

## DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

Work Step		Performed	Alternative Procedures/Notes
3	<p>Review sundry other liabilities listings including provisions and accruals. For all selected items agree to appropriate documentation to assess accuracy of amounts.</p> <p>In particular, consider appropriateness of allocation to Telecom Serbia.</p>	<p>✓</p> <p>✓</p>	<p>Other liabilities comprise:</p> <ul style="list-style-type: none"> <li>- deferred revenue (see results of work performed on Receivables)</li> <li>- accrued interest (see results of work performed on Long term borrowings)</li> <li>- turnover tax</li> </ul>
4	<p>Obtain a listing of all purchase invoices received and cash payments made, since the opening balance sheet date, in excess of 500,000 Dinars:</p> <ul style="list-style-type: none"> <li>- Perform limited procedures work to assess completeness of the purchase invoice and cash payments listings;</li> <li>- Determine if a liability should have been recognized at 30 June 1997 balance sheet date, by considering the period in which the good or service was delivered (i.e.: pre or post the opening balance sheet date).</li> </ul> <p>If a liability should have been recognized, check whether it has been recognized by Telecom Serbia at 30 June 1997.</p>	<p>✓</p> <p>✓</p>	<p>No verification was performed as of 30 June 1997.</p> <p>Audit was carried out in respect of trade payables as of 30 December 1997 and rolled back to 1 June 1997 as an alternative procedure.</p> <p>Liabilities were also determined by verification with suppliers' statements under Work step 2.</p>
5	<p>Discuss with management whether there are any outstanding legal matters that would require a material provision.</p> <p>Organize and obtain legal confirmation letters from Telecom Serbia's lawyers.</p> <p>Discuss with management the key procedures and controls in identifying and addressing legal matters.</p>	<p>✓</p> <p>✓</p>	<p>No discussion was organized with Head of legal department. Only written statements from various departments at Telekom were obtained.</p>

177

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

Work Step		Performed	Alternative Procedures
6	Enquire of management and review documentation provided of following matters: <ul style="list-style-type: none"> <li>- Contingent liabilities</li> <li>- Customers disputes</li> <li>- Guarantees</li> <li>- Commitments</li> <li>- Provision</li> </ul>	 ✓ ✓ ✓ N/A	No written management representation letter regarding contingencies obtained from PTT. Representations were obtained from the heads of Telekom relevant departments.

### 3. Work Performed

Our report is structured to present the work performed relating to main categories of liabilities to be transferred to Telekom Srbija.

Work step 1 relates to all liabilities and is performed as follows:

We were provided by Accounting department of PTT with:

- /i/ a listing of liabilities to suppliers and creditors amounted to 119.075 thousand Dinars as of 1 June 1997, which, at the same time, represents the opening balance sheet liabilities, and
- /ii/ the Report on mutual receivables and liabilities on 6 October 1997 (Report of 6/10/97) between PTT and Telekom Srbija totaling 467.133 thousand Dinars.

Footing was done for those listings.

The amount of opening balance sheet liabilities at Telekom Srbija is produced only on the basis of the listing under a/i/. This amount is subsequently adjusted by the amount of liabilities presented in the Report of 6/10/97, as a result of applied audit procedures and work steps concerning the confirmation of the balances by independent circularization and by other corrections made either by Telekom Srbija, auditors or ourselves.

Due to the reasons stated above, the post-separation listings for different liability captions were not produced as of 1 June 1997. Postings relating to opening balance sheet were made throughout the year by Telekom Srbija.

Breakdowns of the following balance sheet items were produced separately for reporting purposes by ourselves and auditors:

- short term borrowings from domestic banks;
- long term borrowings from foreign creditors; and
- accounts payable and accrued expense.

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

### 3.1. Short term borrowings

Short term borrowings as of 1 June 1997 comprise the loans granted by domestic banks for telecommunications business, with repayment periods from 30 to 60 days and various interest rates. These conditions were confirmed by the agreements signed between relevant banks and PTT.

