Georgian Oil and Gas Corporation JSC

Consolidated Financial Statements for 2013

Contents

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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 2013, and the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

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

KPMG Georgia LLC
25 June 2014

KPMG Georgia LLC

LIMITED LIABILITY COMPANY
404437695
KPMG Georgia

'000 GEL	Note	2013	2012
Assets			
Property, plant and equipment	12	269,576	282,650
Prepayments for non-current assets	23	199,832	-
Intangible assets		114	165
Finance lease receivable	13	48,864	45,882
Loans given	14	89,136	85,322
Other non-current assets		-	107
Term deposits	15	40,083	105,426
Non-current assets		**647,605**	**519,552**
Loans given	14	47,055	48,714
Non-current assets held for distribution		1,141	-
Inventories		657	535
Current tax assets		1,081	6,621
Taxes other than on income		732	990
Prepayments for current assets and expenses		20,058	19,972
Trade and other receivables	16	63,530	86,400
Term deposits	15	78,493	52,854
Cash and cash equivalents	17	194,541	142,672
Current assets		**407,288**	**358,758**
Total assets		**1,054,893**	**878,310**
Equity	18, 19		
Share capital		509,550	509,298
Additional paid in capital		71,718	71,718
Fair value adjustment reserve for non-cash owner contributions		(282,181)	(282,181)
Retained earnings		186,393	99,924
Equity attributable to owners of the Company		**485,480**	**398,759**
Non-controlling interests		83,443	-
Total equity		**568,923**	**398,759**
Liabilities			
Loans and borrowings	20	425,699	406,183
Deferred tax liabilities	11	16,486	9,566
Non-current liabilities		**442,185**	**415,749**
Loans and borrowings	20	6,126	5,090
Trade and other payables	21	30,656	24,822
Dividend payable		-	32,000
Value added tax payable		5,317	1,890
Provisions		1,686	-
Current liabilities		**43,785**	**63,802**
Total liabilities		**485,970**	**479,551**
Total equity and liabilities		**1,054,893**	**878,310**

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 40.

'000 GEL	Note	2013	2012
Revenue	6	325,761	299,551
Cost of gas and oil		(198,483)	(178,230)
Depreciation		(18,241)	(18,662)
Personnel costs		(7,303)	(8,508)
Taxes, other than on income		(6,096)	(6,158)
Impairment of assets related to Namakhvani project	7	-	(7,486)
Other expenses	8	(9,185)	(8,707)
Other income	9	13,906	11,138
Results from operating activities		**100,359**	**82,938**
Finance income	10	40, 727	28,997
Finance costs	10	(29,483)	(19,331)
Net finance income		**11,244**	**9,666**
Profit before income tax		**111,603**	**92,604**
Income tax expense	11	(17,310)	(11,578)
Profit and total comprehensive income for the year		**94,293**	**81,026**
Profit and total comprehensive income attributable to:			
Owners of the Company		94,828	81,026
Non-controlling interests		(535)	-
		94,293	**81,026**

These consolidated financial statements were approved by management on 25 June 2014 and were signed on its behalf by:

David Tvalabeishvili
General Director

David Vardiashvili
Financial Director

The consolidated statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 40.

	Attributable to equity holders of the Company						
'000 GEL	**Share capital**	**Fair value adjustment reserve for non-cash owner contributions**	**APIC**	**Retained earnings**	**Total**	**Non-controlling interests**	**Total equity**
Balance at 1 January 2012	478,772	(282,181)	71,718	90,160	358,469	-	358,469
Total comprehensive income for the year							
Profit and total comprehensive income for the year	-	-	-	81,026	81,026	-	81,026
Contributions by and distributions owners							
Dividends to equity holders	-	-	-	(40,000)	(40,000)	-	(40,000)
Distributions of non-cash assets net of tax of GEL 5,517 thousand	-	-	-	(31,262)	(31,262)	-	(31,262)
Increase in share capital	30,833	-	-	-	30,833	-	30,833
Decrease in share capital	(307)	-	-	-	(307)	-	(307)
Balance at 31 December 2012	**509,298**	**(282,181)**	**71,718**	**99,924**	**398,759**	**-**	**398,759**
Balance at 1 January 2013	509,298	(282,181)	71,718	99,924	398,759	-	398,759
Total comprehensive income for the year							
Profit and total comprehensive income for the year	-	-	-	94,828	94,828	(535)	94,293
Contributions by and distributions to owners							
Dividends to equity holders (see note 18(c))	-	-	-	(8,359)	(8,359)	-	(8,359)
Increase in share capital	252	-	-	-	252	-	252
Total contributions by and distributions to owners	**252**	**-**	**-**	**86,469**	**86,721**	**(535)**	**86,186**
Changes in ownership interests							
Foundation of subsidiary with non-controlling interests (see note 23)	-	-	-	-		83,978	83,978
Balance at 31 December 2013	**509,550**	**(282,181)**	**71,718**	**186,393**	**485,480**	**83,443**	**568,923**

