

**ANNUAL REPORT ON
CORPORATE GOVERNANCE**

2016

**CROATIAN FINANCIAL SERVICES
SUPERVISORY AGENCY**



HANFA

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Introduction

For the seventh consecutive year, the Croatian Financial Services Supervisory Agency (hereinafter: Hanfa) has drawn up the Annual Report on Corporate Governance (hereinafter: the Report), presenting the level of corporate governance reached by issuers whose securities are admitted to trading on the regulated market in the Republic of Croatia.

Corporate governance in the European Union, other countries of the region and worldwide is aimed at increasing the responsibility of relevant persons within companies, strengthening internal and external control mechanisms and more stringent transparency requirements in relation to information provided to shareholders and investors. Good corporate governance is more than just acting in accordance with laws and regulations. It requires dedication of all stakeholders (management board, supervisory board, managers, shareholders) to creating preconditions in which issuers can act in accordance with the highest ethical standards and standards of good corporate governance.

Sources of data

As in the previous years, the seventh edition of the Report has been prepared on the basis of data collected directly from issuers, from Zagrebačka burza d.d (hereinafter: Zagreb Stock Exchange), from Središnje klirinško depozitarno društvo d.d. (Central Depository and Clearing Company, hereinafter: CDCC) and from the register of companies.

The questionnaire for the preparation of the 2016 Annual Report on Corporate Governance (hereinafter: the Questionnaire) was intended for all issuers whose shares and/or bonds were admitted to trading on the regulated market of the Zagreb Stock Exchange as at 31 December 2016. It comprised a comprehensive list of questions relating to general data on the issuer, own shares, management and supervisory board structure, management and supervisory board meetings, supervisory board committees, management and supervisory board members' remuneration and options, all general assembly meetings held, Code of Corporate Governance, internal and external control, risks, conflicts of interest, dividend payments, etc.

Pursuant to the Ordinance on information that needs to be submitted to the Croatian Financial Services Supervisory Agency by issuers whose securities are admitted to trading on a regulated market in the Republic of Croatia, and on the form, time limits and manner of its submission (Official Gazette, No 66/14), the deadline for the submission of the Questionnaire was 30 June 2017.

2016 Capital market

In 2016, especially in the second half of the year, the Croatian capital market was marked by economic recovery, continued increase in investment activities and growth of market indicators. The total trading volume on the Zagreb Stock Exchange amounted to HRK 3.9bn, increasing significantly (16.1%) compared to 2015. Trading in shares within the order book amounted to HRK 1.9bn, a decrease of 13.4%, while block trades in shares amounted to HRK 1.2bn, an increase of 123.4%. Trading in bonds within the order book increased by 48.7% compared to 2015, amounting to HRK 0.4bn, while block trades in bonds amounted to HRK 0.3bn, increasing by 22.7% in relation to 2015. The increase in total turnover was largely contributed by the

increase in block trades in shares and bonds and by the increase in trading in bonds within the order book, due to increased activity of institutional investors. Trading in structured securities decreased by 34.5% compared to the previous year. OTC turnover reached HRK 25.9bn, rising by 15.8% in comparison to 2015.

Market indicators showed positive trends. The main stock index CROBEX increased by 18.1%, while CROBEX10 grew by 17.1%. CROBEXTURIST continued to grow, reaching 27.9%. The CROBIS bond index grew by 3.6%, while CROBIStr rose by 8.6%. 2016 was marked by the removal from trading of all structured products, while the Zagreb Stock Exchange listed its shares on the official market. Block trades in shares were significantly influenced by the sale of the government share in Končar elektroindustrija d.d., Sunčani Hvar d.d. and Imperial d.d., and the sale of a share in Podravka d.d. by an equity fund from Norway (49% of total block trades in shares in 2016).

The beginning of 2016 saw the entry into force of the Income Tax Act, i.e. its part relating to the taxation of capital gains, which probably had a negative impact on the turnover of shares within the order book. Issuers continued delisting their shares from the regulated market.

1 Annual report on corporate governance of share issuers

1.1 Introduction

Out of 139 issuers whose shares were admitted to trading on the regulated market of the Zagreb Stock Exchange as at 31 December 2016, 110 completed and submitted the Questionnaire. The total market capitalisation of the issuers which submitted their data reached HRK 134.1bn, or 93.62% of the market capitalisation of all the issuers with their shares listed on the stock exchange. As at 31 December 2016, three issuers were undergoing bankruptcy proceedings and one issuer was undergoing winding-up proceedings.

Number of issuers and number of shares

In spite of two new share listings, in 2016 the number of issuers on the regulated market continued its downward trend.

As at 31 December 2016, the number of issuers totalled 139, falling by 3.47% compared to the previous year, when there were five issuers more (a total of 144), i.e. by 8.55% in comparison with 31 December 2014, when there were 152 issuers admitted to trading.

Out of 139 issuers admitted to trading as at 31 December 2016, 27 issuers were admitted to trading on the official market and 112 on the regular market. Out of 144 issuers admitted to trading as at 31 December 2015, 26 issuers were admitted to trading on the official market and 118 on the regular market. Out of 152 issuers admitted to trading as at 31 December 2014, 22 issuers were admitted to trading on the official market and 130 on the regular market.

Shares not traded yet

By 31 December 2016, five shares admitted to trading of five different issuers had not been traded yet on the Zagreb Stock Exchange. These were the shares of the following issuers: ordinary share of Dalma d.d. (DAL-S-R-A), ordinary share of PAN-papirna industrija-trgopromet d.d. (PAN-R-A), preference share of Plava laguna d.d. (PPOR-R-A), preference share of Pounje d.d. (PUNT-P-A) and ordinary share of Vodoprivreda Zagreb d.d. (VDZG-R-A).

The number of admitted shares that had not been traded fell by one relative to 31 December 2015, due to trading in ordinary shares of the issuer 3. MAJ BRODOGRADILIŠTE d.d. (3MAJ-R-A) during 2016.

Admissions

In 2016, shares of two issuers were admitted to trading for the first time on the official market of the Zagreb Stock Exchange. Ordinary shares of the issuer Zagreb Stock Exchange were admitted to the official market, while ordinary shares of FTB TURIZAM d.d. were admitted to the regular market.

In 2016, six issuers withdrew their shares from the regular and one from the official market; in 2015, ten issuers withdrew their shares from the regular and none from the official market; while in 2014, 16 issuers withdrew their shares from the regular and none from the official market. In 2016, shares of one issuer transferred from the regular to the official market.

Sector division

a) Classification into the financial and non-financial sector

Issuers are classified into the financial and non-financial sector. The financial sector is comprised of financial institutions and closed-ended alternative investment funds, while the non-financial sector comprises other activities.

At the end of 2016, out of 139 share issuers, there were 15 (10.79%) issuers from the financial and 124 (89.21%) issuers from the non-financial sector. At the end of 2015, out of 144 share issuers, there were 17 (11.81%) issuers from the financial and 127 (88.19%) issuers from the non-financial sector.

b) Classification into groups of activities

The financial and non-financial sectors are divided into subcategories. Table 1.1 shows changes in the number of issuers by activities at the end of 2014, 2015 and 2016.

Table 1.1 Issuers by groups of activities as at 31/12/2014, 2015 and 2016

Group of activities	Number of issuers			
	2014	2015	2016	Change
FINANCIAL SECTOR				
Banks	11	11	10	-1
Insurance	5	3	2	-1
Closed-ended investment funds	4	3	3	0
NON-FINANCIAL SECTOR				
Agriculture	5	3	3	0
Industry				0
a. Shipbuilding	4	4	4	0
b. Wood industry	2	2	2	0
c. Energy	1	1	1	0
d. Pharmaceuticals	3	3	2	-1
e. Food, beverage and tobacco	20	20	20	0
f. Chemical industry	4	4	4	0
g. Metalworking industry	6	6	6	0
h. Textile industry	4	4	4	0
i. Other industries	0	0	0	0
Construction industry	10	9	9	0
Property	4	4	4	0
Telecommunications	4	4	4	0
Transport	8	9	9	0
Trade	18	17	17	0
Tourism	35	33	32	-1
Other activities	4	4	3	-1
TOTAL	152	144	139	-5

Source: Hanfa, Zagreb Stock Exchange

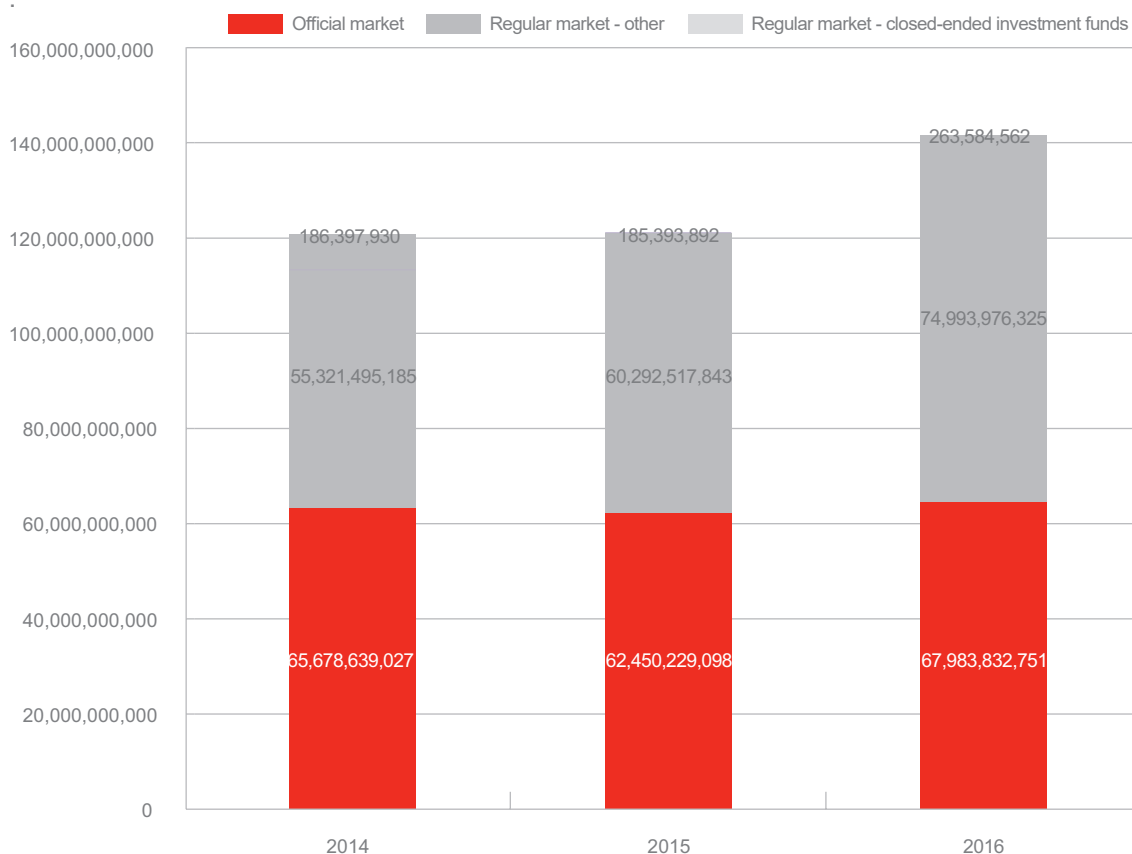
As in the previous year, at the end of 2016, the largest number of issuers belonged to the tourism industry, followed by issuers from the food industry and from trade.

The removals were mostly due to the decision of the general assembly (three issuers). Two issuers removed their shares from trading on the regulated market due to the initiation of the bankruptcy proceedings, meaning that shares of those issuers were removed from trading at the request of the bankruptcy trustee. One issuer merged with another company, while one issuer underwent the procedure of the squeeze-out of minority shareholders.

Market capitalisation

Chart 1.1 shows changes in market capitalisation by types of market at the end of 2014, 2015 and 2016.

Chart 1.1 Market capitalisation of the regulated market of the Zagreb Stock Exchange as at 31/12/2014, 2015 and 2016



Source: Zagreb Stock Exchange

- During 2016, the total market capitalisation of the official market increased by 8.86%, reaching nearly HRK 68bn as at 31 December 2016.
- The total market capitalisation of the regular market increased by 24.44%, reaching HRK 75.26bn as at 31 December 2016.
- Market capitalisation of issuers which submitted their 2016 Questionnaires (110 issuers) amounted to HRK 134.1bn as at 31 December 2016.

1.2 Capital and origin of capital

The following text presents an analysis of the initial capital of issuers based on data from the register of companies, an analysis of the market capitalisation of issuers based on data from the Zagreb Stock Exchange and an analysis of capital distribution, ownership structure and capital origin based on data from the CDCC.

1.2.1 Initial capital

At end-2016, the initial capital of 139 share issuers totalled HRK 60.5bn, while at end-2014, 144 issuers recorded their initial capital in the amount of HRK 61.4bn, i.e. 1.49% more. In comparison with 2014, when there were 13 admitted issuers more, the initial capital increased by HRK 1.9bn.

The amount of share issuers' initial capital ranged between HRK 3.6m and HRK 9.8bn.

According to the data from the register of companies, a total of 13 issuers (16 in 2015) increased their initial capital in 2016, while five issuers (nine fewer than in 2015) reduced their initial capital.

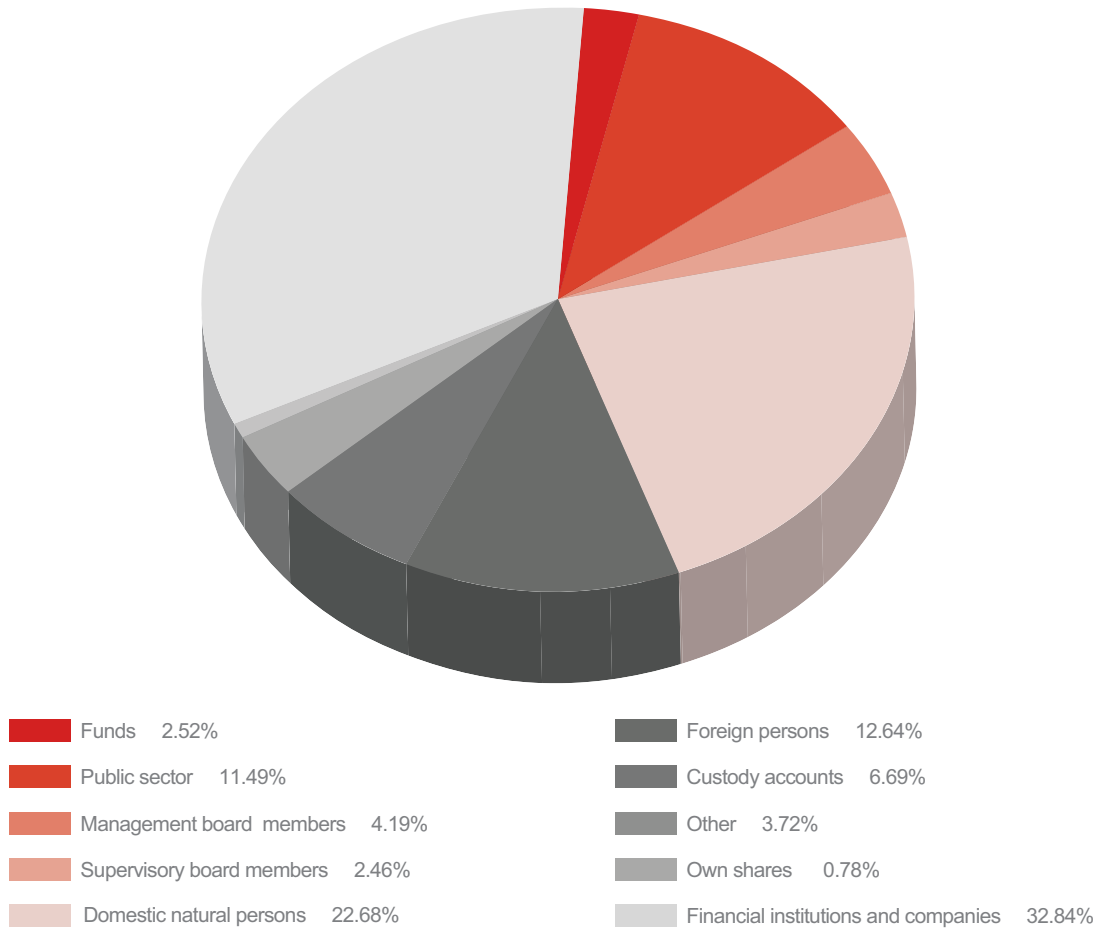
1.2.2 Ownership structure

Data on the ownership structure of share issuers has been provided on the basis of information received from the CDCC. The ownership structure has been analysed according to groups of shareholders, with the sum of all groups making 100% of the ownership structure, meaning that one shareholder can be allocated to one group only. The structure of joint-stock companies is divided into the following groups:

- own shares
- financial institutions and companies
- funds (investment and pension funds with their registered offices in the Republic of Croatia)
- public sector (Republic of Croatia)
- members of the management board
- members of the supervisory board
- domestic natural persons (except for members of the management and supervisory board)
- foreign persons (except for members of the management and supervisory board)
- custody accounts
- other.

Chart 1.2 presents the ownership structure of share issuers as at 31 December 2016 by the above mentioned groups.

Chart 1.2 Ownership structure of share issuers as at 31/12/2016

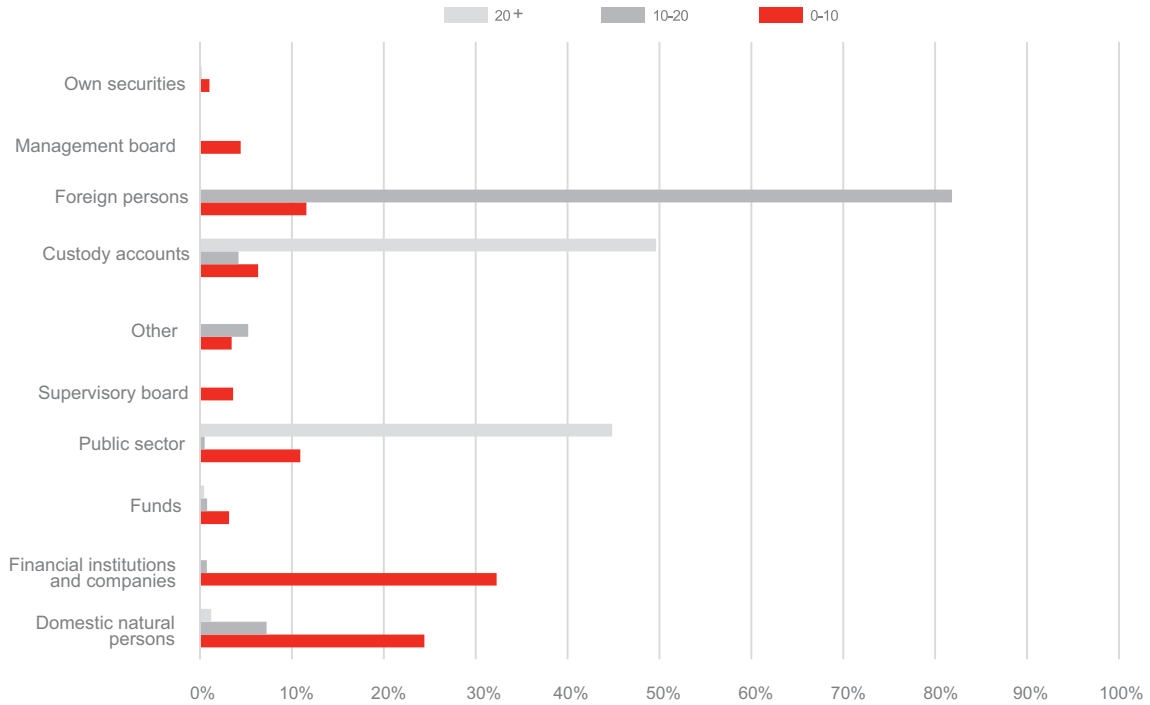


Source: CDCC

- The ownership structure of share issuers as at 31 December 2016 was dominated by financial institutions and companies with a proportion of 32.84% (31.47% in 2015) and domestic natural persons with a 22.68% proportion (22.53% in 2015). Public sector, i.e. the Republic of Croatia continued to reduce its proportion, which stood at 11.49% in 2016 (12.62% at end-2015, and 13.72% at end-2014). Funds reduced their proportion from 5.16% to 2.52%.

