Financial statements and Independent Auditors' Report

Kosovo Energy Corporation J.S.C.

31 December 2006

Contents

Grant Thornton

Independent Auditors' Report

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To the Management and shareholders of

Kosovo Energy Corporation J.S.C.

We were engaged to audit the accompanying financial statements of the Kosovo Energy Corporation J.S.C. (further referred to as "the Company" or "KEK") which comprise of the Balance sheet as at 31 December 2006, and the Statement of income, Statement of changes in equity and Statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, included on pages 5 to 26.

Management's responsibility for financial statements

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

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. Except as disclosed in the following paragraphs, 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 risks of material misstatement of the financial statements, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate 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.

Basis for qualified opinion

As it is disclosed in Note 4 to the accompanying financial statements, at 31 December 2006, the net carrying value of Company's property, plant and equipment amounts EUR 210,922 thousands. The Company's property, plant and equipment are carried at their cost or valuation less accumulated depreciation and accumulated impairment losses. Accumulated impairment losses have been initially recognized in the Company's accounts as of 01 January 2005 (the opening balance sheet date following the process of legal transformation of the Company) in the amount of EUR 101,886 thousands based on the valuation of the Company's assets performed by independent professional appraisers. Subsequent to 01 January 2005 and up to the balance sheet date, as it is disclosed in the table of movement in Note 4, the impairment provision has been changed for the related part included into assets disposed of, than assets transferred to KOSTT JSC as well as for the adjustment occurring upon corrections made in the assets register, so that the balance of impairment provision at 31 December 2006 amounts to EUR 134,376 thousands. However, the accounting policy related to subsequent measurement of the impairment provision on assets subject to depreciation as disclosed in Note 2, requires from the management to perform "impairment" test on an annual basis. We were not able to assure ourselves that such test has been performed over the significant items of Company's property, plant and equipment as of the balance sheet dates. Therefore, we were not able to satisfy ourselves with the net carrying amount of the Company's property, plant and equipment as at 31 December 2006.

Furthermore and at the balance sheet date, the ownership status over the majority of the Company's property, plant and equipment is still unresolved and uncertainties exist in respect to possible future ownership claims.

As it is further disclosed in Note 5 to the accompanying financial statements, at 31 December 2006, the Company's stock amounts EUR 11,623 thousands, net of provision for slow moving and obsolete items in the amount of EUR 26,461 thousands. Such provision was initially recognized in the Company's accounts as of 01 January 2005 (the opening balance sheet date following the process of legal transformation of the Company) at a level of 80% from the stock balance existing on 31 December 2003 upon management estimations and remained unchanged up to the date of this report. There is no updated detailed analysis of the Company's slow – moving and obsolete stock performed as of 31 December 2006. Therefore, we were unable to obtain reasonable assurance for the validity of the stock provision balance as of 31 December 2006.

As it is further disclosed in Note 6 to the accompanying financial statements, at 31 December 2006, included into the total Company's trade and other receivables, the balance of trade receivables amounts to EUR 12,240 thousands, net of provision for impairment amounting EUR 244,500 thousands. We were not able, applying standard and alternative audit procedures, to verify the validity of this balance as of the balance sheet date.

As it is further disclosed in the Note 12 to the accompanying financial statements, at 31 December 2006, the balance of provision for ash dumps amounts EUR 30,000 thousands. The provision was initially established as of 01 January 2005 based on the results from the financial due diligence performed by independent accountants. Owing to the lack of sufficient appropriate analysis supporting the amount accounted for, we were unable to obtain reasonable assurance as for the appropriateness and accuracy of the provision balance as of 31 December 2006.

As it is further disclosed in Notes 2.4 and 2.15 to the financial statements, the major part of the total depreciation charge recognized in the Company's current profit & loss relates to items of property, plant and equipment existing at 01 January 2005 (the opening balance sheet date) which are carried in the Company's accounts at their appraised values determined by the independent professional valuers.

For taxation purposes, the Kosovo Income Tax regulation requires the use of historical cost as a basis for calculating the depreciation charge. According to the accepted accounting framework, the difference between the carrying amounts of the items of property, plant and equipment and their tax base represents taxable or deductible temporary difference, thus creating deferred tax liabilities / assets and accordingly deferred tax expense / benefit.

The Company has not recognized any deferred tax liabilities or assets and accordingly deferred tax expense or benefit in its financial statements as of and for the year ended 31 December 2006 neither and due to the lack of sufficient reliable evidence we were not able to make our own assessments.

Opinion

In our opinion, except for the matters discussed in the preceding paragraphs, the financial statements present fairly, in all material respects, the financial position of the Company as of 31 December 2006, and its financial performance, changes in equity and its cash flows for the year then ended in accordance with the International Financial Reporting Standards.

Emphasis of matter

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

As it is disclosed in the Note 2 to the accompanying financial statements, these financial statements have been prepared on the assumption that the Company will continue as a going concern. Currently, the Company's operations are largely dependent and supported by various grant funds. Management considers that sufficient outside funds will be also available in the foreseeable future so as to enable the Company to continue with its business operations.

