Georgian Oil and Gas Corporation JSC

Consolidated Financial Statements
for the year ended 31 December 2012

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Independent Auditors' Report

Board of Directors
Georgian Oil and Gas Corporation JSC

We have audited the accompanying consolidated financial statements of Georgian Oil and Gas Corporation JSC (the "Company") (and its subsidiaries (the "Group")), which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated statements of 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 2012, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Tbilisi branch of KPMG CIS Limited

Tbilisi Branch of KPMG CIS Limited
27 March 2013

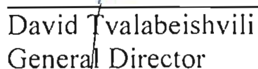
Tbilisi Branch of KPMG CIS Limited, a branch incorporated under the Laws of Georgia, a subsidiary of KPMG Europe LLP, and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

'000 GEL	Note	2012	2011
Assets			
Property, plant and equipment	15	282,650	271,606
Intangible assets		165	222
Prepayment for non-current assets		-	684
Finance lease receivable	16	45,882	43,074
Loans given to the shareholder	17	85,322	-
Other non-current assets		107	-
Term deposits	18	105,426	-
Non-current assets		**519,552**	**315,586**
Loans given to state controlled entity	17	48,714	-
Non-current assets held for distribution	15	-	20,728
Inventories		535	735
Current tax assets		6,621	756
Taxes other than on income		990	-
Prepayments for current assets and expenses		19,972	23,290
Trade and other receivables	19	86,400	30,370
Term deposits	18	52,854	-
Cash and cash equivalents	20	142,672	35,079
Current assets		**358,758**	**110,958**
Total assets		**878,310**	**426,544**
Equity	21		
Share capital		509,298	478,772
Additional paid in capital		71,718	71,718
Fair value adjustment reserve for non-cash owner contributions		(282,181)	(282,181)
Retained earnings		99,924	90,160
Total equity		**398,759**	**358,469**
Liabilities			
Loans and borrowings	22	406,183	654
Deferred tax liabilities	23	9,566	10,635
Non-current liabilities		**415,749**	**11,289**
Loans and borrowings	22	5,090	10,362
Trade and other payables	24	24,822	2,685
Dividend payable	21	32,000	41,700
Value added tax payable		1,890	1,623
Other taxes payable		-	416
Current liabilities		**63,802**	**56,786**
Total liabilities		**479,551**	**68,075**
Total equity and liabilities		**878,310**	**426,544**

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 44.

'000 GEL	Note	2012	2011
Continuing operations			
Revenue	8	299,551	239,917
Cost of gas and oil	9	(178,230)	(111,809)
Depreciation		(18,662)	(19,778)
Personnel costs		(8,508)	(7,906)
Taxes, other than on income		(6,158)	(5,515)
Reversal of impairment loss of property, plant and equipment		-	26,393
Impairment of assets related to Namakhvani project	10	(7,486)	-
Other expenses	11	(8,707)	(6,050)
Other income	12	11,138	5,574
Results from operating activities		**82,938**	**120,826**
Finance income	13	28,997	11,218
Finance costs	13	(19,331)	(1,698)
Net finance income		**9,666**	**9,520**
Profit before income tax		**92,604**	**130,346**
Income tax expense	14	(11,578)	(16,274)
Profit from continuing operations		**81,026**	**114,072**
Discontinued operation			
Profit from discontinued operation (net of income tax)	7	-	8,444
Profit and total comprehensive income for the year attributable to owners of the Company		**81,026**	**122,516**

These consolidated financial statements were approved by management on 27 March 2013 and were signed on its behalf by:



David Tvalabeishvili
General Director

Irakli Chkhaidze
Financial Director

The consolidated statement of 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 44.

'000 GEL	Share capital/ charter capital*	Fair value adjustment reserve for non-cash owner contributions	Additional paid-in capital	Retained earnings	Total
Balance at 1 January 2011	495,532	(282,181)	74,570	58,523	346,444
Total comprehensive income for the year					
Profit and total comprehensive income for the year	-	-	-	122,516	122,516
Contributions by and distributions owners					
Dividends to equity holders (see note 21(c))	-	-	-	(45,000)	(45,000)
Other cash distributions (see note 21(c))	-	-	-	(4,200)	(4,200)
Distributions of non-cash assets net of tax of GEL 1,250 thousand (see note 21(c))	-	-	-	(7,082)	(7,082)
Distributions of non-cash assets (see note 15)	-	-	(2,852)	-	(2,852)
Increase in share capital	11,000	-	-	-	11,000
Decrease in share capital	(26,723)	-	-	-	(26,723)
Transfer of subsidiary (see note 7)	(1,037)	-	-	(34,597)	(35,634)
Balance at 31 December 2011	**478,772**	**(282,181)**	**71,718**	**90,160**	**358,469**
Balance at 1 January 2012	478,772	(282,181)	71,718	90,160	358,469
Total comprehensive income for the year					
Profit and total comprehensive income for the year	-	-	-	81,026	81,026
Contributions by and distributions to owners					
Dividends to equity holders (see note 21(c))	-	-	-	(40,000)	(40,000)
Distributions of non-cash assets net of tax of GEL 5,517 thousand (see note 21 (c))	-	-	-	(31,262)	(31,262)
Increase in share capital	30,833	-	-	-	30,833
Decrease in share capital	(307)	-	-	-	(307)
Balance at 31 December 2012	**509,298**	**(282,181)**	**71,718**	**99,924**	**398,759**

*In September 2011, the Company changed its legal form from a Limited Liability Company to a Joint Stock Company.

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 44.