Chart 1.3 shows the ownership structure of share issuers as at 31 December 2016 in relation to market capitalisation.

Chart 1.3 Ownership structure of share issuers as at 31/12/2016 in relation to market capitalisation (in HRK billion)

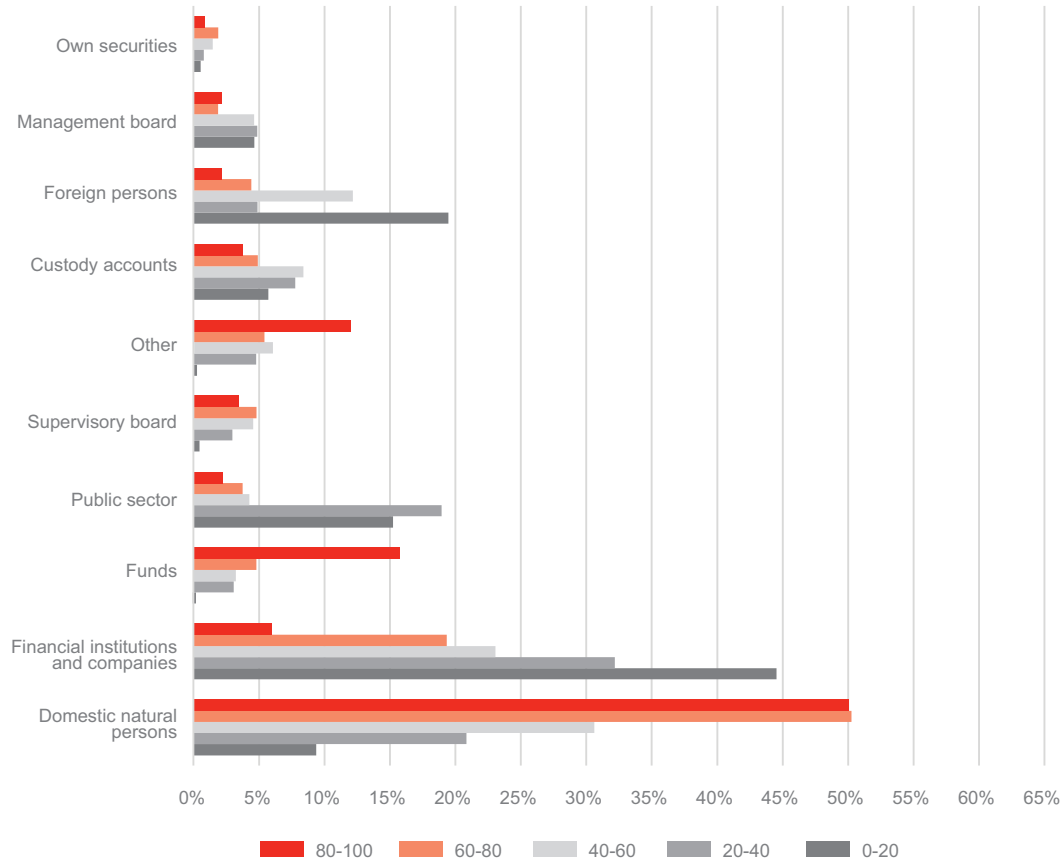


Source: CDCC

- Foreign persons had the highest proportion in issuers with market capitalisation between HRK 10bn and 20bn (81.84%), public sector had the highest proportion in issuers with market capitalisation over HRK 20bn (44.84%), while domestic natural persons had the highest proportion in issuers with market capitalisation under HRK 10bn (24.54%).

Chart 1.4 shows the ownership structure of share issuers as at 31 December 2016 in relation to free float.

Chart 1.4 Ownership structure of share issuers as at 31/12/2016 in relation to free float



Source: CDCC

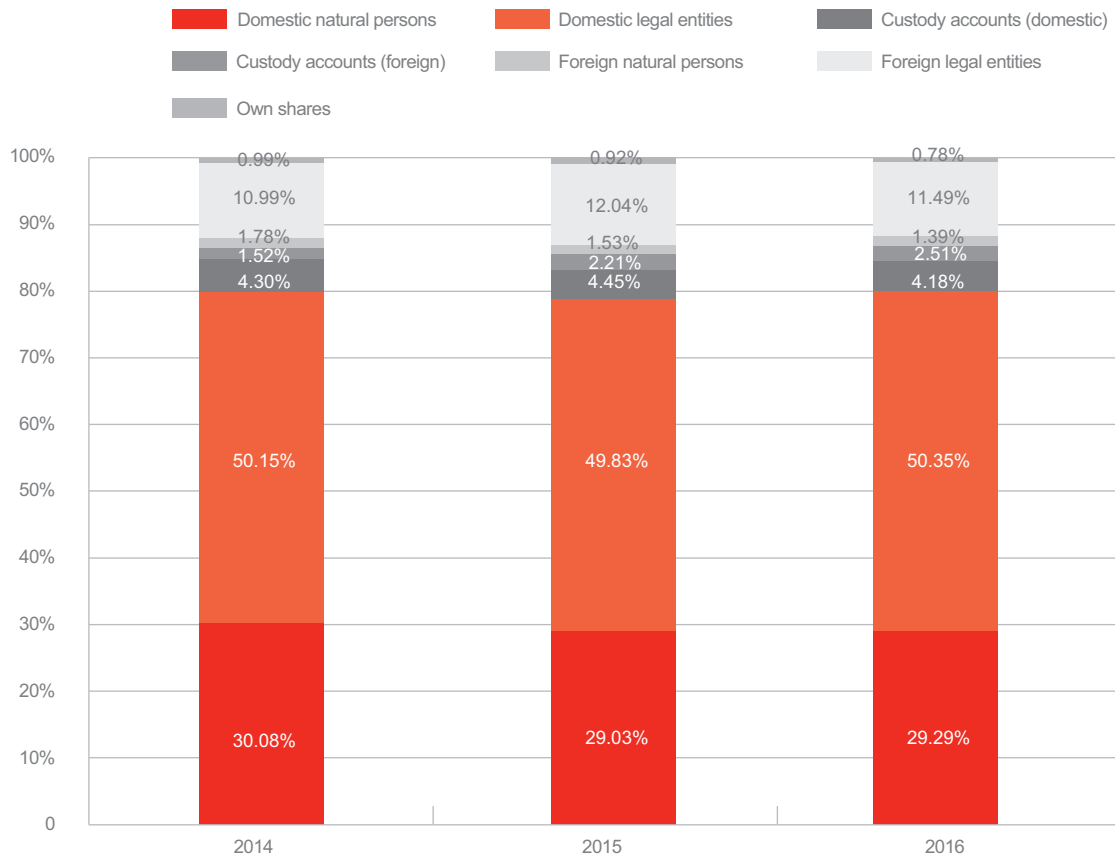
- Issuers with free float between 80% and 100% had the ownership structure dominated by domestic natural persons (50.22%), while issuers whose free float was up to 20% had the ownership structure dominated by financial institutions and companies (44.27%). Domestic natural persons had only 9.17% of ownership in those issuers. Foreign persons dominated the ownership structure of issuers with free float up to 20% (19.24%).

1.2.3 Origin of issuers' capital

Chart 1.3 shows the ownership of individual shares by the following categories:

- domestic natural persons
- domestic legal entities
- custody accounts (domestic)
- custody accounts (foreign)
- foreign natural persons
- foreign legal entities
- own shares

Chart 1.5 Origin of issuers' capital as at 31/12/2014, 2015 and 2016

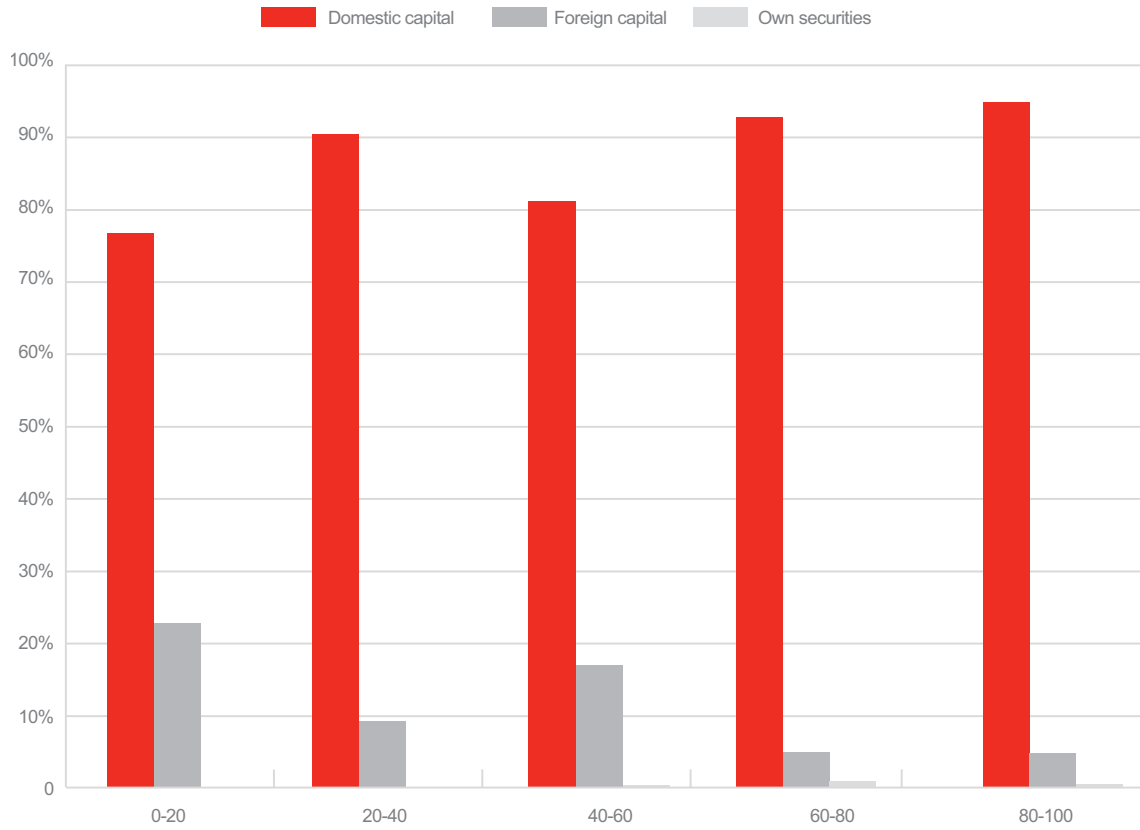


Source: CDCC

- The largest proportion (50.35%) in the share ownership was still accounted for by domestic legal entities (49.83% and 50.15% in 2015 and 2014 respectively). The proportion of domestic natural persons as at 31 December 2016 was 29.29% (29.03% and 30.08% in 2015 and 2014 respectively).
- The proportion of domestic capital as at 31 December 2016 was 83.82% (83.31% in 2015 and 84.53% in 2014), while the proportion of foreign capital was 15.39% (15.78% in 2015 and 14.29% in 2014).

Chart 1.6 shows the proportion of domestic and foreign capital in share issuers as at 31 December 2016, in relation to free float.

Chart 1.6 Proportion of domestic and foreign capital in share issuers as at 31/12/2016 in relation to free float



Source: CDCC



1.3 Issuers' governing bodies

The system of governance of a company is defined by its statute. The general assembly is a mandatory governing body, while governance and supervision of a company may be the function performed by one governing body, namely a board of directors in the case of a one-tier governance system, or by two separate governing bodies, namely a management board and supervisory board in the case of a two-tier governance system.

1.3.1 Management board¹

The function of a management board in a two-tier governance system is the management and representation of the company, and members are appointed by the supervisory board. In a one-tier governance system, this function is performed by executive directors of the company, appointed by the general assembly. As at 31 December 2016, out of the total number of issuers (139), three had a one-tier governance system, while 136 issuers had a two-tier governance system. This chapter presents the analysis of the structure of share issuers' management and supervisory boards. Data relating to executive directors and the chief executive of issuers with a one-tier governance system has been analysed along with data on management board members, while data relating to the board of directors, deputy chairman and chairman of the board of directors has been analysed along with data on members of the supervisory board of issuers with a two-tier governance system. The management board may consist of one or more persons. The number of management board members is stipulated by the statute of the issuer. The Companies Act (Official Gazette, No 111/93, 34/99, 121/99, 52/00, 118/03, 107/07, 146/08, 137/09, 125/11, 152/11, 111/12, 68/13 and 110/15; hereinafter: CA) does not stipulate the minimum number of management board members. Only natural persons with full legal capacity may be appointed members of the management board.

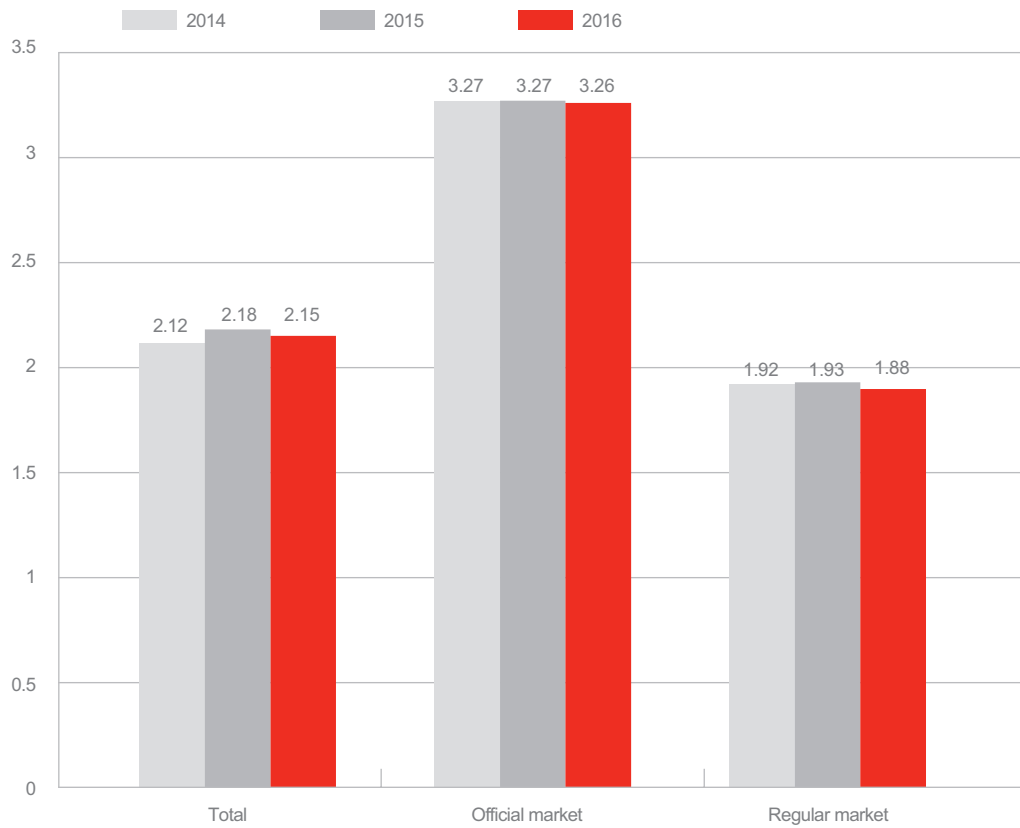
The analysis comprises all issuers of shares admitted to trading on the regulated market of the Zagreb Stock Exchange as at 31 December 2014, 2015 and 2016, except issuers undergoing bankruptcy or winding-up proceedings on that date according to the data from the register of companies. The ratio of the number of management board members to the number of issuers analysed in this Report is an important tool for the interpretation of data.

- As at 31 December 2016, there were 291 management board members in 135 analysed issuers (an average of 2.15 management board members per issuer). As at 31 December 2012, the average number of management board members totalled 2.18, whereas as at 31 December 2014, it amounted to 2.12.
- As at 31 December 2016, a total of 61 issuers (45.19%) had a single management board member. A single management board member was reported by 60 issuers (42.85%) as at 31 December 2015, and by 67 issuers (45.57%) as at 31 December 2014.
- As at 31 December 2016, the maximum number of management board members totalled seven (at three issuers).

Chart 1.7 shows the average number of management board members as at 31 December 2014, 2015 and 2016 with respect to the type of market.

¹ Data on the number and gender of management board members has been analysed based on the data from the register of companies in order for all issuers to be encompassed by the analysis (including those that failed to deliver the Questionnaire). It should be pointed out that there might be certain discrepancies in the numbers in cases where some issuers failed to report changes to the register of companies in a timely manner.

Chart 1.7 Average number of management board members by the type of market as at 31/12/2014, 2015 and 2016



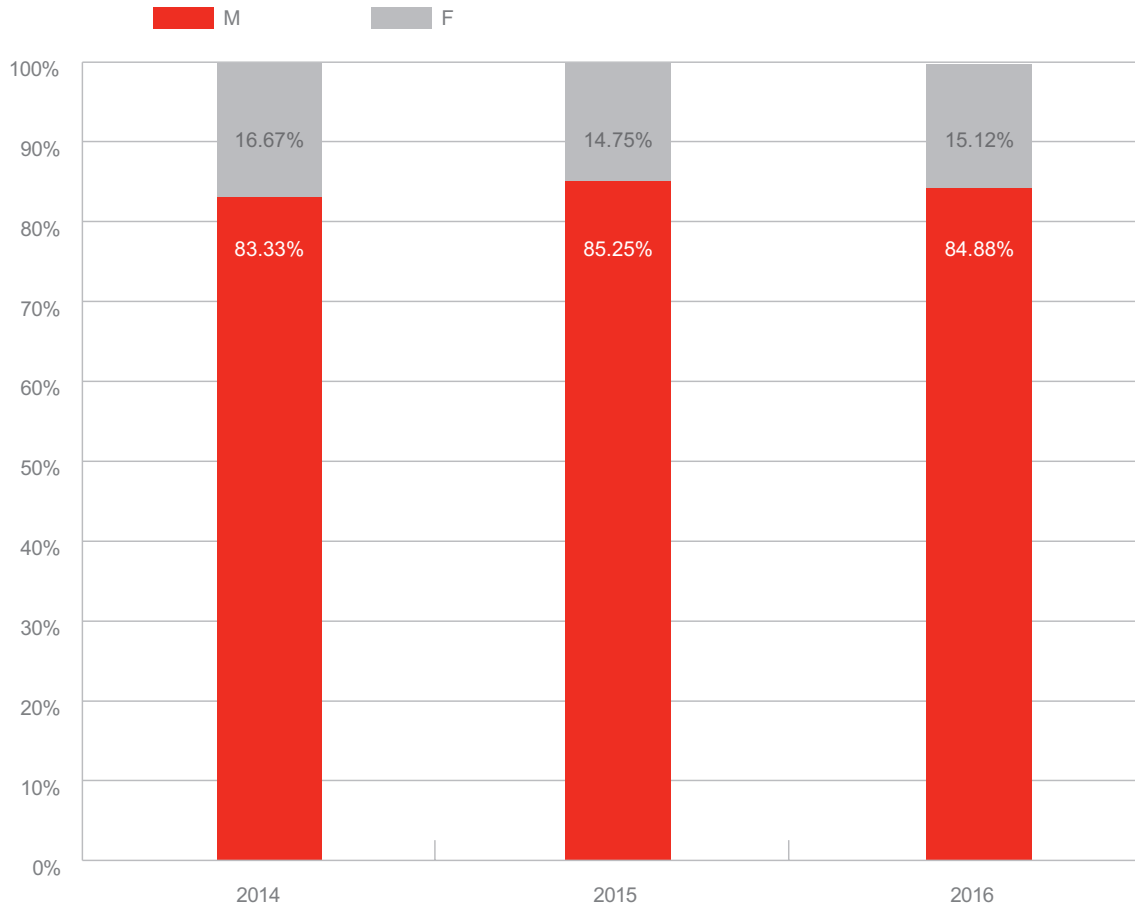
Source: register of companies, Zagreb Stock Exchange

- The average number of management board members of issuers on the official market remained nearly the same as in previous years, while it slightly decreased, to 1.88, on the regular market (1.93 as at 31 December 2015).

