Georgian State Electrosystem JSC

Consolidated Financial Statements for 2013

Contents

KPMG

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Independent Auditors' Report

To the Management Board of
Georgian State Electrosystem JSC

We have audited the accompanying consolidated financial statements of JSC Georgian State Electrosystem (the Company) and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2013, and the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Georgia LLC

KPMG Georgia LLC
17 June 2014

'000 GEL	Note	2013	2012
ASSETS			
Non-current assets			
Property and equipment	8	908,997	876,614
Intangible assets		1,755	2,577
Prepayments for non-current assets		1,246	32,016
Deferred tax assets	9	6,869	11,558
Trade and other receivables	10	38,671	55,217
Total non-current assets		**957,538**	**977,982**
Current assets			
Inventories		7,974	6,262
Trade and other receivables	10	21,572	13,202
Prepayments to suppliers		767	1,570
Cash and cash equivalents	11	35,419	25,343
Total current assets		**65,732**	**46,377**
Total assets		**1,023,270**	**1,024,359**
EQUITY AND LIABILITIES			
Equity	12		
Share capital		510,249	510,108
Unregistered capital		27,457	27,194
Foreign currency translation reserve		(104)	(247)
Retained earnings		(317,796)	(254,618)
Total equity		**219,806**	**282,437**
Non-current liabilities			
Loans and borrowings	14	580,815	487,337
Restructured liabilities	15	59,167	58,370
Grants related to assets	16	71,060	72,183
Other tax liabilities		1,793	2,297
Total non-current liabilities		**712,835**	**620,187**
Current liabilities			
Loans and borrowings	14	47,444	9,402
Trade and other payables	17	35,757	109,447
Current tax liabilities		-	429
Restructured liabilities	15	4,599	2,457
Grants related to assets	16	2,829	-
Total current liabilities		**90,629**	**121,735**
Total liabilities		**803,464**	**741,922**
Total equity and liabilities		**1,023,270**	**1,024,359**

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 36.

'000 GEL	Note	2013	2012
Revenue	5	61,337	54,154
Other income		14,076	6,017
Wages and salaries		(18,810)	(16,542)
Depreciation and amortization		(33,096)	(32,409)
Other operating expenses		(19,577)	(14,139)
Results from operating activities		**3,930**	**(2,919)**
Finance income	6	3,302	7,232
Finance costs	6	(64,757)	(18,866)
Net finance costs		**(61,455)**	**(11,634)**
Loss before income tax		**(57,525)**	**(14,553)**
Income tax (expense)/benefit	7	(5,653)	3,812
Loss for the year		**(63,178)**	**(10,741)**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Foreign currency translation differences for foreign operations		143	(121)
Total comprehensive loss for the year		**(63,035)**	**(10,862)**

These consolidated financial statements were approved by management on 17 June 2014 and were signed on its behalf by:

Sulkhan Zumburidze
Rehabilitation Manager

Nino Maisuradze
Chief Accountant

The consolidated statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 36.

'000 GEL	Share capital	Unregistered capital	Translation reserve	Retained earnings	Total
Balance at 1 January 2012	509,772	27,311	(126)	(243,877)	293,080
Total comprehensive loss for the year					
Loss for the year	-	-	-	(10,741)	(10,741)
Other comprehensive income					
Foreign currency translation differences	-	-	(121)	-	(121)
Total other comprehensive income for the year	**-**	**-**	**(121)**	**-**	**(121)**
Total comprehensive loss for the year	**-**	**-**	**(121)**	**(10,741)**	**(10,862)**
Contributions by and distributions to owners					
Issue of share capital	336	(117)	-	-	219
Total contributions by and distributions to owners	**336**	**(117)**	**-**	**-**	**219**
Balance at 31 December 2012	**510,108**	**27,194**	**(247)**	**(254,618)**	**282,437**
Balance at 1 January 2013	510,108	27,194	(247)	(254,618)	282,437
Total comprehensive loss for the year					
Loss for the year	-	-	-	(63,178)	(63,178)
Other comprehensive income					
Foreign currency translation differences	-	-	143	-	143
Total other comprehensive income for the year	**-**	**-**	**143**	**-**	**143**
Total comprehensive loss for the year	**-**	**-**	**143**	**(63,178)**	**(63,035)**
Contributions by and distributions to owners					
Issue of Share Capital	141	263	-	-	404
Total contributions by and distributions to owners	**141**	**263**	**-**	**-**	**404**
Balance at 31 December 2013	**510,249**	**27,457**	**(104)**	**(317,796)**	**219,806**

The consolidated statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 36.

