

ISTRATURIST UMAG d.d.

**ANNUAL FINANCIAL STATEMENTS
31 DECEMBER 2005**

RESPONSIBILITIES OF THE MANAGEMENT AND SUPERVISORY BOARDS FOR THE PREPARATION AND APPROVAL OF THE ANNUAL FINANCIAL STATEMENTS

The Management Board is required to prepare financial statements for each financial year which give a true and fair view of the financial position of the Group and the Company and of the results of their operations and cash flows, in accordance with applicable accounting standards, 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 Group and the Company 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; make judgements and estimates that are reasonable and prudent; and prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Group and the Company will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the Company including the annual financial statements, following which the Supervisory Board is required to approve the annual financial statements for submission to the General Assembly of Shareholders for adoption.

The financial statements set out on pages 3 to 28 were authorised by the Management Board on 10 March 2006 for issue to the Supervisory Board and are signed below to signify this.

President of the Management Board
Gordana Tomičić



Independent Auditors' Report to the shareholders of Istraturist Umag d.d.

We have audited the accompanying consolidated balance sheet of Istraturist Umag d.d. ("the Group") as of 31 December 2005, and the related consolidated statements of income, changes in equity and cash flows for the year then ended. We have also audited the accompanying unconsolidated balance sheet of Istraturist Umag d.d. ("the Company") as of 31 December 2005, and the related unconsolidated statements of income, changes in equity and cash flows for the year then ended. These financial statements which have been presented together to report the financial position, results of operations, and changes in cash flows for both the consolidated Group and parent Company, are the responsibility of the parent Company's management. 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 plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the financial position of the Group and of the Company as of 31 December 2005 and of the results of their operations and their cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Croatia d.o.o. za reviziju
Registered Auditors
Centar Kaptol
Nova Ves 11
10000 Zagreb
Croatia

10 March 2006

INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2005

In HRK thousand	Notes	Consolidated Group		Parent Company	
		2005	2004	2005	2004
Operating revenue					
Sales revenue	3	284,350	281,692	276,918	275,350
Other operating income	4	12,521	12,090	11,041	11,181
Total operating income		296,871	293,782	287,959	286,531
Operating costs					
Raw material, consumables and services used	5	111,469	107,540	104,356	101,672
Personnel expenses	6	74,881	71,619	74,045	70,827
Depreciation and amortisation	12	37,338	47,117	37,258	47,069
Other operating expenses	7	19,322	19,060	18,613	19,098
Total operating costs		243,010	245,336	234,272	238,666
Operating profit		53,861	48,446	53,687	47,865
Financial income	8	15,830	19,467	15,778	19,397
Financial expense	8	(19,944)	(25,971)	(19,871)	(25,922)
Net financial expense		(4,114)	(6,504)	(4,093)	(6,525)
Profit before tax		49,747	41,942	49,594	41,340
Income tax (charge)/credit	9	(6,295)	38,264	(6,230)	38,407
Profit for the year		43,452	80,206	43,364	79,747
Earnings per share (in HRK)	10	9.29	17.16	9.28	17.06

BALANCE SHEET

AS AT 31 DECEMBER 2005

In HRK thousand	Notes	Consolidated Group		Parent Company	
		2005	2004	2005	2004
ASSETS					
Non-current assets					
Property, plant and equipment	12	893,761	813,652	893,006	813,198
Intangible assets	12	1,168	1,577	1,168	1,577
Loans and receivables	13	455	643	455	643
Other investment		-	-	37	37
Deferred tax assets	14	40,177	46,407	40,177	46,407
Total non-current assets		935,561	862,279	934,843	861,862
Current assets					
Inventories	15	12,750	13,767	12,666	13,754
Trade and other receivables	16	14,143	13,919	12,204	12,154
Other financial assets	17	1,508	783	4,384	3,574
Cash and cash equivalents	18	703	1,773	668	1,491
Total current assets		29,104	30,242	29,922	30,973
TOTAL ASSETS		964,665	892,521	964,765	892,835
EQUITY AND LIABILITIES					
Equity					
Share capital	22	467,500	467,500	467,500	467,500
Legal reserves	22	23,375	23,375	23,375	23,375
Retained earnings		183,244	164,569	183,750	165,163
Total shareholders equity		674,119	655,444	674,625	656,038
Liabilities					
Non-current liabilities					
Loans and borrowings	20	187,495	121,022	187,495	121,022
Trade and other payables	19	21	227	21	227
Total non-current liabilities		187,516	121,249	187,516	121,249
Current liabilities					
Loans and borrowings	20	57,023	81,349	57,023	81,349
Trade and other payables	19	45,387	33,140	44,981	32,860
Provisions	21	620	1,339	620	1,339
Total current liabilities		103,030	115,828	102,624	115,548
Total liabilities		290,546	237,077	290,140	236,797
TOTAL EQUITY AND LIABILITIES		964,665	892,521	964,765	892,835

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2005

Consolidated Group	Share capital	Legal reserves	Retained earnings	Total
In HRK thousand				
Balance at 1 January 2004	467,500	23,375	107,738	598,613
Dividend for 2003 (Note 11)	-	-	(23,375)	(23,375)
Profit for the year (recognised income)	-	-	80,206	80,206
Balance at 31 December 2004	467,500	23,375	164,569	655,444
Dividend for 2004 (Note 11)	-	-	(24,777)	(24,777)
Profit for the year (recognised income)	-	-	43,452	43,452
Balance at 31 December 2005	467,500	23,375	183,244	674,119

Parent Company	Share capital	Legal reserves	Retained earnings	Total
In HRK thousand				
Balance at 1 January 2004	467,500	23,375	108,791	599,666
Dividend for 2003 (Note 11)	-	-	(23,375)	(23,375)
Profit for the year (recognised income)	-	-	79,747	79,747
Balance at 31 December 2004	467,500	23,375	165,163	656,038
Dividend for 2004 (Note 11)	-	-	(24,777)	(24,777)
Profit for the year (recognised income)	-	-	43,364	43,364
Balance at 31 December 2005	467,500	23,375	183,750	674,625