Management board member structure by gender, age and professional qualifications

Chart 1.8 presents the proportion of men to women on management boards of issuers as at 31 December 2014, 2015 and 2016.

Chart 1.8 Proportion of men to women on management boards as at 31/12/2014, 2015 and 2016



Source: register of companies, CDCC

The following text presents the analysis of the data delivered in the 2016 Questionnaire.

- As at 31 December 2016, majority of management board members (38.31%) were between 45 and 55 years old, 33.87% were between 35 and 45 years old, 22.58% were over 55 years of age and 5.24% of management board members were younger than 35 years of age.
- Most board members under 35 came from issuers from the property and funds industry (five board members from four issuers). As in 2015, majority of management board members over 56 years of age came from the tourism industry (13 board members from ten issuers).
- Most management board members had a university degree (95.56%), 3.62% had a PhD, while 1.21% had a secondary school degree or a lower level of education.

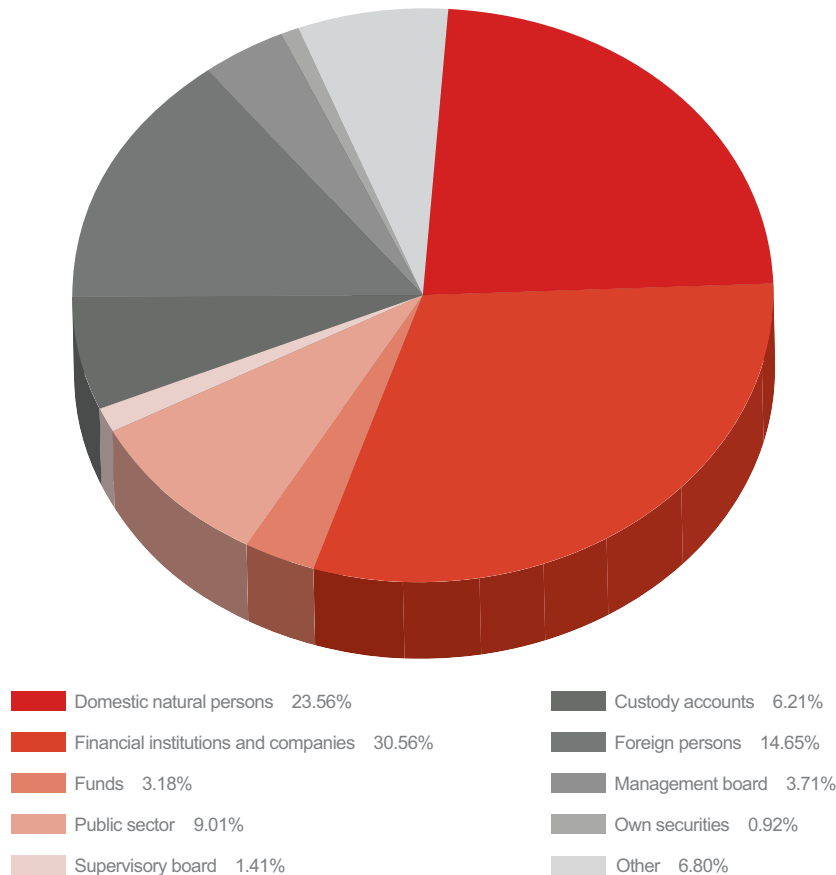
Rules of procedure of the management board

The management board may adopt rules of procedure, provided its adoption does not fall, according to the statute, within the competence of the supervisory board, or provided it has not been adopted by the supervisory board even without it having such competence. Matters otherwise regulated by the rules of procedure may be defined by the statute. Pursuant to the Code of Corporate Governance, rules of procedure of the management board must contain provisions on the area of activity and goals, rules of conduct, rules on handling conflicts of interest, the secretariat of the management board, the manner of convening and conducting meetings, decision-making, agenda, minute-taking and document-keeping, and cooperation with the supervisory board.

- In 2016, a total of 52 issuers (59 issuers in 2015) reported having an internal regulation on management board activities (rules of procedure of the management board).

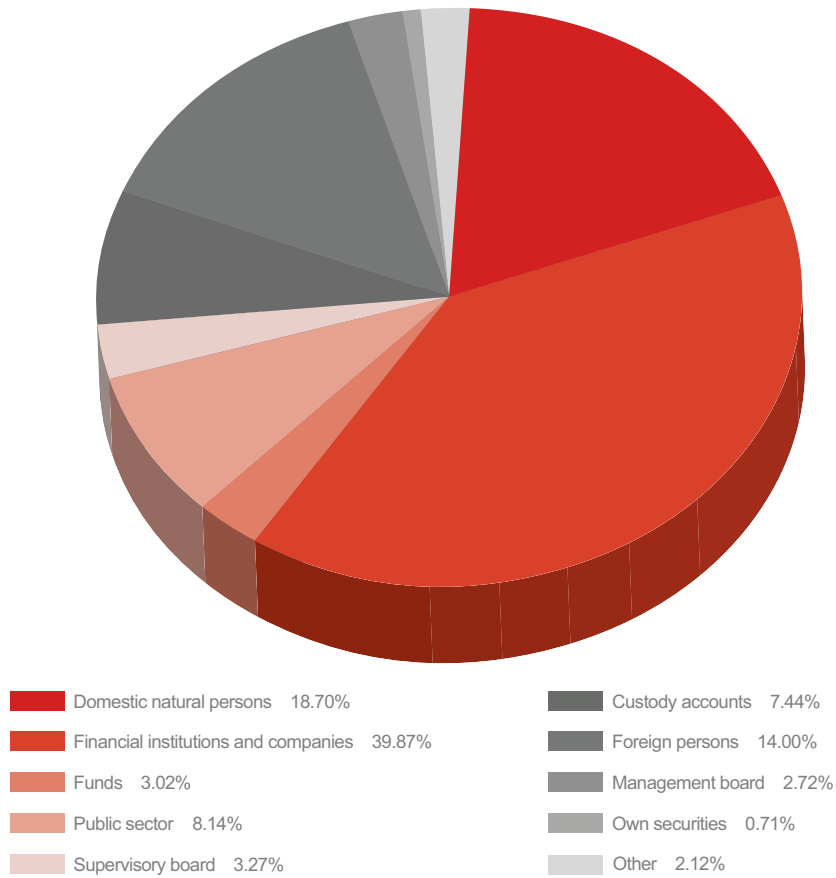
Chart 1.9 shows the ownership structure of share issuers having an internal regulation on management board activities (rules of procedure of the management board) as at 31 December 2016, and Chart 1.10 shows the ownership structure of share issuers without such regulation as at 31 December 2016.

Chart 1.9 Ownership structure of share issuers having an internal regulation on management board activities as at 31/12/2016



Source: CDCC, Questionnaire

Chart 1.10 Ownership structure of share issuers without an internal regulation on management board activities as at 31/12/2016



Source: CDCC, Questionnaire

- The ownership structure of issuers with an internal regulation on management board activities as at 31 December 2016 was dominated by financial institutions and companies (30.56%).
- The ownership structure of issuers without an internal regulation on management board activities was also dominated by financial institutions and companies (39.87%).

Meetings of the management board

- A total of 62 issuers reported the number of management board meetings held in 2016. The number ranged between 1 and 247, with the average number totalling 42.
- A total of 31 issuers reported having a schedule of meetings of the management board in 2016.
- Seven issuers reported having mechanisms for proxy voting at management board meetings in 2016.

Succession planning

Pursuant to the Code of Corporate Governance, the supervisory board of the issuer must provide for a long-term succession planning process, ensuring careful and timely appointment of a successor to any member of the management board of the issuer. The management team of the issuer should also be involved in this process.

- Eight issuers reported having established a succession planning process in 2016 (one more than in 2015). Majority of issuers with an established succession planning process came from the banking sector (three).

Term of office and duration of the management board membership

Members and the chairman of the management board are appointed by the supervisory board of the issuer for a maximum period of five years, and may be reappointed.

- At the end of 2016, the average duration of management board membership was 6.05 years. (at the end of 2015 it was 5.72 years, and at the end of 2014 it was 5.64 years).
- The average number of terms of office of management board members was 2.23 as at 31 December 2016 (it totalled an average of 2.08 in 2015 and 2.05 in 2014). In 2016, the largest number of consecutive terms of office (nine) was reported by one management board member (an issuer from the tourism industry).

Resignation of management board members

Resignation is one of the commonest ways of terminating a function in a governing body.

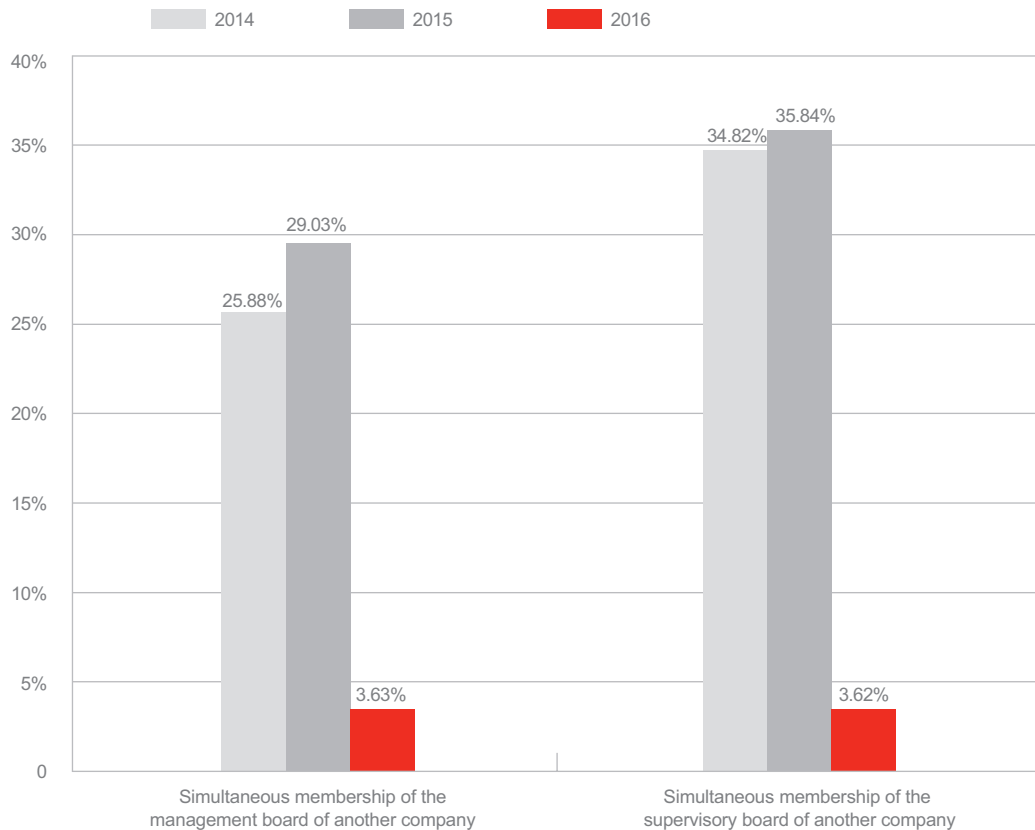
Resignation of the management board member is submitted to the supervisory board in writing.

- In the course of 2016, six management board members resigned before their terms of office expired. In 2014 and 2015, 24 management board members resigned before their terms of office expired. Reasons for the resignations were mostly linked to personal issues and contract termination by mutual consent.
- Most of the management board members who resigned came from the property and funds industry.

Multiple management/supervisory board memberships

Chart 1.11 shows changes in the number of management board members who were at the same time members of management and supervisory boards of other companies.

Chart 1.11 Number of management board members who were at the same time members of management and supervisory boards of other companies in 2014, 2015 and 2016



Source: Questionnaire

It should be noted that, in accordance with positive legal regulations, members of management boards of credit institutions cannot at the same time sit on the management board of another company or be at the head of a general partnership or a limited partnership.

1.3.2 Supervisory board²

The supervisory board is the main supervisory body of the company. Supervisory board members are appointed by the general assembly of the company. The statute of the company may provide for certain shareholders to appoint a certain number of supervisory board members. The statute also stipulates the number of supervisory board members appointed by employees pursuant to the Labour Act (Official Gazette, No. 93/14).

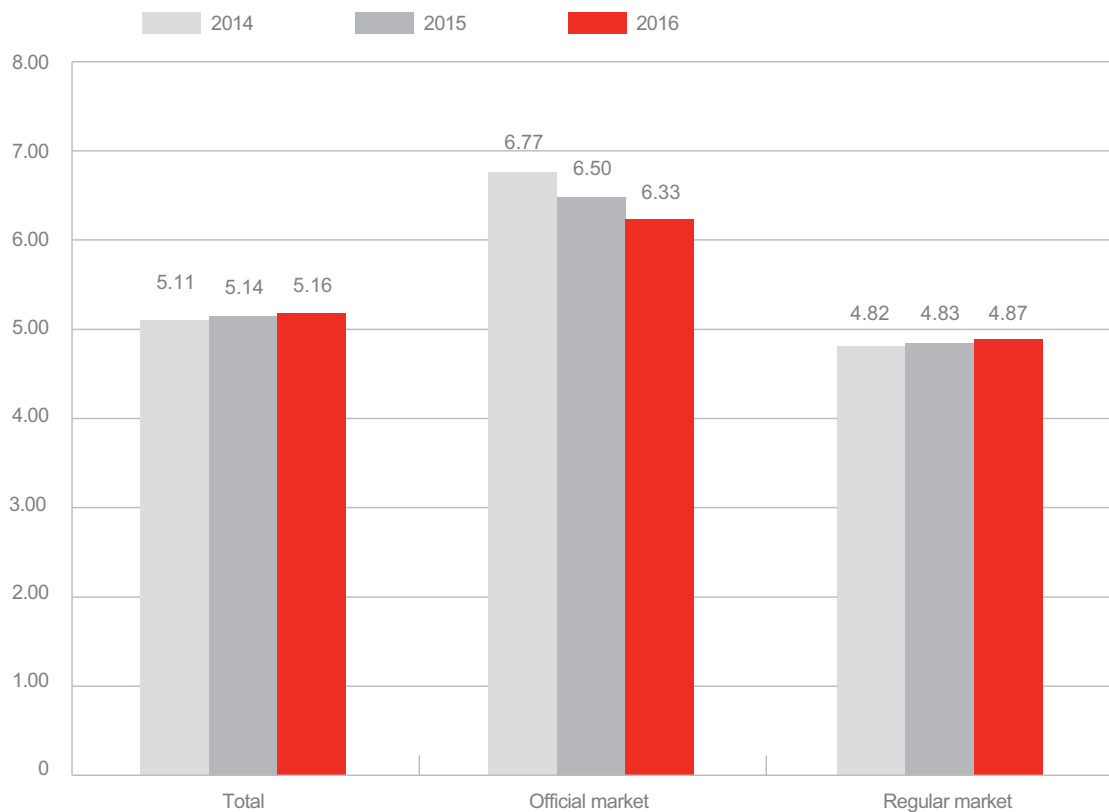
² Data on the number and gender of supervisory board members has been analysed based on the data from the register of companies in order for all issuers to be encompassed by the analysis (including those that failed to deliver the Questionnaire). It should be pointed out that there might be certain discrepancies in the numbers in cases where some issuers failed to report changes to the register of companies in a timely manner.

The following analysis comprises all the issuers of shares admitted to the regulated market of the Zagreb Stock Exchange as at 31 December 2014, 2015 and 2016, except issuers undergoing bankruptcy or winding-up proceedings on that date according to the data from the register of companies.

- As at 31 December 2016, the average number of supervisory board members was 5.16 (it was 5.14 on 31 December 2015, and 5.11 on 31 December 2014).
- The minimum number of supervisory board members (three) was reported by 31 issuers as at 31 December 2016, by 28 issuers as at 31 December 2015 and by 27 issuers as at 31 December 2014.
- As in the previous year, the maximum number of supervisory board members as at 31 December 2016 was 11, as reported by one issuer (from the food industry).

Chart 1.12 shows the average number of supervisory board members as at 31 December 2014, 2015 and 2016 with respect to the type of market.

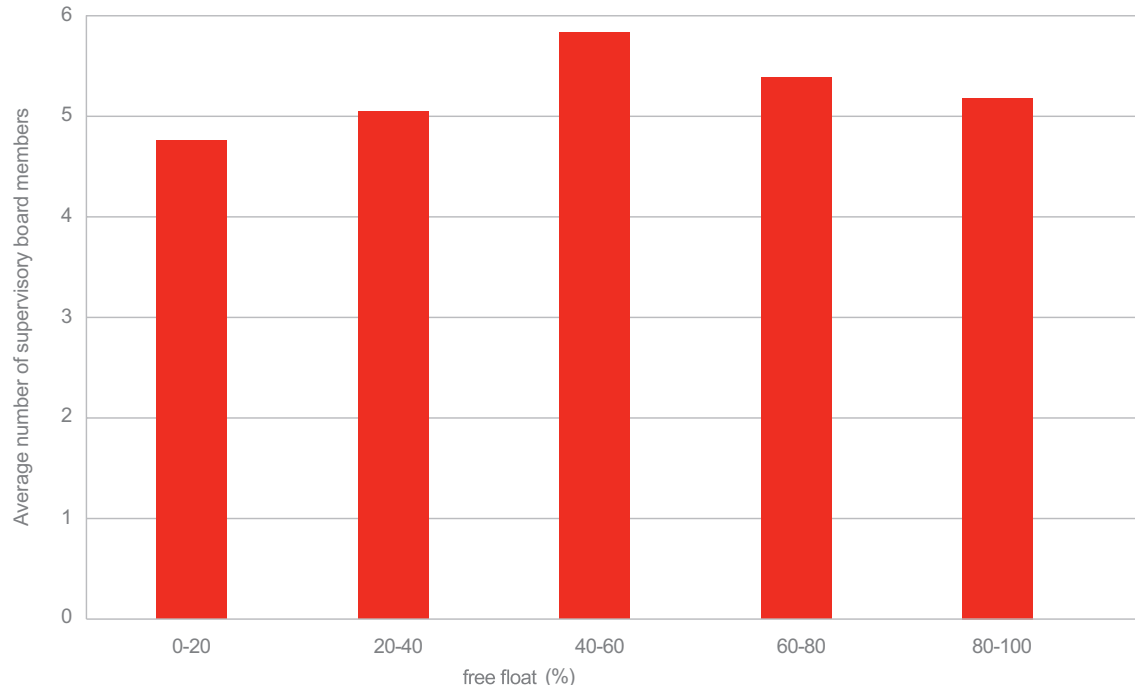
Chart 1.12 Average number of supervisory board members by the type of market as at 31/12/2014, 2015 and 2016



Source: register of companies, Zagreb Stock Exchange

Chart 1.13 shows the average number of supervisory board members as at 31 December 2016 in relation to free float.