'000 GEL	Note	2013	2012
Cash flows from operating activities			
Loss for the year		(63,178)	(10,741)
Adjustments for:			
Depreciation and amortization		33,096	32,409
Loss on disposal of property and equipment, net		1,827	1,918
Net finance costs		61,455	11,634
Income from amortization of grants		(528)	(528)
Income tax expense/(benefit)		5,653	(3,812)
		38,325	**30,880**
Changes in:			
Inventories		(3,320)	1,591
Trade and other receivables		7,059	(25,842)
Trade and other payables		(624)	(3,024)
Restricted cash		960	(3,465)
Grants		2,235	43,924
Prepayments		803	-
Other tax liabilities		(504)	-
Cash flows from operations before interest paid		**44,934**	**44,064**
Interest paid		(4,182)	(4,694)
Net cash from operating activities		**40,752**	**39,370**
Cash flows from investing activities			
Interest received		3,302	7,232
Acquisition of property and equipment and intangible assets		(90,434)	(258,902)
Net cash used in investing activities		**(87,132)**	**(251,670)**
Cash flows from financing activities			
Proceeds from borrowings		67,301	156,840
Repayment of restructured liabilities		(2,922)	(3,232)
Repayment of borrowings		(8,582)	(8,298)
Net cash from financing activities		**55,797**	**145,310**
Net increase/(decrease) in cash and cash equivalents		**9,417**	**(66,990)**
Cash and cash equivalents at 1 January		21,878	89,764
Effect of exchange rate fluctuations on cash and cash equivalents		1,619	(896)
Cash and cash equivalents at 31 December	11	**32,914**	**21,878**

The consolidated statement of cash flows is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 36.

1. Reporting entity

(a) Organisation and operations

Georgian State Electrosystem JSC (the Company) is a joint stock company established under the laws of Georgia on 12 November 2002 by the means of the merger of Electrogadatsema JSC and Electrodispetcherizatsia-2000 LLC and is their legal successor in title. The consolidated financial statements include financial statements of the Company and its subsidiaries (together referred to as the Group and individually as Group entities). The Group entities are joint stock and limited liability companies as defined in the Civil Codes of Georgia and the Republic of Turkey and are disclosed in note 22.

The Company's registered office is 2 Baratashvili Street, Tbilisi 0105, Georgia.

The principle activities of the Company are electricity transmission and dispatching over the entire territory of Georgia that are regulated by the law on Electricity and Natural Gas. EnergoTrans LLC, the major subsidiary of the Company, was established as a state-owned enterprise in 2002. The principal activity of EnergoTrans LLC is electricity transmission, including export and transit of electricity, via the 500kV Vardzia and Zekari energy transmission lines and the 400kV Meskheti interconnection line with Turkey constructed as part of the 'Black Sea Transmission Network Project' (BSTN). The new lines provide additional security to Georgia's transmission network by adding a second west-east 500kV link and create energy export capacity to Turkey. The BSTN project was completed by the end of 2013, with the primary objective of EnergoTrans LLC to serve the BSTN project as an executing agency, carrying out overall control, supervision and monitoring over the performance by the contractors of all project-related construction works and activities. The Group operates under the licenses obtained from the Georgian National Energy and Water Supply Regulatory Commission.

The Company was wholly owned by the Government of Georgia represented by the Ministry of Economic Development of Georgia and Ministry of Energy and Natural Resources of Georgia as at 30 July 2012. From that date the ownership of the Company was transferred to the Partnership Fund JSC, a wholly state-owned entity. At 31 December 2013 and 2012 the parent and ultimate parent of the Group is Partnership Fund JSC. The ultimate controlling party of the Group is the Government of Georgia. Related party transactions are disclosed in note 21.

(b) Georgian business environment

The Group's operations are primarily located in Georgia. Consequently, the Group is exposed to the economic and financial markets of Georgia which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The consolidated financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

2. Basis of preparation

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs").

3. Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL"), which is the Company's functional currency and the currency in which these consolidated financial statements are presented. The functional currency of each of the Group entities is the currency of the primary economic environment in which the entity operates.

All financial information presented in GEL has been rounded to the nearest thousand, except when otherwise indicated.

4. Use of estimates and judgments

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the note 14 - fair value of loans and borrowings at initial recognition.

Management has not identified any assumptions or estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year.

Measurement of fair values

A number of the Group's accounting policies and disclosures require the determination of fair values for financial assets and liabilities. Fair values have been determined for measurement and for disclosure purposes. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

- *Level 1*: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- *Level 2*: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- *Level 3*: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

Further information about the assumptions made in measuring fair values is included in the note 18 (a) - fair values of financial assets and liabilities.

5. Revenue

'000 GEL	2013	2012
Revenue from transmission of electricity	46,282	38,867
Revenue from dispatching of electricity	12,127	11,769
Revenue from exporting electricity	2,928	3,433
Other revenue	-	85
Total revenues	**61,337**	**54,154**

Revenue from export includes both revenue from transmission and dispatching of electricity.

The revenue is calculated based on the transmission and dispatch tariffs established by the Georgian National Energy and Water Supply Regulatory Commission (GNEWRC).

6. Finance income and finance costs

'000 GEL	2013	2012
Recognised in profit or loss		
Interest income on bank balances	3,302	7,232
Finance income	**3,302**	**7,232**
Interest expense on loans and borrowings	(4,927)	(4,581)
Unwinding of discount on restructured liabilities	(5,912)	(6,142)
Net foreign exchange loss	(53,918)	(8,143)
Finance costs	**(64,757)**	**(18,866)**
Net finance costs recognised in profit or loss	**(61,455)**	**(11,634)**

7. Income tax expense

The Group's applicable tax rate is the income tax rate of 15% for Georgian companies.