'000 GEL	Note	2012	2011
Cash flows from operating activities			
Cash receipts from customers		263,856	272,502
Cash paid to suppliers and employees		(178,389)	(183,110)
Cash from operations before income taxes and interest		**85,467**	**89,392**
Income tax paid		(12,996)	(18,140)
Interest paid		(14,323)	(669)
Interest received		7,415	7,663
Net cash from operating activities		**65,563**	**78,246**
Cash flows from investing activities			
Acquisition of property, plant and equipment and intangible assets		(23,111)	(44,523)
Acquisition of non-current assets held for distribution		(6,643)	(20,728)
Loans given to shareholder and state controlled entity		(130,029)	-
Investing in other companies		(107)	(115)
Increase in term deposits		(140,751)	-
Net cash used in investing activities		**(300,641)**	**(65,366)**
Cash flows from financing activities			
Proceeds from borrowings		397,433	-
Repayment of borrowings		(10,541)	-
Dividends paid		(47,500)	(5,500)
Other cash distributions to owners		(2,200)	(2,000)
Cash distributed on the transfer of subsidiaries		-	(26,623)
Cash distributed on the transfer of discontinued operation		-	(1,811)
Net cash from/(used in) financing activities		**337,192**	**(35,934)**
Net increase/(decrease) in cash and cash equivalents		**102,114**	**(23,054)**
Cash and cash equivalents at 1 January		35,079	57,589
Effect of exchange rate fluctuations on cash and cash equivalents		5,479	544
Cash and cash equivalents at 31 December	20	**142,672**	**35,079**

As at 31 December 2012, the Group changed the method of presentation of its statement of cash flows from the indirect to the direct method as management believes this provides more useful information to users. The statement of cash flows for the year ended 31 December 2011 has been represented to conform to the current year presentation.

During 2012 and 2011 the Group received non-cash contributions and made non-cash distributions to the Government of Georgia (see note 15).

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 44.

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1. Background

(a) Organisation and operations

Georgian Oil and Gas Corporation JSC (the "Company"), formerly incorporated as a LLC, and its subsidiaries (the "Group") comprise Georgian Joint Stock and Limited Liability Companies as defined in the "Law of Georgia on Entrepreneurs". In September 2011 the Company changed its legal form from a Limited Liability Company to a Joint Stock Company. The Company was established as a 100% state-owned enterprise by the order of the Ministry of Economy of Georgia on 21 March 2006, on the basis of three Georgian state-owned companies: Georgian International Oil Corporation JSC, Georgian Gas International Corporation JSC and Teleti Oil Company JSC.

In 2006 and 2007, respectively, Georgian International Oil Corporation JSC and Georgian Gas International Corporation JSC ceased legal existence and the assets and liabilities were transferred to the Company. In November 2007 the shares in Teleti Oil Company JSC were taken over by the Government of Georgia. Related party transactions are detailed in note 28.

The Company's registered office is 21 Kakheti Highway, Tbilisi 0190, Georgia.

The Group's principal activities are the importation and sale of gas, the rental of gas pipelines, oil and gas exploration and extraction in the territory of Georgia. Before the transfer of the subsidiary (see note 7), the Group's principal activities also included operation of transitory gas pipelines in the territory of Georgia and transit of gas to the Republic of Armenia.

The Company has also been granted the status of "National Oil Company" in December 2006 by Presidential decree number 736 and it acts on behalf of the State of Georgia, receives and disposes of the State's share of extracted oil and gas produced by contractors in the territory of Georgia in accordance with the "Law of Georgia on Oil and Gas" and production sharing agreements signed between the State and the contractors. The Group has not recognized an intangible asset for this right as the Group does not control the right.

(b) Business environment

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

(a) Statement of compliance

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

(b) Basis of measurement

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

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

(d) 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 following notes:

- Note 15 Property, plant and equipment – determination of the value in use of the gas transportation CGU;
- Note 16 Finance lease receivable – determination of whether the arrangement contains a lease and the fair value of the unguaranteed residual value;
- Note 20 Cash and cash equivalents – classification of term deposits as cash and cash equivalents;
- Note 23 Deferred tax assets and liabilities – determination of whether to recognise a temporary difference on initial recognition of the financial lease receivable.

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year is included in the following notes:

- Note 10 Impairment – impairment of assets related to Namakhvani project;
- Note 25 (b) Credit risk – impairment of trade and other receivables and loans given;
- Note 26 Capital commitments – termination of agreements related to Namakhvani project;
- Note 27 Contingencies – litigation.

3. 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.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. 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. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

(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) Jointly controlled operations

A jointly controlled operation is a joint venture carried on by each venturer using its own assets in pursuit of the joint operations. The consolidated financial statements include the assets that the Group controls and the liabilities that it incurs in the course of pursuing the joint operation, and the expenses that the Group incurs and its share of the income that it earns from the joint operation.

(iv) 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) 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.

(c) Financial instruments

(i) Non-derivative financial assets

The Group initially recognizes loans and receivables and deposits on the date that they are originated.

The Group derecognizes 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 recognized as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement if 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 liability simultaneously.

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

Loans and receivables are a category of financial assets with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are recognized 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 loans given, trade and other receivables, term deposits and cash and cash equivalents.

Cash and cash equivalents comprise cash balances, call deposits and highly liquid investments 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

The Group initially recognises debt securities issued on the date that they are originated. All other financial liabilities are recognized initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group classifies non-derivative financial liabilities into the other financial liability category.
Such financial liabilities are recognized initially at fair value less 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 and trade and other payables.

(d) Share capital

Ordinary shares

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.

Reduction of share capital

Share capital reductions and non-cash distributions are recognized at the carrying amount of the assets distributed. Non-cash distributions of the Company are out of scope of IFRIC 17 *Distributions of Non-cash Assets to Owners* since the ultimate controlling party controls the assets before and after the distribution.

Increase of share capital

Share capital increase is effected through issuance of new shares. When share capital is increased, any difference between the registered amount of share capital and the fair value of the assets contributed is recognized as a separate component of equity as fair value adjustment reserve for non-cash owner contributions.

(e) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Property, plant and equipment contributed by the shareholder are initially measured at fair value. The cost of property, plant and equipment at the date of adopting IFRS, 1 January 2008, was determined by reference to its fair value at that date ("deemed cost").

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 borrowing costs on qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. 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, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

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

(ii) Subsequent costs

The cost of replacing a component of an item of property, plant 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, plant and equipment are recognised in profit or loss as incurred.

(iii) Depreciation

Items of property, plant 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, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

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

- gas and oil pipelines 30-35 years
- buildings 50 years
- oil wells 4-9 years
- plant and equipment 2-14 years
- other 1-6 years

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

(f) 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.

When the Group is the lessor in a lease agreement that transfers substantially all of the risks and rewards incidental to ownership of the asset to the lessee, the arrangement is classified as a finance lease and a receivable equal to the net investment in the lease is recognized and presented within loans and receivables. Subsequently the recognition of finance income is based on a pattern reflecting a constant periodic rate of return on the Group's net investment in the finance lease.

