545**	**21.357.860**

The revenues from withdrawal of long-term reserves amount to 2.498.699 Croatian Kuna and refer to revenues from withdrawal of realized reserves based on issued guarantees for warranty repairs on Annamaria platform, and withdrawal of reserves based on closed disputes and bankruptcy reserves in the amount of 307.910 Croatian Kuna.

Other revenues in the amount of 2.158.765 *Croatian Kuna refer to subsequently recognized revenues from the previous years, inventory surplus, written-off liabilities and similar.*

5. MATERIAL EXPENSES AND EXPENSES OF PRODUCTS SOLD

in HRK

	31.12.2011	31.12.2010
Raw and other material		
Used raw and other material	67.339.210	52.968.920
Used energy	16.715.989	17.646.389
Small inventory and spare parts	798.179	1.388.034
Total raw and other material	**84.853.378**	**72.003.343**
Other external expenses		
Transportation, phone, post and similar services	1.253.372	1.114.061
Production services	76.993.367	73.990.641
Subsupplier services	46.505.249	35.559.706
Maintenance services	15.828.029	9.091.152
Rental expenses	7.073.449	1.419.821
Intellectual services	1.958.296	2.176.165
Other services	1.353.061	1.475.497
Total other external expenses	**150.964.823**	**124.827.043**
TOTAL MATERIAL EXPENSES	**235.818.201**	**196.830.386**

6. EMPLOYEE EXPENSES

in HRK

	31.12.2011	31.12.2010
Net salaries and wages	41.306.662	39.400.342
Taxes and contributions from the salaries	17.827.271	16.609.148
Contributions on the salaries	11.068.839	10.436.965
Terminal pays	214.044	192.000
Compensations for travelling costs, daily allowances, annual bonuses	6.057.557	6.131.999
TOTAL	**76.548.815**	**72.696.012**

In 2011 the Group paid to the employees the annual bonuses in accordance with the Collective Agreement signed with the Unions, where those employees who are members of the Union received larger bonuses than the non-members.

7. DEPRECIATION

in HRK

	31.12.2011	31.12.2010
Buildings, facilities and equipment	16.575.630	22.511.428
TOTAL	**16.575.630**	**22.511.428**

For 2011 the Mother Company applied single rates of depreciation, with respect to the year 2010 where the Company used its legal right to accelerated depreciation. If the accelerated method were used, the depreciation cost would be higher by approximately 14,500,000 Croatian Kuna. The 2011 depreciation rate is 79%.

8. VALUE ADJUSTMENT

No value adjustment was recorded.

9. PROVISIONS

The Mother Company's provisions in the amount of 751.000 Croatian Kuna include provisions for legal proceedings, which started in 2011.

10. OTHER EXPENSES

in HRK

	31.12.2011	31.12.2010
Entertainment and aids	2.246.550	1.656.292
Insurance premiums	5.098.186	3.910.043
Bank services and fees	875.090	387.755
Taxes and contributions not dependant on the result	2.781.846	2.517.160
Other expenses	2.911.619	3.152.403
TOTAL	**14.154.075**	**11.382.869**

11. NET FINANCIAL (EXPENSES)/INCOME

in HRK

	31.12.2011	31.12.2010
Financial income		
Interests	1.697.998	2.450.826
Sale of financial instruments	464.892	395.672
Positive exchange rate differences	1.200.361	-
Total financial income	**3.363.251**	**2.846.498**
Financial expenses		
Interests	471.985	424.575
Negative exchange rate differences	-	885.084
Total financial expenses	**471.985**	**1.309.659**
NET FINANCIAL (EXPENSES)/INCOME	**2.891.266**	**1.536.839**

12. PROFIT TAX

From the difference between revenues and expenses in the period from 1 January to 31 December 2011 the Group realized a profit in the amount of 5.984.889 Croatian Kuna. After deduction of a tax obligation in the amount of 1.253.239 Croatian Kuna, the profit after tax amounted to 4.731.650 Croatian Kuna.