All balances with domestic banks were circularized and banks' confirmations were obtained. The following balances were fully confirmed:

Bank	In thousand of Dinars
Asi banka A.D., Beograd	3.000
Delta banka A.D., Beograd	56.000
Komercijalna banka A.D., Beograd	10.000
Continental banka A.D., Novi Sad	8.000
Postanska Stedionica, Beograd	42.300
Total:	119.300

Source: Accounting department of PTT and banks' statements

We confirmed that these balances were included in the Report of 6/10/97, as a part of total liabilities to PTT, and should be represented as an opening balance sheet item.

We are informed that all outstanding debts, including interest were repaid up to 31 December 1997.

Detailed analysis of short term borrowings by credit party is provided in Appendix II.1.

### 3.2. Long term borrowings

Long term borrowings comprise the loans granted by foreign banks and major foreign suppliers to PTT to finance purchases of plant and equipment and, in most cases, costs of training, installation and putting the plant and equipment into operation.

In the statutory balance sheet as of 1 June 1997, only borrowings from foreign banks (LHB, Frankfurt and Beogradska banka, Cyprus) were transferred, as a part of opening liabilities to PTT.

#### Work Performed

- (a) Circularization of long term borrowings was done in order to confirm the outstanding balances of principals, interest due and conditions and terms of contracts signed between PTT and foreign creditors.

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

15

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

The following balances were confirmed either by the banks' confirmations or suppliers' statements, as of 1 June 1997:

	Supplier/Bank	In thousand of Dinars
1.	Siemens - Switzerland from 1996	18.546
2.	Siemens - Switzerland from 1996 Amendment II	7.358
3.	Alcatel CIT - France from 1996	62.839
4.	Siemens - Munich from 1996	70.459
	Total international suppliers:	<u>159.202</u>
1.	LHB, Frankfurt	1.437
2.	Beogradska banka, Cyprus	51.603
	Total banks:	<u>53.040</u>
	TOTAL:	<u>212.242</u>

Source: PTT and Telekom Accounting departments and Telekom Foreign currency operation department and original creditors' statements

As a result of the confirmation procedure and reconciliation of recorded balances, few adjustments were made:

- accrued interest was added to relevant principals;
- interest in the amount of 1.644 thousand Dinars was accrued and recorded as accrued expenses (item identified under Work step 3);
- liability toward LHB, Frankfurt was reduced by 1.294 thousand Dinars according to the bank's confirmation. This difference arose from the repayment made by the National bank of Yugoslavia. The ultimate resolution whether this amount represent Telekom Srbija liability is uncertain and might present the potential contingent liability.

(b) We confirmed that long term borrowings were recorded by PTT as of 1 June 1997 except Siemens Switzerland, but were not transferred to Telekom Srbija. We also established that, up to 31 December 1997, most of long term borrowings were recorded in PTT books (as their liabilities towards foreign creditors and receivables from Telekom Srbija) but minor amount at Telekom Srbija. Adjustments for reporting purposes were made in order to obtain total amount of long term borrowings.

(c) We were supplied by and reviewed the contracts signed between PTT and foreign suppliers up to 1 June 1997. Work performed was as follows:

/1/ for those contracts where plant and equipment were delivered (two contracts with Siemens, Switzerland for switches installed in Obrenovac, Sabac and Krusevac; one with Alcatel CIT for switching system Center Belgrade and with Siemens, Germany for 17 switches) we confirmed the amounts of initial loans granted, outstanding amount as of 1 June 1997, maturity date and interest rates agreed. We have summarized a current portion, to be paid within next year, of long term borrowings.

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

Detailed analysis of long term borrowings based on the above work performed is provided in Appendix II.2.

/ii/ We have selected following samples from the contracts with:

- Siemens - switches at Sremska Mitrovica; and
- Alcatel CIT - switches at Novi Sad and three tandem switches in Belgrade, as a part of our review regarding fulfillment of contracts (that work or delivery is consistent with investments) and that technical specification agrees with actual purchases or installations made.

Switches at Sremska Mitrovica and Novi Sad were physically verified by SIN/OTB engineers, while tandem switches at Belgrade center, Novi Beograd and Konjarnik were verified together with work done relating to Paying subscriber lines. Special engineers reports are prepared to describe its work.