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 40.

	Note	2013	2012
'000 GEL			
Cash flows from operating activities			
Cash receipts from customers		373,138	263,856
Cash paid to suppliers and employees		(222,161)	(178,389)
Cash from operations before income taxes and interest		**150,977**	**85,467**
Income tax paid		(4,460)	(12,996)
Interest paid		(28,512)	(14,323)
Interest received		34,076	7,415
Net cash from operating activities		**152,081**	**65,563**
Cash flows from investing activities			
Acquisition of property, plant and equipment and intangible assets		(117,525)	(23,111)
Decrease/(increase) in term deposit		49,081	(140,751)
Repayment of loans given		3,707	-
Loans given		-	(130,029)
Acquisition of non-current assets held for distribution		-	(6,643)
Investing in other companies		-	(107)
Net cash used in investing activities		**(64,737)**	**(300,641)**
Cash flows from financing activities			
Dividends paid		(40,359)	(47,500)
Proceeds from borrowings		-	397,433
Repayment of borrowings		(628)	(10,541)
Other cash distributions to owners		-	(2,200)
Net cash (used in)/from financing activities		**(40,987)**	**337,192**
Net increase in cash and cash equivalents		**46,357**	**102,114**
Cash and cash equivalents at 1 January		142,672	35,079
Effect of exchange rate fluctuations on cash and cash equivalents		5,512	5,479
Cash and cash equivalents at 31 December	17	**194,541**	**142,672**

During 2013 and 2012 the Group received non-cash contributions and made non-cash distributions to the Government of Georgia (see note 12 and 18).

During 2013 the Group founded a subsidiary, LLC Gardabani TPP. JSC Partnership Fund's 49% contribution in the charter capital of GEL 83,978 thousand represented prepayments for non-current assets of the subsidiary (see note 23).

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 40.

1. Reporting entity

(a) Organisation and operations

Georgian Oil and Gas Corporation JSC (the "Company") and its subsidiaries (the "Group") comprise Georgian Joint Stock and Limited Liability Companies as defined in the "Law of Georgia on Entrepreneurs". 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 26.

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.

Since December 2006, the Company has been granted the status of "National Oil Company" 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

The Group's operations are 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 the 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 accounting

(a) Statement of compliance

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

3. Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL"), which is the Company's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in GEL has been rounded to the nearest thousand.

4. Use of estimates and judgments

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

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

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

- Note 13 Finance lease receivable – determination of whether the arrangement contains a lease and the fair value of the unguaranteed residual value;
- Note 17 Cash and cash equivalents – classification of term deposits with original maturities of more than three months as cash and cash equivalents;
- Note 11 Deferred tax assets and liabilities – determination of whether to recognise a temporary difference on initial recognition of the financial lease receivable;
- Note 23 Significant subsidiaries – determination of control over subsidiaries.

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 15 Term deposits - recoverability of the term deposit pledged as collateral for a loan obtained by a state controlled entity;
- Note 22 (b) Credit risk – impairment of trade and other receivables and loans given;
- Note 24 Capital commitments – termination of agreements related to Namakhvani project;
- Note 25 Contingencies – litigation.

Measurement of fair values

Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

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

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

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values is included in note 22 (a) - financial instruments.

5. Operating segments

As at 31 December 2013 and 2012, 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:

- *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.
- *Upstream activities*. Includes sale of oil from production sharing arrangements.
- *Oil transportation*. Includes rental income from transportation of oil through the territory of Georgia.

