GEORGIAN STATE ELECTROSYSTEM JSC

Key Performance Indicators

There are ongoing KPIs as opposed to the one-time threshold conditions. This document contains these ongoing KPIs and are tailored to GSE's circumstances.

Additional KPIs to be proposed for Human Resources evaluation of personnel and performance are not covered in this document.

Following each category, an explanation of these KPIs is provided.

Accounting

GSE presently has significant weaknesses in its accounting practices. As described more fully in the main report, GSE's accounting software is not integrated with other systems and does not cover the entire company. There are identified significant, ongoing weaknesses in its accounting practices. Specifically, there are several significant weaknesses in internal control or financial operations, most of which have been identified each year without cure:

- Failure to calculate loan covenants at end of each month;
- Inadequate resources for the preparation of financial statements in accordance with IFRS;
- Failure to undertake formal impairment analysis to determine whether recognition of impairment required under *IAS 36 Impairment of Assets*; a
- Failure to hedge foreign currency risks.

As a result, it is critical that GSE adopt KPIs for accounting systems that are sufficiently granular to measure progress in addressing accounting deficiencies. Presently, GSE would likely not meet any of the proposed KPIs. These KPIs represent material accounting issues faced by publicly traded companies, which are also appropriate to a state-owned enterprise.

The following KPIs are therefore proposed with their specific justification:

Proposed KPI	Justification
Has there been any evidence of material weakness in the company's internal control systems?	Material weaknesses in accounting and internal control systems create a high likelihood of transparency problems. The Supervisory Board, its Audit Committee, external auditor, and GSE Financial Director and Audit Department should be continuously monitoring the corporation for material weaknesses.
Has the company experienced a restatement of financial statements or special charge for inaccuracy/fraud?	Restatements or special charges are a common indicator for past inaccuracy or fraud.
Is the company experiencing a reporting delay?	Reporting delays commonly signal weaknesses in systems, capacity problems, regulatory problems

	and/or fraud.
Are there accounting ratios related to asset-liability valuation that have extreme values either relative to industry peers or to company's own history?	Accounting ratios for asset-liability valuations at extreme values indicate potentially excessive risk taking by management and corporate distress. It may further indicate deeper problems such as fraud or other malfeasance.
Has company announced internal investigation or being investigated?	An internal or external investigation indicates known or suspected problems, potentially carrying civil and/or criminal liability. As such, they indicate serious problems with corporate governance.
Has the company's independent auditor issued qualified, adverse or disclaimer opinion?	Independent auditor is specifically tasked with assessing potential weaknesses in accounting and internal control systems.
Has the company breached any debt covenants?	Breach of debt covenant indicates weakness in internal controls designed to forecast and management.

Supervisory Board

With the establishment of the Supervisory Board the situation whereby GSE's executive management potentially enjoyed unsupervised and unchecked discretion by default has been terminated. Therefore, KPIs addressing the establishment of a supervisory board and implementation of corporate governance arrangements by that board are essential to modernizing GSE's operations.

The following KPIs are proposed that measure the steps taken to establish and strengthen the role of the Supervisory Board and the Supervisory Board's effectiveness in meaningfully implementing governance arrangements.

The following KPIs are therefore proposed with their specific justification:

Did the supervisory board fail to meet each quarter during the past year?	Regular meetings is an indicator of meeting duty of care and level of attention to corporate affairs, and by extension quality of corporate governance.
Does company leadership at Supervisory Board or General Director / Board of Directors exercise excessive influence?	These boards should be collegial panels designed to ensure open discussion and exercise of independent judgment. Excessive influence over either would undermine the corporate governance role of these institutions.
Do less than a majority of the members on the Supervisory Board meet the criteria for being independent of management, government and	Independent members of the Supervisory Board exercising impartial judgment is consistent

other constituencies?	with international best practices and meeting fiduciary duties. Lack of independent members can undermine the corporate governance function designed to ensure the best interests of the corporation are pursued.
Has the company had any related party transactions within the past financial year?	Related party transactions can undermine transparency and the corporate governance function designed to ensure the best interests of the corporation are pursued.
Do any of the Supervisory Board members have substantial outside responsibilities potentially preventing them from fulfilling their Supervisory Board duty?	Substantial outside responsibilities can undermine the capacity of members to fulfill their duties in exercising corporate governance over the corporation.
Did any members of the Supervisory Board fail to attend all Supervisory Board and committee meetings held during the last year?	Attendance at meetings is an indication of the level of commitment of the individual members in meeting their corporate governance duties.
Does the Supervisory Board fail to include any female members?	Diversity on the board is best practice and correlates to better performance. This is now required by EU and other country legislation.
Does the Supervisory Board lack at least one member with expertise in risk management?	Presence of independent members with appropriate backgrounds strengthens corporate governance.
Has the Supervisory Board failed to establish an audit committee comprising only members independent of management, government and other constituencies?	Required by best practices, this committee is central to ensuring financial controls and transparency.
Has the Supervisory Board failed to establish a compensation committee comprising only members independent of management and government?	Required by best practices, this committee is central to aligning incentives with performance and transparency.
Has a current Supervisory Board member or the General Director been accused of any breach of fiduciary duty?	Breach of fiduciary duty by the Supervisory Board members or the General Director indicate weaknesses in corporate governance.

<u>Compensation</u>

Compensation KPIs proposed here are aimed at improving corporate governance. Additional KPIs relating to human resources generally and compensation in particular that aim to improve human resource functions, could be proposed at a later stage and should complement the KPIs here.

Compensation levels for the General Director and Board of Director should be commensurate to the level of responsibilities and duties assumed by the incumbents. Appropriateness of compensation levels is generally determined based on a comparison to other peer companies for similar responsibilities. Additionally, compensation should properly motivate appropriate behavior relative to performance. These principles are reflected in best industry practices generally and the relevant EU guidelines more specifically.

The following KPIs for compensation are proposed to monitor and measure GSE's progress in improving compensation arrangements:

Does the General Director's compensation for the last period exceed the average pay for the other members of the Board of Directors by more than two times?	Compensation should be proportionate to responsibilities for the General Director and other members of the Board of Directors. Excessive compensation of the General Director can demotivate other members or signal lopsided allocation of responsibilities or powers.
Has the company failed to disclose compensation amounts for the General Director?	Required by best practices, disclosure of the General Director compensation is essential to transparency in corporate affairs and prevention of self-dealing by executives.
Did the General Director's annual incentives fail to adjust based on annual performance for the last reported period, including risk?	Compensation should be aligned to performance and risk in line with best practices.