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2005**

In HRK thousand	Note	Consolidated Group		Parent Company	
		2005	2004	2005	2004
<i>Cash flow from operating activities:</i>					
Profit before tax		49,747	41,942	49,594	41,340
<i>Adjustment for:</i>					
Depreciation		36,804	46,544	36,723	46,496
Amortisation		534	573	535	573
Write off of property, plant and equipment		1,245	159	1,246	159
Write off of miscellaneous inventory		6,068	6,337	6,055	6,329
Profit on sale of property, plant and equipment		(902)	(1,570)	(902)	(1,570)
Impairment loss on receivables		325	1,061	325	1,061
Recovery of impaired receivables		(224)	(566)	(224)	(566)
Increase/(decrease) in provision		(719)	644	(719)	644
Fair value gains on financial assets		(719)	-	(719)	-
Dividend income		(113)	(104)	(113)	(104)
Interest income		(184)	(193)	(183)	(191)
Interest expense		9,319	9,366	9,319	9,366
Profit on sale of investments		-	(82)	-	(82)
Foreign exchange (gains)/losses		(7,456)	709	(7,456)	709
Operating profit before working capital changes		93,725	104,820	93,481	104,164
Increase of trade and other receivables		(112)	(2,409)	(23)	(2,051)
Increase of trade and other payables		5,847	2,863	5,744	2,791
Decrease in inventories		34	44	33	44
Cash generated from operations		99,494	105,318	99,235	104,948
Interest paid		(8,958)	(9,681)	(8,958)	(9,681)
Income tax paid		(44)	(52)	-	-
Cash flow from operating activities		90,492	95,585	90,277	95,267
<i>Cash flow from investing activities</i>					
Acquisition of property, plant and equipment		(113,399)	(86,783)	(113,019)	(86,611)
Acquisition of intangible assets		(125)	(536)	(126)	(536)
Acquisition of miscellaneous inventory		(5,085)	(6,517)	(5,001)	(6,508)
Interest received		184	193	183	191
Dividends received		113	104	113	104
Acquisition of other investments		(100)	-	(100)	-
Proceeds from sale of property, plant and equipment		1,911	2,695	1,911	2,695
Proceeds from sale of investments		69	139	69	139
Cash flow from investing activities		(116,432)	(90,705)	(115,970)	(90,526)
<i>Cash flow from financing activities</i>					
Proceeds from loans and borrowings		180,334	142,213	180,334	142,213
Repayment of loans and borrowings		(130,731)	(124,847)	(130,731)	(124,847)
Dividends paid		(24,733)	(23,078)	(24,733)	(23,078)
Cash flow from financing activities		24,870	(5,712)	24,870	(5,712)
Net decrease in cash and cash equivalents		(1,070)	(832)	(823)	(971)
Cash and cash equivalents at the beginning of the year	18	1,773	2,605	1,491	2,462
Cash and cash equivalents at the end of the year		703	1,773	668	1,491

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 1 – GENERAL INFORMATION

Istraturist Umag d.d. is a joint stock company registered and domiciled in Umag, Croatia. These financial statements present together the consolidated Group and unconsolidated parent Company.

The Istraturist Group (“Group”) comprises Istraturist Umag (the “Parent Company” or “Company”), a joint stock company for catering and tourism and its 100% owned subsidiary Istra Golf, a limited liability company which organizes the annual ATP tennis tournament in Umag.

According to the laws of the Republic of Croatia and with the approval of the Croatian Privatisation Fund, the Company was transformed from state ownership into a joint stock company in the year 1993. The Company and its subsidiary are registered at the Commercial Court in Rijeka.

The Istraturist Group is controlled by Zagrebačka banka d.d., Zagreb. The ownership structure as at 31 December 2005 is disclosed in note 22.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

Significant accounting policies adopted in the preparation of these financial statements are set out below:

a) Basis of preparation

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”).

Basis of preparation

These financial statements are presented in the Croatian currency, Kuna (HRK), which is also the functional currency, rounded to the nearest thousand and have been prepared under the historical cost convention except for the assets that are valued at fair values: derivative financial instruments, financial assets at fair value through profit or loss..

The preparation of financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under circumstances, the result of which the bases of making the judgments about carrying values 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 if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of IFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 26 Accounting estimates and judgments.

The accounting policies have been applied consistently by all Group entities and do not differ from accounting policies applied in the previous year.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (continued)

The financial statements have been prepared under the assumption that the Group and Company will continue to operate as a going concern. In view of the Group's and Company's net current liabilities, the Group and Company obtained short term funding after balance date as disclosed in note 27. Further, the majority shareholder and its related parties are also major creditors of the Group and the Company (as disclosed in note 20).

The Group and the Company is currently assessing the potential impact of the new and revised standards in issue that will be effective from 1 January 2006 or later periods. The Group and the Company do not expect that the other new and revised standards and interpretations will have a significant effect on the Group's and Company's results and financial position, although they will expand the disclosures in certain areas.

b) Basis of consolidation

Subsidiaries are those companies in which Istraturist Umag d.d., directly or indirectly, has the power to exercise financial and operating policies of an entity, so as to obtain benefits from its subsidiaries. Subsidiaries are consolidated from the date on which control commences.

Intra-group transactions, balances and unrealised gains on transactions between Group entities are eliminated. Unrealised losses are also eliminated but only to the extent that there is no evidence of impairment.

c) Foreign currency

Transactions in foreign currencies are translated into Croatian kuna (the functional currency) at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into kuna at the foreign exchange rate ruling at balance sheet date. Foreign exchange gains and losses resulting from the settlement of cash transactions and from translation of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

d) Property, plant and equipment

Items of property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and impairment losses as per note 2(f). Cost includes all direct costs attributable to bringing the asset to working condition for its intended use, including the proportion of the related borrowing costs for property, plant and equipment incurred during the period of their construction.

Borrowing costs in relation to borrowings, that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset, net of any interest earned on those borrowings. Qualifying assets are assets which take a substantial period of time to get ready for their intended use or sale.

Depreciation is calculated on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment.

The average estimated useful lives are as follows:

Buildings	35	years
Plant and equipment	4 – 20	years

Freehold land and assets under construction are not depreciated since they have indefinite useful lives.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (continued)

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 Group and the Company 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.

e) Intangible assets

Intangible assets comprise software and are presented at cost less accumulated amortisation and impairment losses. Amortisation is charged to income statement on a straight line basis over the estimated useful life. The estimated useful life is 5 years.

f) Impairment of the assets

The carrying amounts of the Group's and Company's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amount is estimated. The recoverable amount of assets is the greater of their net selling price and value in use.