Grant Thornton

Grant Thornton,

Skopje,
February 03 2009

Balance sheet

	Notes	At 31 December 2006	At 31 December 2005
			(000 EUR)
Assets			
Non-current assets			
Property, plant and equipment	4	210,922	235,454
Other intangible assets	4	56	73
		210,978	**235,527**
Current assets			
Inventories	5	11,623	7,864
Trade and other receivables, net	6	23,422	13,718
Cash and cash equivalents	7	9,901	38,411
		44,946	**59,993**
Total assets		**255,924**	**295,520**
Equity and liabilities			
Equity	8		
Share capital		25	25
Reserves		687,794	675,460
Accumulated (Losses)		(565,266)	(543,952)
Total equity		**122,553**	**131,533**
Liabilities			
Non – current liabilities			
Non - interest bearing borrowings	9	10,000	10,000
Deferred grants	10	32,565	14,704
Pension fund liabilities	11	-	16,939
Provisions	12	30,000	30,000
		72,565	**71,643**
Current liabilities			
Trade and other liabilities	13	47,699	69,895
Accrued expenses	14	13,107	22,449
		60,806	**92,344**
Total liabilities		**133,371**	**163,987**
Total equity and liabilities		**255,924**	**295,520**

These financial statements have been approved by the Board of Management of the Company on January 23 2009 and signed on its behalf by,

Arben Gjukaj
Managing Director
06.04.2009

Mr. Salih Bytyqi
Financial Director
06.04.2009

See accompanying notes to the financial statements

Income statement

	Notes	2006	2005
		(000 EUR)	
		Year ended 31 December	
Operating income			
Sales	**15**	117,632	112,284
Other operating income	**16**	20,011	1,452
Income from grants	**17**	16,977	36,843
		154,620	**150,579**
Less: Operating (expenses)			
Depreciation	**4**	(26,854)	(33,100)
Staff costs	**18**	(41,171)	(38,646)
Electricity and other utilities	**19**	(43,020)	(33,220)
Maintenance costs	**20**	(6,214)	(4,162)
Materials and supplies		(15,009)	(13,257)
Loss from impairment of receivables	**6**	(30,101)	(58,245)
Other operating expenses	**21**	(18,501)	(18,985)
(Loss) from operations		**(26,250)**	**(49,036)**
Financial income	**22**	280	276
Financial (expenses)	**22**	(4)	(13)
(Loss) before tax		**(25,974)**	**(48,773)**
Income tax expense	**23**	-	-
(Loss) for the year		**(25,974)**	**(48,773)**

See accompanying notes to the financial statements

Statement of changes in equity

	Share Capital	Reserves	Accumulated (losses)	(000 EUR) Total
At 01 January 2005	25	675,460	(495,179)	180,306
(Loss) for the year	-	-	(48,773)	(48,773)
At 31 December 2005	**25**	**675,460**	**(543,952)**	**131,533**
At 01 January 2006 as stated	**25**	**675,460**	**(543,952)**	**131,533**
Restatement	-	62,877	(24,903)	37,974
At 01 January 2006 restated	**25**	**738,337**	**(568,855)**	**169,507**
(Loss) for the year	-	-	(25,974)	(25,974)
Transfer of assets to KOSTT (see Notes 4, 5 and 8)	-	(50,915)	29,345	(21,570)
Disposal of assets (see Note 4)	-	(18)	218	200
Additionally identified assets (see Notes 4 and 8)	-	390	-	390
At 31 December 2006	**25**	**687,794**	**(565,266)**	**122,553**

Statement of cash flows

	Notes	(000 EUR) Year ended 31 December 2006	2005
Operating			
Net (loss) before income tax		**(25,974)**	**(48,773)**
Adjusted for:			
Depreciation		26,854	33,100
Income from grants		(16,977)	(36,843)
Allowance for bad and doubtful debts		29,756	58,245
Income from written off pension fund liabilities		(18,220)	-
Net carrying value of disposed assets		303	441
Operating profit before working capital changes:		*(4,258)*	*6,170*
Changes in working capital:			
Inventory		(4,211)	(1,327)
Trade and other receivables		(39,576)	(59,646)
Trade and other liabilities		7,263	39,486
		(40,782)	**(15,317)**
Investing			
Purchase of property, plant and equipment		(25,252)	(19,217)
		(25,252)	**(19,217)**
Financing			
Grants received		37,566	51,547
Loan received		-	10,000
		37,566	**61,547**
Net change in cash and cash equivalents		**(28,468)**	**27,013**
Cash and cash equivalents at beginning as stated		38,411	11,398
Restatement (see Note 2.1)		(42)	-
Cash and cash equivalents at beginning-restated	**7**	**38,369**	**11,398**
Cash and cash equivalents at end	**7**	**9,901**	**38,411**

Notes to the financial statements

1 General

Kosovo Energy Corporation J.S.C. ("the Company" or "KEK") is shareholding Company incorporated in Kosovo and registered with the Provisional Business Registration under Reg.No. 70325399 dated December 27, 2005. The Company is founded following the transformation of the former Publicly Owned Enterprise "Korporata Energjetike e Kosoves" ("KEK") and under the provisions of UNMIK Regulation No. 2001/6 from 8 February 2001. The address of its registered head office is: Mother Teresa Street No. 36, 10 000 Prishtina, Kosovo. The total number of the Company's employees at 31 December 2006 is 7,404 (2005: 8,353 persons).