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

(g) Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first-in first-out 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. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

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

(h) Impairment

(i) Non-derivative financial assets

A financial asset 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, adverse changes in the payment status of borrowers or issuers in the Group, or economic conditions that correlate with defaults.

The Group considers evidence of impairment for loans and receivables 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 loans and 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 in respect of a financial asset measured at amortised cost 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 recognized in profit or loss and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, 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 recognized 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.

Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated to carrying amounts of the assets in the CGU on a pro rata basis.

Impairment losses recognized 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 recognized.

(i) 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.

(j) 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.

(k) Non-current assets held for sale or distribution

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale or distribution rather than through continuing use, are classified as held for sale or distribution. Immediately before classification as held for sale, the assets, or components of a disposal group, are remeasured in accordance with the Group's accounting policies. Thereafter generally the assets, or disposal group, are measured at the lower of their carrying amount and fair value less cost to sell. Any impairment loss on a disposal group is allocated to assets and liabilities on pro rata basis, except that no loss is allocated to inventories, financial assets, deferred tax assets or employee benefit assets, which continue to be measured in accordance with the Group's accounting policies. Impairment losses on initial classification as held for sale or distribution and subsequent gains or losses on remeasurement are recognised in profit or loss. Gains are not recognised in excess of any cumulative impairment loss.

Intangible assets and property, plant and equipment once classified as held for sale or distribution are not amortised or depreciated.

(l) Revenue

(i) Sale of gas and oil

Revenue from the sale of gas and oil in the course of ordinary activities is measured at the fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates.

Revenue is recognized when persuasive evidence exists, usually in the form of an executed sales agreement, that the significant risks and rewards of ownership have been transferred to the customer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably. If it is probable that discounts will be granted and the amount can be measured reliably, then the discount is recognized as a reduction of revenue as the sales are recognized.

The timing of the transfers of risks and rewards varies depending on the individual terms of the sales agreement. For sales of gas, the sale is recognized on the basis of metered usage of gas by customers. For sales of oil, transfer occurs upon loading the product onto the relevant carriers, inspection by an independent inspector and sealing of carriers based on FCA (Incoterms 2000) at Vaziani or Supsa stations (Georgia) terms. The seller is responsible for delivery of goods to the named points, uploading goods to the buyer's wagons and customs registration.

(ii) Rent of pipelines

Revenue from rent of gas pipelines is recognized in profit or loss on the basis of the metered gas transferred through the pipelines at the contract rate.

(iii) Services

Revenue from services rendered is recognized in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

Oil transportation fees received in cash are recognized on the basis of the metered oil transferred through the pipelines at the contract rate for barrels of oil.

(m) Finance income and costs

Finance income comprises interest income on funds invested, unwinding of discount on finance lease receivable and foreign currency gains. Interest income is recognised as it accrues in profit or loss, using the effective interest method.

Finance costs comprise interest expense on borrowings, impairment losses recognised on financial assets and foreign currency losses.

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.

(n) Income tax

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

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.

Deferred tax is recognized 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 recognized for temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; or deferred tax related to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future.

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 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.

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.

A deferred tax asset is recognized 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.

(o) Discontinued operations

A discontinued operation is a component of the Group's business that represents a separate major line of business or geographical area of operations that has been disposed of or is held for sale, or is a subsidiary acquired exclusively with a view to resale. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier. When an operation is classified as a discontinued operation, the comparative statement of comprehensive income is re-presented as if the operation had been discontinued from the start of the comparative period.

(p) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are reviewed regularly by the General Director to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the General Director include items directly attributable to a segment.

4. 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 2012, 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* will be effective for annual periods beginning on or after 1 January 2015. The new standard 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 remaining parts of the standard are expected to be issued during 2013. 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 11 *Joint Arrangements* will be effective for annual periods beginning on or after 1 January 2013 with retrospective application required. The new standard supersedes IAS 31 *Interests in Joint Ventures*. The main change introduced by IFRS 11 is that all joint arrangements are classified either as joint operations, in which case these arrangements are treated similarly to jointly controlled assets/operations under IAS 31s, or as joint ventures, for which the equity method only is applied. The type of arrangement is determined based on the rights and obligations of the parties to the arrangement arising from joint arrangement's structure, legal form, contractual arrangement and other facts and circumstances. When the adoption of IFRS 11 results a change in the accounting model, the change is accounted for retrospectively from the beginning of the earliest period presented. Under the new standard all parties to a joint arrangement are within the scope of IFRS 11 even if all parties do not participate in the joint control. Early adoption of IFRS 11 is permitted provided the entity also early-adopts IFRS 10, IFRS 12, IAS 27 (2011) and IAS 28 (2011). The Group has not yet analyzed the likely impact of the new Standard on its financial position or performance.

- IFRS 12 *Disclosure of Interests in Other Entities* will be effective for annual periods beginning on or after 1 January 2013. 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. Entities may early present some of the IFRS 12 disclosures early without a need to early-adopt the other new and amended standards. However, if IFRS 12 is early-adopted in full, then IFRS 10, IFRS 11, IAS 27 (2011) and IAS 28 (2011) must also be early-adopted. The new Standard will not have any impact on the Group's financial position or performance.

- IFRS 13 *Fair Value Measurement* will be effective for annual periods beginning on or after 1 January 2013. The new standard replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It provides a revised definition of fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. IFRS 13 does not introduce new requirements to measure assets or liabilities at fair value, nor does it eliminate the practicability exceptions to fair value measurement that currently exist in certain standards. The standard is applied prospectively with early adoption permitted. Comparative disclosure information is not required for periods before the date of initial application. The new Standard is not expected to have a significant effect on the consolidated financial statements of the Group.

- 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 after 1 January 2013. The Group has not yet analysed the likely impact of the improvements on its financial position or performance.

5. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and for disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant and equipment

The fair value of property, plant and equipment contributed by the shareholder is based on market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. The fair value of items of plant, equipment, fixtures and fittings is based on market approach and cost approaches using quoted market prices for similar items when available.

When no quoted market prices are available, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

(b) Financial assets

The fair value of financial assets is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

(c) Financial liabilities

Fair value, which is determined for disclosure purposes, 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.