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**	
'000 GEL	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**
External revenues	240,619	232,402	42,666	39,592	30,524	15,995	11,952	11,562	325,761	299,551
Cost of gas and oil	(198,483)	(178,230)	-	-	-	-	-	-	(198,483)	(178,230)
Reportable segment profit before unallocated costs, net finance cost and income tax	42,136	54,172	42,666	39,592	30,524	15,995	11,952	11,562	127,278	121,321

’000 GEL	**2013**	**2012**
Revenues		
Total revenue for reportable segments	325,761	299,551
Profit or loss		
Total profit or loss for reportable segments	127,278	121,321
Unallocated personnel expenses	(7,303)	(8,508)
Unallocated depreciation expenses	(18,241)	(18,662)
Net finance income	11,244	9,666
Other net unallocated costs	(1,375)	(11,213)
Consolidated profit before income tax	**111,603**	**92,604**

(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 2013, one customer of the Group’s gas supply segment represented approximately 73% of the Group’s total revenue or GEL 238,309 thousand (2012: 77% or GEL 230,131 thousand).

6. Revenue

’000 GEL	**2013**	**2012**
Sales of gas	240,619	232,402
Rent of gas pipelines	42,666	39,592
Income from crude oil	30,524	15,995
Oil transportation fee	11,952	11,562
Total revenues	**325,761**	**299,551**

The Company rents its gas pipeline to Georgian Gas Transportation Company LLC. The contract is valid until 1 January 2020. The lease payments are contingent on the volume of gas transported through the leased gas pipeline.

7. 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 thousand 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 has been 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. In April 2014, Namakhvani HPP was transferred to the Government of Georgia (see note 27).

8. Other expenses

'000 GEL	**2013**	**2012**
Provision for litigation case	1,686	-
Banking, consulting and other professional services	1,161	2,278
Regulatory expenses	721	1,151
Representative and business trip expenses	517	604
Office and related equipment maintenance	364	446
Transportation, materials and repair and maintenance	328	451
Materials granted to a state controlled entity	-	1,074
Impairment of investment in other companies	-	266
Other	4,408	2,437
	9,185	**8,707**

9. Other income

'000 GEL	**2013**	**2012**
Customer penalties for late payment	10,161	8,312
Oil processing	1,109	898
Other	2,636	1,928
	13,906	**11,138**

10. Finance income and finance costs

'000 GEL	**2013**	**2012**
Recognised in profit or loss		
Interest income on bank deposits	24,450	22,165
Interest income on loans given	13,295	4,024
Unwinding of discount on finance lease receivable	2,982	2,808
Finance income	**40,727**	**28,997**
Interest expense on bond issue	(29,032)	(18,639)
Net foreign exchange loss	(451)	(456)
Interest expense on bank overdrafts	-	(176)
Interest expense on loans from the Government of Georgia	-	(60)
Finance costs	**(29,483)**	**(19,331)**
Net finance income recognised in profit or loss	**11,244**	**9,666**

11. Income tax expense

(a) Amount recognized in profit and loss

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

'000 GEL	**2013**	**2012**
Current tax expense		
Current year	8,225	11,634
Under provided in prior years	2,165	1,013
	10,390	**12,647**
Deferred tax expense/(benefit)		
Origination and reversal of temporary differences	6,920	(1,069)
	17,310	**11,578**

(b) Recognized in equity

In 2012 current tax deducton of GEL 5,517 thousand relating to distribution of non-cash assets was recognized directly in equity.

Reconciliation of effective tax rate:

	2013		2012	
	’000 GEL	**%**	**’000 GEL**	**%**
Profit before income tax	111,603	100	92,604	100
Income tax at applicable tax rate	16,740	15	13,891	15
Non-deductible expenses / (Non-taxable income)	648	1	(907)	(1)
Under provided in prior years	2,165	2	1,013	1
Change in unrecognised temporary differences on finance lease receivable	(2,243)	(2)	(2,419)	(3)
	17,310	**16**	**11,578**	**12**

(c) 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 13). 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 2013 is GEL 24,422 thousand (2012: GEL 26,665 thousand).