The Company's initial registered capital amounts Euro 25 thousands. The Company's books have been opened as of 01 January 2005 based on the Financial Due Diligence Report as at 01 January 2005 issued by the consortium consisting of Deloitte Central Europe Limited, Wolf Theiss and American Appraisal Hungary (the "Consortium"), as well as the results from the appraisal performed by independent qualified valuers - American Appraisal Hungary.

The Company is 100% subsidiary of Kosovo Energy Corporation Holding J.S.C.

The Company's principal activities are generation, transmission and distribution of electricity, mining activities as extraction of lignite used in its thermal power plants.

The Company's current operational structure consists of the corporate headquarters and the following divisions:

- Coal Production Division;
- Electricity Production Division;
- Network Division;
- Supply Division;
- Human Resources Division;
- Business Support Division;
- Corporate Services;
- Internal Audit Office; and
- Financial Division.

2 Accounting policies

Following are the principal accounting policies adopted in the preparation of these financial statements:

2.1 Basis of preparation

These financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS). The financial statements have been prepared under the historical cost convention, modified for the presentation of the property, plant and equipment at their valuation.

Preparation of these financial statements requires use of estimates and assumptions that have an effect on the disclosed amounts of assets and liabilities, on disclosures related to contingent assets and liabilities as of the financial statements date, as well as on the disclosed amounts of revenues and costs during the reporting period. Even though these estimates are based on the best judgment of ongoing events and activities made by the Company's Management, the achieved results might, eventually, differ from such estimates. Estimations made are evaluated continuously and are based on historical experience and other factors, including the expectations of future events believed to be reasonable within the given circumstances.

These financial statements are prepared as of and for the years ended 31 December 2006 and 2005. Current and comparative data are expressed in thousands of Euros (000 EUR) unless otherwise stated.

The Company's opening balance sheet as of 01 January 2006 has been restated subsequent to the issuance of 2005 financial statements. Adjustments that have been made relate to corrections of errors identified and related to certain positions in the balance sheet as of 01 January 2006. The summary of adjustments is disclosed in the following table (all amounts in thousands of Euros):

01 January 2006	As initially issued	Restatements Debit	Restatements Credit	Restated
Assets				
Property, plant and equipment PE and other intangible assets	235,527	-	212	235,315
Inventories	7,864	-	-	7,864
Trade and other receivables, net	13,718	-	5,805	7,913
Cash and cash equivalents	38,411	-	42	38,369
Total assets	**295,520**	**-**	**6,059**	**289,461**
Equity and liabilities				
Equity				
Share capital	25	-	-	25
Reserves	675,460	-	62,877	738,337
Accumulated (Losses)	(543,952)	24,903	-	(568,855)
	131,533	**24,903**	**62,877**	**169,507**
Liabilities				
Borrowings	10,000	-	-	10,000
Deferred grants	14,704	824	-	13,880
Pension fund liabilities	16,939	-	-	16,939
Provisions	30,000	-	-	30,000
Trade and other liabilities	69,895	43,628	-	26,267
Accrued expenses	22,449	-	419	22,868
Total liabilities	**163,987**	**44,452**	**419**	**119,954**
Total equity and liabilities	**295,520**	**69,355**	**63,296**	**289,461**

Basis of preparation (continued)

These financial statements have been prepared on the assumption that the Company will continue as a going concern. The Company's operations are largely dependent and supported by various grant funds. Management considers that sufficient outside funds will be also available in the foreseeable future so as to enable the Company to pay its debts as they fall due and do not reflect the adjustments, which would be required to the value of assets and maturity of liabilities if this were not the case.

2.2 Adoption of new and revised Standards

In the current year, the Company has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the IASB) and the International Financial Reporting Interpretations Committee (the IFRIC) of the IASB that are relevant to its operations and effective for annual reporting periods beginning on 1 January 2006.

Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company

The following standards, amendments and interpretations to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 May 2006 or later periods but that the Company has not early adopted:

- IFRS 7, Financial Instruments: Disclosures, and the complementary Amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective for annual periods beginning on or after1 January 2007),
- IFRIC 8, Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006),
- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006).

Interpretations to existing standards that are not yet effective and not relevant for the Company's operations

The following interpretations to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after 1 May 2006 or later periods but are not relevant for the Company's operations:

- IFRIC 7, Applying the Restatement Approach under IAS 29 (effective from 1 May 2006), and
- IFRIC 9, Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006).

The Company's management considers that the application of new standards, amendments of existing standards and interpretations of existing standards will not cause materially significant effects on the Company's financial statements in the period of their initial application.