6. Operating segments

As at 31 December 2012 and 2011, the Group has four reportable segments, as described below, which are the Group's strategic business units. The strategic business units offer different products and services, and are managed separately. For each of the strategic business units, the Company's General Director reviews internal management reports on at least a quarterly basis. The following summary describes the operations in each of the Group's reportable segments:

Continuing operations

- *Gas Supply*. Includes purchase and sale of gas.
- *Pipeline rental*. Includes rental income earned by the Company from the lease of gas pipelines to Georgian Gas Transportation Company LLC. As a consequence of the transfer of Georgian Gas Transportation Company LLC to the shareholder in August 2011 (see note 7), the rental income is presented as external revenue and became a separately monitored segment.
- *Upstream activities*. Includes sale of oil from production sharing arrangements.
- *Oil transportation*. Includes rental income from transportation of oil through the territory of Georgia.

Discontinued operations

- *Gas transportation*. This segment previously included revenues earned from transportation of gas within the territory of Georgia and transit to Armenia. This segment was discontinued in August 2011 (see note 7).

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before infrastructure costs, central over heads, interest and income tax, as included in the internal management reports that are reviewed by the Company's General Director. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries. The Company's General Director does not monitor segment assets or liabilities.

(i) *Information about reportable segments*

	Gas supply		Pipeline rental		Upstream activities		Oil transportation		Total (continuing operations)		Gas transportation (discontinued operations)		Total	
'000 GEL	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**
External revenues	232,402	199,365	39,592	11,048	15,995	14,291	11,562	10,970	299,551	235,674	-	31,695	299,551	267,369
Inter-segment revenues	-	-	-	16,144	-	-	-	-	-	16,144	-	-	-	16,144
Cost of gas and oil	(178,230)	(123,535)	-	-	-	(361)	-	-	(178,230)	(123,896)	-	-	(178,230)	(123,896)
Other expenses	-	-	-	-	-	-	-	-	-	-	-	(21,773)	-	(21,773)
Reportable segment profit before unallocated costs, net finance cost and income tax	54,172	75,830	39,592	27,192	15,995	13,930	11,562	10,970	121,321	127,922	-	9,922	121,321	137,844

'000 GEL	2012	2011
Revenues		
Total revenue for reportable segments	299,551	283,513
Adjustment to bring transportation revenue in the form of gas to the fair value of gas received	-	23,176
Other revenue	-	987
Presentation of continuing nature of transactions between continuing and discontinued operations	-	28,666
Reclassification of discontinued operations	-	(96,425)
Consolidated revenue	**299,551**	**239,917**
Profit or loss		
Total profit or loss for reportable segments	121,321	137,844
Reversal of impairment loss of property, plant and equipment	-	26,393
Unallocated personnel expenses	(8,508)	(7,906)
Unallocated depreciation expenses	(18,662)	(19,778)
Net finance income	9,666	10,722
Other net unallocated costs	(11,213)	(6,545)
Reclassification of discontinued operations	-	(10,384)
Consolidated profit from continuing operations before income tax	**92,604**	**130,346**

(ii) Geographical information

Substantially all of the Group's revenue is from and the non-current assets of the Group are located in Georgia.

(iii) Major customer

In 2012, one customer of the Group's gas supply segment represented approximately 77% of the Group's total revenue (GEL 230,131 thousand). In 2011, one customer of the Group's gas supply segment represented approximately 82% of the Group's total revenue from continuing operations (GEL 197,913 thousand).

7. Discontinued operation

On 31 August 2011 the Group transferred its wholly owned subsidiary, Georgian Gas Transportation Company LLC, to the Ministry of Energy and Natural Resources of Georgia. The subsidiary was transferred for the purpose of separation of supply and transportation in the Georgian Energy Market.

'000 GEL	2011
Results of discontinued operation	
Revenue	96,425
Cost of gas and oil	(65,471)
Depreciation and amortization	(1,064)
Personnel costs	(3,225)
Taxes, other than on profit	(58)
Rent of gas pipelines	(16,144)
Other expenses	(1,771)
Other income	490
Results from operating activities	**9,182**
Finance income	1,202
Net finance income	**1,202**
Profit before income tax	**10,384**
Income tax expense	(1,940)
Profit for the year	**8,444**

The transactions between continuing and discontinued operations continue after the transfer of the subsidiary to the shareholder. The discontinued operations are presented so as to reflect the continuance of the relationship.

8. Revenue

	Continuing operations	
'000 GEL	2012	2011
Sales of gas	232,402	187,438
Rent of gas pipelines	39,592	27,218
Income from crude oil	15,995	14,291
Oil transportation fee	11,562	10,970
Total revenues	**299,551**	**239,917**

The Company rents its gas pipeline to Georgian Gas Transportation Company LLC (former subsidiary, see note 7). The contract is valid until 1 January 2020. The lease payments are contingent on the volume of gas transported through the leased gas pipeline.

9. Cost of gas and oil

'000 GEL	2012	2011
Cost of gas	178,230	111,448
Cost of crude oil	-	361
	178,230	**111,809**

10. Impairment of assets related to Namakhvani HPP project

Impairment of assets related to Namakhvani HPP project as at 31 December 2012 represent construction in progress of GEL 6,179 thousand and prepayments for current assets of GEL 1,307 for the construction of Namakhvani Hydro Power Plant.

Following the October 2012 parliamentary elections, the Government of Georgia's strategy in terms of constructing large hydro power plants is being reviewed. The construction of Namakhvani Hydro Power Plant was put on hold because during the preparation of the detailed project design of the plant, international consultants have identified the need for additional geological and hydrological studies. In light of these circumstances and high level of uncertainty over the resumption of the project, the assets related to the construction of Namakhvani Hydro Power Plant were considered fully impaired.