Chart 1.13 Average number of supervisory board members as at 31/12/2016 in relation to free float



Source: register of companies, CDCC

Pursuant to the Code of Corporate Governance, the majority of supervisory board members must be independent, and must not have any business, family or other relationships with the company, majority shareholder or group of majority shareholders or with members of the management board or supervisory board of the company or majority shareholders.

The most important feature of an independent supervisory board member is lack of any conflict of interest. Independent supervisory board members ensure the adoption of objective decisions relating to management board members, the company itself and its shareholders, such as decisions on remuneration, new appointments, substantial changes in the ownership structure, anti-takeover measures, large takeovers and audit function.

The employee/trade union representative is a supervisory board member appointed by the works council. There may be only one such representative on the supervisory board, although their number is not limited by law. The supervisory board member appointed by the works council has the same legal status as other appointed members of the supervisory board.

The right to appoint supervisory board members may only be granted to certain shareholders or servient holders of certain shares (the representative of significant shareholder/group of shareholders). Holders of certain shares may be granted the right by the statute to appoint supervisory board members if the transfer of those shares requires the consent of the company. Such shares do not constitute a special class of shares. Shareholders may appoint a maximum of one third of supervisory board members. All supervisory board members have equal rights in the decision-making process irrespective of the above-mentioned classification.

- According to the data from the 2016 Questionnaire, independent supervisory board members accounted for 40.07% in the total number of members of share issuers' supervisory boards (41.82%

in issuers on the official market, and 39.37% in issuers on the regular market). Employee/trade union representatives made up an 11.4% share, whereas the largest share was accounted for by representatives of significant shareholders/group of shareholders and it amounted to 48.53%.

Chart 1.14 shows the proportion of independent supervisory board members in issuers on the official market in relation to the market capitalisation of those issuers, whereas Chart 1.15 shows the proportion of independent supervisory board members in issuers on the regular market in relation to the market capitalisation of those issuers.

Chart 1.14 Proportion of independent supervisory board members in issuers on the official market in relation to the total market capitalisation

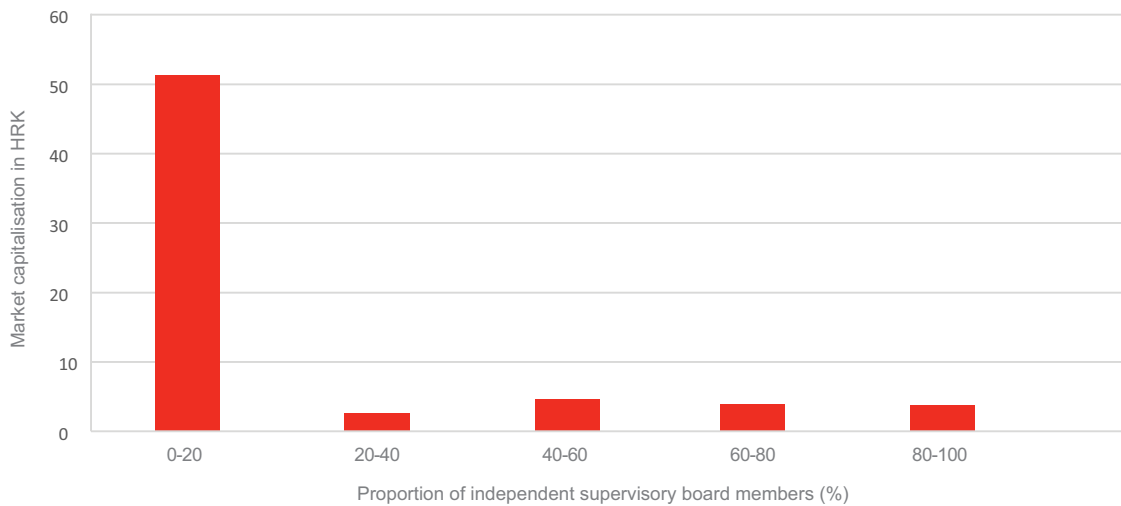
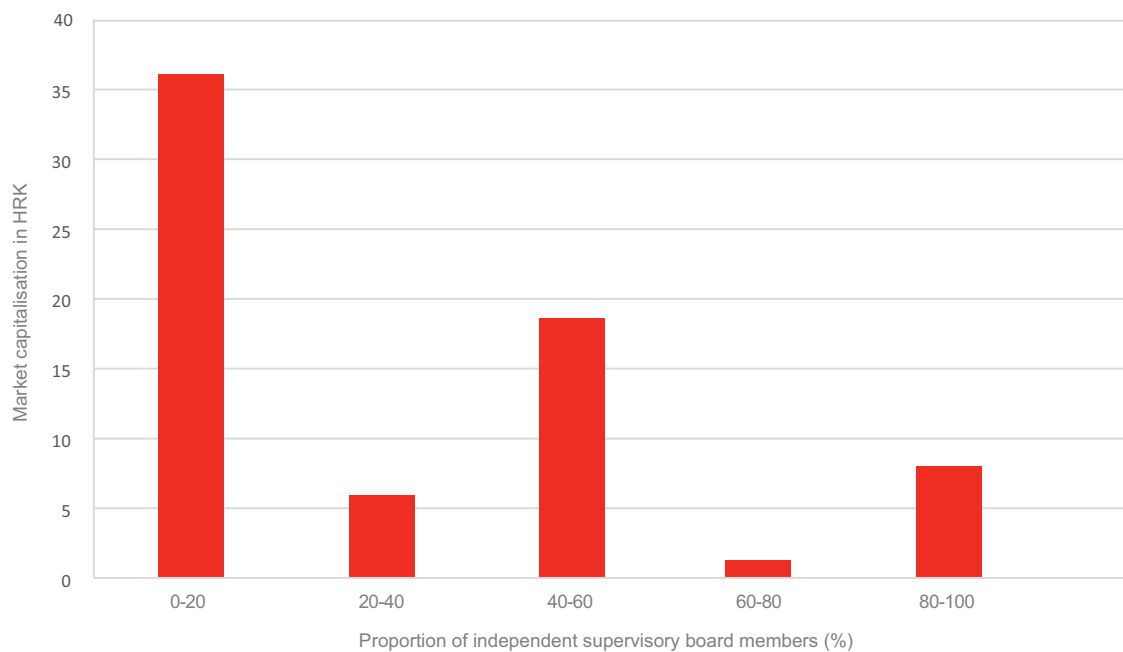


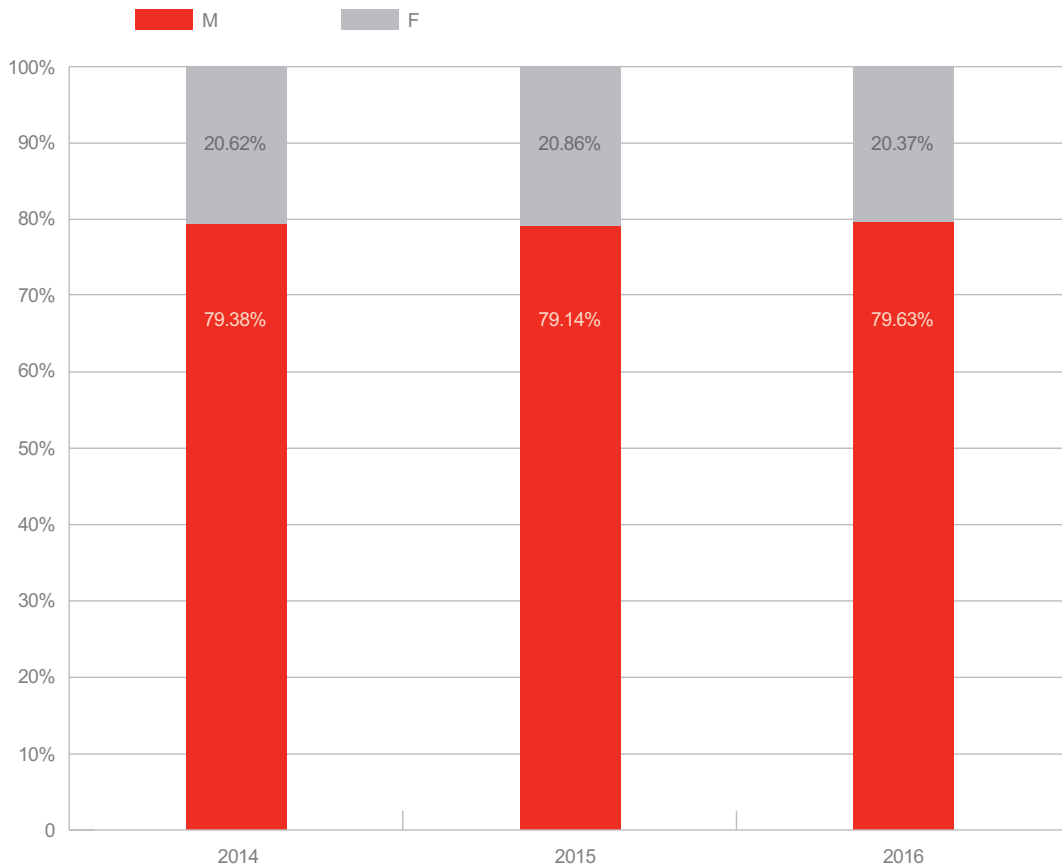
Chart 1.15 Proportion of independent supervisory board members in issuers on the regular market in relation to the total market capitalisation



Supervisory board member structure by gender, age and professional qualifications

Chart 1.16 shows the proportion of men to women on supervisory boards of issuers in 2014, 2015 and 2016.

Chart 1.16 Proportion of men to women on supervisory boards of issuers in 2014, 2015 and 2016



Source: register of companies

- In 2016, out of 697 analysed supervisory board members, 142 were women, with a 20.37% share. The average proportion of women on supervisory boards totalled 20.62% in all the three analysed years.
- In 2016, the proportion of women on supervisory boards was by 34.72% larger than the share of women on management boards.
- According to data from the Questionnaire, as at 31. December 2016, majority of supervisory board members (41.97%) were over 55 years old, 28.67% were between 45 and 55 years old, 24.7% were between 35 and 45 years old, and only 4.66% of supervisory board members were younger than 35 years of age.
- The majority of supervisory board members younger than 35 years of age came from the tourism industry (eight members from six issuers) followed by the food industry (four members from three issuers) and the property and funds industry (four members from three issuers).
- As at 31 December 2016, most supervisory board members had a university degree (83.59%), 10.71% of them had a secondary school degree, 7.95% had a PhD, and only one member (0.17%) had a lower level of education.

Meetings of the supervisory board

- In 2016, 44 issuers reported having a schedule of meetings of the supervisory board.
- A total of 36 issuers reported having mechanisms for proxy voting at supervisory board meetings.
- A total of 72 issuers (65.45% of issuers that submitted their Questionnaires) reported having an internal regulation on supervisory board activities. A total of 66.41% of issuers that submitted the Questionnaire reported having such regulation in the previous year.
- In 2016, supervisory boards held an average of 8.32 meetings, with the number of the meetings ranging from 1 to 115.

Term of office and duration of the supervisory board membership³

- At end-2016, the average duration of management board membership was 5.56 years, in 2015 it was 5.43 years, while in 2014 it was 5.31 years.
- The average number of terms of office of supervisory board members as at 31 December 2016 totalled 2.11 (it was 2.05 in 2015, and 2.02 in 2014). In 2016, the largest number of consecutive terms of office (14) was reported by one supervisory board member.

Resignation of supervisory board members

In the course of 2016, 12 supervisory board members resigned before their terms of office expired. Reasons for the resignations were mostly linked to personal issues or the assumption of another role.

Supervisory board committees

Pursuant to the Code of Corporate Governance, supervisory boards must establish the following committees:

- audit committee (audit board)
- nomination committee
- remuneration committee.

The majority of committee members must be selected from among independent supervisory board members. Each committee must have at least three members. The supervisory board must prescribe in detail the term of office and competence of the committees it has established.

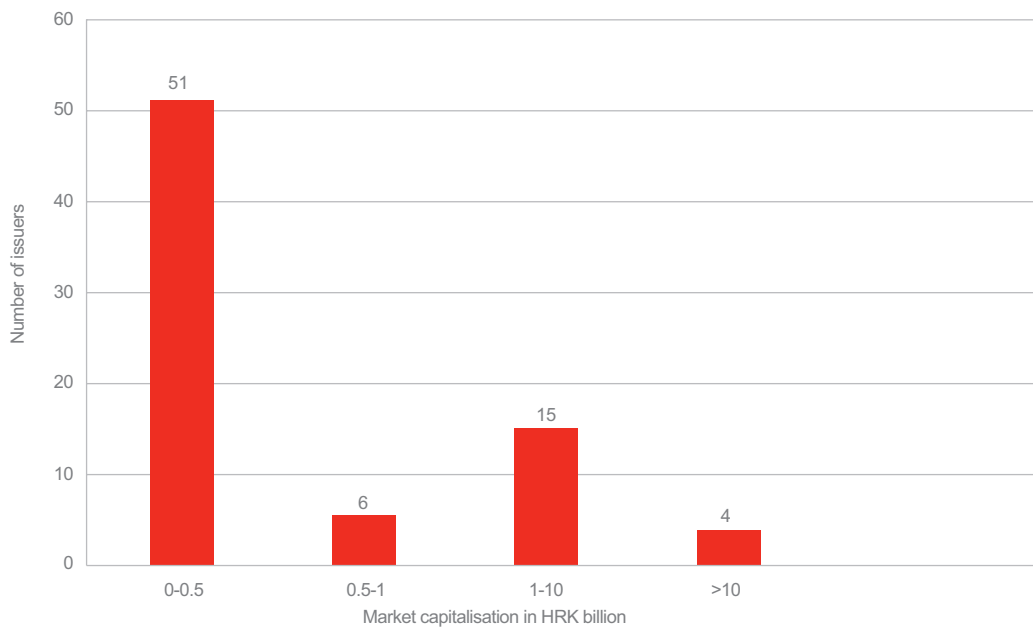
- The audit committee was established by most of the issuers: 76 issuers or 69.1% of the issuers that submitted their 2016 Questionnaire (60.16% of the issuers in 2015 and 53.19% of the issuers in 2016). In 2016, the remuneration committee was established by 11 issuers and the nomination committee by eight issuers.

³ The following analysis presents the data on supervisory board members according to the data from 110 Questionnaires submitted. Therefore, the total number of supervisory board members differs with respect to the data from the register of companies, which relates to all issuers.

- Internal working procedures were established by 40 audit committees (52.63%), nine remuneration committees (81.82%) and seven nomination committees (87.5%).
- Apart from having established these committees, ten issuers (the same as in 2015) reported having set up another committee (investments committee, corporate governance committee, risk committee, strategic development committee, committee for monitoring synergistic effects and legal advice committee).
- During 2016, a total of 23 issuers reported being in the process of preparing a report on the work of their committees, whereas five issuers made their committee reports publicly available.

Chart 1.17 shows the number of issuers with an established audit committee as at 31 December 2016 in relation to market capitalisation of issuers.

Chart 1.17 Ownership structure of issuers with an established audit committee as at 31/12/2016 in relation to market capitalisation of issuers

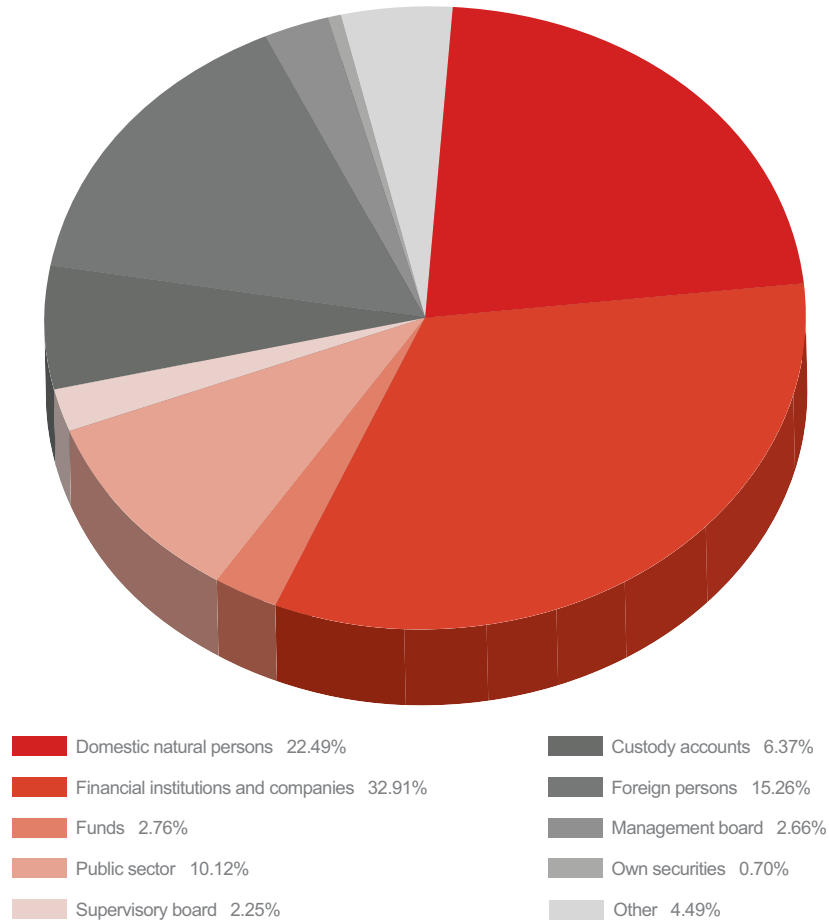


Source: Questionnaire, Zagreb Stock Exchange



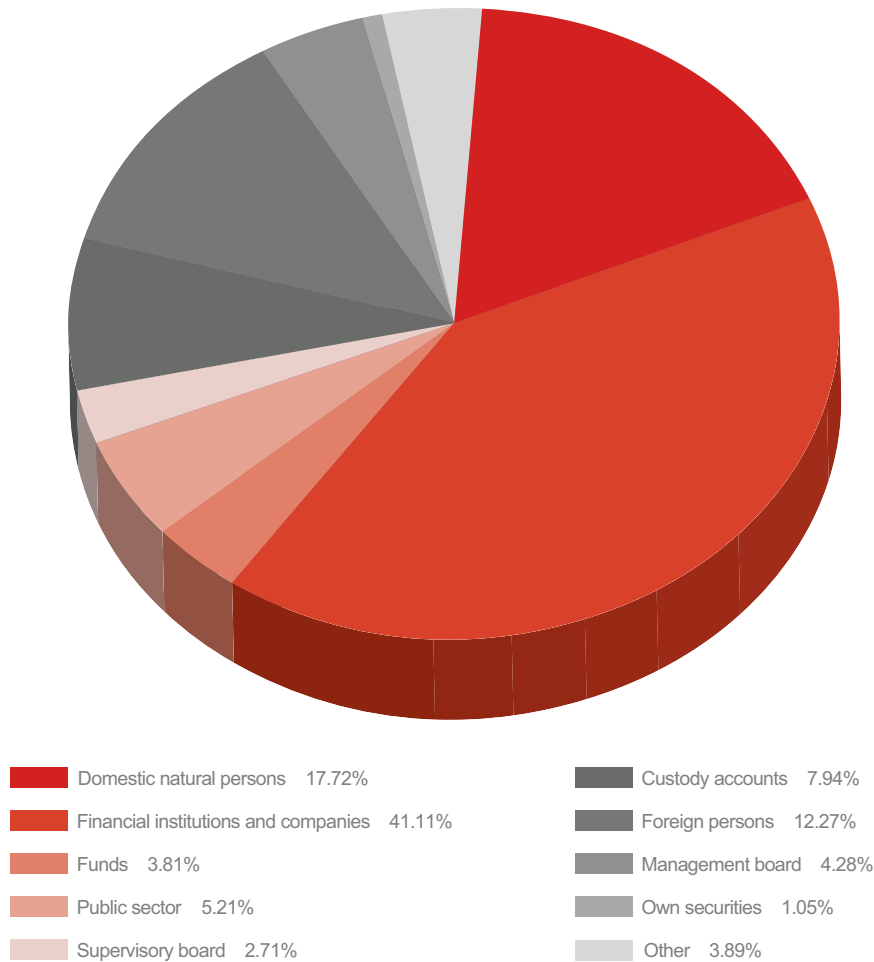
Chart 1.18 shows the ownership structure of issuers with an established audit committee as at 31 December 2016, and Chart 1.19 shows the ownership structure of issuers without an established audit committee as at 31 December 2016.