2.3 Foreign currency transactions

Foreign currency transactions are translated into the reporting currency using exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

2.4 Property, plant and equipment

Property, plant and equipment existing at 01 January 2005 – the effective date of valuation, are carried at valuation, determined by external independent valuers, less subsequent accumulated depreciation and accumulated provision for impairment. All other property, plant and equipment are stated at historical cost less accumulated depreciation. Historical cost includes expenditures that are directly attributable to the acquisition of the items.

Property, plant and equipment (continued)

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to 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. Increases in the carrying amount arising on the revaluation of items of property, plant and equipment are credited to the reserves within the shareholders' equity. Decreases that offset previous increases of the same asset are charged against other reserves directly in equity; all other decreases are charged to the income statement. Each year the difference between depreciation based on the revalued carrying amount of the asset charged to the income statement and depreciation based on the asset's original cost is transferred from 'other reserves' to 'retained earnings'.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

Land in mines	6 – 50 years
Buildings	10 – 50 years
Industrial Heavy Equipment	10 – 15 years
Vehicles	6 – 7 years
Furniture, fittings and equipment	5 – 7 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the income statement. When revalued assets are sold, the amounts included in other reserves are transferred to retained earnings.

2.5 Impairment of non – financial assets

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

2.6 Financial assets and liabilities

Financial assets and liabilities carried on the balance sheet include cash, cash equivalents, receivables and liabilities. The accounting policies on recognition and measurement of these items are disclosed in the respective accounting policies included in this note. The Company classifies its financial instruments as assets, liabilities or equity in accordance with the substance of the related contractual arrangement. Interest, gains and losses relating to financial instruments classified as assets or liabilities are reported as income or expense, respectively. Financial instruments are offset when the Company has a legally enforceable right to offset and intends to settle either on a net basis or to realize the asset and settle the liability simultaneously.

2.7 Fair value of financial assets and liabilities

The carrying amounts reflected in the accompanying balance sheets of cash and cash equivalents, receivables and current liabilities approximate their respective fair values due to the relatively short-term maturity of these financial instruments.

2.8 Trade and other receivables

Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired.

The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. Assets with a short maturity are not discounted.

The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in the income statement within 'selling and marketing costs'. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against 'selling and marketing costs' in the income statement.

2.9 Inventory

Materials and spare parts principally relate to power plant, transmission and distribution network maintenance and are valued at the lower of cost and net realizable value, the cost being determined using the weighted average method. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. Materials and spare parts are expensed or capitalized to plant, as appropriate, when installed. A provision for slow moving materials and spare parts is accounted for the financial statements.

Lignite. The Company extracts its coal, which is used in the production process for the generation of electricity at its thermal power plants, from the two mines it operates. Lignite stocks are stated at cost, which comprises direct costs of extraction and an appropriate portion of those overheads that have been incurred in extracting it.

2.10 Cash and cash equivalents

Cash and cash equivalents comprise of cash at bank and in hand. For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above.

2.11 Equity

Share capital

Share capital is determined using the nominal value of shares that have been issued.

Reserves

Reserves represent difference between the registered share capital and the value of net assets as determined by independent valuation at the date of Company incorporation.

2.12 Borrowings

Borrowings, consisting of long-term non – interest bearing loans granted by the Kosovo Consolidated Budget, are carried at the proceeds received, net of transaction costs incurred.

2.13 Retirement benefit costs

The Company makes no provision and has no obligation for employee pensions over and above the contributions paid into the state pension plan, Kosovo Pension Saving Trust (KPST).

2.14 Trade and Other Payables

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

2.15 Current and deferred income tax

The current income tax charge is calculated on the basis of the tax law enacted at the balance sheet date.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using a tax rate that has been enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

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

The Company has not recognized any deferred tax liabilities or assets at 31 December 2006.

2.16 Revenue and expense recognition

Revenue from sale of electricity comprises of the invoiced value of electricity supplied. Billings for electricity sale are made every month within the first five (5) days of the month following the month in which the consumption of electricity was performed.

Operating expenses are recognized in the income statement upon utilization of the service or at the date of the origin.

2.17 Government grants

Grants from the government are recognized at their fair value where there is a reasonable assurance that the grant will be received and the Company will comply with all attached conditions.

Government grants relating to costs are deferred and recognized in the income statement over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred government grants and are credited to the income statement on a straight-line basis over the expected lives of the related assets.

2.18 Provisions

A provision is recognized when the Company has a present obligation as a result of a past event and 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 each balance sheet date and adjusted to reflect the current best estimate. Where the effect of the time value of money is material, the amount of provision is the present value of the expenditures expected to be required to settle the obligation.

2.19 Commitments and contingencies

Contingent liabilities are not recognized in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is not recognized in the financial statements but disclosed when an inflow of economic benefits is probable. The amount of a contingent loss is recognized as a provision if it is probable that future events will confirm that, a liability incurred as at the balance sheet date and a reasonable estimate of the amount of the resulting loss can be made.

2.20 Subsequent events

Post-year-end events that provide additional information about a company's position at the balance sheet date (adjusting events) are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes when material.