(d) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
’000 GEL	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**
Property, plant and equipment	-	-	(17,306)	(11,281)	(17,306)	(11,281)
Inventories	280	1,466		-	280	1,466
Trade and other receivables	203	174		-	203	174
Loans and borrowings	337	75		-	337	75
Tax (assets)/liabilities	820	1,715	(17,306)	(11,281)	(16,486)	(9,566)
Set off of tax	(820)	(1,715)	820	1,715	-	-
Net tax (assets)/liabilities	**-**	**-**	**(16,486)**	**(9,566)**	**(16,486)**	**(9,566)**

Movement in temporary differences during the year:

’000 GEL	**1 January 2013**	**Recognised in profit or loss**	**31 December 2013**
Property, plant and equipment	(11,281)	(6,025)	(17,306)
Inventories	1,466	(1,186)	280
Trade and other receivables	174	29	203
Loans and borrowings	75	262	337
	(9,566)	**(6,920)**	**(16,486)**

’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)**

12. 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 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**
Balance at 1 January 2013	259,272	33,859	29,834	6,383	4,712	60,520	394,580
Additions	51	1,626	-	807	616	3,263	6,363
Transfers	43,853	-	-	-	-	(43,853)	-
Disposals	-	(481)	-	(203)	(537)	-	(1,221)
Balance at 31 December 2013	**303,176**	**35,004**	**29,834**	**6,987**	**4,791**	**19,930**	**399,722**
Depreciation and impairment losses							
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	-	-	-	-	-	6,179	6,179
Balance at 31 December 2012	**77,192**	**3,828**	**17,481**	**4,726**	**2,524**	**6,179**	**111,930**
Balance at 1 January 2013	77,192	3,828	17,481	4,726	2,524	6,179	111,930
Depreciation for the year	15,297	622	1,603	322	385	-	18,229
Disposals	-	-	-	-	(13)	-	(13)
Balance at 31 December 2013	**92,489**	**4,450**	**19,084**	**5,048**	**2,896**	**6,179**	**130,146**
Carrying amounts							
At 1 January 2012	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
At 31 December 2013	**210,687**	**30,554**	**10,750**	**1,939**	**1,895**	**13,751**	**269,576**

During 2013 the Government of Georgia contributed certain land plots in the form of an increase in share capital. The share capital has been increased by the nominal amount of these assets of GEL 252 thousand which approximates the fair value of these assets (2012: nominal value of GEL 30,833 thousand which approximates the fair value of these assets), which are included in total additions of GEL 6,363 thousand (2012: GEL 46,578 thousand).

13. 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	**2013**	**2012**
Balance at beginning of the year	45,882	43,074
Unwinding of discount on finance lease receivable	2,982	2,808
Balance at end of the year	**48,864**	**45,882**

Contingent rents related to oil transportation recognized in the consolidated statement of comprehensive income during 2013 amounted to GEL 11,952 thousand (2012: GEL 11,562 thousand).

14. Loans given

’000 GEL	**2013**	**2012**
Non-current		
Loan given to the shareholder	89,136	85,322
Current		
Loans given to state controlled entity	47,055	48,714
	136,191	**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 Combined Cycle Power Plant (CCPP).

Loans given to state controlled entity bears a contractual rate of interest of 11% per annum and was overdue for over 2 months at 31 December 2013. In April 2014, the Group signed a restructuring agreement with the borrower. The contractual rate of interest was changed to 9.5% and a repayment schedule was agreed with payments scheduled from 2014 to 2017. 100% shares of a wholly owned subsidiary of the borrower with an estimated fair value approximating the carrying value of the loan were pledged to secure the loan given to state controlled entity. In addition management believes that the National Agency of State Property of the Ministry of Economy and Sustainable Development of Georgia will provide further 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 22.