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 risk specific to the assets. For assets that do not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which the assets belong.

g) Financial assets

The Group and the Company classifies its financial assets into the following categories: at fair value through profit or loss, and loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as 'held for trading' unless they are designated as hedges. Assets in those category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Group and the Company intends to sell immediately or in the near term, which are designated at fair value through profit or loss or as available for sale.

Initial and subsequent measurement

All financial assets at fair value through profit or loss are recognised on the trade date, which is the date that the Group and the Company commits to purchase the asset. Loans and receivables are recognised on the day they are transferred to the Group and the Company.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets are initially measured at the fair value of the consideration given for them, including transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets at fair value through profit or loss are initially recognised at fair value and transaction costs are expenses in the income statement. All financial assets at fair value through profit or loss are subsequently carried at fair value without any deduction for transaction costs that the Group and the Company may incur on sale or other disposal.

Valuation

The fair value of financial instruments at fair value through profit or loss is based on their quoted market price at the balance sheet date, without any deduction for transaction costs. The fair value of derivatives that are not exchange-traded is estimated at the amount that the Group and the Company would receive or pay to terminate the contract at the balance sheet date.

Realised and unrealised gains and losses

Realised and unrealised gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are recognised in the income statement in the period in which they arise.

Derecognition

A financial asset is derecognised when the Group and the Company loses the contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when it is extinguished. Financial assets at fair value through profit or loss that are derecognised and corresponding receivables from the buyer for the payment are recognised as of the date the Group and the Company commits to sell the assets. The Group and the Company uses the specific identification method to determine the gain or loss on derecognition. Loans and receivables are derecognised on the day they are transferred by the Group and the Company.

h) Leases

Assets leased to others are included in the balance sheet under “Property, plant and equipment”. Assets are depreciated on a straight-line basis over their expected useful lives on a basis consistent with similar owned property and equipment. Rental income is recognised over the lease term.

i) Inventories

Inventories of raw materials and consumable goods are stated at the lower of cost or net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and selling expenses. Inventories are valued based on purchase price, using the weighted average costs principle.

Small miscellaneous inventory is stated at cost less accumulated depreciation and impairment as per note 2 (f). Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of inventories.

The estimated useful lives of small miscellaneous inventory is as follows:

Glassware and cutlery:	2 years
Porcelain, kitchen appliances and linens:	3 years
Curtains and blankets:	5 years
Other small inventory:	5 years

Other miscellaneous inventories (goods for resale) are stated at the lower of purchase price or net realisable value using the FIFO method (first in, first out).

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (continued)

j) Trade receivables

Trade receivables are initially measured at the fair value and subsequently stated at amortised cost less impairment loss as per note 2 (f).

k) Cash and cash equivalents

Cash and cash equivalents, for the purpose of the balance sheet and the statement of cash flows, consist of cash in hand and balances with banks.

l) Borrowings

Interest bearing loans and borrowings are recognised initially at fair value of the proceeds received, less attributable transaction costs. In subsequent periods, interest bearing loans and borrowings are stated at amortised cost using the effective interest method. Any difference between proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings on an effective interest basis.

m) Employee entitlements

(i) Defined contribution pension funds contributions

Obligations for defined contributions to pension funds are recognised as an expense in the income statement when incurred.

(ii) Bonus plans

A liability for employee benefits is recognised in provisions based on the Group's and Company's formal plan and when past practice has created a valid expectation by the Management Board/key employees that they will receive a bonus and the amount can be determined before the time of issuing the financial statements.

Liabilities for bonus plans are expected to be settled within 12 months of the balance sheet date and are measured at the amounts expected to be paid when they are settled.

n) Taxation

Corporate income taxes are computed on the basis of reported income under Croatian laws and regulations.

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

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

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (continued)

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

o) Dividend distribution

Dividend distribution to the Group's and the Company's shareholders are recognised as a liability in the Group's and the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

p) Provisions

A provision is recognised when the Group or the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where the Group or the Company expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

q) Revenue recognition

Revenue from services is recognised in the period in which services are provided in proportion to the stage of completion of the transaction at the balance sheet date. Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership are transferred to the buyer. Revenues are stated net of taxes, discounts and volume rebates. Provisions for rebates to customers are recognised in the same period that the related sales are recorded, based on contract terms.

r) Net financing income and costs

Net financial costs comprises interest payable on borrowings calculated using the effective interest rate method, interest receivable on funds invested, dividend income, foreign exchange gains and losses, gains and losses on financial assets at fair value through profit and loss and gains and losses on forward exchange contracts that are recognised in the income statement.

Interest income is recognised in the income statement as it accrues, using the effective interest method. Dividend income is recognised in the income statement in the period when the dividend is received.

s) Derivative financial instruments

The Group and the Company use derivative financial instruments to hedge economically its exposure to foreign exchange risk arising from operational activities. Hedge accounting has not been applied and those derivative instruments are accounted for as financial instruments held for trading. Derivative instruments are measured initially at fair value of consideration given for them and subsequent to initial recognition, are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss. The fair value of forward exchange contract is their quoted price at the balance sheet date, being the present value of the quoted forward price.

t) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Group's current operation is in the segment of tourism (business segment) and its operations, and the majority of its assets are located in Croatia (geographical segment). Hence, segment reporting is not considered relevant.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 3 – SALES REVENUE

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Income from sale to domestic guests	63,106	60,859	56,361	54,737
Income from sale to foreign guests	221,244	220,833	220,557	220,613
	284,350	281,692	276,918	275,350

NOTE 4 – OTHER OPERATING INCOME

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Income from sale of property, plant and equipment (i)	3,327	2,695	3,327	2,695
Rental income	3,948	4,418	3,982	4,463
Sponsorships	1,369	1,598	46	35
Sale of materials	1,397	1,020	1,397	1,020
Insurance recoveries	532	570	532	555
Recovery of impairment loss and income from prior years	1,261	853	999	716
Release of provisions	506	717	506	717
Other income	181	219	252	980
	12,521	12,090	11,041	11,181

- (i) The net profit from the sale of property, plant and equipment amounts to HRK 1,044 thousand (2004: HRK 1,411 thousand). Corresponding carrying amount of assets sold is disclosed in note 7 (Other operating expenses).