3 Financial risk management

The Company's risk management is carried out by the Board of Directors. Risk management is focused on the unpredictability of markets and seeks to minimize any potential adverse effects over the Company's business performance.

3.1 Credit risk

The Company has no significant concentrations of credit risk with any single counter party. The maximum exposure to credit risk is represented by the carrying amount of each asset in the balance sheet.

3.2 Market risk

The Company has not entered into any hedging transactions to cover its exposure to price movements arising from the purchases of energy.

3.3 Interest credit risk

The Company does not enter into interest rate currency swap contracts since it does not have any interest bearing loans denominated in foreign currencies.

3.4 Capital risk management

When managing capital, the Company's objectives are to safeguard its ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Company may increase or return capital to shareholders or sell assets to reduce debt.

Notes to the financial statements (continued)
As of and for the years ended 31 December 2006 and 2005
(All amounts are expressed in Euro thousands, unless otherwise stated)

4 Property, plant and equipment and other intangible assets

	Land and forest	Land in mines	Buildings	Industrial Heavy Equipment	Other Equipment	Construct. in progress	Total	Other intangibles (Software)
At 01 January 2005								
Valuation	64,206	12,540	142,651	257,184	2,494	9,831	488,906	602
Accumulated depreciation	-	(796)	(23,689)	(48,879)	(836)	-	(74,200)	(125)
Accumulated impairment	(45,232)	(2,344)	(36,546)	(72,731)	(1,155)	(6,863)	(164,871)	(461)
Net carrying amount	**18,974**	**9,400**	**82,416**	**135,574**	**503**	**2,968**	**249,835**	**16**
At 31 December 2005								
Cost or Valuation	64,206	12,557	151,325	265,138	3,602	9,245	506,073	818
Accumulated depreciation	-	(2,363)	(34,775)	(69,118)	(1,047)	-	(107,303)	(122)
Accumulated impairment	(45,232)	(2,344)	(39,076)	(72,522)	(1,137)	(3,005)	(163,316)	(623)
Net carrying amount	**18,974**	**7,850**	**77,474**	**123,498**	**1,418**	**6,240**	**235,454**	**73**
At 31 December 2006								
Cost or Valuation	61,702	15,512	113,225	267,352	4,093	4,962	466,846	818
Accumulated depreciation	-	(3,950)	(33,719)	(83,159)	(1,343)	-	(122,171)	(139)
Accumulated impairment	(44,452)	(2,344)	(21,455)	(63,097)	(1,044)	(1,361)	(133,753)	(623)
Net carrying amount	**17,250**	**9,218**	**58,051**	**121,096**	**1,706**	**3,601**	**210,922**	**56**

Notes to the financial statements (continued)
As of and for the years ended 31 December 2006 and 2005
(All amounts are expressed in Euro thousands, unless otherwise stated)

Property, plant and equipment and other intangible assets (continued)

Movements during the year 2005

	Land and forest	Land in mines	Buildings	Industrial Heavy Equipment	Other Equipment	Construct. in progress	Total	Other intangibles (Software)
Opening net carrying amount	18,974	9,400	82,416	135,574	503	2,968	249,835	16
Additions	-	17	-	1,562	757	2,789	5,125	48
Donation	-	-	5,164	6,504	394	1,967	14,029	15
Disposals	-	-	(30)	(395)	(8)	(8)	(441)	-
Depreciation for the year	-	(1,567)	(11,094)	(20,201)	(231)	-	(33,093)	(7)
Internal transfers	-	-	1,018	454	3	(1,476)	(1)	1
Closing net carrying amount	**18,974**	**7,850**	**77,474**	**123,498**	**1,418**	**6,240**	**235,454**	**73**

Movements during the year 2006

	Land and forest	Land in mines	Buildings	Industrial Heavy Equipment	Other Equipment	Construct. in progress	Total	Other intangibles (Software)
Opening net carrying amount as stated	18,974	7,850	77,474	123,498	1,418	6,240	235,454	73
Restatement	-	-	-	128	-	(340)	(212)	-
Opening net carrying amount -restated	**18,974**	**7,850**	**77,474**	**123,626**	**1,418**	**5,900**	**235,242**	**73**
Additions	-	-	797	2,247	670	362	4,076	-
Donations	-	2,955	2,065	14,980	308	1,258	21,566	-
Transfer to KOSTT JSC	(1,724)	-	(14,948)	(5,243)	(293)	(814)	(23,022)	-
Disposals	-	-	(8)	(81)	(14)	-	(103)	-
Internal transfers	-	-	-	3,095	10	(3,105)	-	-
Depreciation for the year	-	(1,587)	(7,329)	(17,528)	(393)	-	(26,837)	(17)
Closing net carrying amount	**17,250**	**9,218**	**58,051**	**121,096**	**1,706**	**3,601**	**210,922**	**56**

(All amounts are expressed in Euro thousands, unless otherwise stated)

Property, plant and equipment and other intangible assets (continued)

Transfer of assets to KOSTT JSC

During 2006, and based on the process of legal and operational transformation of the former Publicly Owned Enterprise "Korporata Energjetike e Kosoves" ("KEK") in two new legal entities, Kosovo Energy Corporation JSC (KEK JSC) and Transmission System and Market Operator JSC (KOSTT JSC), part of KEK JSC' property, plant and equipment, amounting EUR 23,022 thousands was transferred to KOSTT JSC. Accordingly, the Company has reduced its reserves for the amount of EUR 21,118 thousands (see Note 8) and also, the balance of its deferred grants, related to assets received through grants and disposed off, for the remaining EUR 1,904 thousands (see also Note 10).