'000 GEL	**2013**	**2012**
Current tax expense		
Current year	-	4,911
Adjustment for prior years	964	-
	964	**4,911**
Deferred tax expense/(benefit)		
Origination and reversal of temporary differences	4,689	(8,723)
	4,689	**(8,723)**
Total income tax expense/(benefit)	**5,653**	**(3,812)**

Reconciliation of effective tax rate:

	2013		**2012**	
	'000 GEL	**%**	**'000 GEL**	**%**
Loss before income tax	(57,525)	100	(14,553)	100
Income tax benefit at applicable tax rate	(8,629)	15	(2,183)	15
Current-year losses for which no deferred tax asset is recognized	12,967	(23)	(1,807)	12
Previously recognized deferred tax assets derecognized	-	-	338	(2)
Under-provided in prior years	964	(2)	-	-
Non-deductable expenses/ (tax exempt income)	351	(1)	(160)	1
Income tax expense/(benefit)	**5,653**	**(10)**	**(3,812)**	**26**

8. Property and equipment

'000 GEL	Land, buildings and constructions	Power transmission lines	Equipment, vehicles and other	Under construction	Total
Cost or deemed cost					
Balance at 1 January 2012	62,956	144,148	204,581	281,750	693,435
Additions	299	-	592	324,171	325,062
Disposals	-	-	(1,207)	(1,052)	(2,259)
Transfers	1,847	10,345	13,174	(25,366)	-
Balance at 31 December 2012	**65,102**	**154,493**	**217,140**	**579,503**	**1,016,238**
Balance at 1 January 2013	65,102	154,493	217,140	579,503	1,016,238
Additions	151	-	195	66,032	66,378
Disposals	(198)	-	(900)	(1,518)	(2,616)
Transfers	36,224	181,887	390,235	(608,346)	-
Balance at 31 December 2013	**101,279**	**336,380**	**606,670**	**35,671**	**1,080,000**
Depreciation					
Balance at 1 January 2012	(15,577)	(40,805)	(52,890)	-	(109,272)
Depreciation for the year	(2,663)	(13,391)	(14,639)	-	(30,693)
Disposals	-	-	341	-	341
Transfers	98	8	(106)	-	-
Balance at 31 December 2012	**(18,142)**	**(54,188)**	**(67,294)**	-	**(139,624)**
Balance at 1 January 2013	(18,142)	(54,188)	(67,294)	-	(139,624)
Depreciation for the year	(2,780)	(15,244)	(14,144)	-	(32,168)
Disposals	25	-	764	-	789
Transfers	(5)	-	5	-	-
Balance at 31 December 2013	**(20,902)**	**(69,432)**	**(80,669)**	-	**(171,003)**
Carrying amounts					
At 1 January 2012	47,379	103,343	151,691	281,750	584,163
At 31 December 2012	**46,960**	**100,305**	**149,846**	**579,503**	**876,614**
At 31 December 2013	**80,377**	**266,948**	**526,001**	**35,671**	**908,997**

(a) Security

At 31 December 2013 properties (land plots with power-transmission lines and related technical equipment) with a carrying amount of GEL 109,001 thousand (2012: GEL 83,192 thousand) are pledged as a security for loans and borrowings and restructured liabilities to the Ministry of Finance of Georgia (see notes 14 and 15).

(b) Construction in progress

In 2013 the construction of new energy transmission lines within the framework of the 'Black Sea Transmission Network' project was completed. The project was financed by credit facilities and grants provided by the European Bank for Reconstruction and Development, the European Investment Bank and Kreditanstalt für Wiederaufbau (KfW) (see notes 14 and 16).

All the borrowing costs from the credit facilities above were capitalised from the date when expenditures for the project were incurred until the BSTN project was substantially completed and ready for use. Capitalised borrowing costs related to the construction of the new energy transmission lines amounted to GEL 18,996 thousand (2012: GEL 9,516 thousand).

9. Deferred tax assets and liabilities

(a) Unrecognised deferred tax assets

Deferred tax assets of GEL 47,401 thousand (2012: GEL 34,434 thousand) have not been recognised in respect of tax losses carried forward because it is not probable that future taxable profit will be available against which the Group can utilise the benefits there from.

The Group's tax loss carry-forwards by expiration date comprise:

'000 GEL	**31 December 2013**	**31 December 2012**
2015	34,434	34,434
2018	12,967	-
	47,401	**34,434**

(b) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
'000 GEL	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**
Property and equipment and intangible assets	-	-	(15,398)	(10,556)	(15,398)	(10,556)
Trade and other receivables	10,902	11,603	-	-	10,902	11,603
Grants related to assets	10,968	10,485	-	-	10,968	10,485
Inventories	397	-	-	-	397	-
Trade and other payables	-	26	-	-	-	26
Net tax assets/ (liabilities)	**22,267**	**22,114**	**(15,398)**	**(10,556)**	**6,869**	**11,558**

(c) Movement in deferred tax balances

'000 GEL	**1 January 2013**	**Recognised in profit or loss**	**31 December 2013**
Property and equipment and intangible assets	(10,556)	(4,842)	(15,398)
Trade and other receivables	11,603	(701)	10,902
Grants related to assets	10,485	483	10,968
Inventories	-	397	397
Trade and other payables	26	(26)	-
	11,558	**(4,689)**	**6,869**