11. Other expenses

'000 GEL	2012	2011
Banking, consulting and other professional services	2,278	766
Regulatory expenses	1,151	930
Materials granted to a state controlled entity	1,074	-
Representative and business trip expenses	604	558
Transportation, materials and repair and maintenance	451	398
Office and related equipment maintenance	446	395
Impairment of investment in other companies	266	115
Communication expenses	120	161
Other	2,317	2,727
	8,707	**6,050**

12. Other income

'000 GEL	2012	2011
Customer penalties for late payment	8,312	3,673
Oil processing	898	1,094
Other	1,928	807
	11,138	**5,574**

13. Finance income and finance costs

'000 GEL	2012	2011
Recognised in profit or loss		
Interest income on bank deposits	22,165	7,663
Interest income on loans given	4,024	-
Unwinding of discount on finance lease receivable	2,808	2,629
Reversal of impairment on trade and other receivables	-	926
Finance income	**28,997**	**11,218**
Interest expense on bond issue	(18,639)	-
Net foreign exchange loss	(456)	(667)
Interest expense on bank overdrafts	(176)	(731)
Interest expense on loans from the Government of Georgia	(60)	(300)
Finance costs	**(19,331)**	**(1,698)**
Net finance income recognised in profit or loss	**9,666**	**9,520**

14. Income tax expense

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

'000 GEL	2012	2011
Current tax expense		
Current year	11,634	13,577
Under provided in prior years	1,013	-
	12,647	**13,577**
Deferred tax (benefit)/expense		
Origination and reversal of temporary differences	(1,069)	2,697
	11,578	**16,274**

In 2012 current tax deduction of 5,517 thousand relating to the distribution of non-cash assets (2011: GEL 1,250 thousand) was recognised directly in equity.

Reconciliation of effective tax rate:

	2012		2011	
	'000 GEL	%	'000 GEL	%
Profit before income tax	92,604	100	130,346	100
Income tax at applicable tax rate	13,891	15	19,552	15
(Non-taxable income) / Non-deductible expenses	(907)	(1)	(668)	(1)
Under provided in prior years	1,013	1	-	-
Change in unrecognised temporary differences on finance lease receivable (note 23)	(2,419)	(3)	(2,610)	(2)
	11,578	**12**	**16,274**	**12**

15. Property, plant and equipment

'000 GEL	Gas and oil pipelines	Land and buildings	Oil wells	Plant and equipment	Other	CIP	Total
Cost							
Balance at 1 January 2011	230,618	31,310	29,834	8,904	10,128	11,713	322,507
Additions	1,256	449	-	333	1,633	49,675	53,346
Disposals	(27)	(1,702)	-	(3,742)	(7,232)	(4,269)	(16,972)
Balance at 31 December 2011	**231,847**	**30,057**	**29,834**	**5,495**	**4,529**	**57,119**	**358,881**
Balance at 1 January 2012	231,847	30,057	29,834	5,495	4,529	57,119	358,881
Additions	27,533	3,804	-	982	652	13,607	46,578
Disposals	(108)	(2)	-	(94)	(469)	(10,206)	(10,879)
Balance at 31 December 2012	**259,272**	**33,859**	**29,834**	**6,383**	**4,712**	**60,520**	**394,580**
Depreciation and impairment losses							
Balance at 1 January 2011	68,508	6,618	12,986	5,056	4,312	188	97,668
Depreciation for the year	14,887	741	2,892	995	1,306	-	20,821
Disposals	-	(158)	-	(1,565)	(3,034)	(64)	(4,821)
Impairment loss reversal	(21,983)	(3,988)	-	-	(298)	(124)	(26,393)
Balance at 31 December 2011	**61,412**	**3,213**	**15,878**	**4,486**	**2,286**	**-**	**87,275**
Balance at 1 January 2012	61,412	3,213	15,878	4,486	2,286	-	87,275
Depreciation for the year	15,815	615	1,603	316	313	-	18,662
Disposals	(35)	-	-	(76)	(75)	-	(186)
Impairment loss (note 10)	-	-	-	-	-	6,179	6,179
Balance at 31 December 2012	**77,192**	**3,828**	**17,481**	**4,726**	**2,524**	**6,179**	**111,930**
Carrying amounts							
At 1 January 2011	162,110	24,692	16,848	3,848	5,816	11,525	224,839
At 31 December 2011	170,435	26,844	13,956	1,009	2,243	57,119	271,606
At 31 December 2012	**182,080**	**30,031**	**12,353**	**1,657**	**2,188**	**54,341**	**282,650**

During 2012 the Government of Georgia contributed certain land plots and gas and oil pipelines in the form of an increase in share capital. The share capital has been increased by the nominal amount of these assets of GEL 30,833 thousand which approximates the fair value of these assets (2011: nominal value of GEL 10,900 thousand which approximate the fair value of these assets), which are included in total additions of GEL 46,578 thousand (2011: GEL 53,346 thousand). The basis for determining fair values is disclosed in note 5.

Included in total disposals with a carrying amount of GEL 10,693 thousand (2011: GEL 12,151 thousand) are assets with a carrying amount of GEL 10,218 thousand (2011: GEL 9,277 thousand) which have been withdrawn by the Government of Georgia through a distribution from retained earnings (2011: GEL 2,852 thousand deducted from additional paid in capital and decrease in retained earnings of GEL 6,425 thousand due to transfer of 100% shares of Georgian Gas Transportation Company LLC). The assets with a carrying amount of GEL 10,218 thousand are included in electric lines and substations distributed to the Government of Georgia with a total carrying amount of GEL 36,779 thousand. Out of the total distribution of GEL 36,779 thousand, assets with a carrying amount of GEL 20,728 thousand were classified as non-current assets held for distribution as at 31 December 2011.

(a) Impairment loss and subsequent reversal

As at 31 December 2009, following a decline in gas prices, the economic slowdown in the Republic of Armenia and Georgia and the related significant decline in the gas consumption of both countries in 2009, the Group determined that there was an indication of impairment of its property, plant and equipment of the gas transportation business. The Group estimated the recoverable amount of the property, plant and equipment based on its value in use. Based on the assessment, the carrying amount of the property, plant and equipment was determined to be GEL 75,909 thousand higher than its recoverable amount, and an impairment loss of GEL 75,909 thousand was recognized as at 31 December 2009.

In 2010, following certain increase in gas prices and economic activity in Georgia, as well as a change in the Group's contractual arrangements, the Group reassessed its estimate of the recoverable amount of the property, plant and equipment of the gas transportation business and GEL 43,150 thousand of the initially recognized impairment was reversed as at 31 December 2010.

In 2011, following the transfer of shares of Georgian Gas Transportation Company LLC (see note 7), the Group's business model for the gas transportation business has changed significantly.

As a result of this change in the business model, when making investment decisions in relation to the gas pipelines, management also considers the cash flows generated from the sale and purchase of gas from Azerbaijan, which was previously considered a separate cash generating unit.

Management has reassessed the recoverable amount of the pipeline network based on the new cash generating unit and, as a consequence, the previously recognized impairment loss has been fully reversed as at 31 December 2011.

The impairment loss and its subsequent reversal were allocated pro rata to property, plant and equipment constituting the gas transportation business.