/iii/ We have also reviewed five contracts signed up to 1 June 1997 between PTT and Siemens, Germany, for various types of plant and equipment, and Alcatel CIT, France, for 300.000 equivalent lines, for which, as we were told, the plant and equipment had not been delivered up to 1 June 1997. For some of these contracts advances were paid and verification work was performed under Section 3 - Payments in advance.

Transfer of long term borrowings from foreign banks and suppliers from PTT to Telekom Srbija is, at present, in course. Approvals for official transfer of liabilities were obtained from creditors and procedure to obtain approval from the Yugoslav banks, guarantors for these liabilities, is in progress.

### 3.3. Trade payable and other liabilities

#### *Scope limitations*

The major scope limitations concerning the opening balance of trade payables may be summarized as follows:

- listing of opening liabilities in the amount of 119,075 thousand Dinars was not properly documented and does not represent all current liabilities at the date of separation;
- Report on mutual receivables and liabilities between PTT and Telekom Srbija dated 6 October 1997 (Report of 6/10/97) comprises payments made by PTT in the period subsequent to the date of separation and outstanding liabilities recorded with significant delays, so uncertainty as to the completeness of this Report exists. Furthermore, these liabilities were not transferred to Telekom Srbija as of 1 June 1997;
- no proper reconciliation of intercompany balances was made between PTT and Telekom Srbija at the latter date and, as a consequence, there is a risk that all liabilities have not been transferred to Telekom Srbija;
- the balances with major suppliers were independently confirmed by suppliers' statements as of 31 December 1997 and adjustments were made in Telekom Srbija accounts.



## DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

We would like to point out that majority of these limitations were mitigated by the suppliers' confirmations with major suppliers and satisfactory results of other tests performed.

Therefore, those limitations should not have a significant, final effect on the opening balances.

*Work Performed**Work Step 2*

- (a) We were provided by supplier's statements obtained by Price Waterhouse in order to confirm outstanding balances of the ten largest suppliers (Jugotrade, Telefonkabl, Alcatel Zemun, DKTS, Elektromontaza, Salus International, VF TEL, IBIS Instruments, Savezna uprava carina and Beogradelektro), nine of which are suppliers for plant and equipment. The balances were confirmed as of 31 December 1997 and rolled back to 31 May 1997 to get the opening liabilities. This sample covers 83% of the liabilities presented in the Report of 6/10/97. Further verification of non-reconciled balances in respect of Jugotrade, Telefonkabl, Alcatel Zemun, DKTS and VF TEL was performed.

As a result of these procedures Price Waterhouse increased the amount of Trade payables by 62.737 thousand Dinars. These adjustments were recorded in Telekom Srbija books in 1998.

- (b) We have reviewed the contracts signed by domestic suppliers which are mainly sub-contractors or importers of plant and equipment contracted with the main foreign suppliers. We have selected 5 to 6 contracts of the following suppliers: VF TEL, Alcatel CIT Yugoslavia, Beogradelektro, Telefonkabl and DKTS, vouched relevant invoices and supporting documentation. In order to verify that purchased plant and equipment were recorded in PTT books as fixed assets or capital WIP and subsequently transferred to Telekom Srbija we traced all selected invoices to PTT records of WIP, but, out of 26 items only five were directly traced to the post-separation listing of WIP, due to different method of recording of fixed assets valuation as the opening balance at Telekom Srbija, as of 1 June 1997.

The same sample was used for Work step 4, relating to the completeness of purchase invoices.

*Work Step 4*

- (a) In order to assess the completeness of the purchase invoices and cash payments we performed the following steps:

*/i/ sample selection:*

- listings from all Working units were obtained for purchase invoices received and cash payments made in excess of 500 thousand Dinars;
- extended by 26 purchase invoices selected for Work step 2/iii/;
- additional tests for purchase invoices selected on a random basis from the Report of 6/10/97;

*/ii/ verification of invoices to contracts signed, technical specifications attached to, and interim calculation for completed construction made by contractor and internally signed calculations by PTT personnel;**/iii/ verification of payments made by giro payments order, by compensation or cession.*

## DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

Generally, the results of the above steps were satisfactory with minor discrepancies from technical specifications and in some instances significant difference in price.