Additionally identified assets during 2006

During 2006 and included into total additions for the year, the amount of EUR 390 thousands represents identified assets (20 mini substations) that were not previously recognized in the Company's accounts. This was accounted for as increase of the reserves (see also Note 8).

Disposal of assets during 2006

During 2006, the Company disposed off part of its property, plant and equipment out of use, the net carrying amount of which was EUR 103 thousands. For the amount of EUR 303 thousands, related to the assets' cost less accumulated depreciation, the Company charged its current profit & loss (see Note 21) and for the released accumulated impairment, amounting EUR 200 thousands, the Company has increased its reserves (see Note 8).

In - kind donations received during 2006

During 2006, the Company received in - kind donations totaling EUR 21,566 thousands accounted for through deferred grant account. The related depreciation on these assets for 2006 charged to the current profit and loss in the amount of EUR 977 thousands has caused release of equal amount from the balance of deferred grants (see Notes 10 and 17).

Assets rendered under operating lease

Included in to the balance of property, plant and equipment at 31 December 2006, amount of EUR 1,940 thousands represents assets rendered under operating lease terms to several organizational units separated from the Company during 2006, as well as to other entities. Following are the details of net carrying value of assets leased:

Description	Net carrying amount
Buildings	1,282
Industrial Heavy Equipment	620
Other Equipment	37
Construction in progress	1
	1,940

At 31 December 2006, there are no items of property, plant and equipment, pledged as guarantee on any liability.

(All amounts are expressed in Euro thousands, unless otherwise stated)

Property, plant and equipment and other intangible assets (continued)

Accumulated impairment

Accumulated impairment has been initially recognised at the valuation date (01 January 2005- the Company's opening balance sheet date) in the amount of EUR 102,820 thousand. This amount has been initially accounted for and carried up to 31 December 2005 within the accumulated loss account, net of revaluation surplus in the amount of EUR 62,512 thousand. At 01 January 2006 the balance carried forward from prior year has been split into two separate accounts of accumulated impairment (included into accumulated loss account) amounting EUR 163,939 thousand and account of revaluation surplus (part of reserves account) amounting 62,512 thousand.

Table bellow provides for the movement of the accumulated impairment account:

	2006	2005
Balance, 01 January	163,939	165,332
Release of provision for assets transferred to KOSTT	(29,345)	-
Release of provision for assets disposed off	(218)	(460)
Correction on impairment	-	(933)
Balance, 31 December	**134,376**	**163,939**

5 Inventories

	2006	2005
Materials and consumables	25,610	24,107
Lignite	547	733
Fuel	1,336	2,372
Spare parts	5,912	4,170
Other	4,679	3,508
	38,084	**34,890**
Less: Provision for slow moving and obsolete stock	(26,461)	(27,026)
	11,623	**7,864**

Transfer of assets to KOSTT JSC

During 2006 and based upon the processes explained in Note 4: Transfer to KOSTT JSC, part of inventories, amounting EUR 452 thousands, were transferred to KOSTT JSC. The Company's reserves have been reduced accordingly (see also Note 8).

Provision for slow moving and obsolete stock

The provision for slow moving and obsolete items of stock was initially established at a level of 80% from the stock balance as of 31 December 2003 (excluding lignite and fuel inventories) and is based on management estimations as of that date. Decrease of the provision in the amount of EUR 565 thousands relates to inventories actually expensed during 2006.

(All amounts are expressed in Euro thousands, unless otherwise stated)

6 Trade and other receivables

	2006	2005
Trade receivables		
Local customers	252,898	221,629
Foreign customers	3,842	3,963
	256,740	**225,592**
Less: Provision for impairment	(244,500)	(214,745)
	12,240	**10,847**
Other current receivables		
Advances to suppliers	9,664	2,616
Non - interest bearing borrowings	1,151	-
Advances to employees	366	254
Excise tax refundable	1	1
	11,182	**2,871**
	23,422	**13,718**

The movement in the impairment provision is as follows:

	2006	2005
Balance, 01 January	214,745	157,438
Charge for the year	29,755	57,307
Balance, 31 December	**244,500**	**214,745**

In addition to the total impairment charge for 2006 and due to their entire non - recoverability, the Company wrote off part of its non - interest bearing borrowings in the amount of EUR 346 thousands (2005: EUR 938 thousand).

7 Cash and cash equivalents

	2006	2005
Current accounts with Banks	9,871	38,401
Cash on hand	30	10
	9,901	**38,411**

Current accounts with banks are non – interest bearing.