'000 GEL	**1 January 2012**	**Recognised in profit or loss**	**31 December 2012**
Property and equipment and intangible assets	(12,446)	1,890	(10,556)
Trade and other receivables	10,748	855	11,603
Grants related to assets	3,976	6,509	10,485
Trade and other payables	219	(193)	26
Tax loss carry-forwards	338	(338)	-
	2,835	**8,723**	**11,558**

10. Trade and other receivables

'000 GEL	2013	2012
Non-current receivables		
VAT receivable	**38,671**	**55,217**
Current receivables		
Trade receivables	81,936	79,108
Impairment allowance on trade receivables	(73,800)	(73,370)
	8,136	5,738
VAT receivable	12,694	6,534
Other receivables	3,190	2,875
Impairment allowance on other receivables	(2,448)	(1,945)
	21,572	**13,202**

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 18.

11. Cash and cash equivalents

'000 GEL	2013	2012
Petty cash	9	28
Bank balances	35,410	25,315
Cash and cash equivalents in the consolidated statement of financial position	**35,419**	**25,343**
Restricted cash	(2,505)	(3,465)
Cash and cash equivalents in the consolidated statement of cash flows	**32,914**	**21,878**

As at 31 December 2013 the bank balances with a carrying amount of GEL 2,505 thousand (2012: GEL 3,465 thousand) were pledged as security for trade and other payables.

No cash and cash equivalents are impaired or past due.

The Group's bank balances are held in one of the top 5 Georgian banks (rated B by Fitch rating agency).

The Group's exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities are disclosed in note 18.

12. Equity

(a) Share capital

Number of shares unless otherwise stated	Ordinary shares 2013	Ordinary shares 2012
Par value	GEL 1	GEL 1
On issue at 31 December, fully paid	**510,248,607**	**510,107,699**

(b) Unregistered capital

The unregistered capital comprises contributions of assets made by shareholders which are in the ownership of the Company but have not been registered in the Company's charter.

(c) Dividends

In accordance with Georgian legislation the Company's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with International Financial Reporting Standards.

(d) Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations.

13. Capital management

The Group has no formal policy for capital management but management seeks to maintain a sufficient capital base for meeting the Group's operational and strategic needs as well as the main objectives of the Rehabilitation Plan. This is achieved with efficient cash management, constant monitoring of Group's revenues and profit, and long-term investment plans mainly financed by the Group's operating cash flows as well as loans and borrowings.

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

14. Loans and borrowings

This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group's exposure to interest rate, foreign currency and liquidity risk, see note 18.

'000 GEL	2013	2012
Non-current liabilities		
Unsecured loans from financial institutions	505,557	421,205
Secured loans from financial institutions	44,716	47,885
Secured loans from related party	30,542	18,247
	580,815	**487,337**
Current liabilities		
Current portion of unsecured loans from financial institutions	32,491	2,709
Current portion of secured loans from financial institutions	7,025	6,693
Current portion of secured loans from related party	7,928	-
	47,444	**9,402**

(a) Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

				31 December 2013		31 December 2012	
'000 GEL	**Currency**	**Nominal interest rate**	**Year of maturity**	**Face value**	**Carrying amount**	**Face value**	**Carrying amount**
Unsecured loans from financial institutions:							
Ministry of Finance of Georgia - KfW	EUR	KfW reference rate +4%	2024	178,173	178,173	162,963	162,963
Ministry of Finance of Georgia - KfW	EUR	1%-1.5%	2025-2037	50,538	50,538	48,879	48,879
Ministry of Finance of Georgia - EIB	EUR	Euribor+0.75%	2033	189,746	189,746	107,164	107,164
Ministry of Finance of Georgia - EBRD	EUR	Euribor+1%	2025	119,591	119,591	104,908	104,908
Secured loans from financial institutions:							
Ministry of Finance of Georgia - KfW	EUR	4%	2021	14,418	14,418	14,818	14,818
Ministry of Finance of Georgia - IDA	USD	World Bank's lending treasury rates	2022	37,323	37,323	39,760	39,760
Secured loan from related party:							
Ministry of Finance of Georgia	EUR	7.50%	2018	38,470	38,470	18,247	18,247
Total interest-bearing liabilities				**628,259**	**628,259**	**496,739**	**496,739**

Loans from EBRD, EIB and KfW were disbursed to the Government of Georgia in relation to the BSTN project for the construction of a new power transmission line.

Loans from IDA and KfW were disbursed to the Government of Georgia for the implementation of the Electricity Market Support Project (the "EMSP"), "Energy IV", "Sector Program Power Supply" and "Regional Power Network Rehabilitation 1" projects.

The Government of Georgia, in its turn, transferred amounts received under the facilities, together with an obligation to repay them, to the Group. The lender has not legally released the Government of Georgia from the primary responsibility for the repayment of the loans, accordingly the Government of Georgia acted as a principal in this transaction and accordingly the loans payable by the Group are towards the Ministry of Finance of Georgia. Secured loan from related party represents interest accrued on part of the unsecured loans from financial institutions and paid by the Government of Georgia on behalf of the Group.

Management estimates that the fair values of loans and borrowings are not different from loaned amounts at initial recognition as these loans are provided in a separate market segment which is different from the commercial lending market.