Chart 1.18 Ownership structure of issuers with an established audit committee as at 31/12/2016



Source: Questionnaire, CDCC

Chart 1.19 Ownership structure of issuers without an established audit committee as at 31/12/2016



Source: Questionnaire, CDCC

- Same as in previous years, financial institutions and companies dominated the ownership structure of issuers with an established audit committee as at 31 December 2016, as well as the ownership structure of issuers without an established audit committee (32.91% and 41.11% respectively).

1.3.3 Remuneration

The supervisory board of the issuer is responsible for the adoption of decisions on the remuneration of management and supervisory board directors, which must be in line with the long-term interests of issuers and their shareholders. It is considered a good governance practice to ensure a transparent relationship between the governance and remuneration policies and performance of the company, for the purpose of which issuers should publicly disclose a remuneration statement and allow the shareholders to express their views on the remuneration policy.

1.3.4 Remuneration of management board members

The criteria and amounts of remuneration of management board members are determined by the supervisory board. Pursuant to Article 247(1) of the CA, when determining the aggregate income of a particular management board member (salary, profit participation, reimbursement of expenses, payment of insurance premiums, commissions and all other benefits), the supervisory board must ensure that the aggregate income bears a reasonable relationship to the work done by that management board member and to the financial position of the company.

Pursuant to the Code of Corporate Governance, the remuneration of management board members must consist of:

- fixed remuneration, which is invariable and does not depend on the performance of the company (salary, reimbursement of travel and other expenses, payments of life and health insurance premiums, additional retirement premiums, etc.)
- variable remuneration, which is linked to the performance of the company in a particular business year (profit participation, commission, royalties)
- share options and similar instruments with the effect of long-term incentives.

Table 1.2 presents the number of issuers which reported the average gross amount of fixed and variable remuneration paid to management board members of share issuers, the average amount of other benefits paid to management board members and the average value of options held by management board members, as well as the respective amounts in 2016, 2015 and 2014. The amounts shown in Table 1.2 are average amounts paid to the entire management board (not to a single management board member).

Table 1.2 Amount of remuneration of management board members of share issuers in 2016, 2015 and 2014 (in HRK)

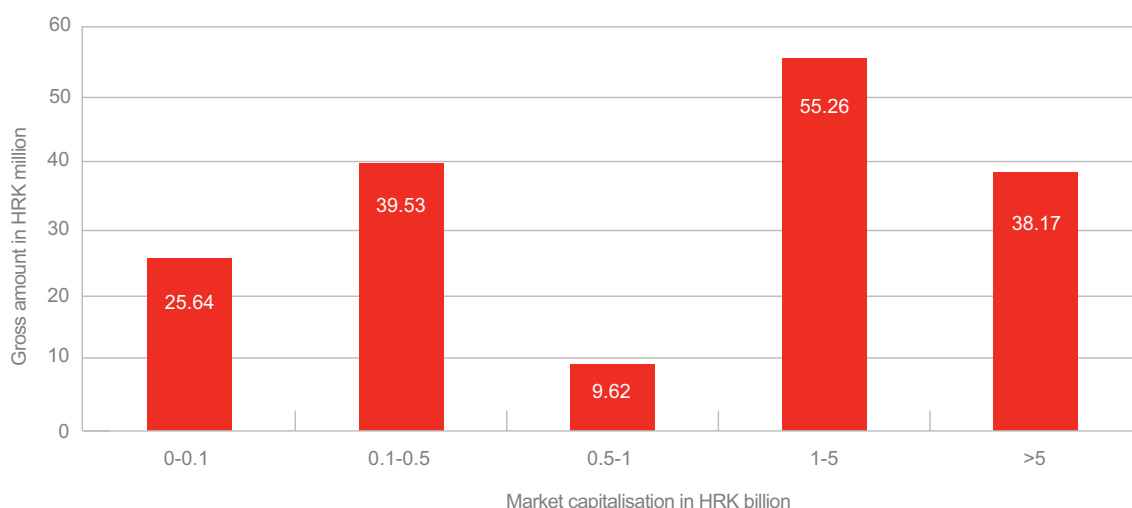
		Average gross amount paid to management board members during the year		Average amount of other benefits paid to management board members	Average value of options held by management board members
		Fixed remuneration	Variable remuneration		
2016	Number of issuers	72	19	7	3
	Amount	2,236,450	1,752,400	1,349,549	11,886,341
2015	Number of issuers	85	20	7	4
	Amount	1,918,047	2,845,726	463,883	10,673,739
2014	Number of issuers	94	14	8	4
	Amount	1,840,885	1,969,520	712,865	8,615,272

Source: Questionnaire

- In 2016, gross amounts of fixed remuneration paid to management board members ranged between HRK 26.7 thousand and HRK 17.78m.

- In 2016, nominally highest gross amounts of fixed remuneration were paid to management board members of issuers from the banking sector, followed by issuers from the tourism industry, while nominally lowest gross amounts of fixed remuneration were paid to management board members in the property and funds industry.
- In 2016, gross amounts of variable remuneration paid to management board members ranged between HRK 16.9 thousand and HRK 7.3m. The highest amount of variable remuneration was paid to management board members from the banking sector and the lowest to management board members from the agriculture sector.
- In the course of 2016, the total value of options held by management board members ranged from HRK 1.9m to HRK 31.6m (an issuer from the food industry).
- The total amount of other benefits paid to management board members ranged between HRK 28.6 thousand and HRK 4.8m.
- A total of 20 issuers (16 issuers in 2015) reported having submitted the annual remuneration policy statement relating to management board members to the general assembly in 2016.

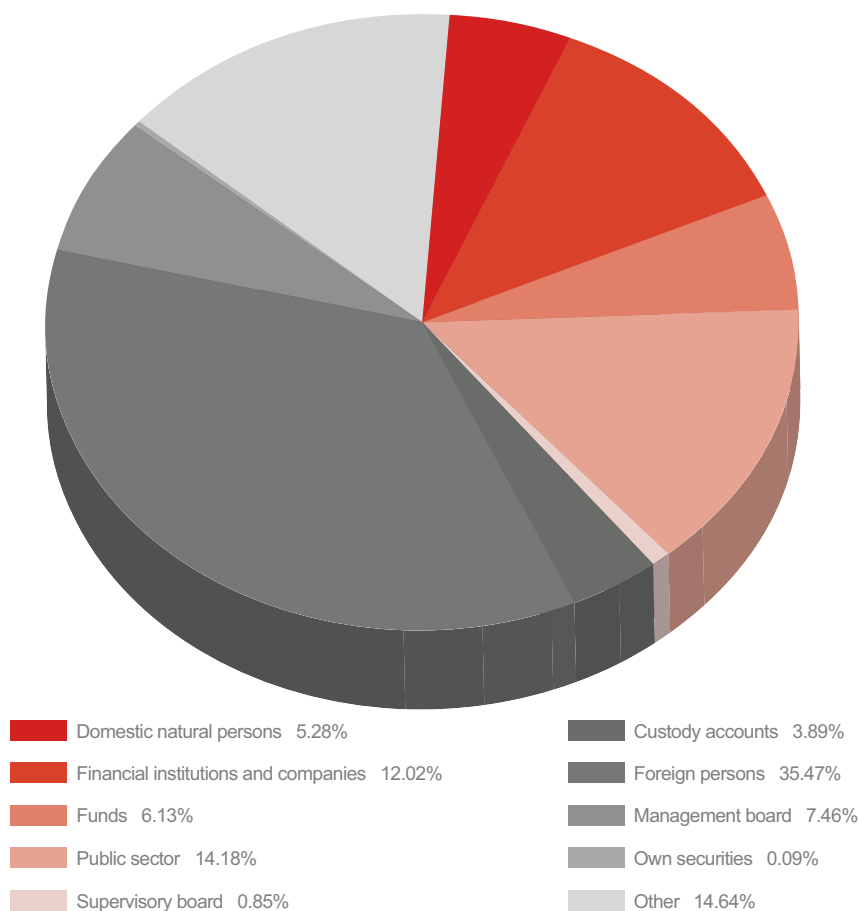
Chart 1.20 Total gross amount of fixed remuneration paid to management board members in 2016 in relation to market capitalisation (in HRK billion)



Source: Questionnaire, Zagreb Stock Exchange

In 2016, issuers with market capitalisation totalling HRK 0-0.1bn paid to their management board members an average gross fixed amount reaching HRK 827 thousand; issuers with market capitalisation totalling HRK 0.1-0.5bn paid to their management board members an average gross fixed amount reaching HRK 2.1m; issuers with market capitalisation totalling HRK 0.5-1bn paid to their management board members an average gross fixed amount reaching HRK 1.4m; issuers with market capitalisation totalling HRK 1-5bn paid to their management board members an average gross fixed amount reaching HRK 5m, and issuers with market capitalisation larger than HRK 5bn paid to their management board members an average gross fixed amount reaching HRK 9.5m.

Chart 1.21 Ownership structure of share issuers that paid a gross fixed amount to management board members over HRK 5m in the course of 2016



Source: Questionnaire, CDCC

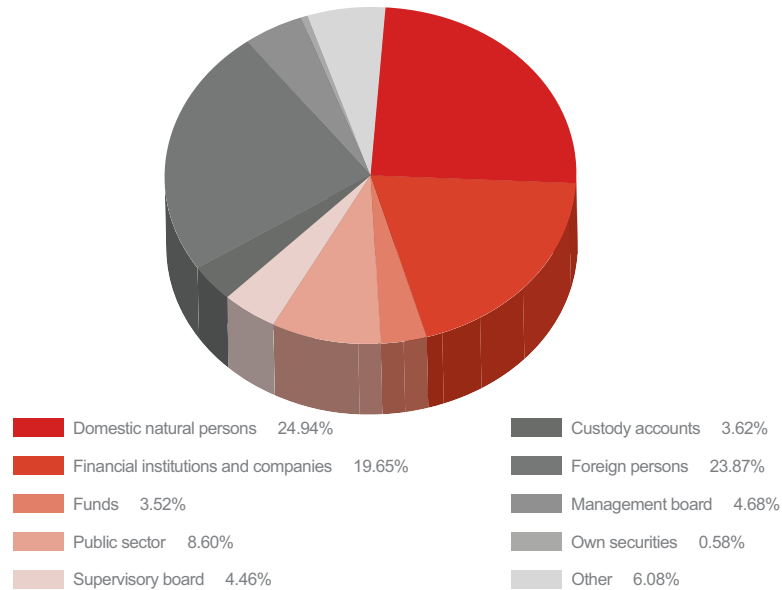
- As in 2015, the ownership structure of issuers that paid a gross fixed amount to their management board members over HRK 5m in the course of 2016 is dominated by foreign persons (35.47%).

Management board remuneration policy

Pursuant to the Code of Corporate Governance (section 6.3 Remuneration), the issuer must disclose a remuneration policy statement relating to management and supervisory board members as part of its annual report. The remuneration policy statement must be permanently available on the website of the issuer.

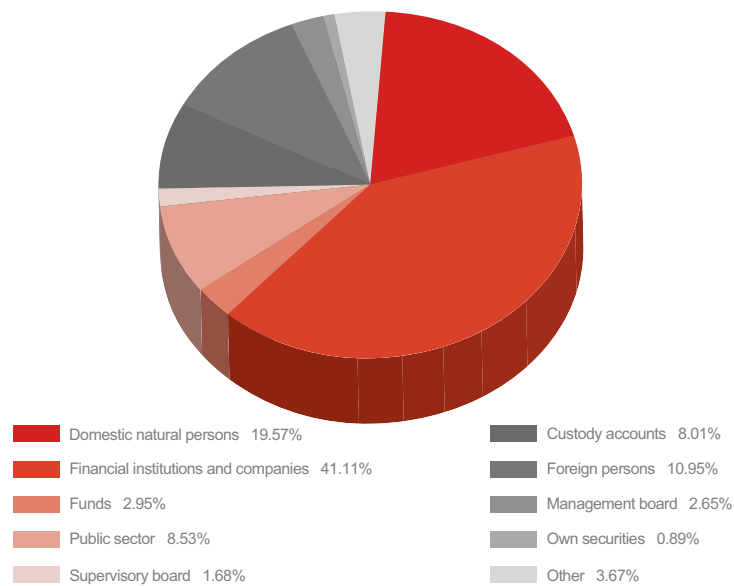
- A total of 27 issuers (the same as in 2015) reported having a remuneration policy for management board members in place for 2016.
- A total of 16 issuers that reported having a remuneration policy for management board members in place do not make this policy publicly available. Data on remuneration policy for management board members has been made available by the remaining issuers on their websites, the Zagreb Stock Exchange, and Hanfa, i.e. the Officially Appointed Mechanism for the Central Storage of Regulated Information (OAM).

Chart 1.22 Ownership structure of share issuers with an established remuneration policy for management board members in place as at 31/12/2016



Source: Questionnaire, CDCC

Chart 1.23 Ownership structure of share issuers without an established remuneration policy for management board members in place as at 31/12/2016



Source: Questionnaire, CDCC

- The ownership structure of issuers without an established remuneration policy for management board members in place as at 31 December 2016 was dominated by financial institutions and companies (41.11%) and domestic natural persons (19.57%), while the ownership structure of issuers with an established remuneration policy for management board members as at 31 December 2016 was dominated by domestic natural persons (24.94%) and foreign persons (23.87%).



Severance pay

- A total of 11 issuers reported total amounts of severance pay for management board members defined in contracts in 2016, which ranged from HRK 40 thousand to HRK 21.4m
- Two issuers reported total amounts of severance pay given to management board members in 2016, which ranged from HRK 257.4 thousand to HRK 585 thousand.

1.3.5 Remuneration of supervisory board members

Pursuant to Article 269 of the CA, members of the supervisory board may receive remuneration for their services that may be defined as the participation by the supervisory board member in the profit of the issuer. The remuneration is determined by the statute or by the decision of the general assembly of the issuer, and it must be in line with the activities carried out by the supervisory board members and with the performance of the issuer.

- In 2016, a total of 24 issuers reported the level of supervisory board member remuneration being prescribed by the statute, whereas 57 issuers reported the level of supervisory board member remuneration being determined by the decision of the general assembly. Other issuers did not respond, or they reported that the amount of remuneration of supervisory board members was determined in some other way.

Table 1.3 presents the number of issuers which reported the average gross amount of fixed and variable remuneration paid to supervisory board members of share issuers, the average amount of other benefits paid to supervisory board members, the average value of options held by supervisory board members and the respective amounts paid in 2016, 2015 and 2014. The amounts shown in Table 1.3 are average amounts paid to the entire supervisory board (not to a single supervisory board member).

Table 1.3 Amount of remuneration of supervisory board members of share issuers in 2016, 2015 and 2014 (in HRK)

		Average gross amount of remuneration paid to supervisory board members during the year		Average amount of other benefits paid to supervisory board members
		Fixed remuneration	Variable remuneration	
2016	Number of issuers	78	5	0
	Amount	406,855	774,894	0
2015	Number of issuers	89	5	1
	Amount	452,469	358,579	14,870
2014	Number of issuers	96	6	0
	Amount	391,127	479,791	0

Source: Questionnaire

- A total of 78 issuers reported the total gross amount of fixed remuneration paid to supervisory board members in 2016, which ranged from HRK 16.1 thousand to HRK 2.1m.
- Five issuers reported the total gross amount of variable remuneration paid to supervisory board members, which ranged from HRK 1.2 thousand to HRK 2.3m.
- A total of 20 issuers (19 issuers in 2015) reported having submitted the annual remuneration policy statement relating to supervisory board members to the general assembly.

1.3.6 Remuneration of the senior management of share issuers

- The total gross amount of fixed remuneration paid to the senior management in 2016 was reported by 60 issuers, with the amounts ranging between HRK 470.5 thousand (an issuer from the tourism industry) and HRK 23.1m (also an issuer from the tourism industry).
- The total gross amount of variable remuneration paid to the senior management in 2016 was reported by 16 issuers, with the amounts ranging between HRK 17 thousand (an issuer from the telecommunications industry) and HRK 5.9m (an issuer from the tourism industry).
- The total value of options held by the senior management was reported by one issuer, in the amount of HRK 9.7m.
- The total gross amount of severance pay agreed with the senior management in 2016 was reported by ten issuers, with the amounts ranging from HRK 101 thousand to HRK 11.8m.
- The total gross amount of severance pay given to the senior management in 2016 was reported by 14 issuers, with the amounts ranging from HRK 57.6 thousand to HRK 560.6 thousand.
- The total amount of other benefits paid to the senior management was reported by nine issuers, with the amounts ranging from HRK 3 thousand to HRK 5.9m.

1.3.7 Related party transactions

In 2016, a total of 24 issuers reported having an internal regulation in place for cases of related party transactions. Such a regulation was reported by 25 and 26 issuers in 2015 and 2014 respectively.

Table 1.4 sets out the average value of reported transactions concluded by the share issuer with the following stakeholder groups: shareholders with more than 5% of the initial capital of the issuer, management and supervisory board members of the issuer, senior management of the issuer and within the group the issuer belongs to or is its parent, during 2014, 2015 and 2016.

Table 1.4 Average value of reported related party transactions in 2014, 2015 and 2016 (in HRK)

		Average gross value of related party transactions concluded by the issuer			
		with shareholders owning more than 5% of the initial capital of the issuer	with management and supervisory board members of the issuer	with senior management of the issuer	within the group the issuer belongs to or is its parent
2016	Number of issuers having reported the transaction	36	22	12	46
	Transaction value	252,381,830	12,715,746	7,139,912	363,163,243
2015	Number of issuers	37	19	9	50
	Amount	271,561,189	10,144,030	5,623,301	408,656,623
2014	Number of issuers	39	18	9	49
	Amount	299,218,739	5,201,024	9,171,700	395,999,671

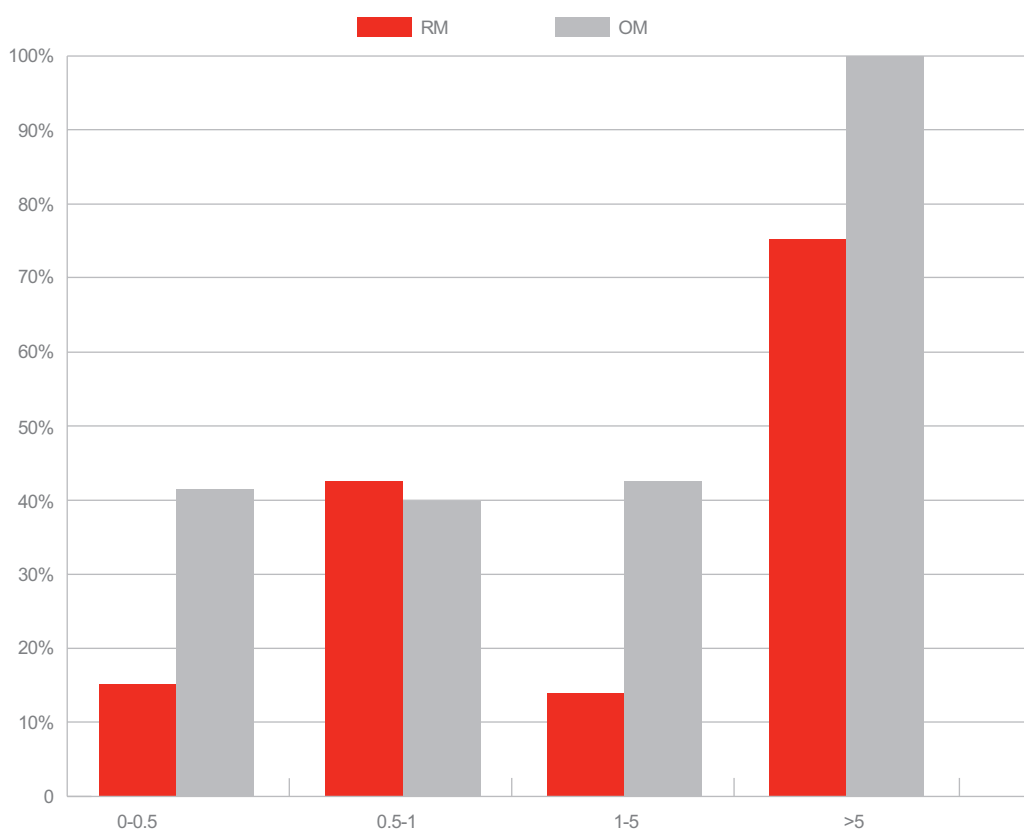
Source: Questionnaire

1.3.8 Conflicts of interest

Conflicts of interest arise if a member of the management or supervisory board or board of directors is not impartial with respect to the subject under consideration, and may affect the decision-making process on the basis of interests which differ from interests of the issuer.