15. Term deposits

Terms and conditions of the term deposits are as follows:

				31 December 2013		31 December 2012	
'000 GEL	**Currency**	**Nominal interest rate**	**Year of maturity**	**Face value**	**Carrying amount**	**Face value**	**Carrying amount**
Non-current term deposit	USD	7.125%	2017	40,083	40,083	105,426	105,426
				40,083	**40,083**	**105,426**	**105,426**
Current term deposits	USD	8%	2014	78,493	78,493	52,854	52,854
				78,493	**78,493**	**52,854**	**52,854**

The Group's non-current term deposits include GEL 17,363 thousand (2011: 16,567 thousand) which have been pledged as collateral for a loan obtained by a state controlled entity. The Ministry of Agriculture has confirmed its intent to provide support to the state controlled entity to enable it to repay the loan. The loan obtained by the state controlled entity was not overdue at 31 December 2013.

The Group's exposure to credit and currency risks and impairment losses related to term deposits are disclosed in note 22.

16. Trade and other receivables

'000 GEL	**2013**	**2012**
Trade receivables	63,143	86,163
Other receivables	387	237
	63,530	**86,400**

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 22.

17. Cash and cash equivalents

'000 GEL	**2013**	**2012**
Current accounts in banks	42,710	19,828
Call deposits	151,831	122,844
Cash and cash equivalents in the consolidated statement of cash flows and in the consolidated statement of financial position	**194,541**	**142,672**

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 22.

18. Equity

(a) Share capital

Number of shares unless otherwise stated	**Ordinary shares**	
	2013	**2012**
Par value	GEL 20	GEL 20
On issue at 1 January	25,464,900	23,938,610
Issue of shares in exchange for non-cash assets	12,576	1,532,430
Acquisition of own shares in exchange for non-cash assets	-	(6,140)
On issue at 31 December	25,477,476	25,464,900

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 distribution to shareholders

In 2013 dividends of GEL 8,359 thousand in total or GEL 0.328 per issued share were declared and GEL 40,359 thousand were paid (2012: GEL 40,000 thousand in total or GEL 1.57 per issued share were declared and GEL 47,500 thousand were paid).

In 2012 non-cash assets with a carrying amount of GEL 36,779 thousand were transferred to the shareholder.

(d) Non-controlling interests

Non-controlling interests (NCI) represents Partnership Fund JSC's contribution to the charter capital of the subsidiary, LLC Gardabani TPP (see note 23).

19. 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.

20. 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 22.

'000 GEL	**2013**	**2012**
Non-current liabilities		
Unsecured bond issue	425,699	406,183
	425,699	**406,183**
Current liabilities		
Current portion of unsecured bond issue	6,126	4,423
Current portion of loans issued by the Government of Georgia	-	667
	6,126	**5,090**

Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

				31 December 2013		**31 December 2012**	
'000 GEL	**Currency**	**Nominal interest rate**	**Year of maturity**	**Face value**	**Carrying amount**	**Face value**	**Carrying amount**
Unsecured bond issue	USD	6.875%	2017	434,075	431,825	414,175	410,606
Loans issued by the Government of Georgia	GEL	0.5%	2013	-	-	617	667
Total interest-bearing liabilities				**434,075**	**431,825**	**414,792**	**411,273**

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. The Namakhvani Hydro Power Plant was put on hold and the proceeds are planned to be used for the Gardabani Combined Cycle Power Plant (CCPP) construction (see note 23).

21. Trade and other payables

’000 GEL	2013	2012
Trade payables	30,597	24,778
Other payables	59	44
	30,656	**24,822**

The Group’s exposure to currency and liquidity risk related to trade and other payables is disclosed in note 22.

22. Fair values and risk management

(a) Accounting classifications and fair values

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

(i) Measurement of fair values

Financial instruments not measured at fair value

Type	Fair value	Valuation technique	Significant unobservable inputs
Financial assets	Level 2	Discounted cash flows	Not applicable
Financial liabilities	Level 2	Discounted cash flows	Not applicable

The carrying values of financial assets and liabilities of the Group are a reasonable approximation of their fair values.

(b) Financial risk management

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

- credit risk (see 22 (b)(ii));
- liquidity risk (see 22 (c));
- market risk (see 22 (d)).

(i) Risk management framework

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.

(ii) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers, loans given, term deposits and cash and cash equivalents.