NOTE 5 – RAW MATERIALS, CONSUMABLES AND SERVICES USED

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Raw materials and consumables				
Raw materials and consumables	38,552	39,519	38,098	39,160
Energy, water and telephone	18,438	17,322	18,363	17,252
Spare parts and miscellaneous inventory	5,937	6,066	5,927	6,062
	62,927	62,907	62,388	62,474
External services				
Services of Sol Melia	17,036	17,604	17,036	17,604
Maintenance services	5,938	5,693	5,758	5,677
ATP services (tennis tournament)	3,483	3,468	-	-
Utility services	3,020	2,956	3,020	2,956
Advertising and promotion	2,380	2,284	2,335	2,155
Entertainment and music services	5,034	3,966	4,832	4,043
Other services	11,651	8,662	8,987	6,763
	48,542	44,633	41,968	39,198
	111,469	107,540	104,356	101,672

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 5 – RAW MATERIALS, CONSUMABLES AND SERVICES USED (CONTINUED)

The Group and the Company appointed Sol Melia by contract as its representative in managing and operating its properties and is obliged by contract to pay a basic monthly and quarterly incentive fee.

NOTE 6 – PERSONNEL EXPENSES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Gross salaries	62,040	61,399	61,564	60,898
Other employee expenses	12,841	10,220	12,481	9,929
	74,881	71,619	74,045	70,827

Other employee expenses include travel reimbursements, redundancy payments, anniversary awards, temporarily contracted staff fees and author fees.

During 2005, the average number of employees in the Istraturist Group was 775 (2004: 773 employees), and in the Company there were 770 employees (2004: 770 employees),

Personnel expenses for Group include HRK 10.5 million (2004: HRK 10.5 million) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross II).

Personnel expenses for the Company include HRK 10.3 million (2004: HRK 10.4 million) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross II).

NOTE 7 – OTHER OPERATING EXPENSES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Utility rates and taxes	6,785	6,664	6,777	6,657
Promotions and travel	2,515	2,177	2,118	1,694
Net book value of property, plant and equipment	2,283	1,284	2,283	1,284
Insurance premiums	2,267	2,153	2,264	2,149
Subscriptions and membership fees	1,507	1,524	1,481	1,500
Bank service charges	1,641	1,279	1,616	1,256
Impairment losses on receivables	334	696	153	695
Increase in provisions	98	1,568	98	1,568
Other	1,892	1,715	1,823	2,295
	19,322	19,060	18,613	19,098

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 8 – NET FINANCIAL EXPENSES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Interest income	184	193	183	191
Dividend income	113	104	113	104
Income from equity instruments at fair value through profit and loss	722	82	722	82
Foreign exchange gain	14,811	14,233	14,760	14,165
Net income from financial instruments	-	4,855	-	4,855
Financial income	15,830	19,467	15,778	19,397
Interest expense	9,319	9,509	9,319	9,509
Foreign exchange loss	6,978	16,462	6,905	16,413
Net loss from sale of financial instruments	3,647	-	3,647	-
Financial expense	19,944	25,971	19,871	25,922
Net financial expenses	(4,114)	(6,504)	(4,093)	(6,525)

NOTE 9 – INCOME TAX (CHARGE)/CREDIT

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Current tax expense	(65)	(143)	-	-
Deferred tax (charge)/credit (note 14)	(6,230)	38,407	(6,230)	38,407
Income tax (charge)/credit	(6,295)	38,264	(6,230)	38,407

The following table presents the reconciliation of profit tax calculated at the applicable tax rate 20% (2004:20%):

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Profit before tax	49,747	41,942	49,594	41,340
Profit tax expense at 20% (2004:20 %)	(9,949)	(8,388)	(9,919)	(8,268)
Non deductible costs	(817)	(2,714)	(782)	(2,691)
Non taxable income	25	21	25	21
Recognition of deferred tax assets from previously unrecognised temporary differences	4,446	49,345	4,446	49,345
Income tax (charge)/credit	(6,295)	38,264	(6,230)	38,407
Effective tax rate	(13%)	91%	(13%)	93%

NOTES TO THE FINANCIAL STATEMENTS**FOR THE YEAR ENDED 31 DECEMBER 2005****NOTE 9 – INCOME TAX (CHARGE)/CREDIT (CONTINUED)**

Significant tax benefit in 2004 was due to the recognition of tax losses and temporary differences as a deferred tax assets in the balance sheet. In 2005 additional temporary differences were recognised given the Company believes these temporary differences will be utilised. The recognition of these deferred tax assets has resulted in a effective tax rate substantially lower when compared to the statutory tax rate.

NOTE 10 – EARNINGS PER SHARE

Earnings per share are calculated based on the net profit to the owners of ordinary shares and the average number of ordinary shares.

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Profit after tax	43,452	80,206	43,364	79,747
Number of shares issued (in thousands)	4,675	4,675	4,675	4,675
Earnings per share (in HRK)	9.29	17.16	9.28	17.06

NOTE 11 – PROPOSED DIVIDEND

During 2004, the Company paid out a dividend in the amount of HRK 23,375 thousands. The decision for the dividend payment of HRK 5.00 per share was made at the annual Shareholder assembly held during 2004.

At the annual Shareholder assembly held during 2005, the shareholders approved a dividend in respect of 2004 of HRK 5.30 per share, totalling HRK 24,777 thousand. The majority of the dividend was paid out on 1 September 2005.