15. Restructured liabilities

'000 GEL	2013	2012
Payables to the state budget	76,000	78,536
Trade payables	26,281	26,939
Loans and interest accrued	3,929	3,708
	106,210	**109,183**
Amortised cost adjustment	(42,444)	(48,356)
Balance at 31 December	**63,766**	**60,827**
Current	4,599	2,457
Non-current	59,167	58,370
	63,766	**60,827**

Restructured liabilities represent the amounts originated before 2006, the repayments of which have been deferred due to the financial difficulties of the Group. According to the Rehabilitation Plan, drawn-up initially in 2006 through court proceedings and agreed with the majority of creditors, the repayments of these debts have been deferred until 2011, thereafter the amounts will be repaid by instalments until 2023, the end of the rehabilitation period.

The Rehabilitation Plan sets out the strategic targets of the Group for the coming 15 years, as well as defines the main operating and financial objectives of the Group. According to the Rehabilitation Plan, the Rehabilitation Manager has been appointed to undertake the governance of the Group throughout the entire rehabilitation period.

The main creditor of the Group is the Ministry of Finance of Georgia. The amounts payable to the Ministry of Finance of Georgia are taxes and duties, as well as loans and interest accrued.

Restructured liabilities are presented at discounted amounts. Following the approval of the new Rehabilitation Plan in 2008, the Group has estimated the fair value of deferred payables, to effect the amendments in the repayment terms. The fair value of these liabilities on the Rehabilitation Plan approval date has been determined by discounting future cash flows at an average market interest rate of 9.57 %.

16. Grants related to assets

'000 GEL	2013	2012
Balance at 1 January	72,183	28,787
Credited to profit and loss	(528)	(528)
Received during the year	2,234	43,924
Balance at 31 December	**73,889**	**72,183**
Non-current	71,060	72,183
Current	2,829	-
	73,889	**72,183**

Grant related to assets of EUR 25,000 thousand represents financial contribution received from KfW within the framework of the Black Sea Transmission Network project for the construction of new energy transmission lines. The financial contribution is not repayable unless the Group misuses the funds received or seriously jeopardizes the implementation of the project.

17. Trade and other payables

'000 GEL	2013	2012
Payables for construction works under BSTN project	32,686	102,445
Trade payables	1,489	6,207
Other payables	1,582	795
	35,757	**109,447**

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 18.

18. Fair values and risk management

(a) Fair values of financial assets and liabilities

The estimates of fair value are intended to approximate the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realizable in an immediate sale of the assets or transfer of liabilities.

The Group has determined the fair values of financial assets and liabilities using valuation techniques. The objective of the valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date. The valuation technique used is the discounted cash flow model. Fair value of all financial assets and liabilities is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

Management believes that the fair values of the Group's financial assets and liabilities approximate their carrying amounts.

(b) Financial risk management

The Group has exposure to the following risks from its use of financial instruments:

- credit risk – note 18 (b)(ii);
- liquidity risk – note 18 (b)(iii);
- market risk – note 18 (b)(iv).

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

(i) Risk management framework

The Management Board has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Management Board is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Management Board.

(ii) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and bank balances.

The carrying amount of financial assets represents the maximum credit risk exposure.

Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. Geographically, the credit risk is concentrated mainly in Georgia.

Management has established a credit policy under which each new customer is analysed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered. The Group's review includes external ratings, when available, and in some cases bank references. Approximately 40% (2012: 44%) of the Group's revenue is attributable to sales transactions with a single customer.

More than 70% of the Group's customers have been transacting with the Group for over five years, and losses have occurred infrequently during this period. Nearly all of the credit losses have occurred before this period.

No collateral in respect of trade and other receivables is generally required.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The main component of this allowance is a specific loss component that relates to individually significant exposures.

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	Carrying amount	
'000 GEL	**2013**	**2012**
Domestic	**8,136**	**5,738**

Impairment losses

The aging of trade receivables at the reporting date was:

'000 GEL	**Gross 2013**	**Impairment 2013**	**Gross 2012**	**Impairment 2012**
Not past due	7,131	-	5,738	-
Past due 31-120 days	1,005	-	46	46
Past due 121-365 days	-	-	217	217
Past due more than one year	73,800	73,800	73,107	73,107
	81,936	**73,800**	**79,108**	**73,370**

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

'000 GEL	**Individual impairments**	
	2013	**2012**
Balance at beginning of the year	73,370	73,467
Increase during the year	753	53
Decrease due to reversal	(323)	(150)
Balance at end of the year	**73,800**	**73,370**

The allowance account in respect of trade receivables is used to record impairment losses until all possible opportunities for recovery have been exhausted; at that point the amounts are written off against the financial asset directly.

Based on historic default rates, the Group believes that, apart from the above, no impairment allowance is necessary in respect of trade receivables.

Cash and cash equivalents

The cash and cash equivalents are held with bank, which is rated B based on rating agency Fitch ratings.

(iii) *Liquidity risk*

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group manages liquidity requirements by the use of both short-term and long-term projections. Management regularly monitors monthly forecasts of the Group's cash flows. The Company has established an annual budgeting process with the owner. The budget is reviewed by the Supervisory Board and approved by the owner. The budget is updated on a monthly basis based on the actual results. The Group aims to maintain the level of cash and cash equivalents at an amount in excess of expected cash outflows on financial liabilities over the next 60 days.