- At the end of 2016, a total of 29 issuers (the same as in 2015) reported having an internal regulation in place to identify, prevent and report conflicts of interest. The internal regulations contained the following basic provisions relating to conflicts of interest: identifying potential and/or actual conflicts of interest, protecting investors through the prevention of use of inside information, monitoring transactions by relevant persons, ensuring that interests of issuers' clients come before the interests of issuers and their employees, preventing bribery and corruption.
- The majority of 29 issuers that reported having an internal regulation in place to identify, prevent and report conflicts of interest at the end of 2016 came from the banking sector (seven), followed by tourism industry (four), property and fund industry (three) and telecommunications industry (three).
- In 2016, a total of 11 cases of conflicts of interest were reported by one issuer, whereas other issuers did not report any conflicts of interest. All the reported cases of conflicts of interest involved persons who failed to abstain from voting on entering related party transactions.

Chart 1.24 Issuers having an internal regulation to identify, prevent and report conflicts of interest in relation to market capitalisation of issuers (in HRK billion) and market where shares are admitted, as at 31/12/2016



Source: Questionnaire, Zagreb Stock Exchange

1.3.9 General assembly

The general assembly is the only governing body of the issuer whose work is open to participation by all shareholders. The main function of the general assembly is to ensure that the shareholders' will is expressed. As opposed to the management and supervisory board or board of directors, the general assembly is not a permanent governing body of the issuer and is convened ad hoc, but at least once a year.

- According to the data from 110 completed Questionnaires, three issuers did not hold any general assembly meetings in 2016. In 2015, according to the data from 128 Questionnaires completed, five issuers did not hold any general assembly meetings, whereas two issuers reported not having held any general assembly meetings in 2014 pursuant to the data from 141 completed Questionnaires.
- As a reason for not having held any general assembly meetings in 2016, one issuer reported undergoing bankruptcy proceedings, while two issuers did not state their reasons.
- According to data from 110 completed Questionnaires, a total of 83 issuers reported having held only one general assembly meeting, 20 issuers held two general assembly meetings, three issuers held three general assembly meetings, while one issuer held four general assembly meetings.
- Out of a total of 136 general assembly meetings held during 2016, there were 109 regular and 27 extraordinary general assembly meetings.

Remote voting

Pursuant to the Code of Corporate Governance, shareholders must be allowed to participate and, in particular, to vote in the general assembly meeting by using modern communication technologies (e.g. by electronic means).

- Remote voting (e.g. by electronic means) was provided for at two general assembly meetings held by one issuer in 2016.

Internal rules of procedure of the general assembly

- A total of 41 issuers reported having rules of procedure of the general assembly in place for 2016, with none of the issuers having reported changes in their rules of procedure during the year.
- A total of ten issuers reported having sent the invitation to the general assembly meeting by registered post.

Participation in the general assembly meeting

Participation in the work of the general assembly is a fundamental and indefeasible right of shareholders (right to participate). This right may be exercised through a representative, but in majority of cases it is exercised by proxy.

All members of the issuer's governing bodies must participate in the work of the general assembly. The obligation to attend the general assembly meeting relates to all members of the management and supervisory board or board of directors, and not only to their members who submit reports or draft decisions. In other words, even those members of the management and supervisory board or board of directors who are not submitters or petitioners are obliged to attend the general assembly meeting.

- General assembly meetings held in 2016 were attended by 21 shareholders (20 shareholders in 2015). The largest number of shareholders attending a general assembly meeting was 451, while 20 general assembly meetings were attended by only one shareholder.

Voting limitations, attendance conditions and decision making

Shareholders cannot in general be denied their voting rights. In certain circumstances, the exercise of voting rights in the general assembly meeting is prohibited by law, namely in cases of conflicts between the interests of a shareholder and the interests of the issuer.

- Voting rights were restricted for some shareholders at six general assembly meetings of six issuers in the course of 2016. In most of those cases, voting rights were restricted due to the reason referred to in Article 293(1) of the CA (issuance of clearance to members of management or supervisory boards or boards of directors). Pursuant to the above-mentioned provision of the CA, voting rights may not be exercised by any person on their own behalf or on behalf of another person in the process of adopting a decision on whether the person should be issued clearance, on releasing the person from an obligation or on exercising rights claimed by the company with respect to that person. With respect to shares not permitting shareholders to exercise voting rights in this manner, no other person can do so on their behalf, either.

1.4 Audit and control

Audit and control are important self-regulatory mechanisms of the issuer. This chapter provides an analysis of the internal and external audit and control of issuers.

Internal control is the main regulatory mechanism for business operations within the company or issuer, including that for the corporate governance.

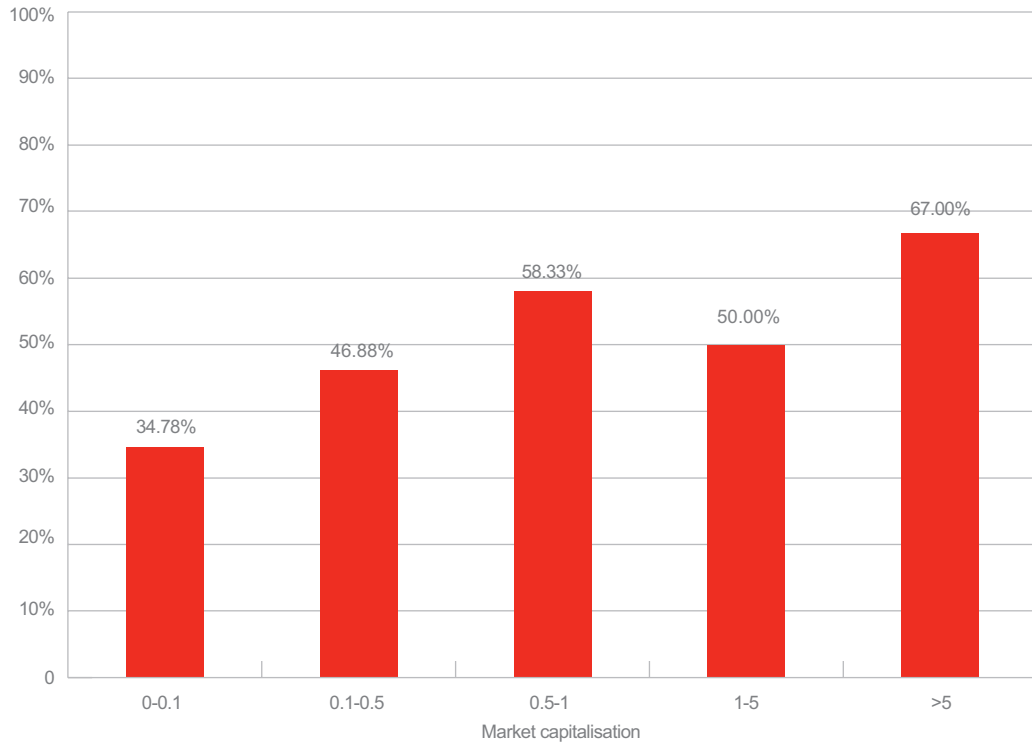
1.4.1 Internal audit and control

Pursuant to the Code of Corporate Governance, internal auditors' task is to carry out internal audit activities and to verify the compliance with regulations, guidelines and instructions. Internal auditors submit performance reports directly to the audit committee or to the supervisory board of the company.

One of the prerequisites to sound corporate governance in the interest of all shareholders is an adequate and efficient internal audit and internal control mechanism.

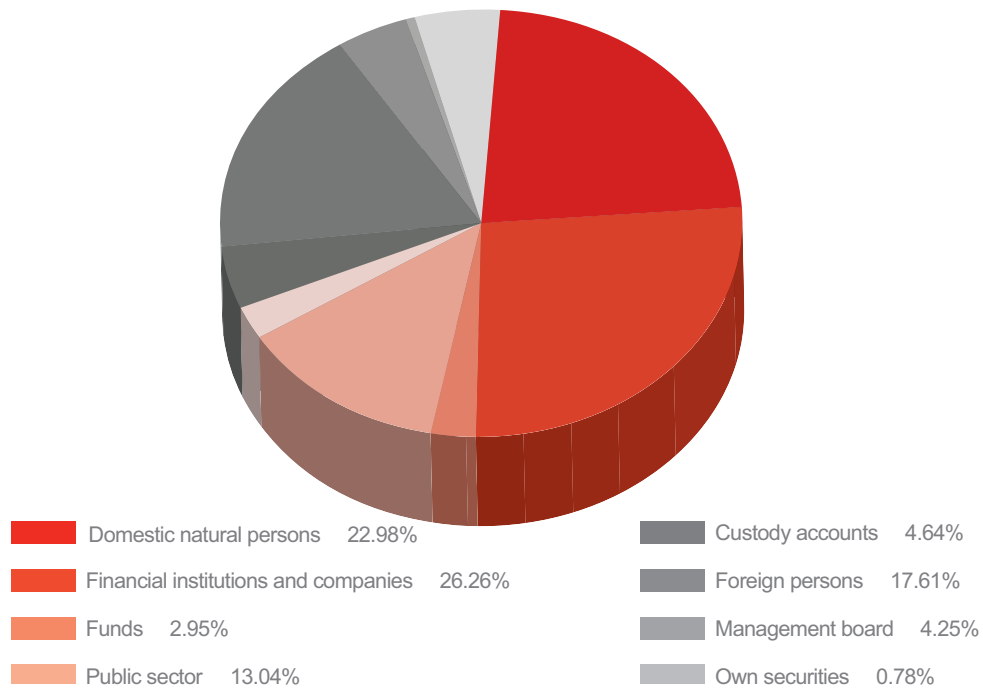
- A total of 49 or 44.55% of the issuers that submitted the 2016 Questionnaire reported having an internal audit system in place (42.19% and 40.43% of the issuers that submitted the Questionnaire for 2015 and 2014 respectively reported having an internal audit system in place).
- As at 31 December 2016, a total of 49 issuers with an internal audit system in place had a total market capitalisation of HRK 101.1bn (the total market capitalisation of 110 issuers that submitted their 2016 Questionnaires reached HRK 134.1bn as at 31 December 2016).
- Most of the issuers with an internal audit system in place belonged to the tourism industry (ten) and banking sector (nine), followed by food industry (six).
- A total of 80 or 72.73% of the issuers that submitted the 2016 Questionnaire reported having an internal control system in place (69.53% in 2015 and 69.50% in 2014).
- Most of the issuers with an internal control system in place belonged to the tourism industry (20 issuers), followed by those from the food industry and banking sector (nine issuers from each of the sectors).

Chart 1.25 Share of issuers having an internal audit system in place with respect to market capitalisation of issuers (in HRK billion)



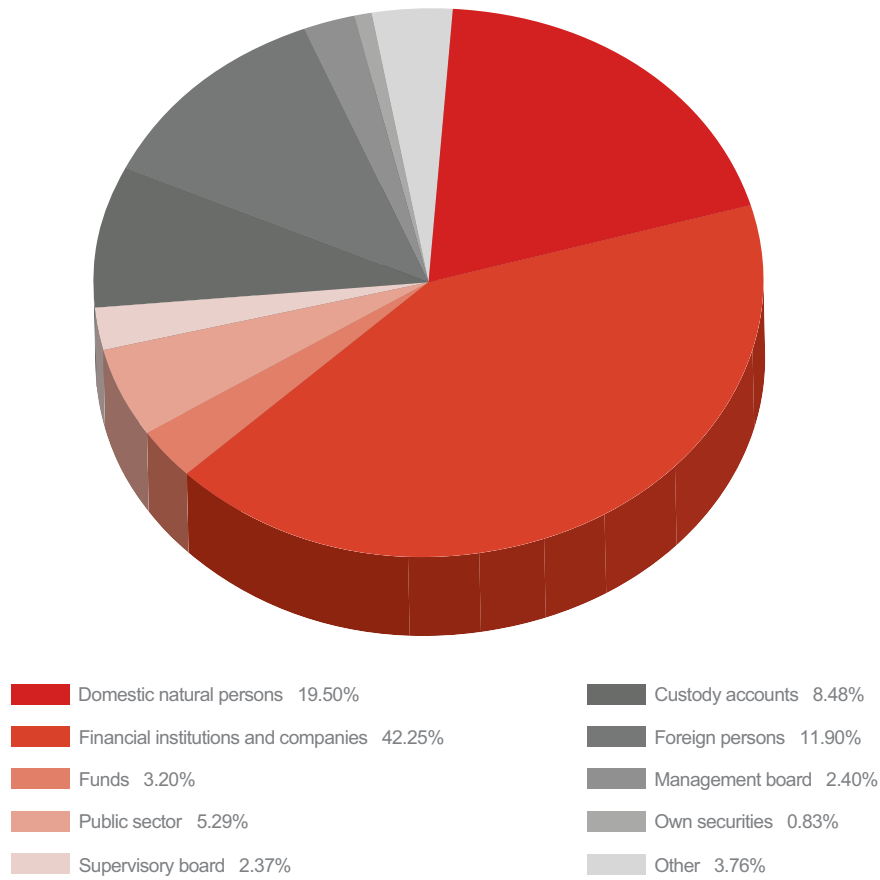
Source: Questionnaire, Zagreb Stock Exchange

Chart 1.26 Ownership structure of share issuers with an established internal audit system as at 31/12/2016



Source: Questionnaire, CDCC

Chart 1.27 Ownership structure of share issuers without an established internal audit system as at 31/12/2016



Source: Questionnaire, CDCC

- Financial institutions and companies dominate the ownership structure of issuers with an established internal audit system as at 31 December 2016, as well as the ownership structure of issuers without an established internal audit system (26.26% and 42.25% respectively).

1.4.2 Managing company risks

Managing company risks has proved to be of special importance, especially at the time of economic and financial crisis and uncertain business environment. Particular emphasis has been placed on financial institutions. The measurement of prudential risks, which comprise market, credit, operational and liquidity risks, has been regulated by specific regulations. Apart from these risks, there is a whole range of other risks that may arise in the course of business operations of a company.

- A total of 38 issuers (one fewer than in the previous year) reported having an internal regulation in place for the identification, management and prevention of risks.

- A total of 31 issuers (the same as in 2015) reported having appointed persons in charge for risk management. Majority of issuers that appointed a person to be in charge of risk management came from the banking sector (nine), followed by issuers from the food industry, tourism and other activities (three issuers from each sector).
- The most common risks reported by issuers were liquidity risk (57.27%) and credit risk (30.9%), followed by interest rate risk, macroeconomic environment risk, operational risk and reputational risk.
- A total of 36 issuers reported some risks having materialised during 2016, and 33 of them (91.67%) managed to control and manage those risks.
- The most common materialised risks were credit risk, liquidity risk, operational and currency risk.

1.4.3 External audit

Pursuant to the Code of Corporate Governance, companies must have independent external auditors, who represent an important corporate governance tool. The main function of an external auditor is to ensure that financial statements of the company adequately reflect the current financial position of the company as a whole. Independent external auditors are not related through ownership or other interests with the company, nor do they provide any services to the company.

Auditors have a crucial role in ensuring true and fair presentation of financial statements.

- A total of 33 various audit firms providing external audit services to issuers were reported in the 110 Questionnaires submitted for 2016. The largest number of issuers using services of the same audit firm was 21.
- A total of 55 issuers used services of the largest audit firms (the Big Four). The majority of issuers using services of the mentioned audit firms came from the tourism industry (nine), banking sector (seven), food industry and industry - other (six issuers in each sector).
- The market capitalisation of issuers using services of the largest audit firms amounted to HRK 124.9bn, or 93.14% of the total market capitalisation of issuers that submitted the 2016 Questionnaire.
- The average length of the time period during which issuers used services of the same audit firm was 6.46 years.
- The average length of time during which issuers used services of the same certified auditor in the same audit firm was 4.6 years.
- A total of 101 issuers reported the gross amount paid to an external audit firm for auditing services provided in 2016. The amount totalled an average of HRK 315.2 thousand, ranging from HRK 18.75 thousand to almost HRK 4.9m. The average gross amount paid to an external audit firm in 2015 reached HRK 330.1 thousand.
- Six issuers reported having paid an external audit firm for services other than auditing services provided in 2016. The average gross amount paid totalled HRK 293.4 thousand, with all the amounts ranging from HRK 14.2 thousand to HRK 969.9 thousand. Other services provided to issuers by external auditors in 2016 were legal and tax advice and due diligence.

- None of the issuers reported family or business relations between the external audit firm and auditor and the issuer, i.e. management and supervisory board members and senior management of the issuer.

Chart 1.28 Gross amount paid to external audit firms for audit services provided during 2016 in relation to market capitalisation (in HRK billion) of issuers



Source: Questionnaire, Zagreb Stock Exchange

The correlation between the gross amount paid to external audit firms for audit services provided during 2016 and market capitalisation of issuers was as high as 0.840904.

1.5 Investor relations

Pursuant to the Code of Corporate Governance, the management board of the issuer must provide investors with access to accurate and precise information related to positive and negative aspects of issuer's business operations, which will allow investors to properly understand and assess the issuer's position, and to make informed investment decisions.

1.5.1 Website of the issuer

Issuers are obliged to ensure an efficient and practical information exchange through their publicly available websites. For the purpose of equal treatment of all shareholders irrespective of the country of origin, all the information published by issuers on their websites must be provided both in Croatian and English.

- According to the data from Questionnaires submitted in 2016, all issuers reported having their website in Croatian, and 76 issuers (69.1%) reported having their website in English, as well.
- A total of 33 issuers (30%) reported having a separate organisational unit or employees in charge of public (investor) relations. These issuers mostly belonged to the banking sector (seven issuers), food industry (four issuers) and telecommunications and tourism industry (three issuers from each of the industries).
- A total of 26 issuers (23.64%) reported having published the calendar of significant events on their websites. In 2015, a total of 31.25% of the issuers provided the same answer.
- A total of 14 issuers reported having held one or more press conferences during 2016. The largest number of press conferences held by one issuer was 12, while the average number of press conferences was three. The most common reasons for convening a press conference were presentations of business results, including significant activities and investments, and presentations of new products.

1.5.2 Dividend payments

Ownership of shares entitles shareholders to receive dividends. A decision on dividend payment is adopted by the general assembly upon the proposal of the management board. Dividends may be paid out in money or in shares. In addition, the management board may, subject to the consent of the supervisory board, adopt a decision on advance dividend payment.