16. Finance lease receivable

In 1996 the Government of Georgia entered into a 30 year arrangement with a consortium of oil companies that undertook construction and development of a pipeline system from the border with Azerbaijan to the Supsa oil terminal on the Georgian Black Sea coast. The arrangement granted the oil companies the right to transport of oil across the territory of Georgia through that pipeline system. The pipeline infrastructure on Georgian territory became the property of the Government of Georgia and ownership of this infrastructure was transferred to the Company in June-July 2010 through a contribution to the charter capital of the Company with a nominal value of GEL 269,299 thousand. In exchange for the oil companies use of the pipeline, the Group receives a transit fee for each barrel of oil transported through the pipeline. Management has determined that the initial arrangement contained a finance lease at inception.

The Group has recognized a lease receivable of GEL 39,229 thousand at the date that title was transferred to the business. The lease receivable is the present value of the net investment in the lease comprising the present value of the assets' unguaranteed residual value at the end of the lease term. The difference of GEL 230,070 thousand between the nominal amount and the present value of the net investment in the lease has been recognized in equity as fair value adjustment for non-cash owner contributions.

'000 GEL	2012	2011
Balance at beginning of the year	43,074	40,445
Unwinding of discount on finance lease receivable	2,808	2,629
Balance at end of the year	**45,882**	**43,074**

Contingent rents related to oil transportation recognized in the consolidated statement of comprehensive income during 2012 amounted to GEL 11,562 thousand (2011: GEL 10,970 thousand).

17. Loans given

'000 GEL	2012	2011
Non-current		
Loan given to the shareholder	85,322	-
Current		
Loans given to state controlled entity	48,714	-
	134,036	-

Loan given to the shareholder bears a contractual rate of interest of 9% per annum and is repayable in equal semi-annual instalments from 2015 to 2019. The loan was given for the purpose of construction of Gardabani Thermo Electric Power Station. Also see note 30.

Loans given to state controlled entity bear a contractual rate of interest of 11% per annum and are repayable on maturity in 2013. The National Agency of State Property of the Ministry of Economy and Sustainable Development of Georgia has confirmed its intent to provide support to the extent permitted by the Georgian legislation, if required, to the state controlled entity to enable it to repay these loans.

The Group's exposure to credit risks and impairment losses related to loans are disclosed in note 25.

18. Term deposits

Terms and conditions of the term deposits are as follows:

				31 December 2012		31 December 2011	
'000 GEL	Currency	Nominal interest rate	Year of maturity	Face value	Carrying amount	Face value	Carrying amount
Non-current term deposit	USD	7.125%-8%	2014-2017	105,426	105,426	-	-
				105,426	**105,426**	**-**	**-**
Current term deposits	USD	10.25% - 11.25%	2013	52,854	52,854	-	-
				52,854	**52,854**	**-**	**-**

The Group's non-current term deposits include GEL 16,567 thousand (2011: nil) which have been pledged as collateral for a loan obtained by a state controlled entity. The Ministry of Agriculture has confirmed that relevant funding has been included in its 2013 budget for repayment of the loan obtained by the state controlled entity.

The Group's exposure to credit and currency risks and impairment losses related to term deposits are disclosed in note 25.

19. Trade and other receivables

'000 GEL	2012	2011
Trade receivables	86,163	30,357
Other receivables	237	13
	86,400	**30,370**

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 25.

20. Cash and cash equivalents

'000 GEL	2012	2011
Current accounts in banks	19,828	35,079
Call deposits	122,844	-
Cash and cash equivalents in the consolidated statement of cash flows and in the consolidated statement of financial position	**142,672**	**35,079**

Call deposits represent term deposits with banks with maturities greater than three months from the acquisition date but for which the Group has the unilateral right to withdraw the deposits within a few days of providing notification without incurring significant penalties or loss of interest. Consequently, these term deposits have been classified in accordance with their nature which is that of a call deposit.

The Group's exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities are disclosed in note 25.

21. Equity

(a) Share capital

Number of shares unless otherwise stated	Ordinary shares	
	2012	**2011**
Par value	GEL 20	GEL 20
On issue at 1 January /1 September	23,938,610	23,916,265
Issue of shares in exchange for non-cash assets	1,532,430	22,345
Acquisition of own shares in exchange for non-cash assets	(6,140)	-
On issue at 31 December	25,464,900	23,938,610

Ordinary shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time, and are entitled to one vote per share at meetings of the Company.

(b) Additional paid in capital

Additional paid in capital represents benefits provided to the Group by the Government of Georgia acting in its role of the shareholder and non-cash assets transferred by the Group to the Government of Georgia.

(c) Dividends and other distributions to shareholders

In 2012 dividends of GEL 40,000 thousand were declared and GEL 47,500 thousand paid (2011: GEL 45,000 thousand declared and GEL 5,500 thousand paid).

In 2011, upon request of the shareholder, the Company agreed to pay GEL 4,200 thousand to a State-owned fund out of which GEL 2,200 thousand and GEL 2,000 thousand were paid during 2012 and 2011, respectively.

In 2012 non-cash assets with a carrying amount of GEL 36,779 thousand were transferred to the shareholder (2011: GEL 8,332 thousand).

22. 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 25.

'000 GEL	2012	2011
Non-current liabilities		
Unsecured bond issue	406,183	-
Loans issued by the Government of Georgia	-	654
	406,183	**654**
Current liabilities		
Current portion of unsecured bond issue	4,423	-
Current portion of loans issued by the Government of Georgia	667	1,950
Bank overdraft	-	8,412
	5,090	**10,362**

Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

				31 December 2012		31 December 2011	
'000 GEL	Currency	Nominal interest rate	Year of maturity	Face value	Carrying amount	Face value	Carrying amount
Unsecured bond issue	USD	6.875%	2017	414,175	410,606	-	-
Loans issued by the Government of Georgia	GEL	0.5%	2013	617	667	1,162	1,026
Loans issued by the Government of Georgia	GEL	7%	2012	-	-	1,620	1,578
Bank overdraft	USD	9%	2012	-	-	8,412	8,412
Total interest-bearing liabilities				414,792	411,273	11,194	11,016

In May 2012, the Group issued Eurobonds with face value of USD 250 mln maturing in 2017 in London Stock Exchange. The bonds bear a contractual rate of interest of 6.875% per annum on the nominal amount. The proceeds initially were planned to be used for Namakhvani Hydro Power Plant cascade construction and for general corporate purposes. Subsequent to 31 December 2012 the Group plans to use the proceeds for Gardabani CCPP construction (see note 30).