In addition, the Group maintains an unused credit line facility of GEL 16 million with EBRD within the framework of the BSTN project.

The Group has contractual commitments to purchase property and equipment (see note 19).

The following are the remaining contractual maturities of financial liabilities at the reporting date. The amounts are gross and undiscounted, include estimated interest payments and exclude the impact of netting agreements.

31 December 2013

'000 GEL	Carrying amount	Contractual cash flows	Up to 1 year	1-5 years	Over 5 years
Non-derivative financial liabilities					
Loans from financial institutions	589,789	699,569	54,038	227,839	417,692
Secured loans from related party	38,470	45,666	7,927	37,739	-
Restructured liabilities	63,766	106,210	5,000	37,000	64,210
Trade and other payables	34,175	34,175	34,175	-	-
	726,200	**885,620**	**101,140**	**302,578**	**481,902**

31 December 2012

'000 GEL	Carrying amount	Contractual cash flows	Up to 1 year	1-5 years	Over 5 years
Non-derivative financial liabilities					
Loans from financial institutions	478,492	594,357	11,538	218,068	364,751
Secured loans from related party	18,247	40,297	-	32,945	7,352
Restructured liabilities	60,827	109,183	2,671	27,000	79,512
Trade and other payables	109,375	109,375	109,375	-	-
	666,941	**853,212**	**123,584**	**278,013**	**451,615**

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

(iv) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

The Group does not apply hedge accounting in order to manage volatility in profit or loss.

Currency risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Group's exposure to the risk of changes in foreign exchange rates relates primarily to the financial liabilities denominated in foreign currencies.

The Group does not hedge its exposure to currency risk.

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows based on notional amounts:

'000 GEL	USD-denominated 2013	EUR-denominated 2013	USD-denominated 2012	EUR-denominated 2012
Trade and other receivables	73	19	669	4
Cash and cash equivalents	3	17,153	176	7,587
Loans and borrowings	(37,323)	(590,936)	(39,760)	(456,979)
Trade and other payables	(100)	(25,408)	(1,865)	(105,674)
Restructured liabilities	(5,024)	(4,099)	(4,799)	(3,817)
Net exposure	**(42,371)**	**(603,271)**	**(45,579)**	**(558,879)**

The following significant exchange rates applied during the year:

in GEL	Average rate		Reporting date spot rate	
	2013	**2012**	**2013**	**2012**
USD 1	1.6634	1.6513	1.7363	1.6567
EUR 1	2.2094	2.1232	2.3891	2.1825

Sensitivity analysis

A strengthening/weakening of the GEL, as indicated below, against the EUR and USD at 31 December would have increased (decreased) profit or loss before income tax by the amounts shown below. There would have been no impact on other comprehensive income or directly on equity. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

The analysis is performed on the same basis for 2012.

'000 GEL	Strengthening	Weakening
	Profit or loss	**Profit or loss**
31 December 2013		
USD (10% movement)	4,237	(4,237)
EUR (10% movement)	60,327	(60,327)
31 December 2012		
USD (10% movement)	4,558	(4,558)
EUR (10% movement)	55,888	(55,888)

Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

Profile

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

'000 GEL	Carrying amount	
	2013	**2012**
Fixed rate instruments		
Financial assets	35,410	17,715
Financial liabilities	(103,426)	(81,944)
	(68,016)	**(64,229)**
Variable rate instruments		
Financial liabilities	(524,833)	(414,795)
	(524,833)	**(414,795)**

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial instruments as fair value through profit or loss or as available-for-sale. Therefore a change in interest rates at the reporting date would not have an effect in profit or loss or in equity.

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss net of taxes by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2012.

	Profit or loss	
'000 GEL	**100 bp increase**	**100 bp decrease**
2013		
Variable rate instruments	(4,461)	4,461
Cash flow sensitivity (net)	**(4,461)**	**4,461**
2012		
Variable rate instruments	(3,526)	3,526
Cash flow sensitivity (net)	**(3,526)**	**3,526**

19. Capital commitments

As at 31 December 2013 the Group had contractual commitments to purchase equipment for the construction and rehabilitation of energy-transmission lines for GEL 17,937 thousand (2012: GEL 17,599 thousand).

20. Contingencies

(a) Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

(b) Litigation

In the ordinary course of business, the Group is subject to legal actions, litigations and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations.

(c) Taxation contingencies

The taxation system in Georgia is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes unclear, contradictory and subject to varying interpretation. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by the tax authorities after six years have passed since the end of the year in which the breach occurred.

These circumstances may create tax risks in Georgia that are more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Georgian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

21. Related party transactions

(a) Control relationships

The Company's immediate and ultimate parent company is Partnership Fund JSC and the Company's ultimate controlling party is the Government of Georgia. Partnership Fund JSC produces publicly available financial statements which are available on the entity's website.