The Management board propose a dividend in the amount of HRK 5.30 per share in respect of 2005, which is subject to Shareholder approval and will be paid out of 2005 profits in the total amount of HRK 24,777 thousand. Payment of proposed dividend is expected in the year 2006.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 12 – PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

Consolidated Group

In HRK thousand	Property, plant and equipment				Intangible assets
	Land and buildings	Computers, equipment and vehicles	Assets under construction	Total tangible assets	Software
Cost or deemed cost					
Balance at 1 January 2004	890,378	197,388	329	1,088,095	4,225
Additions	-	-	87,319	87,319	-
Transfer to intangible assets	-	(19)	-	(19)	19
Transfer from assets under construction	68,015	18,042	(86,593)	(536)	536
Disposals	(3,313)	(8,516)	-	(11,829)	-
Balance at 31 December 2004	955,080	206,895	1,055	1,163,030	4,780
Depreciation and impairment losses					
Balance at 1 January 2004	184,814	128,571	-	313,385	2,624
Disposals	(2,188)	(8,357)	-	(10,545)	-
Transfer to intangible assets	-	(6)	-	(6)	6
Depreciation and impairment losses	32,461	14,083	-	46,544	573
Balance at 31 December 2004	215,087	134,291	-	349,378	3,203
Carrying amount					
At 1 January 2004	705,564	68,817	329	774,710	1,601
At 31 December 2004	739,993	72,604	1,055	813,652	1,577

In HRK thousand	Property, plant and equipment				Intangible assets
	Land and buildings	Computers, equipment and vehicles	Assets under construction	Total tangible assets	Software
Cost or deemed cost					
Balance at 1 January 2005	955,080	206,895	1,055	1,163,030	4,780
Additions	-	-	119,167	119,167	125
Transfer	9,818	(9,818)	-	-	-
Transfer from assets under construction	99,516	13,044	(112,560)	-	-
Write-off and disposal	(1,861)	(12,413)	-	(14,274)	-
Balance at 31 December 2005	1,062,553	197,708	7,662	1,267,923	4,905
Depreciation and impairment losses					
Balance at 1 January 2005	215,087	134,291	-	349,378	3,203
Transfer	3,241	(3,241)	-	-	-
Disposals	(841)	(12,097)	-	(12,938)	-
Impairment	918	-	-	918	-
Depreciation charge for the year	22,559	14,245	-	36,804	534
Balance at 31 December 2005	240,964	133,198	-	374,162	3,737
Carrying amount					
At 1 January 2005	739,993	72,604	1,055	813,652	1,577
At 31 December 2005	821,589	64,510	7,662	893,761	1,168

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 12 – PROPERTY, PLANT, EQUIPMENT AND INTANGIBLE ASSETS (continued)

Parent Company

In HRK thousand	Property, plant and equipment				Intangible assets
	Land and buildings	Computers, equipment and vehicles	Assets under construction	Total tangible assets	Software
Cost or deemed cost					
Balance at 1 January 2004	890,378	197,000	329	1,087,707	4,225
Additions	-	-	87,147	87,147	-
Transfer to intangible assets	-	(19)	-	(19)	19
Transfer from assets under construction	68,015	17,870	(86,421)	(536)	536
Disposals	(3,313)	(8,516)	-	(11,829)	-
Balance at 31 December 2004	955,080	206,335	1,055	1,162,470	4,780
Depreciation and impairment losses					
Balance at 1 January 2004	184,814	128,513	-	313,327	2,624
Disposals	(2,188)	(8,357)	-	(10,545)	-
Transfer to intangible assets	-	(6)	-	(6)	6
Depreciation and impairment losses	32,461	14,035	-	46,496	573
Balance at 31 December 2004	215,087	134,185	-	349,272	3,203
Net book value					
At 1 January 2004	705,564	68,487	329	774,380	1,601
At 31 December 2004	739,993	72,150	1,055	813,198	1,577

In HRK thousand	Property, plant and equipment				Intangible assets
	Land and buildings	Computers, equipment and vehicles	Assets under construction	Total tangible assets	Software
Cost or deemed cost					
Balance at 1 January 2005	955,080	206,335	1,055	1,162,470	4,780
Additions	-	-	118,787	118,787	126
Transfer	9,818	(9,818)	-	-	-
Transfer from assets under construction	99,516	12,663	(112,179)	-	-
Disposals	(1,861)	(12,415)	-	(14,276)	-
Balance at 31 December 2005	1,062,553	196,765	7,663	1,266,981	4,906
Depreciation and impairment					
Balance at 01 January 2005	215,087	134,185	-	349,272	3,203
Impairment	918	-	-	918	-
Disposals	(842)	(12,096)	-	(12,938)	-
Transfer	3,241	(3,241)	-	-	-
Depreciation charge for the year	22,560	14,163	-	36,723	535
Balance at 31 December 2005	240,964	133,011	-	373,975	3,738
Carrying amount					
At 1 January 2005	739,993	72,150	1,055	813,198	1,577
At 31 December 2005	821,589	63,754	7,663	893,006	1,168

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 12 – PROPERTY, PLANT, EQUIPMENT AND INTANGIBLE ASSETS (continued)

Assets under construction relate to the new construction project for Garden Istra. Completion of the project is expected during 2006.

As at 31 December 2005, buildings owned by the Group and Company with a carrying value of HRK 357,564 thousands (2004: HRK 399,950 thousands) were secured against loans as disclosed in note 20 – Loans and borrowings.

Borrowing costs amounting to HRK 1,130 thousand (2004: HRK 848 thousand) have been capitalised during 2005 and included in the value of buildings. The borrowing costs comprise interest and other expenses of financing construction work performed on the tourism properties. The capitalisation rate is 5.58% (2004: 6.33%).

In 2004, the Group and Company recorded an impairment for assets not in use. The Company started with reconstructions of Istra Hotel, which at year end was partly demolished. Value of assets put out of use amounted to HRK 918 thousand (2004: HRK 12,255 thousand).

NOTE 13 – NON-CURRENT LOANS AND RECEIVABLES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Non-current loans to employees	531	744	531	744
Current portion of long term receivables (Note 17)	(76)	(101)	(76)	(101)
Total non-current loans and receivables	455	643	455	643

Loans to employees are granted for the purchase of residential apartments and are repayable over 10 to 32 years at an interest rate of 1% to 10% p.a. and educational loans repayable over 2-5 years at an interest rate of 6% p.a.

NOTE 14 – DEFERRED TAX ASSETS

Tax losses in the amount of HRK 2,072 thousand arising from the 2001 (2004: HRK 16,309 thousand of which HRK 6,321 thousand was utilised, HRK 7,916 thousand expired and HRK 2,072 thousand was carried forward), are available for offsetting against future taxable profits of the Company until 31 December 2006.

Other deferred tax asset consists of temporary differences between accounting depreciation that is presented in this financial statements and depreciation that is used in the profit tax computation. These deductible temporary differences do not expire under current tax legislation.