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	**2013**	**2012**
Trade and other receivables	63,530	86,400
Loans given	136,191	134,036
Term deposits	118,576	158,280
Cash and cash equivalents	194,541	142,672
	512,838	**521,388**

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

	Carrying amount	
'000 GEL	**2013**	**2012**
Domestic	63,044	80,145
Euro-zone countries	8	5,112
CIS countries	91	906
	63,143	**86,163**

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

	Carrying amount	
'000 GEL	**2013**	**2012**
Gas distributors	61,935	79,600
Others	1,208	6,563
	63,143	**86,163**

As at 31 December 2013 the Group had one customer whose balances exceeded 10% of total trade receivables (31 December 2012: one customer). The carrying value of these balances as of 31 December 2013 was GEL 61,866 thousand (31 December 2012: GEL 78,819 thousand).

Impairment losses

The ageing of trade and other receivables the reporting date was as follows:

’000 GEL	Gross 2013	Impairment 2013	Gross 2012	Impairment 2012
Not past due	50,042	-	43,119	-
Past due 0- 30 days	12,538	-	25,321	-
Past due 31-120 days	950	-	17,879	-
Past due more than one year	1,444	1,444	1,525	1,444
	64,974	**1,444**	**87,844**	**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.

(iv) Loans given

The Group provided loans to the shareholder (see note 14) and a state controlled entity. The loan to the shareholder is not overdue and management expects that the amount is collectible based on an analysis of the borrower’s credit risk and financial performace.

The loan to the state controlled entity was past due as at 31 December 2013. In April 2014, the Group signed a restructuring agreement with the borrower. 100% of the shares of a wholly owned subsidiary of the borrower with an estimated fair value approximating the carrying value of the loan were pledged to secure the loan. Management believes that the loan is collectible based on the review of the value of collateral and willingness of the National Agency of State Property of the Ministry of Economy and Sustainable Development of Georgia to provide further support to the borrower to enable it to repay these loans. Cash and cash equivalents and term deposits.

As at 31 December 2013 the Group had placements with 2 banks whose balances exceeded 10% of total term deposits and cash and cash equivalents (31 December 2012: 2 banks). The carrying value of these balances as of 31 December 2013 was GEL 223,617 thousand (31 December 2012: GEL 266,587 thousand). The long-term credit rating of the Banks according to Fitch Ratings as at 31 December 2013 was BB-.

(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 17,000 thousand unused overdraft facility that is unsecured. Interest on this facility is payable at the rate of 8.5%.

The Group has contractual commitments for construction of cycle power plant and purchase of inventory (see note 24).

Exposure to liquidity risk

The following are the contractual maturities of financial liabilities at the reporting date. The amounts include estimated interest payments. It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

2013

	Carrying amount	Contractual cash flows	0-6 mths	6-12 mths	1-2 yrs	2-3 yrs	3-5 yrs
Non-derivative financial liabilities							
Unsecured bond issues	431,825	538,524	14,921	14,921	29,843	29,843	448,996
Trade and other payables	30,656	30,656	30,656	-	-	-	-
	462,481	**569,180**	**39,726**	**14,921**	**29,843**	**29,843**	**448,996**

2012

	Carrying amount	Contractual cash flows	0-6 mths	6-12 mths	1-2 yrs	2-3 yrs	3-5 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**

(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.

The Group's exposure to foreign currency risk was as follows:

Exposure to currency risk

'000 GEL	**USD-denominated 2013**	**USD-denominated 2012**
Trade and other receivables	1,569	5,112
Loans given	136,191	134,036
Term deposits	118,576	158,280
Cash and cash equivalents	171,176	126,027
Trade and other payables	(25,847)	(20,826)
Loans and borrowings	(431,825)	(410,606)
Net exposure	**(30,160)**	**(7,977)**

The following significant exchange rates have been applied during the year:

in GEL	**Average rate**		**Reporting date spot rate**	
	2013	**2012**	**2013**	**2012**
USD	1.6634	1.6513	1.7363	1.6567

Sensitivity analysis

A reasonably possible 10% strengthening of the GEL, as indicated below, against USD at 31 December would have affected the measurement of financial instruments denominated in a foreign currency and increased/(decreased) profit or loss by the amounts shown below. The analysis assumes that all other variables, in particular interest rates, remain constant and ignores any impact of forecast sales and purchases.

'000 GEL	**Profit or loss**
31 December 2013	2,564
31 December 2012	678

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.