(b) Transactions with key management personnel

(i) Key management remuneration

Key management received the following remuneration during the year, which is included in wages and salaries:

'000 GEL	**2013**	**2012**
Salaries and bonuses	**1,402**	**1,226**

(c) Transactions with Government related entities

The Group transacts in its daily operations with a number of entities that are either controlled, jointly controlled or under significant influence of the Government of Georgia. The Group has opted to apply the exemption in IAS 24 *Related Party Disclosures* that allows the presentation of reduced related party disclosures regarding transactions with government-related entities.

All of the Group's loans and borrowings and interest expense on loans and borrowings are payable to the Ministry of Finance of Georgia. The Group's grants related to assets are mainly received in the transactions where the Government of Georgia acted as an intermediary. The Group's restructured liabilities mainly consist of payables to the Government of Georgia or Government bodies.

Approximately 26% of the Group's revenue (2012: 30%) is from three entities significantly influenced or controlled by the Government of Georgia.

22. Subsidiaries

Subsidiary	Country of incorporation	2013 Ownership/voting	2012 Ownership/voting
EnergoTrans LLC	Georgia	100%	100%
Karcal Energy JSC	Turkey	100%	100%

23. Basis of measurement

The consolidated financial statements are prepared on the historical cost basis.

24. Accounting developments

Changes in accounting policies and presentation

The Group has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 January 2013.

- IFRS 13 *Fair Value Measurements* (see (i));
- *Presentation of Items of Other Comprehensive Income* (Amendments to IAS 1) (see (ii));
- IFRS 10 *Consolidated Financial Statements (2011)*(see (iii));
- IFRS 12 *Disclosure of Interests in Other Entities* (see (iv)).

The nature and the effect of the changes are explained below.

(i) Fair value measurement

IFRS 13 establishes a single framework for measuring fair value and making disclosures about fair value measurements, when such measurements are required or permitted by other IFRSs. In particular, it unifies the definition of fair value as the prices at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date. It also replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7.

As a result, the Group adopted a new definition of fair value. The change had no significant impact on the measurements of assets and liabilities. However, the Group included new disclosures in the consolidated financial statements that are required under IFRS 13.

(ii) Presentation of items of other comprehensive income

As a result of the amendments to IAS 1, the Group modified the presentation of items of other comprehensive income in its consolidated statement of profit or loss and other comprehensive income, to present separately items that would be reclassified to profit or loss in the future from those that would never be. The adoption of the amendment to IAS 1 has no impact on the recognised assets, liabilities or comprehensive income.

(iii) Subsidiaries, including structured entities

As a result of adoption of IFRS 10, the Group changed its accounting policy with respect to determining whether it has control over and consequently whether it consolidates its investees. IFRS 10 introduces a new control model that is applicable to all investees, including structured entities. In accordance with the transitional provisions of IFRS 10, the Group reassessed the control conclusion for its investees as at 1 January 2013. The Group determined that its consolidated group structure remained unchanged under IFRS 10, and as a result, the consolidated financial statements are unaffected.

(iv) Disclosure of interests in other entities

The new standard contains disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. Interests are widely defined as contractual and non-contractual involvement that exposes an entity to variability of returns from the performance of the other entity. The expanded and new disclosure requirements aim to provide information to enable the users to evaluate the nature of risks associated with an entity's interests in other entities and the effects of those interests on the entity's financial position, financial performance and cash flows.

The adoption of IFRS 12 has no impact on the disclosures in the consolidated financial statements.

25. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities, except as explained in note 24, which addresses changes in accounting policies.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

(ii) Loss of control

Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in profit or loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or as an available-for-sale financial asset depending on the level of influence retained.

(iii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(b) Revenue

(i) Services

Revenue is recognized to the extent the Group has rendered services under an agreement, the amount of revenue can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group. Revenue is measured at the fair value of the consideration received, exclusive of sales taxes and discounts.

The Group primarily derives revenue from *transmission* and *dispatching* of electric power over the entire territory of Georgia. Revenue is recognized when the actual services are delivered based on the volume of transmitted and dispatched electricity at the reporting date.

(ii) Government grants

Grants are recognised initially as deferred income at fair value when there is reasonable assurance that they will be received and that the Group will comply with the conditions associated with the grant and are then recognised in profit or loss as other income on a systematic basis over the useful life of the asset. Grants that compensate the Group for expenses incurred are recognised in profit or loss as other income on a systematic basis in the same periods in which the expenses are recognised.

(c) Finance income and costs

The Group's finance income and finance costs include:

- interest income on funds invested;
- interest expense on financial liabilities measured at amortized cost;
- the foreign currency gain or loss on financial assets and financial liabilities.

Interest income or expense is recognised as it accrues in profit or loss using the effective interest method. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance cost depending on whether foreign currency movements are in a net gain or net loss position.

(d) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period.

Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising in retranslation are recognised in profit or loss.

(ii) Foreign operations

The assets and liabilities of foreign operations are translated to GEL at the exchange rates at the reporting date. The income and expenses of foreign operations are translated to GEL at exchange rates at the dates of the transactions.

Foreign currency differences are recognised in other comprehensive income and are presented in the foreign currency translation reserve in equity. When a foreign operation is disposed of such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to profit or loss as part of the gain or loss on disposal.

(e) Short term employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee, and the obligation can be estimated reliably.

(f) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

(g) Income tax

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that it relates to the items recognised directly in equity or in other comprehensive income.