13. EARNINGS PER SHARE

in HRK

	31.12.2011	31.12.2010
Net profit	4.731.650	6.068.552
Shares exclusive of own shares	14.522.286	13.767.190
Earnings per share (Croatian Kuna)	**0,33**	**0,44**

14. BUILDINGS, FACILITIES AND EQUIPMENT

[redacted]

15. INVESTMENT IN ASSOCIATES

Net accounting value of investment in associates includes:

	31.12.2011		31.12.2010	
	in HRK	Share (%)	in HRK	Share (%)
North Adriatic Offshore Ravenna	-	-	38.018	49%

The North Adriatic Offshore company went into liquidation. After the liquidation proceedings was finished, a share adjustment was made in the amount of 38,018 Croatian Kuna. In January 2011, an amount of 122,192.31 EUR was received as share in the remaining value after completion of the liquidation proceedings (Note 4).

16. SHORT-TERM FINANCIAL ASSETS

The short-term financial assets in the amount of 26.464.892 Croatian Kuna include loans to companies abroad.

17. INVENTORIES

in HRK

	31.12.2011	31.12.2010
Raw and other material	27.100.198	16.958.369
Raw and other material under transportation	3.677.702	-
Production in progress	2.239.620	3.950.145
Small inventory	6.818.790	6.401.674
Small inventory value adjustment	(6.818.790)	(6.399.320)
TOTAL	**33.017.520**	**20.910.868**

The raw and other material was recorded on the basis of purchase prices decreased by a value adjustment of the inventories. The inventories value adjustment was performed upon the opening of the bankruptcy proceedings when the Mother Company evaluated the assets recorded in the books on the day of the opening of the bankruptcy proceedings. Taking into consideration the complexity of inventories issue, for purpose of the analytical evaluation, based on the then assumption that the Group was not continuing its business, but the assets would be sold for settling the bankruptcy debts, an estimate of inventories encashment according to the liquidation value was made which produced a book item for adjustment of value as per estimate.
The Group continued with its business that ultimately resulted in the termination of the bankruptcy proceedings, and the stock was used in the normal production activities, noting that during the entire period of bankruptcy the stock was equally supplied and used.

In 2010, the Group performed a value adjustment of the analytical structure of raw and other material on stock to the collective adjustment of inventories as per estimate. The value adjustment of inventories as per estimate represents collective adjustment of inventories not recorded analytically.

18. TRADE AND OTHER RECEIVABLES

in HRK

	31.12.2011	31.12.2010
Receivables from customers	49.144.869	30.411.749
Receivables from employees	5.492	30.510
Receivables from state	12.250.143	9.524.167
Prepaid expenses	23.500.350	18.712.679
Other receivables	2.257.129	5.475.568
Total	**87.157.983**	**64.154.673**

Age structure of matured receivables from customers:

in HRK

	31.12.2011	31.12.2010
1 -90 days	38.821.560	29.099.579
91 -180 days	2.514.969	1.176.537
181 - 365 days	7.774.582	85.234
Over 365 days	33.758	50.399
TOTAL	**49.144.869**	**30.411.749**

Age structure of decrease of value of receivables:

	31.12.2011	31.12.2010
HRK	3.761.758	2.600.115
EUR	45.383.111	27.811.634
USD	-	-
Other currency	-	-
Total	**49.144.869**	**30.411.749**

19. CASH AND CASH EQUIVALENTS

in HRK

	31.12.2011	31.12.2010
Money in bank	2.817.396	8.578.256
Cash in register	6.539	6.908
Time deposits	34.976.697	57.265.108
TOTAL	**37.800.632**	**65.850.272**

20. EQUITY AND RESERVES

(i) *On the day of 31 December 2011 the issued share capital, fully paid, amounted to 168,132,470 Croatian Kuna and was divided in 16.813.247 ordinary shares each having a nominal value of 10 Croatian Kuna.*

The owners of ordinary shares are entitled to dividends and one vote per share. The Mother Company did not pay out dividends for the year 2008 neither 2009 nor 2010, as in accordance with the Company's General Assembly's decisions on profit distribution.

(ii) *On the day of 31 December 2011 the Mother Company owned 825.187 own shares (31 December 2010: 282.308), making 4.90% of the share capital.*

(iii) *On the day of 31 December 2011 the statutory reserve within the frame of the statutory and other reserves, amounted to 6.922.223 Croatian Kuna (2010: 6.922.223 Croatian Kuna). The statutory reserve was formed in accordance with the Croatian law stipulating that 5% of the profit for the year is transferred to the statutory reserve until it grows to 5% of the issued share capital.*
In accordance with the Mother Company's General Assembly's decision, the 2011 profit was distributed to other reserves and reserves for own shares, and the subsidiary company's profit was distributed to retained profit.
The statutory and other reserves for own shares include 17.462.223 Croatian Kuna (2010: 14.462.223 Croatian Kuna) of reserves for own shares which cannot be distributed to shareholders.