- Based on data from 110 Questionnaires, 32 share issuers (29.1%) issued a decision on dividend payment in 2016.
- The average amount of dividend per share in 2016 totalled HRK 94.78 (HRK 218.13 in 2015).

- As in 2015, most of the issuers that adopted a decision on dividend payment in 2016 belonged to the tourism industry (seven issuers), followed by food industry and banking sector (four issuers from each of the sectors).
- The total market capitalisation of issuers that adopted a decision on dividend payment in 2016 reached HRK 72.34bn. Among these issuers, the largest market capitalisation was reported by an issuer from the banking sector (HRK 14.7bn), and the smallest by an issuer from other activities (HRK 20.65m).

2 Annual report on corporate governance of corporate bond issuers

- At the end of 2016, a total of 16 corporate bonds were issued by 14 different issuers. Twelve of the issuers completed and submitted the Questionnaire for 2016.
- The interest rate ranged between 3.1250% and 9.7500% and totalled an average of 5.7695% (at the end of 2015, it amounted to an average of 6.1083%).
- Corporate bonds of three issuers were removed from the official market in 2016 (bonds came due in the course of 2016).
- In 2016, four issuers issued new corporate bonds, three of which were listed on the regular market, and one on the official market of the Zagreb Stock Exchange.
- At the end of 2016, one bond issuer belonged to the financial sector (banking) and 13 issuers to the nonfinancial sector. Regarding the non-financial sector, issuers came from telecommunications industry, construction industry and other activities (three issuers from each of the sectors), as well as from transport industry, trade, pharmaceutical industry and energy sector (one issuer from each of the sectors).
- As at 31 December 2016, none of the corporate bond issuers was undergoing bankruptcy proceedings.

2.1 Capital and origin of capital

Initial capital

Table 2.1 shows data on the initial capital of corporate bond issuers and share and corporate bond issuers.

Table 2.1 Initial capital of bond issuers as at 31/12/2014, 2015 and 2016

Bond issuers	Number of issuers						
	2014	2015	2016		2014	2015	2016
with admitted shares	3	5	4	Initial capital	385,428,710	1,268,189,840	1,132,737,840
				Market Capitalisation	171,500,273	257,339,378	382,968,369
without admitted shares	9	8	10	Initial capital	23,190,111,948	23,044,712,948	26,877,969,148
				Market Capitalisation	2,471,273,177	1,531,809,372	4,414,822,544
TOTAL	12	13	14	Initial capital	23,575,540,658	24,312,902,788	28,010,706,988
				Market capitalisation	2,642,773,449	1,789,148,749	4,797,790,912

Source: register of companies, Zagreb Stock Exchange

- At the end of 2016, out of 14 corporate bond issuers, four also had their shares on the regulated market of the Zagreb Stock Exchange.
- At the end of 2016, the total initial capital of all corporate bond issuers increased by 15.21%, while the number of issuers increased by one. The initial capital of corporate bond issuers with admitted shares decreased by 10.68% in relation to the previous year, with the number of issuers also having decreased by one. The initial capital of corporate bond issuers without admitted shares increased by 16.63% (the number of issuers increased by two).
- The total market capitalisation of all corporate bonds issuers increased by 168.16% relative to the previous year. At the end of 2016, the total market capitalisation of corporate bond issuers with admitted shares fell by 48.82%, whereas a 188.21% decrease in market capitalisation was reported by corporate bond issuers without admitted shares.

2.1.1 Ownership structure of corporate bond issuers

Data on the ownership structure of bond issuers has been provided on the basis of data received from the CDCC; therefore the following analysis comprises only corporate bond issuers established as joint-stock companies (ten issuers).

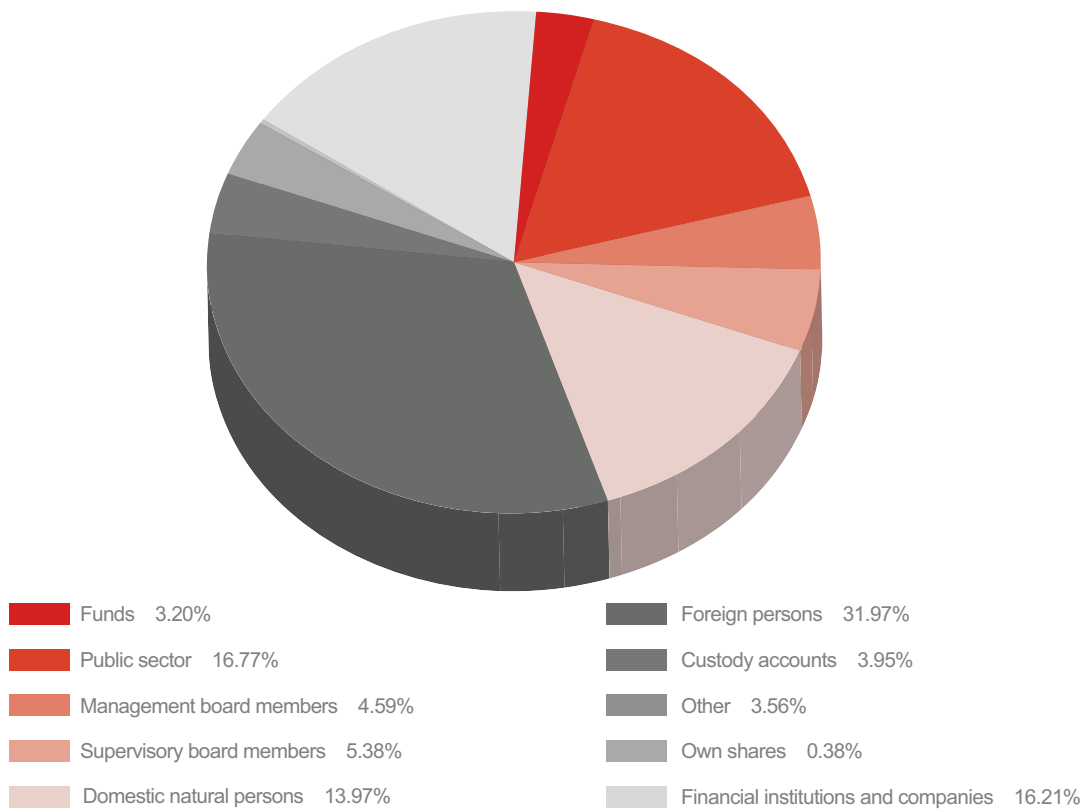
The ownership structure has been analysed by groups of the shareholders, with the sum of all groups making 100% of the ownership structure, meaning that one shareholder can be allocated to a single group only.

The structure of joint-stock companies is divided into the following groups:

- own shares
- financial institutions and companies
- funds (investment and pension funds with their registered offices in the Republic of Croatia)
- public sector (Republic of Croatia)
- members of the management board
- members of the supervisory board
- domestic natural persons (except for members of the management and supervisory board)
- foreign persons (except for members of the management and supervisory board)
- custody accounts
- other.

Chart 2.1 shows the ownership structure of share issuers as at 31 December 2016, according to the above mentioned groups.

Chart 2.1 Ownership structure of corporate bond issuers as at 31/12/2016



Source: CDCC

- The ownership structure of corporate bond issuers established as joint-stock companies was dominated by foreign persons with a 31.97% share (29.85% in 2015), followed by the public sector with a 16.77% share (15.51% in 2015) and financial institutions and companies with a share of 16.21% (15.44% in 2015).

2.2 Issuers' governing bodies

This chapter presents an analysis of data on governing bodies of bond issuers, for the management board and supervisory board separately. Data on the general assembly has not been analysed due to the fact that bond issuers have different legal forms (joint-stock company, limited liability company, special legal form).

Nine bond issuers established as joint-stock companies have a two-tier governance system, meaning that, besides a general assembly, they have two more governing bodies: a management board, which manages and represents the company, and a supervisory board, which supervises the company's business operations. One issuer has a one-tier governance system.

2.2.1 Management board

The following text presents an analysis of data on management board members of bond issuers established as joint-stock companies, as at 31 December 2014, 2015 and 2016.

The management board may consist of one or more persons. The number of management board members is defined by the statute of the issuer. The CA does not stipulate the minimum number of management board members.

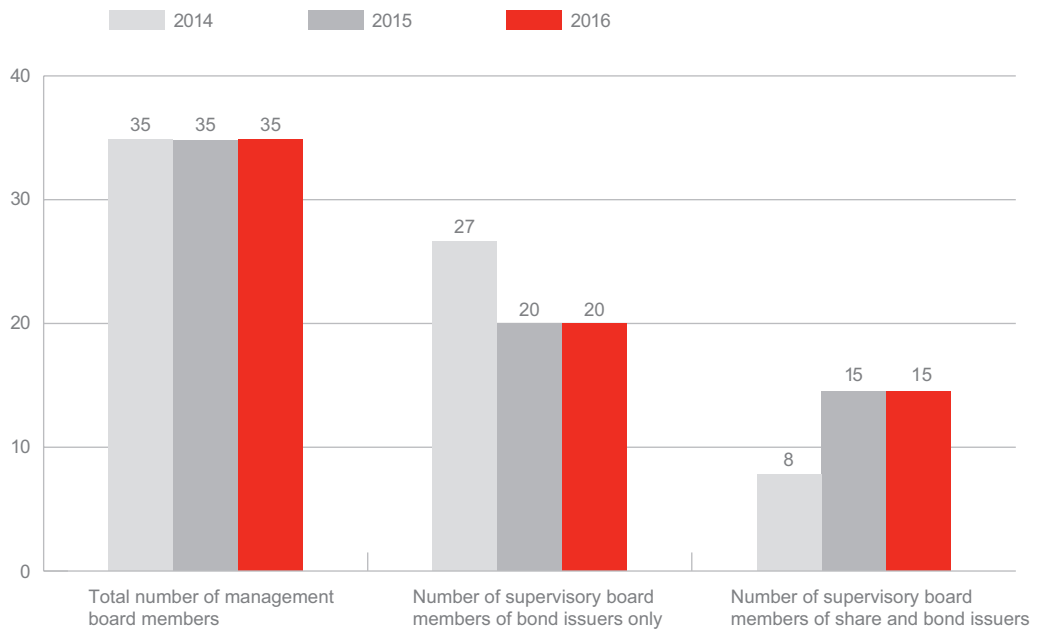
Only natural persons with full legal capacity may be appointed members of the management board.

The analysis of data on the size and structure of the management and supervisory board has taken into account only bond issuers established as joint-stock companies (ten issuers).

The following analysis shows the number of management board members of joint-stock companies – corporate bond issuers, totalling ten at the end of 2016 and 2014 and 11 at the end of 2015.

Chart 2.2 shows the total number of management board members of bond issuers as at 31 December 2014, 2015 and 2016.

Chart 2.2 Total number of management board members as at 31/12/2014, 2015 and 2016



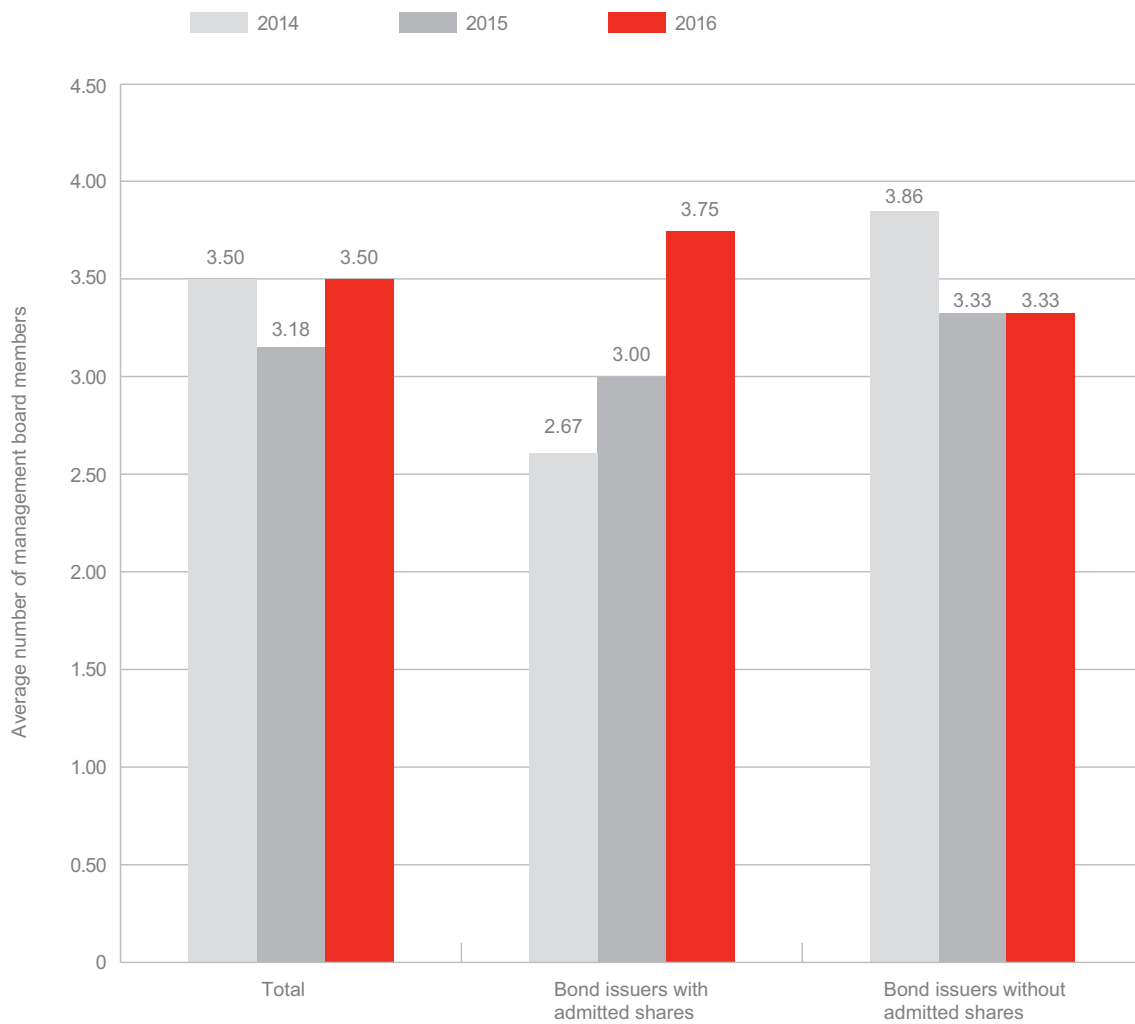
Source: register of companies, Hanfa

- As at 31 December 2016, the maximum number of management board members was five, as reported by two bond issuers. Five issuers had four members of the management board, two issuers had two members, while one issuer had one member of the management board.

Chart 2.3 shows the average number of management board members of corporate bond issuers as at 31 December 2014, 2015 and 2016.



Chart 2.3 Average number of management board members of bond issuers as at 31/12/2014, 2015 and 2016



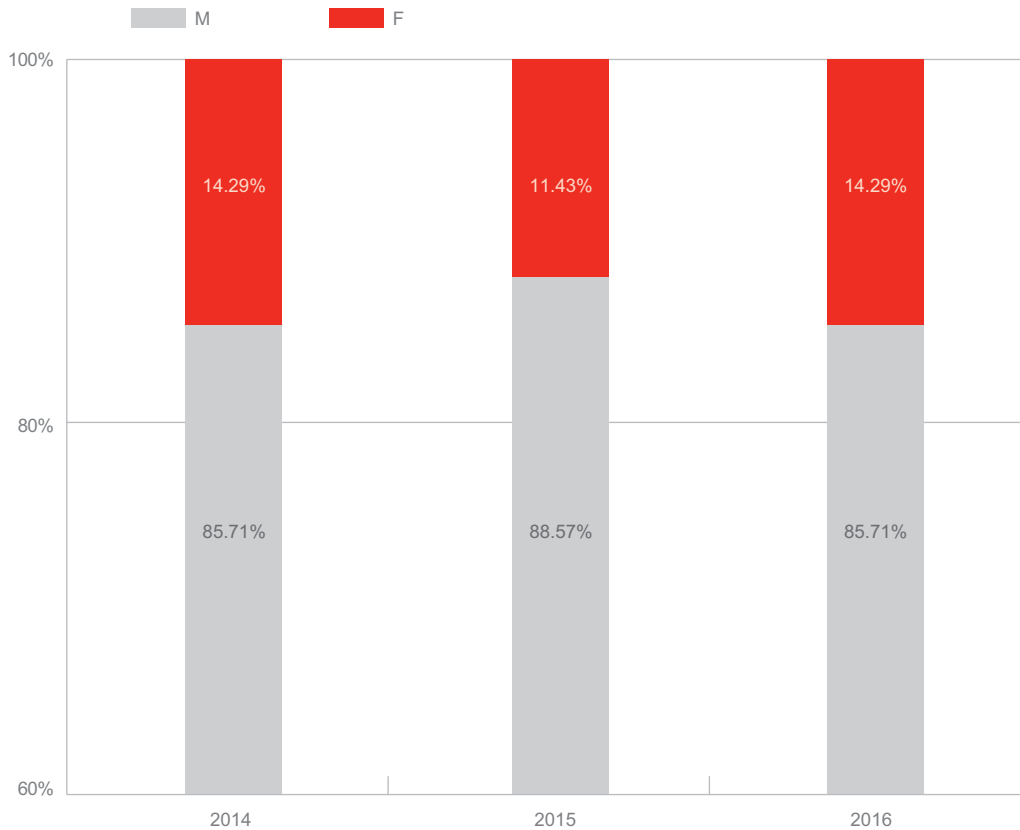
Source: register of companies, Hanfa

Management board member structure by gender, age and professional qualifications

- As at 31 December 2016, five women sat on management boards of corporate bond issuers. Four corporate bond issuers had a woman on their management board as at 31 December 2015.
- As at 31 December 2016, most management board members of corporate bond issuers (48.72%) were between 35 and 45 years old, 30.76% were 45 to 55 years old, 15.39% were older than 55 years of age, and only 5.13% were younger than 35 years of age.
- As regards the formal qualifications of management board members of corporate bond issuers, all of them had a university degree, and 7.69% had a PhD.

Chart 2.4 shows the proportion of men to women on management boards of corporate bond issuers as at 31 December 2014, 2015 and 2016.

Chart 2.4 Proportion of men to women on management boards of corporate bond issuers as at 31/12/2014, 2015 and 2016



Source: register of companies, Hanfa

Rules of procedure of the management board

- Eight corporate bond issuers reported having an internal regulation on management board activities (rules of procedure of the management board) for the year 2016, of which one issuer reported changes in this regulation occurring during the year. The reason for the change of internal regulation of management board activities as reported by this issuer was a change of management board members' duration of term.