In HRK thousand	Consolidated Group			Parent Company		
	Depreciation differences	Tax losses	Total	Depreciation differences	Tax losses	Total
Balance at 1 January 2005	39,477	6,930	46,407	39,477	6,930	46,407
Decrease of deferred tax in the income statement	(1,372)	(4,858)	(6,230)	(1,372)	(4,858)	(6,230)
Balance at 31 December 2005	38,105	2,072	40,177	38,105	2,072	40,177

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 15 – INVENTORIES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Raw material and consumables	760	817	759	817
Goods for resale	12	7	12	7
Miscellaneous inventory	11,978	12,943	11,895	12,930
	12,750	13,767	12,666	13,754

NOTE 16 – TRADE AND OTHER RECEIVABLES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Domestic trade receivables	11,020	11,636	9,210	9,922
Receivables from related parties (Note 25)	48	181	48	181
Foreign trade receivables	2,770	3,729	2,770	3,684
Provision for impairment of receivables	(5,202)	(5,101)	(5,202)	(5,101)
Net trade receivables	8,636	10,445	6,826	8,686
VAT receivables	3,790	224	3,715	221
Receivables from employees	49	82	40	80
Receivables for advances given	144	3,000	144	3,000
Receivables for insurance claims	63	61	63	61
Other receivables	1,449	93	1,404	92
Other receivables from related companies (Note 25)	12	14	12	14
Total other receivables	5,507	3,474	5,378	3,468
Total trade and other receivables	14,143	13,919	12,204	12,154

NOTE 17 – FINANCIAL ASSETS

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Financial assets at fair value through profit or loss				
Equity securities	1,432	682	1,432	682
Other loans and receivables				
Current portion of loans and receivables	76	101	2,952	2,892
	1,508	783	4,384	3,574

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 18 – CASH AND CASH EQUIVALENTS

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Giro accounts	318	727	315	721
Foreign currency accounts	225	856	194	580
Cash in hand	160	190	159	190
	703	1,773	668	1,491

NOTE 19 – TRADE AND OTHER PAYABLES

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Non current liabilities				
Other employee entitlements (i)	21	227	21	227
Total non-current liabilities	21	227	21	227
Current liabilities				
Trade payables	33,117	22,509	32,867	22,491
Liabilities towards related parties	6	30	6	30
Other employee entitlements (i)	6,429	4,815	6,325	4,712
Liability for net salary	2,228	1,976	2,209	1,962
Liability for tax and contributions	1,446	2,185	1,430	1,948
Liability for advances	1,074	827	1,068	827
Liabilities for dividends	487	443	487	443
Other liabilities	600	355	589	447
Total current liabilities	45,387	33,140	44,981	32,860

(i) Other employee entitlements comprise constructive and contractual obligations arising from organisational changes and contracts signed with employees in respect of overtime hours.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 20 – LOANS AND BORROWINGS

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Current				
Related parties (Note 25):				
<i>Zagrebačka Banka Group</i>				
Zagrebačka Banka d.d., Zagreb	28,350	2,325	28,350	2,325
Zagrebačka Banka Bosnia and Herzegovina, Mostar	-	24,111	-	24,111
<i>UniCredito Italiano Group</i>				
UniBanka a.s., Bratislava	8,517	8,924	8,517	8,924
Bulbank AD, Sofija	16,868	45,989	16,868	45,989
UniCredit Romania	3,288	-	3,288	-
Total current loans	57,023	81,349	57,023	81,349
Non-current				
Related parties (Note 25):				
<i>UniCredito Italiano Group</i>				
UniBanka a.s., Bratislava	33,697	44,233	33,697	44,233
Bulbank AD, Sofija	84,311	76,789	84,311	76,789
UniCredit Romania	16,435	-	16,435	-
<i>Other non related parties</i>				
HBOR	53,052	-	53,052	-
Total non-current loans	187,495	121,022	187,495	121,022
Total loans and borrowings	244,518	202,371	244,518	202,371

Loans and borrowings include amounts secured against property in the amount of HRK 357,564 thousand (2004: HRK 399,950 thousand). Refer to note 12 – Property, plant and equipment and intangible assets.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 20 – LOANS AND BORROWINGS (CONTINUED)

In HRK thousand		Total 2005	Repayment period			
Creditor	Interest rate		1 year or less	1-2 years	2-5 years	More than 5 years
Loans		216,168	28,673	36,252	108,385	42,858
UniBanka, a.s., Bratislava, in CHF	3 month Libor for CHF +1.8% margin	42,214	8,517	8,517	25,180	-
Bulbank AD, Sofia, in EUR	3 month Libor for EUR +1.8% margin	101,179	16,868	16,868	50,604	16,839
HBOR, in HRK	4%, Fixed	53,052	-	7,579	22,737	22,736
UniCredit Romania, in CHF	3 month Libor for CHF +1.8% margin	19,723	3,288	3,288	9,864	3,283
Revolving loans		28,350	28,350	-	-	-
Zagrebacka banka d.d., in HRK	RS +2.35% margin	17,300	17,300	-	-	-
Zagrebacka banka d.d., in HRK	RS +2.35% margin	11,050	11,050	-	-	-
Total loans and borrowings:		244,518	57,023	36,252	108,385	42,858

Revolving loans interest rates are based on the Croatian referent rate (RS) which represents the weighted average yield value for State treasury notes.

At 31 December 2005, the Company had unused revolving credit line facilities at Zagrebačka banka d.d., Zagreb totalling HRK 2.8 million (2004: HRK 28.8 million),

The fair value of the HBOR borrowing at 31. December 2005 amounts to HRK 52,644 thousand. The fair value is based on cash flows discounted using a rate based on the average borrowing rate of 4.23%.

NOTE 21 – PROVISIONS

Provisions for court cases

In HRK thousand	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Balance at 1 January 2005	1,339	695	1,339	695
Additional provisions	98	1,568	98	1,568
Unused amounts reversed	(506)	(717)	(506)	(717)
Used during the year	(311)	(207)	(311)	(207)
Balance at 31 December 2005	620	1,339	620	1,339

The provision represents certain legal claims brought against the Group and the Company. The provision charge is recognised in the profit or loss. Management believe, based on legal advice, that the outcome of these legal claims will not give rise to any significant loss beyond the amounts provided for at 31 December 2005.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 22 – SHARE CAPITAL AND RESERVES

Issued share capital comprises 4,674,995 ordinary shares (2004: 4,674,995 ordinary shares). The nominal value of each share is HRK 100 (2004: HRK 100). The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

The legal reserve is formed in accordance with the Companies Act which prescribes that the Company must transfer 5% of the current year's profit into these reserves until these reserves total five per cent (5%) of the company's share capital. This legal reserve now corresponds to 5% of the Company's share capital. This reserve is not distributable.