21. DEBENTURES WITH INTEREST CHARGE

The total debentures with interest charge for the year 2011 amounted to 809.209 Croatian Kuna of long-term debentures and 8.070.672 Croatian Kuna for short-term debentures.

The long-term debentures include finance lease liabilities to the BKS Bank BKS leasing Croatia as well as 540.252 Croatian Kuna on the account of short-term debentures. The remaining part of the short-term debentures in the amount of 7.530.420 Croatian Kuna is a short-term loan.

The debenture payment terms on 31 December 2011:

in HRK

	Total	1 year of less	2 -5 years	More than 5 years
Finance lease	1.349.461	540.252	809.209	-
Short-term loan	7.530.420	7.530.420	-	-
Total	**8.879.881**	**8.070.672**	**809.209**	

22. TRADE AND OTHER LIABILITIES

in HRK

	31.12.2011	31.12.2010
Trade payables	74.407.679	46.712.690
Employee payables	4.295.789	3.787.261
Taxes and contributions	3.879.123	3.723.356
Advance payments	490	1.035.779
Accrued costs	3.016.602	5.493.042
Other liabilities	2.891.489	3.001.964
TOTAL	**88.491.172**	**63.754.092**

Trade payables structure as per currency:

in HRK

	31.12.2011	31.12.2010
HRK	63.441.261	44.207.667
EUR	10.966.418	2.505.023
USD	-	-
Other currency	-	-
Total	**74.407.679**	**46.712.690**

23. RELATIONSHIP WITH RELATED ENTERPRISES

in HRK

Related enterprises and key shareholders	2011	2010
Sale to related enterprises		
Sale to associates	-	-
Sale to key shareholders	17.866.392	15.976.285
Purchase from related enterprises		
Purchase from associates	-	-
Purchase from key shareholders	-	-
Receivables from related enterprises		
Receivables from associates	-	-
Receivables from key shareholders	1.381.735	-
Liabilities to related enterprises		
Liabilities to associates	-	-
Liabilities to key shareholders	-	-

Transactions between related enterprises are realized under normal market conditions.

Key Management

The Management Board of the Mother Company is composed of the Chairman of the Board and two members of the Board.
The total compensation (gross) for the members of the Mother Company's Management Board for the year 2010 amounted to 2.132.294 Croatian Kuna.
The total compensation (gross) for the members of the Supervisory Board for the year 2010 amounted to 571.802 Croatian Kuna.
The Mother Company has not granted any loans to the members of the Supervisory Board or Mother Company's Management Board.

24. PROVISIONS

The provisions of the Mother Company amounted to 3.119.105 Croatian Kuna and include provisions for opened legal proceedings.

25. OTHER LONG-TERM LIABILITIES

Other liabilities as at 31 December 2011 in the amount of 10.281.159 Croatian Kuna comprise of potential liabilities for disputed bankruptcy creditors' claims, securities and legal fees, as in accordance with the bankruptcy plan.

26. FINANCIAL INSTRUMENTS

The operations of the Mother Company bear various financial risks: market risk (including currency, interest rate and price risk), credit risk and liquidity risk. The Mother Company is exposed to currency, interest rate and credit risk while performing its regular business operations.
The policy of risk management related to the financial management is as follows:

Financial risk factors

The operations of the Mother Company bear various financial risks including the effects of market price changes, changes of foreign exchange rates and interest rates. The Mother Company does not use derivative financial instruments as an active security from exposure to financial risks.

Currency risk

All revenues from rendering services of the Mother Company on the foreign market is denominated generally in EUR (smaller amount in USD) as well as the payments. Revenues from rendering services in domestic market are denominated in Croatian kuna with EUR currency clause.

Approximately merely 5-10% of expenses are denominated in EUR. The currency risk also affects foreign exchange deposits which the Mother Company can have, if those deposits are dedicated and set at a longer period, i.e. as collateral to bank guarantees in favour of the client.
Therefore, changes in currencies between EUR and HRK, and USD and HRK have an effect on the operation result, however due to high turnover ratio of receivables and low levels of production in progress, the currency risk is not materially significant so for that reason the Mother Company does not perform active security for exposure to foreign currency operations.