8 Equity

Share capital

At 31 December 2006 and according to the Provisional Business Registration issued by the UNMIK administration dated 27 December 2005 under Business Reg. No. 70325399, total subscribed capital amounts to EUR 25,000 at the date of registration. It comprises of 25,000 ordinary shares at 1 (one) Euro per share. The sole Company's shareholder is Kosovo Energy Corporation Holding J.S.C.

(All amounts are expressed in Euro thousands, unless otherwise stated)

Equity (continued)

Reserves

Reserves which at 31 December 2006 amounts EUR 687,794 thousands (2005: 675,460 thousands) have been initially accounted for in the Company's books as difference between the registered share capital and the value of Company's net assets as determined by independent valuation at the date of its incorporation as JSC. Included into the total reserves the amount of EUR 60,304 thousands (2005: 62,512 thousands) represents surplus related to valuation of property, plant and equipment as of 01 January 2005 (the opening balance sheet date).

The components of the reserve account for the periods considered are as follows:

	Revaluation surplus	Other reserves	Total
At 01 January 2005 / 31 December 2005	**-**	**675,460**	**675,460**
At 01 January 2006	**-**	**675,460**	**675,460**
Restatement	62,512	365	62,877
At 01 January 2006 –Restated	**62,512**	**675,825**	**738,337**
Transfers of assets to KOSTT JSC:			
- Property, plant and equipment (Note 4)	(2,208)	(48,273)	(50,481)
- Inventories (Note 5)	-	(452)	(452)
Additionally Identified assets (Note 4)	-	390	390
At 31 December 2006	**60,304**	**627,490**	**687,794**

9 Borrowings

At 31 December 2006 and 2005 the balance of Company's borrowings amounts to EUR 10,000 thousands and entirely consists of non - interest bearing funds borrowed during 2005 from the Kosovo Consolidated Budget, with a maturity no later than 31 December 2008. These funds are intended to support the Company's operating business activities.

10 Deferred grants

The balance of deferred grant account as of 31 December 2006 and 2005 represents various in - kind donations received during the periods considered from the European Agency for Reconstruction and Kosovo Trust Agency during.

Movements in the deferred grant account are as follows:

	2006	2005
At 01 January as stated	**14,704**	**-**
Restatement	(824)	
At 01 January 2006-restated	**13,880**	**-**
Additions in property, plant and equipment (Note 4)	21,566	14,704
Amortized during the year (Notes 4 and 17)	(977)	-
Transfer of donated assets to KOSTT (Notes 4 & 5)	(1,904)	-
Balance, 31 December	**32,565**	**14,704**

(All amounts are expressed in Euro thousands, unless otherwise stated)

Deferred grants (continued)

Following are grant components received during the years considered:

	2006	2005
Property, plant and equipment (Note 4)	21,566	14,044
Income for recovering operating expenses (N.17)	16,000	19,929
Income for working capital requirements (Note 17)	-	16,914
	37,566	**50,887**

11 Pension fund liabilities

As of 31 December 2006, and based on decision 3873/11-c dated 31 July 2006, the Company has terminated its operational activities with the pension fund. The balance of Company's liabilities, which at the date of termination amounted EUR 18,220 thousand was released as income in the current profit and loss (see Note 16).

12 Provisions

The balance of Company's provisions which at 31 December 2006 and 2005 amounts to EUR 30,000 thousands entirely relates to provision for ash dumps. This amount has been initially recognized as of 01 January 2005 based on the results from the financial due diligence performed by an independent accountant - Deloitte Central Europe Limited.

13 Trade and other liabilities

	2006	2005
Trade creditors		
Local suppliers	18,484	12,020
Foreign suppliers	14,997	6,443
	33,481	**18,463**
Other current liabilities		
VAT payables	99	26,334
Broadcasting tax	1,241	17,827
Income tax payables	7,881	-
Salaries to employees	2,863	3,085
Excise duties	1,440	1,218
Customers' advances	370	563
Other payables	324	2,405
	14,218	**51,432**
	47,699	**69,895**

14 Accrued expenses

	2006	2005
Accrued concession fees	5,816	6,354
Obligation from means for Investment A3	4,391	9,740
Lost of court disputes	2,900	2,439
Current maturity of pension fund liability	-	3,020
Other accrued liabilities	-	896
	13,107	**22,449**

(All amounts are expressed in Euro thousands, unless otherwise stated)

Accrued expenses (continued)

Obligation from means for Investment A3

This balance represents unspent cash received through means of grant from the Kosovo Consolidated Budget (KCB). During the year ended 31 December 2006 the Company received additional grant in the total amount of EUR 21,276 thousands and made payments from these funds to its suppliers for purchased assets, in the total amount of EUR 26,625 thousands.