The ownership structure of the company Istraturist Umag d.d. as at 31 December 2005 according to the Central Deposit Agency is as follows:

	share
1. ZAGREBAČKA BANKA D.D.	71.80%
2. PBZ D.D./KAPITALNI FOND D.D. CLOSED INVESTMENT FUND	8.77%
3. HVB SPLITSKA BANKA D.D./COLLECTIVE ACCOUNT, FOR SKAN, ENSK, BANK,, ŠVED, REZIDENTI	2.41%
4. HRVATSKI FOND ZA PRIVATIZACIJU	1.75%
5. PBZ D.D./NLB/HANSBANK CLIENTS ACCOUNT	1.40%
6. MEĐIMURSKA BANKA D.D. ČAKOVEC	0.45%
7. HVB SPLITSKA BANKA D.D./COLLECTIVE ACCOUNT, FOR BANK AUSTRIA CREDITANSTALT AG	0.43%
8. P.B.Z. D.D./NLB/HANSABANK CLIENTS ACCOUNT	0.39%
9. P.B.Z. D.D./SKRBNIČKI ZBIRNI RACUN KLIJENT	0.20%
10. OTHER SHAREHOLDERS	12.40%
	<u>100.00%</u>

The ownership structure of the company Istraturist Umag d.d. as at 31 December 2004 according to the Central Deposit Agency is as follows:

1. ZAGREBAČKA BANKA D.D.	71.80%
2. PBZ D.D./KAPITALNI FOND D.D. ZATVORENI INVESTICIJSKI FOND	8.77%
3. HRVATSKI FOND ZA PRIVATIZACIJU	1.79%
4. DOM HOLDING D.D.	1.38%
5. PBZ D.D./NLB/HANSBANK CLIENTS ACCOUNT	1.32%
6. HVB SPLITSKA BANKA D.D./ZBIRNI RN. ZA SKAN. ENSK. BANK., ŠVED. REZIDENTI	1.17%
7. HVB SPLITSKA BANKA D.D./ZBIRNI RN. ZA BANK AUSTRIA CREDITANSTALT AG	0.86%
8. MEĐIMURSKA BANKA D.D. ČAKOVEC	0.49%
9. RAIFFEISENBANK AUSTRIA D.D. ZAGREB/ZBIRNI SKRBNIČKI RAČUN ZA DP	0.31%
10. OTHER SHAREHOLDERS	12.11%
	<u>100.00%</u>

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 23 – FINANCIAL RISK MANAGEMENT

Financial risk factors

The Group and Company is exposed to various financial risks that are related to foreign currency, interest rates, credit and liquidity risk. The Group monitors these risks and seeks to minimise their potential effect on the Group's financial exposure, using protective instruments that are available on the financial market.

(i) Foreign currency and interest rate risk

Income from foreign sales is predominantly realised in Euro (EUR). Income from domestic sales is realised in Croatian kuna (HRK). Long-term loans mainly comprise loans in Euro (EUR) and Swiss francs (CHF). Foreign currency risk is present due to possible changes in the exchange rates of foreign currencies. The Group is also exposed to interest rate risk as loans are agreed at floating rates.

Derivative financial instruments are entered into for the purpose of hedging the Group's exposure to foreign exchange and interest rate risk.

(ii) Credit risk

Financial assets that may expose the Group to credit risk comprise cash, receivables from customers and loan receivables. The Group keep its cash in the bank that is also the majority owner of the Group. Provisions for impairment of receivables from customers are made for bad and doubtful receivables. The Group decreases credit risk by short-term deposits at the bank, that is the owner of the Group. Loans given are secured by payment instruments.

Concentration of credit risk from receivables is limited due to the large number of customers. Management believes that there are no additional credit risks that might require an increase in provisions for impairment for trade and other receivables.

(iii) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, as well as the availability of financial assets in the form of credit lines.

NOTE 24 – CONTINGENCIES

Legal cases

Prior to 1991, the Company owed approximately DEM 31 million (equivalent of approximately EUR 16 million) to Ljubljanska banka d.d., Ljubljana in respect of borrowings and other financial obligations. Following the dissolution of former Yugoslavia, entities resumed their operating activities within separate independent republics. It is against this background, that the Company reached a contractual agreement with Zagrebačka banka d.d., Zagreb.

Pursuant to the regulations passed in the Republic of Croatia upon becoming an independent state, which define the settlement of the deposits of Croatian citizens with banks domiciled in the Republic of Croatia, and pursuant to a contract concluded with the Croatian Ministry of Finance, Zagrebačka banka d.d., Zagreb retained a part of its receivables from Ljubljanska banka d.d., Ljubljana amounting to DEM 31 million with the objective to sell them to its customer Istraturist Umag d.d., Umag.

On the basis of this transaction, the Company assumed a receivable from Ljubljanska banka d.d., Ljubljana of DEM 31 million; in accordance with the Law on Obligations, the Company offset the

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 24 – CONTINGENCIES (continued)

The operations and assets of Ljubljanska banka d.d., Ljubljana were subsequently acquired by and transferred to Nova Ljubljanska banka d.d., Ljubljana; Nova Ljubljanska banka d.d., Ljubljana does not recognise the liabilities of Ljubljanska banka d.d., Ljubljana, including liabilities to Croatian depositors and the receivable purchased by the Company from Zagrebačka banka d.d., Zagreb.

Nova Ljubljanska banka d.d. brought legal action against the Company in Slovenian courts demanding the repayment of the original liability of DEM 31 million plus interest.

The first instance Court in Slovenia brought decisions in favour of Ljubljanska banka d.d. and Nova Ljubljanska banka d.d., upon which the Company lodged an appeal:

- The second instance Court confirmed one of the first judgements, to which the Company, within the statutory limit lodged an extraordinary appeal against this judgement, which included revision, application for protection of legality and application for a retrial.