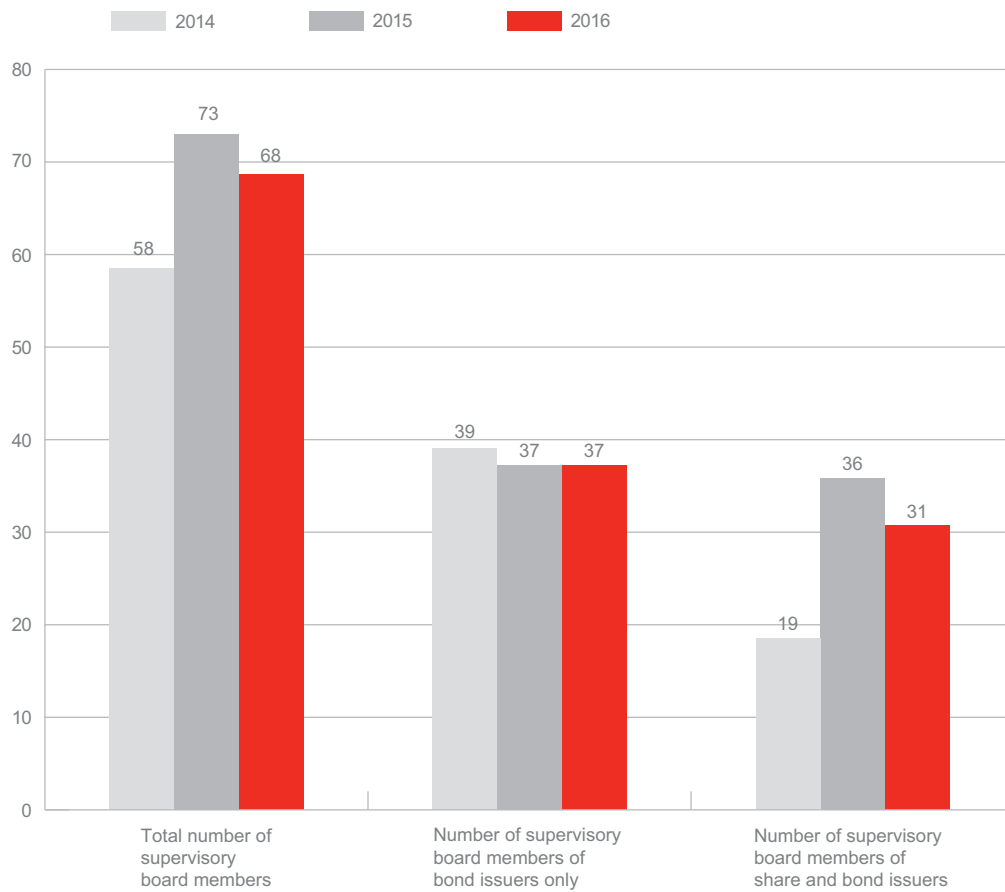
Meetings of the management board

- In 2016, six corporate bond issuers reported having a schedule of meetings of the management board, while three issuers reported having mechanisms for proxy voting at management board meetings.
- The average number of management board meetings was 45 (the maximum number of meetings held was 124, and the minimum number eight).

2.2.2 Supervisory board

Chart 2.5 presents the total number of supervisory board members of corporate bond issuers at the end of 2014, 2015 and 2016.

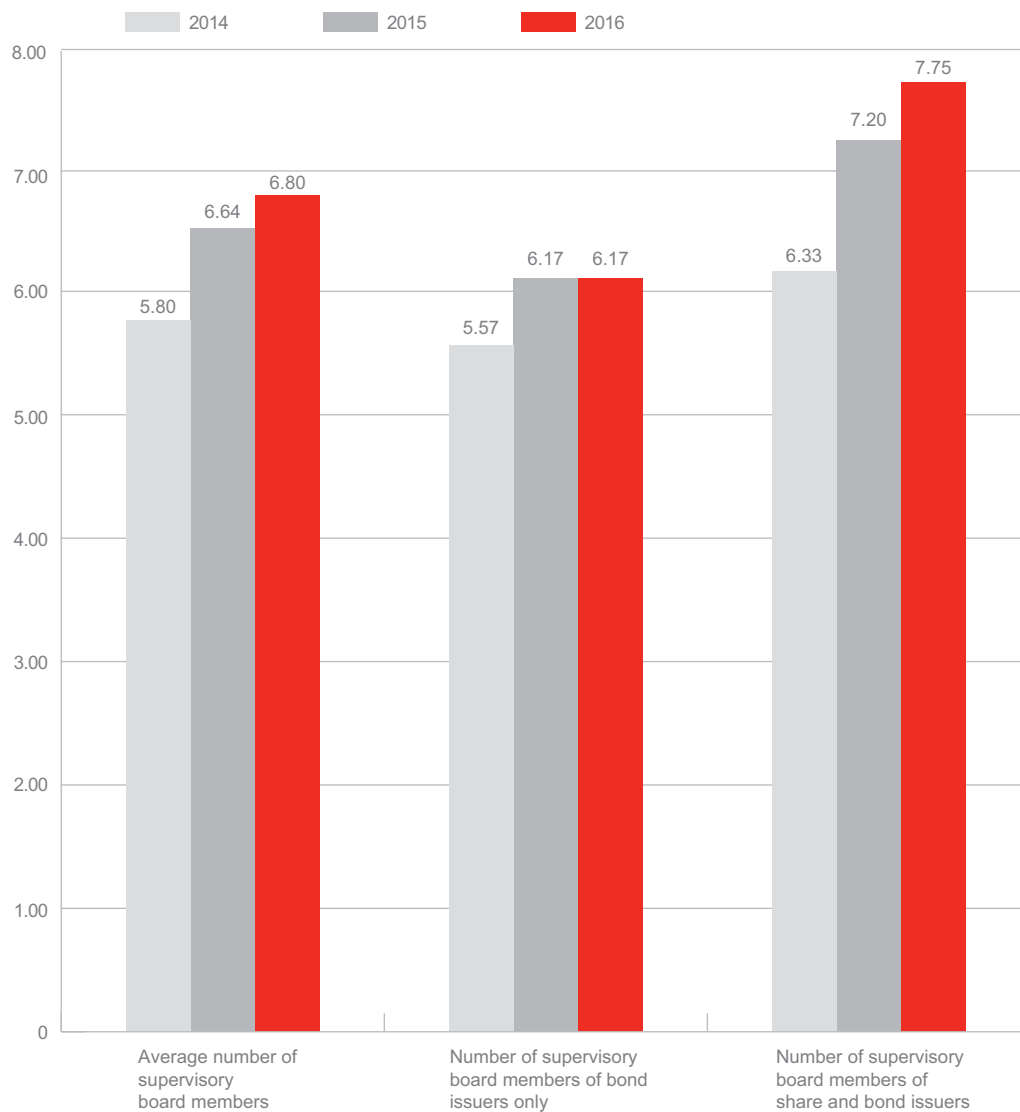
Chart 2.5 Total number of supervisory board members as at 31/12/2014, 2015 and 2016



Source: register of companies

Chart 2.6 shows the average number of supervisory board members of corporate bond issuers as at 31 December 2014, 2015 and 2016.

Chart 2.6 Average number of supervisory board members of corporate bond issuers as at 31/12/2014, 2015 and 2016

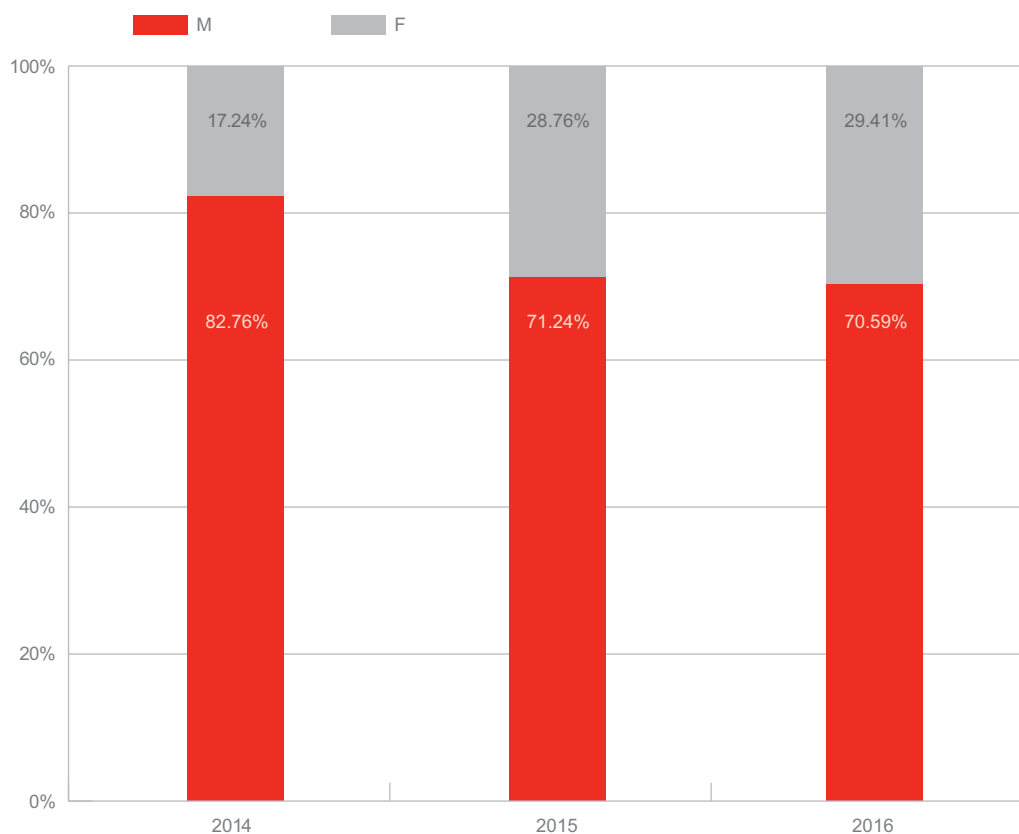


Source: register of companies

Supervisory board member structure by gender, age and professional qualifications

Chart 2.7 shows the proportion of men to women on supervisory boards of corporate bond issuers as at 31 December 2014, 2015 and 2016.

Chart 2.7 Proportion of men to women on supervisory boards of corporate bond issuers as at 31/12/2014, 2015 and 2016



Source: register of companies

- In the observed period, the proportion of women on supervisory boards of corporate bond issuers totalled 25.14%, exceeding the average proportion of women on management boards of corporate bond issuers in the same period (13.34%), but still being far from the defined gender-balanced representation.
- As at 31 December 2016, most supervisory board members of corporate bond issuers (33.33%) were older than 55 years of age, 34.92% were between 35 and 45 years old, 26.99% were 45 to 55 years old, while 4.76% were younger than 35 years of age.
- As regards the formal qualifications of supervisory board members of corporate bond issuers, most of them had a university degree (84.13%), 15.87% had a secondary school degree or a lower level of education, while 12.7% had a PhD.

Supervisory board committees

- Nine issuers reported having the audit committee and four issuers reported having the remuneration committee and the nomination committee each in 2016.

Internal working procedures of the committees

- Seven out of nine issuers that had the audit committee in place in 2016 reported having established internal working procedures for the audit committee.
- Three out of four issuers that reported having the remuneration committee in place also reported having established its internal working procedures. One issuer with a nomination committee in place did not have internal working procedures for that committee.
- Three issuers reported the preparation of a report on the work of committees, with reports of one issuer being available to the public.

Meetings

- Seven out of nine issuers that had the audit committee in place reported the committee meetings having been held in 2016. The average number of audit committee meetings during the year was 2.56.
- Two issuers held six meetings of the remuneration committee in 2016, while two issuers held six meetings of the nomination committee.

Other committees

- In 2016, four issuers reported having set up another committee. These were a risk committee, corporate governance committee and committee for monitoring synergistic effects.

2.3 Remuneration

2.3.1 Remuneration of management board members

In 2016, six corporate bond issuers reported having a remuneration policy for management board members (the same as in 2015 and 2014).

Table 2.2 presents the number of issuers which reported the average gross amount of fixed and variable remuneration paid to management board members of corporate bond issuers, the average amount of other benefits paid to management board members and the average value of options held by management board members, as well as the respective amounts in 2016, 2015 and 2014.

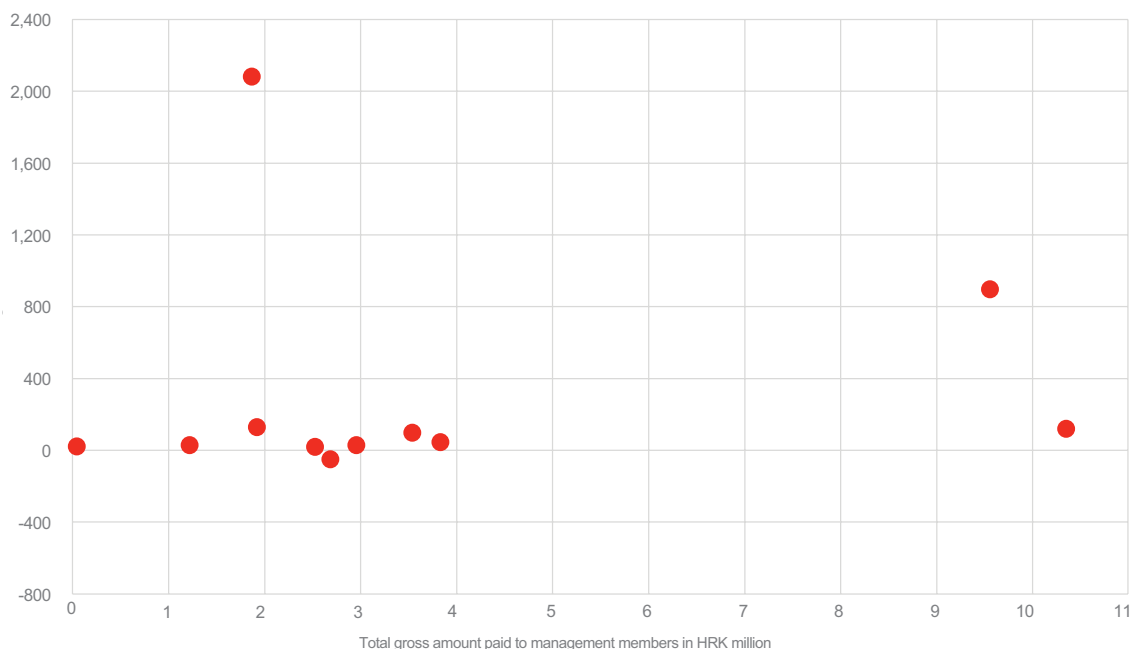
Table 2.2 Amount of remuneration of management board members of corporate bond issuers in 2016, 2015 and 2014

		Average gross amount paid to management board members during the year		Average amount of other benefits paid to management board members during the year	Average value of options held by management board members
		Fixed remuneration	Variable remuneration		
2016	Number of issuers	11	4	1	1
	Amount	4,263,922	1,004,093	4,796,452	2,181,511
2015	Number of issuers	11	4	0	1
	Amount	3,676,886	2,675,902	0	5,622,555
2014	Number of issuers	11	4	1	2
	Amount	2,858,047	1,222,545	2,304,000	85,187,595

Source: Questionnaire

- In 2016, there was a significant increase in average gross fixed amount paid to management board members, while the average gross variable amount paid to management board members decreased by 62.78% relative to 2015.
- Two issuers reported the submission of the annual remuneration policy statement relating to management board members to the general assembly.

Chart 2.8 Total gross fixed amount (in HRK million) paid to management board members in 2016 in relation to consolidated financial statements of issuers (in HRK million)



Source: Questionnaire, Zagreb Stock Exchange

2.3.2 Remuneration of supervisory board members

- Two corporate bond issuers reported the level of supervisory board member remuneration being prescribed by the statute, while one issuer reported the level being determined by the general assembly. Other issuers failed to provide their answers.

Table 2.3 shows the number of issuers which reported the average gross amount of fixed and variable remuneration paid to supervisory board members of corporate bond issuers, the average amount of other benefits paid to supervisory board members, as well as the respective amounts in 2016, 2015 and 2014.

Table 2.3 Amount of remuneration of supervisory board members of corporate bond issuers in 2016, 2015 and 2014

		Average gross amount of remuneration paid to supervisory board members during the year		Average amount of other benefits paid to supervisory board members
		Fixed remuneration	Variable remuneration	
2016	Number of issuers	9	1	1
	Amount	423,449	21,760	9,910
2015	Number of issuers	9	1	1
	Amount	505,085	25,680	6,897
2014	Number of issuers	9	0	1
	Amount	493,758	0	126,951

Source: Questionnaire

- Only one issuer (three in 2015) reported having submitted the annual remuneration statement relating to supervisory board members to the general assembly in 2016.

2.3.3 Related party transactions

- Five issuers (the same as in 2015) reported having an internal regulation in place for cases of related party transactions in 2016.

Table 2.4 sets out the value of reported transactions during 2014, 2015 and 2016 concluded by the corporate bond issuer with the following stakeholder groups: shareholders with more than 5% of the initial capital of the issuer, management and supervisory board members of the issuer, senior management of the issuer and within the group the issuer belongs to or is its parent.

Table 2.4 Average value of reported related party transactions in 2014, 2015 and 2016

		Gross value of related party transactions concluded by the issuer			
		with shareholders owning more than 5% of the initial capital of the issuer	with management and supervisory board members of the issuer	with senior management of the issuer	within the group the issuer belongs to or is its parent
2016	Number of issuers having reported the transaction	2	2	1	4
	Average transaction value (in HRK)	3,780,588,017	9,111,820	29,761,977	361,361,308
2015	Number of issuers having reported the transaction	2	1	1	4
	Average transaction value (in HRK)	2,740,055,064	13,065,650	34,542,009	284,748,431
2014	Number of issuers having reported the transaction	3	2	1	2
	Average transaction value (in HRK)	3,100,146,394	39,994,278	65,746,601	867,586,358

Source: Questionnaire

- As in the previous years, during the year 2016, the highest transaction value by far was related to transactions concluded by issuers with shareholders owning more than 5% of the initial capital of the issuer.

2.3.4 Conflicts of interest

- In 2016, five issuers reported having an internal regulation in place to identify, prevent and report conflicts of interest (two fewer than in 2015). The internal regulations contained the following basic provisions relating to conflicts of interest: legality of work and operations, professionalism, expertise, integrity, objectivity, independence, principle of non-discrimination and fight against corruption.
- In 2016, no cases of conflicts of interest were reported in relation to any of the issuers.

2.4 Audit and control

2.4.1 Internal audit and control

- In 2016, nine issuers reported having an internal control system in place (the same as in 2015).
- Eight issuers reported having an internal audit system in place (the same as in 2015).

2.4.2 Managing company risks

- In 2016, five issuers (one fewer than in 2015) reported having an internal regulation in place for the identification, management and prevention of risks.
- Seven issuers (eight issuers in 2015) reported having appointed persons in charge for risk management. These persons performed the function of CFO, management board member, internal auditor and security and environmental protection officer.
- According to corporate bond issuers, the most frequent risk was operational risk. Other risks were liquidity risk, interest rate risk, credit risk, political risk and macroeconomic environment risk.
- Three issuers (four in 2015) reported some of the following risks having materialised in 2016: macroeconomic risk, credit risk and counterparty risk. According to the issuers, the reasons for the risks having materialised were overall economic situation and poor financial situation of customers.
- All issuers that reported some of the risks having materialised were able to control and manage those risks.

2.4.3 External audit

- In 2016, a total of 12 corporate bond issuers used services of eight different external auditors. Eight issuers used services of the largest audit firms (the Big Four).
- The largest number of issuers using services of the same audit firm was five.
- Three out of four corporate bond issuers which are at the same time share issuers used services of the same audit firm, from the group of largest audit firms.
- At the end of 2016, the average length of the time period during which issuers used services of the same external audit firm was 3.67 years (3.92 years in 2015 and 5.08 years in 2014).
- At the end of 2016, the average length of the time period during which issuers used services of the same external audit firm was 2.5 years (2.42 years in 2015 and 3.82 years in 2014).
- Twelve issuers reported the gross amount paid to the external audit firm for other services provided in 2016, and the amount ranged from HRK 68.5 thousand to HRK 912.5 thousand. External auditors were paid on average HRK 412.1 thousand (HRK 350.3 thousand in 2015) for auditing services provided in 2016.

- Two issuers reported the gross amount paid to the external audit firm for other services provided in 2016, and the average amount was HRK 174.4 thousand. Professional training and tax advice were services other than auditing services provided by external audit firms in 2016.
- None of the corporate bond issuers reported relations between the external audit firm and auditor and the issuer, i.e. management and supervisory board members and senior management of the issuer.



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