(i) Current tax

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

(ii) Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for temporary differences in connection with the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit nor loss.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

In determining the amount of current and deferred tax the Group takes into account the impact of uncertain tax positions and whether additional taxes, penalties and late-payment interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretations of tax law and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Group to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact the tax expense in the period that such a determination is made.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(h) Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the weighted average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(i) Property and equipment

(i) Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property and equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

Any gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of property and equipment, and is recognised net within other income/other expenses in profit or loss.

(ii) Subsequent costs

The cost of replacing a component of an item of property and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Group, and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

(iii) Depreciation

Items of property and equipment are depreciated from the date that they are installed and are ready for use, or in respect of internally constructed assets, from the date that the asset is completed and ready for use. Depreciation is based on the cost of an asset less its residual value.

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Land is not depreciated.

The estimated useful lives of significant items of property and equipment for the current and comparative periods are as follows:

- buildings and constructions 15-25 years;
- power transmission lines 20-35 years;
- equipment 10-25 years;
- vehicles and other 5-7 years.

Depreciation methods, useful lives and residual values are reviewed at each financial year end and adjusted if appropriate.

(j) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised on the Group's statement of financial position.

(k) Financial instruments

The Group classifies non-derivative financial assets into loans and receivables category and non-derivative financial liabilities into other financial liabilities category.

(i) Non-derivative financial assets and financial liabilities – recognition and derecognition

The Group initially recognises loans and receivables and deposits on the date that they are originated. All other financial assets and liabilities are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire. Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Loans and receivables

Loans and receivables are a category of financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables category comprise the following classes of financial assets: trade and other receivables as presented in note 10 and cash and cash equivalents as presented in note 11.

Cash and cash equivalents

Cash and cash equivalents comprise bank balances with maturities of three months or less from the acquisition date that are subject to insignificant risk of changes in their fair value.

(ii) Non-derivative financial liabilities - measurement

Other financial liabilities are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortised cost using the effective interest method. Other financial liabilities comprise loans and borrowings as presented in note 14, restructured liabilities as presented in note 15 and trade and other payables as presented in note 17.

(l) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

(m) Impairment

(i) Non-derivative financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include:

- default or delinquency by a debtor;
- restructuring of an amount due to the Group on terms that the Group would not consider otherwise;
- indications that a debtor will enter bankruptcy;
- economic conditions that correlate with defaults.

Financial assets measured at amortised cost

The Group considers evidence of impairment for those assets at both a specific asset and collective level. All individually significant loans and receivables are assessed for specific impairment. All individually significant loans and receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables that are not individually significant are collectively assessed for impairment by grouping together receivables with similar risk characteristics.

In assessing collective impairment the Group uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in the allowance account against receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease and the decrease can be related objectively to an event occurring after the impairment was recognised, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGU. The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated to the carrying amount of the assets in the unit (group of CGUs) on a pro rata basis.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

26. New standards and interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2013, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the Group's operations. The Group plans to adopt these pronouncements when they become effective.

- IFRS 9 *Financial Instruments* is to be issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement*. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding classification and measurement of financial liabilities was published in October 2010. The third phase of IFRS 9 was issued in November 2013 and relates to general hedge accounting. The final standard is expected to be issued in 2014 and will be effective for years beginning on or after 1 January 2018. The Group recognises that the new standard introduces many changes to the accounting for financial instruments and is likely to have a significant impact on Group's consolidated financial statements. The impact of these changes will be analysed during the course of the project as further phases of the standard are issued. The Group does not intend to adopt this standard early.

- IFRS 15 *Revenue from Contracts with Customers* will be effective for annual periods beginning on or after 1 January 2017. Earlier application is permitted. The standard supersedes IAS 11 *Construction Contracts*; IAS 18 *Revenue*; IFRIC 13 *Customer Loyalty Programmes*; IFRIC 15 *Agreements for the Construction of Real Estate*; IFRIC 18 *Transfers of Assets from Customers* and SIC-31 *Revenue - Barter Transactions Involving Advertising Services*. The core principle of the standard is for entities to recognise revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration (that is, payment) to which the Group expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively and improve guidance for multiple-element arrangements. The Group has not yet analysed the likely impact of the standard on its financial position or performance. The Group does not intend to adopt this standard early.

- Various *Improvements to IFRSs* have been dealt with on a standard-by-standard basis. All amendments, which result in accounting changes for presentation, recognition or measurement purposes, will come into effect for annual periods beginning on or after 1 July 2014. Entities are permitted to apply them earlier. The Group has not yet analysed the likely impact of the improvements on its financial position or performance.

27. Events subsequent to the reporting date

In 2013 the Government of Georgia signed the Loan and Project Agreements on "Regional Power Transmission Enhancement Project" with Asian Development Bank (ADB), KFW and EBRD for SDR 30,981 thousand, EUR 35,000 thousand and EUR 25,205 thousand respectively. In 2014 the Government of Georgia transferred these credit facilities, together with an obligation to repay them, to the Company. The credit facilities received will be used by the Company mainly for the construction and enhancement of Jvari - Khorga electricity transmission lines and substations as well as other transmission network rehabilitation projects. The construction and rehabilitation process is expected to start in 2014 and be completed in 2-3 years.