23. Deferred tax assets and liabilities

(a) Unrecognised deferred tax assets

No deferred tax asset has been recognized for the temporary difference between the tax and accounting base of the finance lease receivable that was contributed during 2010 (see note 16). Management has not recognized deferred tax on this temporary difference as the initial recognition of the financial lease affected neither accounting nor taxable profit or loss.

The unrecognised deferred tax asset on the above transaction as at 31 December 2012 is GEL 26,665 thousand (2011: GEL 29,084 thousand).

(b) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
'000 GEL	2012	2011	2012	2011	2012	2011
Property, plant and equipment	-	-	(11,281)	(11,059)	(11,281)	(11,059)
Inventories	1,466	240	-	-	1,466	240
Loans and borrowings	75	-	-	(32)	75	(32)
Trade and other receivables	174	216	-	-	174	216
Tax (assets)/liabilities	1,715	456	(11,281)	(11,091)	(9,566)	(10,635)
Set off of tax	(1,715)	(456)	1,715	456	-	-
Net tax (assets)/liabilities	**-**	**-**	**(9,566)**	**(10,635)**	**(9,566)**	**(10,635)**

Movement in temporary differences during the year:

'000 GEL	1 January 2012	Recognised in profit or loss	31 December 2012
Property, plant and equipment	(11,059)	(222)	(11,281)
Inventories	240	1,226	1,466
Trade and other receivables	216	(42)	174
Loans and borrowings	(32)	107	75
	(10,635)	**1,069**	**(9,566)**

'000 GEL	1 January 2011	Recognised in profit or loss	Disposed off	31 December 2011
Property, plant and equipment	(8,879)	(2,836)	656	(11,059)
Inventories	521	240	(521)	240
Trade and other receivables	1,119	(140)	(763)	216
Loans and borrowings	(71)	39	-	(32)
	(7,310)	**(2,697)**	**(628)**	**(10,635)**

24. Trade and other payables

'000 GEL	2011	2011
Trade payables	24,778	2,636
Other payables	44	49
	24,822	**2,685**

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 25.

25. Financial instruments and risk management

(a) Overview

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

- credit risk
- liquidity risk
- market risk

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.

The Executive Directors have 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.

(b) 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, loans given, term deposits and cash and cash equivalents.

(i) *Exposure to credit risk*

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was as follows:

	Carrying amount	
'000 GEL	**2012**	**2011**
Trade and other receivables	86,400	30,370
Loans given	134,036	-
Term deposits	158,280	-
Cash and cash equivalents	142,672	35,079
	521,388	**65,449**

As at 31 December 2012 the Group had placements with 2 banks whose balances exceeded 10% of total term deposits and cash and cash equivalents (31 December 2011: 1 bank). The carrying value of these balances as of 31 December 2012 was GEL 266,587 thousand (31 December 2011: GEL 35,042 thousand). The long-term credit rating of the Banks according to Standard & Poors as at 31 December 2012 was BB-.

(ii) *Trade and other receivables*

Credit risk is managed by requesting prepayments from customers or assessing their creditworthiness prior to extending credit. 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 components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

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

	Carrying amount	
'000 GEL	**2012**	**2011**
Domestic	80,145	26,021
Euro-zone countries	5,112	3,668
CIS countries	906	668
	86,163	**30,357**

The maximum exposure to credit risk for trade receivables at the reporting date by type of customer was:

	Carrying amount	
'000 GEL	**2012**	**2011**
Gas distributors	79,600	25,675
Others	6,562	4,682
	86,163	**30,357**

As at 31 December 2012 the Group had one customer whose balances exceeded 10% of total trade receivables (31 December 2011: two customers). The carrying value of these balances as of 31 December 2012 was GEL 78,819 thousand (31 December 2011: GEL 27,986 thousand).

Impairment losses

The aging of trade and other receivables at the reporting date was:

'000 GEL	Gross 2012	Impairment 2012	Gross 2011	Impairment 2011
Not past due	43,119	-	15,778	-
Past due 0- 30 days	25,321	-	14,324	-
Past due 31-120 days	17,879	-	195	-
Past due more than one year	1,525	1,444	1,517	1,444
	87,844	**1,444**	**31,814**	**1,444**

The Group believes that the unimpaired amounts that are past due by more than 30 days are still collectible, based on historic payment behaviour and analysis of customer credit risk.

(iii) Loans given

The Group provided loans to the shareholder (see note 17) and a state controlled entity. The loans are not overdue and management expects that the amounts are collectible based on an analysis of the borrowers' credit risk. In assessing the recoverability of the loan to the state controlled entity, the Group also considered the intent from the Government of Georgia to provide support to repay the loan at maturity should the state controlled entity be unable to.

(c) 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's liquidity management also involves monitoring the covenants embedded in the bond issue agreement.

Typically the Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of 60 days, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. In addition, the Group maintains a USD 53,000 thousand unused overdraft facility that is unsecured. Interest on this facility is payable at the rate of 8.69%-9.69%.

The Group has contractual commitments for construction and purchase of pipes (see note 26).

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements.

2012

	Carrying amount	Contractual cash flows	0-6 mths	6-12 mths	1-2 yrs	2-3 yrs	3-5 yrs	Over 5 yrs
Non-derivative financial liabilities								
Unsecured bond issues	410,606	542,309	14,237	14,237	28,474	28,474	456,887	-
Loans issued by the Government of Georgia	667	667	667	-	-	-	-	
Trade and other payables	24,822	24,822	24,822	-	-	-	-	-
	436,095	**567,798**	**39,726**	**14,237**	**28,474**	**28,474**	**456,887**	-

2011

	Carrying amount	Contractual cash flows	0-6 mths	6-12 mths	1-2 yrs	2-3 yrs	3-5 yrs	Over 5 yrs
Non-derivative financial liabilities								
Unsecured bond issues	2,604	2,782	1,620	330	832	-	-	-
Loans issued by the Government of Georgia	8,412	8,412	8,412	-	-	-	-	-
Trade and other payables	2,685	2,685	2,685	-	-	-	-	-
	13,701	**13,879**	**12,717**	**330**	**832**	-	-	-

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

(d) 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.