Credit risk

Financial assets that can potential bring the Mother Company to a credit risk includes trade receivables, value of works on construction of offshore projects and ship modifications. Trade receivables are shown decreased for doubtful and uncertain receivables. The Group does not have any other concentration of credit risk.

Interest rate risk

The Group does not have any significant assets or significant liabilities with interest rates except for deposits, and hence does not perform active security from exposure to interest rate risk.

Liquidity risk

Liquidity risk, also called financing risk, is a risk of coping with difficulties in procurement of funds for settlement of liabilities against financial instruments.
Short-term liabilities are completely covered by short-term assets.

Fair value

The Management's estimate on the fair value of financial assets and liabilities and accounting value as shown in the balance sheet are set forth below:

in HRK

	2011	
	Accounting value	**Fair value**
Financial assets available for sale	-	-
Investment in subsidiaries and associates	-	-
Receivables from customers and other receivables	87.157.983	87.157.983
Liabilities from debentures with interest charge	8.879.881	8.879.881
Other long-term liabilities	10.281.159	10.281.159
Trade and other payables	88.491.172	88.491.172

The fair value of the financial assets and liabilities is based on the quoted market price as at the balance sheet date, if available. Where the market price is not available, the Group makes an estimate of the fair value on the basis of the publicly disclosed information from external sources or on the basis of the discounted cash flow method if applicable.
It is considered that the value of the receivables/liabilities with less than one year to maturity corresponds to the fair value. The other receivables/liabilities are discounted to determine the fair value.

Equity management

The main goal of the equity management is to ensure support to business and maximize shareholder value. The Group adjusts its equity policy in accordance with economic changes. With purpose to maintain or adjust the equity structure, the Group may re-adjust dividends payouts or return on capital or place a new emission of shares. There were no changes in the goals, policies or processes during the years 2010 and 2011.

27. POTENTIAL LIABILITIES

Potential liabilities and court disputes

As of 31 December 2011, the Mother Company was involved in several disputes which have arisen from its business and a few disputes over indemnity obligations deriving from employment relationships. The Mother Company already made provisions in its books for such claims in case of unfavourable outcomes.

28. IMPORTANT ACCOUNTING ESTIMATES AND JUDGEMENTS

In the application of accounting policies, the Mother Company's Management made following judgements, independently of those which include estimates, and which have the most important influence to the amounts shown in the financial statements.

Recognition of revenues

Revenue is recognized when the goods have been delivered or services have been rendered, or when the risks and rewards of ownership of goods have been substantively transferred to the customer. The estimate of the expected return of goods and other discounts is deducted from the revenues from sales and is recorded as included liabilities or provisions. Such estimates were made on the basis of the analysis of the existing contractual or legal obligations, historical trends and experience of the Group.

Profit tax

The profit tax was calculated on the basis of the interpretation of rules and laws in force.

Decrease in value of receivables

Estimate of an irretrievable value of sales of goods and services is made on the balance sheet date (plus monthly) based on the estimated probability of collection of doubtful receivables. Each client is evaluated separately concerning its status (a client having its account blocked, or legal action has been started), receivable maturity, stage of the legal process or payment security instruments such as promissory note.

Provisions for potential liabilities

The Group recognizes provisions which result from court disputes in which the Group is defendant most likely to have unfavourable outcomes and where the outflows may be reliably estimated. In estimating such provisions, the Group regularly consults with legal professionals.

29. EVENTS AFTER BALANCE SHEET DATE

There were no significant events after the balance sheet date.

30. INFORMATION ON KEY ASSUMPTIONS REGARDING FUTURE BUSINESS OPERATIONS AND EVALUATION OF UNCERTAINTY AS AT BALANCE SHEET DATE

There are no significant information nor uncertainty which might influence the Group's business.

31. COURT DISPUTES

On the day of 31 December 2011 the Mother Company participated in 43 disputes, worth about 6,070,000 Croatian Kuna in principal, as defendant and 11 disputes, worth about 7,850,000 Croatian Kuna in principal, as distrainee.

32. MORTGAGE

The Group is free of any mortgage or other burden.

33. CASH FLOW STATEMENT

The Cash Flow Statement 2011 was made by use of the indirect method.

34. PREPARATION AND APPROVAL OF FINANCIAL STATEMENTS

The financial statements have been prepared and approved by the Management Board of the Company on 13 April 2012.

Robert Škifić, Chairman of the Board

Sandra Uzelac, Member of the Board

Davor Lukeš, Member of the Board