In December 2004, the Supreme Court of the Republic of Slovenia agreed with the request for a revision, terminated the decisions of the courts of first and second instance and returned the case to the first instance Court for a retrial.

The Supreme Court of Slovenia concluded that the courts have incorrectly applied material law concerning:

- Legal interpretation of the contract of sale of receivable made between the Company and Zagrebačka banka, d.d., on the basis of which the Company assumed a receivable from Ljubljanska banka, d.d. and
- Legal provisions concerning the presumptions for settlement of receivables between entities.
- In second instance trial of the second instance trial Court in March 2005, the complete judgement of the first instance Court was cancelled and the entire case was returned for re-trial.

This ruling significantly influences the future of this case and also other similar cases between the parties that are in progress in courts in Slovenia and Croatia.

The Company brought legal action against Ljubljanska Banka d.d. and Nova Ljubljanska Banka d.d. at the Commercial Court in Zagreb regarding the termination of liabilities, due to the offset against receivables.

The receivables claimed by the Company are not recognised in the financial statements of the Company, nor is any liability recognised to Ljubljanska Banka d.d. or Nova Ljubljanska Banka d.d.

Should the legal proceedings not be positively resolved for the Company, the Company's Management believes that this resolution will be the topic of constant negotiations between the Government of the Republic of Slovenia and the Government of the Republic of Croatia dealing with the issues of foreign currency savings of Croatian citizens with banks domiciled in the Republic of Slovenia.

Ownership of land and buildings

As at 31 December 2005, the ownership over the Company's land and buildings was registered partly under the name of Istraturist Umag d.d. and partly under the name of Istraturist holding company for hotel management and tourism s.p.o., Umag prior to privatisation. The process of re-registering ownership over land and buildings with Istraturist Umag d.d. is still in progress. The financial statements have been compiled under the assumption of the complete Court registration of ownership of land and buildings which upon privatisation were included in the equity of Istraturist Umag d.d.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005

NOTE 25 – RELATED PARTY TRANSACTIONS

- a) The Istraturist Umag Group is controlled by Zagrebačka Banka d.d., Zagreb by their 71.8% shareholding. The remaining 28.2% is owned by various individuals and legal entities. The ultimate parent company is UniCredito Italiano S.p.A..
- b) Subsidiaries of the Company

	Country of registration	Share of ownership	
		2005	2004
Istra Golf Umag d.o.o.	Croatia	100%	100%

The core activity of the subsidiary is the organisation of the annual ATP tennis tournament in Umag, Croatia.

- c) The nature of transactions between related parties and the Group comprises financing and banking services.
- a. During the year, the following transactions with the Zagrebačka Banka Group were included in the income statement:

In HRK thousand	2005	2004
Zagrebačka banka d.d. Zagreb		
Interest income	40	170
Income from financial instruments	1,390	4,855
Other income	302	225
Interest expense	757	747
Fee expense	371	394
Zagrebačka banka BH Mostar		
Interest expense	474	477

- b. During the year, the following transactions with other related parties within the UniCredito Group were included in the income statement:

In HRK thousand	2005	2004
Interest expense		
UniBanka a.s. Bratislava	1,704	2,338
Bulbank AD, Sofija	5,148	5,782
UniCredit Romania	281	-
	7,133	8,120
Fee expense		
UniBanka a.s., Bratislava	51	61
Bulbank AD, Sofija	484	103
UniCredit Romania	91	-
	626	164

On 31 December 2005 the Company had receivables from operating activities towards the group of HRK 60 thousand (2004: HRK 195 thousand), and total liabilities arising from loans and other liabilities of HRK 191,465 thousands (2004: HRK 202,401 thousand).

NOTES TO THE FINANCIAL STATEMENTS**FOR THE YEAR ENDED 31 DECEMBER 2005****NOTE 25 – RELATED PARTY TRANSACTIONS (continued)**

d) Key management compensation

In HRK '000	Consolidated Group		Parent Company	
	2005	2004	2005	2004
Key management compensation	6,894	6,140	6,639	5,889

Key management includes the Management Board, department and executive directors. Key management comprises 23 persons (2004: 23 persons).

NOTE 26 – ACCOUNTING ESTIMATES AND JUDGEMENTS**(a) Key sources of estimation***Income tax*

Tax calculations are performed based on the Company's interpretation of current tax laws and regulations. These calculations which support the tax return may be subjected to review and approval by the local tax authorities.

Trade receivable impairment

Trade receivables have been estimated on each balance sheet date (and monthly) and are impaired according to an estimate of the probability to collect amounts. Each customer is evaluated separately based on its status (for example, customer is blocked and is a cash only customer, legal procedures have commenced), the ageing of the amount due, stage of legal case (short-legal procedure or regular legal procedure), security of payment (e.g. bill of exchange).

Management Bonuses

Each manager has a range of goals: financial goals; qualitative goals and goals for the development of organisation including projects. For 2005, the total amount of management bonuses amounted to HRK 2,510 thousand.

(b) Critical accounting judgments in applying accounting principles

Management believes there were no material judgment matters to report, except provisions for legal claims as disclosed in Note 21.

NOTE 27 – EVENTS AFTER THE BALANCE SHEET DATE AND CAPITAL COMMITMENTS

As at 31 December 2005, the Company entered in contracts totalling HRK 5.3 million with various suppliers for renovation and construction work in 2006, mainly related to the construction of the new Garden Istra Hotel.

To complete the 2006 investment plan, on 31 December 2005 the Company signed a long term loan agreement in the amount of HRK 138.7 millions with the Croatian Bank for Reconstruction and Development (HBOR) which will finance the construction of the new Garden Istra Hotel. Repayment of the loan will start on 31 December 2007. The interest rate will be 2% on the loan amount of HRK 108 million, and interest charge on the remaining part of the loan in the amount of HRK 30.75 million will be 4%. Interest will be charged on a quarterly basis.

On 08 February 2006, the Company signed a short term loan agreement in the amount of HRK 10 million with Erste & Steiermaerkische bank d.d. The purpose of the loan is to increase current liquidity. The revolving short term loan matures on 31 July 2006. Interest will be charged at interest rate for treasury bills of the Ministry of finance plus a margin of 1.34%.