(i) Currency risk

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the respective functional currencies of Group entities. The currency in which these transactions primarily are denominated is USD. The Company generally does not hedge its exposure to foreign 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 2012	USD-denominated 2011
Trade and other receivables	5,112	4,753
Loans given	134,036	-
Term deposits	158,280	-
Cash and cash equivalents	126,027	52
Trade and other payables	(20,826)	(29)
Loans and borrowings	(410,606)	(8,412)
Net exposure	**(7,977)**	**(3,636)**

The following significant exchange rates applied during the year:

in GEL	Average rate		Reporting date spot rate	
	2012	2011	2012	2011
USD	1.6513	1.6703	1.6567	1.6860

Sensitivity analysis

A 10% strengthening of the GEL, as indicated below, against USD at 31 December would have increased/(decreased) profit or loss for the year by the amounts shown below. 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 2011.

'000 GEL	Profit or loss
31 December 2012	678
31 December 2011	309

A weakening of the GEL against USD at 31 December would have had the equal but opposite effect to the amounts shown above, on the basis that all other variables remain constant. There would be no impact directly in equity as a result of foreign currency fluctuations.

(ii) 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:

	Carrying amount	
'000 GEL	**2012**	**2011**
Fixed rate instruments		
Loans given	134,036	-
Term deposits	158,280	-
Loans and borrowings	(411,273)	(11,016)
	(118,957)	**(11,016)**

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.

Fair values versus carrying amounts

Management believes that the fair value of the Group's financial assets and liabilities approximates their carrying amounts. The basis for determining fair values is disclosed in note 5.

The interest rates used to discount estimated cash flows, where applicable, are based on the government yield curve at the reporting date plus an adequate credit spread, and were as follows:

	2012	2011
Financial assets and liabilities	7.5%-12%	9%-13%

(e) 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, and to maintain confidence of market participants. 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. With these measures the Group aims for steady profits growth.

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.

26. Capital commitments

During the year ended 31 December 2012 the Group entered into contracts for construction and purchase of pipes for GEL 25 thousand (2011: GEL 27,455 thousand).

As at 31 December 2012 the Group has commitments related to the construction of Namakhvani HPP cascade of GEL 17,388 thousand (2011: nil). The construction has been suspended and the Group is in the process of terminating the construction related agreements (see notes 10 and 30). These agreements are cancellable without penalty on a written notice from the Group and management assesses that the termination of the agreements will not result in a significant cash outflow to the Group.

27. Contingencies

(a) Insurance

The insurance industry in the 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

The Group is defending a claim brought to the courts in 2010 by a foreign company that is seeking contractual payments and interest accrued for non-payment as well as other damages and lost profits from non-performance of a contract concluded in 2003 to 2004 by the Company. In 2010, the Group hired legal advisors to represent the Group in the dispute. The Group disputes the validity of the claim. Management assesses the likelihood that the Group will be required to make a contractual payment of USD 5 million to the foreign company as possible. Management assesses the probability that the Group will also be required to pay accrued interest as well as other damages and lost profits as remote.

(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.

(d) Environmental matters

The enforcement of environmental regulation in Georgia is evolving and the enforcement posture of government authorities is continually being reconsidered. The Company periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognized immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

28. Related party transactions

(a) Control relationships

The Company was wholly owned by the state of Georgia represented by the Ministry of Economic Development of Georgia as at 31 December 2010. In November 2011, 24% and in August 2012, the remaining 76% interest in Georgian Oil and Gas Corporation JSC was transferred to JSC Partnership Fund, a wholly state owned entity. The ultimate controlling party of the Group is the Government of Georgia.

(b) Transactions with key management personnel

(i) Key management remuneration

Key management received the following remuneration during the year, which is included in personnel costs:

'000 GEL	2012	2011
Salaries and bonuses	**1,010**	**935**

(c) Other related party transactions

The Group's other related party transactions are disclosed below. The transactions with Georgian Gas Transportation Company are presented from the date it was transferred to the Ministry of Energy and Natural Resources of Georgia. Transactions with the Government of Georgia are disclosed in notes 15, 16 and 21 of these consolidated financial statements.

(i) Revenue

	Transaction value for the year ended 31 December		Outstanding balance as at 31 December	
'000 GEL	**2012**	**2011**	**2012**	**2011**
State controlled entities:				
Rent of pipelines	38,390	11,049	-	-
Sale of gas and gas transportation	-	27	-	61
	38,390	**11,076**	-	**61**

(ii) Expenses

	Transaction value for the year ended 31 December		Outstanding balance as at 31 December	
'000 GEL	**2012**	**2011**	**2012**	**2011**
State controlled entities:				
Purchase of Gas	39,522	5,472	785	1,402
Materials granted	1,074	-	-	-
	40,596	**5,472**	**785**	**1,402**

(iii) Loans

'000 GEL	Interest expense		Outstanding balance	
	2012	**2011**	**2012**	**2011**
Loans given:				
Shareholder	2,490	-	85,322	-
State controlled entity	1,534	-	48,714	-
	4,024	-	**134,036**	-
Loans received:				
State controlled entities	-	300	667	2,604
	-	300	667	**2,604**

29. Significant subsidiaries

In January 2012 a new subsidiary, JSC Namakhvani Hes Cascade, was created with charter capital of GEL 20,000 thousand (paid capital as at 31 December 2012: GEL 8,766 thousand). The subsidiary was created for the construction of Namakhvani HPP cascade. As at 31 December 2012 the construction was suspended (see note 10).

At 31 December 2012, the Company did not have any significant subsidiaries.

30. Events subsequent to the reporting date

In February 2013, JSC Partnership Fund commenced construction of the Gardabani Thermo Electric Power Station (Gardabani CCPP) and announced that it is envisaged that the loan of USD 50 million from the Group to JSC Partnership Fund used for the advance payment to the contractor of the project will be fully converted into equity holding of the Company in Gardabani CCPP.

The estimated project cost is USD 205 million and the Group will use the proceeds from its issuance of Eurobonds to fund the project. The construction works are planned to be completed by the end of 2014. The Gardabani CCPP is expected to be fully operational from 2015.

The JSC Partnership Fund also announced that in the event of the resumption of the Namakhvani project, the Group will not be responsible for funding the Namakhvani HPP construction.