Exposure to interest rate risk

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

	Carrying amount	
'000 GEL	**2013**	**2012**
Fixed rate instruments		
Loans given	136,191	134,036
Term deposits	118,576	158,280
Cash anc cash equivalents	194,541	142,672
Loans and borrowings	(431,825)	(411,273)
	17,483	**23,715**

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.

23. Significant subsidiaries

In October 2013 a new subsidiary, LLC Gardabani TPP, was created by the Company and JSC Partnership Fund with 51% and 49% interest respectively. The charter capital was defined at USD 100,000 thousand (paid charter capital as at 31 December 2013: GEL 170,296 thousand).

In accordance with the charter of the subsidiary, unanimous agreement is required for certain decisions. Management has concluded that the Group has control over the subsidiary because the Group is exposed to (has rights to) variable returns from its involvement with the subsidiary, and has the ability to affect those returns through its power over the subsidiary. The conclusion is based on the percentage of the ownership interest and the significance of decisions defined in the charter of the subsidiary for which only a simple majority of votes is required.

The subsidiary was created for the construction of Gardabani Combined Cycle Power Plant (CCPP). The construction works are planned to be completed by the end of 2015. The Gardabani CCPP is expected to be fully operational from 2016. As at 31 December 2013, the prepayment of GEL 199,832 thousands represents amounts paid to constructor and supervisor of the construction.

31 December 2013

’000 GEL	**LLC Gardabani TPP**
NCI percentage	49%
Non-current assets	201,738
Current assets	169
Non-current liabilities	(32,048)
Current liabilities	(658)
Net assets	169,201
Carrying amount of NCI	83,443
Revenue	-
Loss	(1,091)
Total comprehensive income	(1,091)
Loss allocated to NCI	(535)
Cash flows used in operating activities	(162)
Cash flows used in investment activities	(117,315)
Cash flows from financing activities (dividends to NCI: nil)	32,048
Net decrease in cash and cash equivalents	(85,429)

24. Capital commitments

The Group had entered into contracts for construction of the Gardabani Combined Cycle Power Plant (CCPP) and purchase of inventory with outstanding capital commitments of GEL 149,719 thousand at 31 December 2013 (2012: contract for construction of pipes of GEL 25 thousand).

As at 31 December 2013 the Group has commitments related to the construction of Namakhvani HPP cascade of GEL 18,056 thousand (2012: GEL 17,388 thousand). The construction has been suspended and the Group was in the process of terminating the construction related agreements (see note 7). 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. Later, the Company and the Government of Georgia signed an agreement to transfer JSC Namakhvani HPP to the Government of Georgia (see note 27). The commitments related to the Namakhvani HPP cascade were also transferred to the Government of Georgia.

25. 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.

26. Related party transactions

(a) Control relationships

As at 31 December 2013 and 2012 Georgian Oil and Gas Corporation JSC is wholly owned by JSC Partnership Fund. The ultimate controlling party of the Group is the Government of Georgia. The Group's parent company produces publicly available financial statements.

(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	2013	2012
Salaries and bonuses	**435**	**1,010**

(c) Other related party transactions

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

Management estimates that the aggregate amounts of other income and expenses and the related balances with Government-related entities, except as disclosed below are not significant.

The Group’s other related party transactions are disclosed below. Transactions with the Government of Georgia are disclosed in notes 12, 13 and 18 of these consolidated financial statements.

(i) Revenue

	Transaction value for the year ended 31 December		Outstanding balance as at 31 December	
’000 GEL	**2013**	**2012**	**2013**	**2012**
State controlled entities:				
Rent of pipelines	42,666	38,390	-	-
	42,666	**38,390**	**-**	**-**

(ii) Expenses

	Transaction value for the year ended 31 December		Outstanding balance as at 31 December	
’000 GEL	**2013**	**2012**	**2013**	**2012**
State controlled entities:				
Purchase of gas	33,918	39,522	608	785
Materials granted	-	1,074	-	-
	33,918	**40,596**	**608**	**785**

(iii) Loans

’000 GEL	**Interest accrued**		**Outstanding balance**	
	2013	**2012**	**2013**	**2012**
Loans given:				
Shareholder	7,832	2,490	89,136	85,322
State controlled entity	5,463	1,534	47,055	48,714
	13,295	**4,024**	**136,191**	**134,036**

27. Subsequent events

In April 2014, the Company and the Government of Georgia signed an agreement to transfer JSC Namakhvani HPP to the Government of Georgia free of charge. 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 project (see note 24).