- (b) Most of the above work steps performed in respect of liabilities were directed to determine the outstanding liabilities as of 1 June 1997 which should be transferred from PTT to Telekom Srbija. In addition, we scrutinize the list of opening liabilities (119,075 thousand Dinars) at various dates and find out that, apart from the amount relating to long term borrowings of 45,708 thousand Dinars, outstanding liabilities at 31 May 1998 amounted to 6,672 thousand Dinars at PTT records. However, the reconciliation of the opening balance in the amount of 73,367 thousand Dinars has not been made between PTT and Telekom Srbija. Accordingly, the adjustments have been booked.

We have also reviewed the Report of 6/10/97 and summarized the liabilities relating to telecommunication business which should be transferred to Telekom Srbija as of 1 June 1997:

	In thousand of Dinars
Liabilities for material	45.138
Liabilities for capital WIP	205.884
Liabilities for capital expenditure	29.987
Liabilities of Working units	35.923
Liabilities to suppliers in foreign currencies	21.246
	<u>338.176</u>

The structure of these liabilities is as follows:

	In thousand of Dinars
Liabilities paid by PTT for telecommunications	236.977
Outstanding liabilities (unpaid liabilities)	<u>101.201</u>
	<u>338.176</u>

We confirmed that out of 101.201 thousand Dinars, liabilities in the amount of 53.080 thousand Dinars were properly transferred, with suppliers' approval, to Telekom Srbija by the end of 1997.

- (c) We have reviewed the reconciliation of receivables and liabilities carried out at 31 December 1997 between PTT and Telekom Srbija books. However, the reconciliation includes the balances recorded at Report of 6/10/97, with cumulative balances stated in the request sent for confirmation and opening balances, which were already identified as incorrect and adjusted, accordingly. Complete reconciliation of all receivables and payables should be made in form of Minutes as of 1 June 1997, taking into account numerous adjustments made, different way of posting in both accounting, partially transferred liabilities and other matters which effect total liabilities to be transferred to Telekom Srbija.

DRAFT - PRELIMINARY AND TENTATIVE, FOR DISCUSSION PURPOSES ONLY

### 3.4. Legal matters, commitments and contingencies

#### Work steps 5 & 6

##### 1. Legal matters and contingencies

We requested written statements from PTT and Telekom Srbija management as to the:

- (a) legal matters with material effects concerning customers claims, creditors compliance, employees requests or any other significant matters; and
- (b) contingent liabilities with respect to:
  - /i/ damages of existing fixed assets;
  - /ii/ insurance premiums claims;
  - /iii/ unfulfilled commitments taken over for telecommunication business (in dispute or on court);
  - /iv/ year 2000 issue concerning computer software upgrading;
  - /v/ retirement redundancy payments;
  - /vi/ visible regulatory and legislation policy which could cause contingencies;
  - /vii/ disputes with Mobtel, JUPAK or other specialized institutions or regulatory agencies.

We were provided by Telekom Srbija management representation (by Director of Secretariat for legal and general affairs and Director of Division for personnel and organization) as to the legal matters referred under (a) and the contingent liabilities stated above, except under /iv/ and /vii/. Based on the statement provided, except for the following matters, there is no significant legal disputes or contingent liabilities up to 31 December 1997, which require provision to be set up:

- customers claims in the amount of 4.387 thousand Dinars; and
- court claims from Radio Televizija Srbije against Telekom Srbija, opened at the end of 1997 and continued in 1998, with disputed amount of 4.971 thousand Dinars.

Provision has been assessed as necessary for customers claims to be included in the opening balance sheet as of 1 June 1997 in the amount of 2.000 thousand Dinars (rounded).

No representation from PTT management as to contingencies existing as of 1 June 1997, has been provided.

We were provided by PTT with the list of guarantees issued by Beobanka A.D., Beograd and Beogradska udružena banka, Beograd to foreign creditors for all outstanding long term borrowings. Guarantees were issued on the name of PTT for telecommunication business and at present amendments were submitted to those banks in order to obtain approval for its cession from PTT to Telekom Srbija.

We were told by Telekom Srbija responsible officer from Accounting Department in addition to the written statement issued by PTT for Due Diligence Segment Report, that there is no pledges, mortgages or other form of security on or applied to tangible and intangible assets for telecommunication business.