15 Sales

	2006	2005
Sales of electricity		
Consumers (10 kV, 35 kV and 0,4kV)	34,256	32,905
Industrial customers	3,140	3,131
Householders	63,418	64,322
Export of electricity	6,778	5,132
	107,592	**105,490**
Other sales		
Income from re-connection services	7,135	3,234
Sales of coal	896	1,484
Other	2,009	2,076
	10,040	**6,794**
	117,632	**112,284**

16 Other income

	2006	2005
Write off of pension fund liabilities (Note 11)	18,220	-
Other	1,791	1,452
	20,011	**1,452**

17 Income from grants

	2006	2005
Income for recovering operating expenses (Note10)		
Electricity imported	11,600	10,433
Repairs and maintenance	1,278	4,282
Other	3,122	5,214
	16,000	**19,929**
Working capital requirements (Note 10)	-	16,914
Released from deferred income from grants (Notes 4 & 10)	977	-
	16,977	**36,843**

18 Staff cost

	2006	2005
Net salaries	31,090	32,066
Contributions and tax	6,217	5,677
Other	3,864	903
	41,171	**38,646**

Notes to the financial statements (continued)
As of and for the years ended 31 December 2006 and 2005
(All amounts are expressed in Euro thousands, unless otherwise stated)

19 Electricity and other utilities

	2006	2005
Electricity	24,820	19,880
Fuel	9,491	8,837
Gas and water	1,141	1,198
Transmission and exchange of electricity	7,568	3,305
	43,020	**33,220**

20 Maintenance costs

	2006	2005
Repairs	5,432	2,328
Current maintenance	782	1,834
	6,214	**4,162**

21 Other operating expense

	2006	2005
Management fees	3,055	5,937
Transport services	2,635	2,013
Insurance expenses	2,273	2,423
Concessions fee	1,703	1,668
Outsourcing services (surface excavation)	1,412	72
Damages	878	2,478
Coal Analysis's	735	35
Net carrying value of assets disposed off (Note 4)	303	441
Other expenses	5,507	3,918
	18,501	**18,985**

22 Financial result, net

	2006	2005
Finance income		
Interest income on overdue balances	280	276
Finance costs		
Interest expense on delayed payments	(4)	(13)
Finance (costs) / income, net	**276**	**263**

(All amounts are expressed in Euro thousands, unless otherwise stated)

23 Income tax expense

The charge for the year can be reconciled to the profit per 2006 income statement as follows:

	2006	2005
Loss before income tax	(25,974)	(48,773)
Tax at rate of 20%	(5,195)	(9,755)
Expenditure not allowable for income tax purposes	-	-
Income not taxable for income tax purposes	-	-
Unrecognized tax losses carries forward	5,195	9,755
	-	-

According to the UNMIK Regulation No. 2004/51, enforced on 01 January 2005, the Company is required to pay income tax at a rate of 20% on the taxable profit, as calculated in the annual Income Tax Return Statement.

The Company incurred loss from its operations for 2006 and 2005 thus has no income tax liability for the periods considered.

Tax losses may be carried forward to be set of the next five years following the year in which the tax loss was incurred. During 2006 and previous years the Company has incurred tax losses. No provision for deferred tax on past losses or timing differences has been made due to the uncertainty as to when or if the Company will start earning taxable profits.

24 Contingencies and commitments

Litigations

At 31 December 2006, legal proceedings raised against the Company amount to EUR 5,745 thousands (2005: EUR 6,531 thousand). No provision has been made as of the balance sheet date, as the Company's legal department indicates that it is unlikely that any significant loss will arise.

Long – term debt

Various legal actions and claims may be asserted in the future against the Company based upon possible long – term obligations that existed prior to the establishing of UNMIK administration on the territory of Kosovo. At the date of issuance of these financial statements, the outcome of these matters cannot be determined with sufficient reliability and no provision has been recognized regarding such long – term obligations at the balance sheet date.

Mineral rights

The Company has received an exploration license over the current mining areas and the process of obtaining an exploration license over a new mining area is ongoing. It is likely that granting the exploitation license for a new mine will be accompanied by clauses requiring the rehabilitation and removal of contaminated materials. Work will be undertaken during the next years to evaluate the extent of this problem, however it represents a potential liability which has not been accounted for in these financial statements.

Commitments

KEK plans to develop a new coalmine, which would require the relocation of approximately 400 houses in Hade village. The amount estimated to be paid for such relocation is approximately EUR 36 million.

25 Mineral reserves

The Company has made an estimation of the reserves and resources within its historical license areas at the end of 2003. The relevant governmental authority, the Directorate of Mines and Minerals, has confirmed these.

The Company has applied for an exploration license over a new area of 834 hectares that extends to the north of the existing mines. This has not yet been granted but the application secures the Company's rights to the reserves in the area, which are considered to be approximately 700 million tones of exploitable lignite. A feasibility study will be carried out to demonstrate the economic viability of extracting these reserves and this will be used to apply for an extraction license.

26 Technological losses

The Company incurs substantial technical and trade losses of electrical power in its operations.

Technical losses arise upon the transmission of electrical power, as well as from one voltage to another.

Trade losses represent electricity consumed by customers, which the Company fails to identify and invoice. Management estimates total technological losses of electric power, for the year ended 31 December 2006, to amount to 48% (2005: 50.9%) of the total electricity supplied.