28. Basis of measurement

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

29. Changes in accounting policies

Except for the changes below, the Group has consistently applied the accounting policies set out in Note 30 to all periods presented in these consolidated financial statements.

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

a. IFRS 10 Consolidated Financial Statements (2011);
b. IFRS 12 Disclosure of Interests in Other Entities;
c. IFRS 13 Fair Value Measurement;
d. Presentation of Items of Other Comprehensive Income (Amendments to IAS 1).

The nature and effects of the changes are explained below.

(a) Subsidiaries

As a result of IFRS 10 (2011), the Group has changed its accounting policy for determining whether it has control over and consequently whether it consolidates its investees. IFRS 10 (2011) introduces a new control model that focuses on whether the Group has power over an investee, exposure or rights to variable returns from its involvement with the investee and ability to use its power to affect those returns. The adoption of this Standard had no impact on the Group’s financial position or performance.

(b) Disclosure of interests in other entities

As a result of IFRS 12, the Group has expanded its disclosures about its interests in subsidiaries (see note 23).

(c) Fair value measurement

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

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively and has not provided any comparative information for new disclosures. Notwithstanding the above, the change had no significant impact on the measurements of the Group’s assets and liabilities.

(d) Presentation of items of Other Comprehensive Income (OCI)

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

30. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities, except as explained in note 29, which addresses changes in accounting policies.

(a) Basis of consolidation

(i) Non-controlling interests

Non-controlling interests are measured at their proportionate share of the acquiree’s identifiable net assets at the acquisition date.

(ii) Subsidiaries

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

(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.

(b) 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.

(c) Finance income and costs

The Group’s finance income and finance costs include:

- interest income;
- unwinding of discount on finance lease receivable;
- interest expense.

Interest income or expense is recognised using the effective interest method.

Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

(d) 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.

(e) Employee benefits

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

(f) Income tax

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

(i) Current tax

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

(ii) Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

- temporary differences 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;
- temporary differences related to investments in subsidiaries and joint arrangements to the extent that the Group is able to control the timing of the reversal of the temporary differences and it is probable that they will not reverse in the foreseeable future.

A deferred tax asset is recognised for unused tax losses, unused 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 used. 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.

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

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

(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) 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 capitalized borrowing. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

If significant 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.

Any 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 expenditure

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 reporting date and adjusted if appropriate.

(i) Financial instruments

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

The Group classifies non-derivative financial liabilities into the other financial liabilities category.

(i) Non-derivative financial assets

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

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.

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

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

Loans and receivables

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

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-measerement

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.

(j) Share capital

Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to issue of ordinary shares and share options are recognized 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.

(k) 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 or issuer will enter bankruptcy;
- adverse changes in the payment status of borrowers or issuers in the Group;
- economic conditions that correlate with defaults; or
- observable data indicating that there is measurable decrease in expected cash flows from a group of financial assets.

Financial assets measured at amortised cost

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

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

An impairment loss is calculated as the difference between an asset's 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. When the Group considers that there are no realistic prospects of recovery of the asset, the relevant amounts are written off. 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 and the decrease can be related objectively to an event occurring after the impairment was recognised, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

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

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGU.

The 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.

Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated to reduce the 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.

(l) 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.

(m) Leased assets

Assets held by the Group under leases that transfer to the Group 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.

(n) 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.

31. New standards and interpretations not yet adopted

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

- IFRS 9 *Financial Instruments* is to be issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement*. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding classification and measurement of financial liabilities was published in October 2010. The third phase was issued in November 2013 and relates to general hedge accounting. 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.

- Amendments to IAS 32 *Financial Instruments: Presentation - Offsetting Financial Assets and Financial Liabilities* specify that an entity currently has a legally enforceable right to set-off if that right is not contingent on a future event; and enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties. The amendments are effective for annual periods beginning on or after 1 January 2014, and are to be applied retrospectively.

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

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