Georgian Railway JSC

Consolidated Financial Statements
for 2015

Contents

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Independent Auditors' Report

To the Management Board
Georgian Railway JSC

We have audited the accompanying consolidated financial statements of Georgian Railway JSC (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2015, 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 2015, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Georgia LLC

KPMG Georgia LLC
13 May 2016

შეზღუდული პასუხისმგებლობის საზოგადოება
LIMITED LIABILITY COMPANY
404437695
KPMG Georgia

'000 GEL	Note	2015	2014
Assets			
Property, plant and equipment	11	2,483,393	2,378,228
Deferred tax assets	10	1,094	1,557
Other non-current assets	12	147,998	170,190
Non-current assets		**2,632,485**	**2,549,975**
Inventories	13	34,768	34,008
Loan receivable	27	38,341	-
Current tax assets		10,993	10,924
Trade and other receivables	14	70,645	53,944
Prepayments and other current assets	15	11,901	18,547
Cash and cash equivalents	16	294,784	300,983
Current assets		**461,432**	**418,406**
Total assets		**3,093,917**	**2,968,381**
Equity	17		
Share capital		1,052,605	1,052,202
Non-cash owner contribution reserve		34,214	34,214
Retained earnings		384,391	476,335
Total equity		**1,471,210**	**1,562,751**
Liabilities			
Loans and borrowings	19	1,193,301	929,373
Advance received from the Government	17(e)	221,788	229,377
Trade and other payables		52	52
Deferred tax liabilities	10	43,928	59,998
Non-current liabilities		**1,459,069**	**1,218,800**
Loans and borrowings	19	44,855	87,330
Trade and other payables	20	89,258	78,480
Liabilities to the Government	17(c)	8,009	8,467
Provisions	21	8,325	6,447
Dividend payable	17(d)	2,762	-
Other current liabilities		10,429	6,106
Current liabilities		**163,638**	**186,830**
Total liabilities		**1,622,707**	**1,405,630**
Total equity and liabilities		**3,093,917**	**2,968,381**

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 9 to 40.

'000 GEL	Note	2015	2014
Revenue	6	574,773	511,570
Other income	17(e)	30,771	12,353
Employee benefits expense		(148,625)	(145,174)
Depreciation and amortization expense		(104,416)	(105,258)
Electricity and materials used	7	(45,507)	(47,239)
Other expenses	8	(88,625)	(81,480)
Results from operating activities		**218,371**	**144,772**
Finance income	9	20,932	11,666
Finance costs	9	(315,355)	(111,269)
Net finance costs		**(294,423)**	**(99,603)**
(Loss)/ profit before income tax		**(76,052)**	**45,169**
Income tax benefit/ (expense)	10	10,555	(5,883)
(Loss)/ profit and total comprehensive (loss)/ income for the year		**(65,497)**	**39,286**

These consolidated financial statements were approved by the Management Board on 13 May 2016 and were signed on its behalf by:

Mamuka Bakhtadze
General Director

Tamaz Jgerenaia
Chief Accountant

The consolidated statement of profit or loss and other comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 9 to 42.

	Share capital	Non-cash owner contribution reserve	Retained earnings	Total equity
Balance at 1 January 2014	1,050,075	31,673	487,379	1,569,127
Total comprehensive income for the year				
Profit for the year	-	-	39, 286	39, 286
Transactions with owners, recorded directly in equity				
Dividends to equity holders (note 17(d))	-	-	(50,330)	(50,330)
Net non-cash contributions by and distributions to owners (note 17(b))	2,127	2,541	-	4,668
Total transactions with owners, recorded directly in equity	**2,127**	**2,541**	**(50,330)**	**(45,662)**
Balance at 31 December 2014	**1,052,202**	**34,214**	**476,335**	**1,562,751**
Balance at 1 January 2015	1,052,202	34,214	476,335	1,562,751
Total comprehensive loss for the year				
Loss for the year	-	-	(65,497)	(65,497)
Transactions with owners, recorded directly in equity				
Dividends to equity holders (note 17(d))	-	-	(25,537)	(25,537)
Net non-cash contributions by and distributions to owners (note 17 (b))	403	-	(910)	(507)
Total transactions with owners, recorded directly in equity	**403**	**-**	**(26,447)**	**(26,044)**
Balance at 31 December 2015	**1,052,605**	**34,214**	**384,391**	**1,471,210**

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 9 to 40.

'000 GEL	Note	2015	2014
Cash flows from operating activities			
Cash receipts from customers		564,849	526,862
Cash paid to suppliers and employees		(260,232)	(243,832)
Cash flows from operations before income taxes paid		**304,617**	**283,030**
Income tax paid		(5,121)	(2,925)
Net cash from operating activities		**299,496**	**280,105**
Cash flows from investing activities			
Acquisition of property, plant and equipment		(156,993)	(86,776)
Interest received		20,992	11,523
Issuance of the loan	27	(38,507)	-
Net cash used in investing activities		**(174,508)**	**(75,253)**
Cash flows from financing activities			
Repayment of borrowings		(62,514)	-
Interest paid		(85,731)	(72,826)
Dividends paid	17(d)	(21,852)	(50,330)
Net cash used in financing activities		**(170,097)**	**(123,156)**
Net (decrease)/ increase in cash and cash equivalents		**(45,109)**	**81,696**
Cash and cash equivalents at 1 January		300,983	208,996
Effect of exchange rate fluctuations on cash and cash equivalents		38,910	10,291
Cash and cash equivalents at 31 December	16	**294,784**	**300,983**

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 9 to 40.

1. Reporting entity

(a) 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.

(b) Organisation and operations

Georgian Railway JSC (the "Company") and its subsidiaries (the "Group") comprise Georgian joint stock and limited liability companies as defined in the Civil Code of Georgia. The Company was established as a state-owned enterprise in December 1998 by the Decree of the President of Georgia # 929 as an entity engaged in the provision of railway transportation services in Georgia.

The Company's registered office is 15 Queen Tamar Avenue, Tbilisi 0112, Georgia.

The Group's principal activity is the operation of a nationwide railway system providing freight and passenger transportation services, freight forwarding services, maintenance and development of railway infrastructure and construction of railway lines within Georgia.

The Company is wholly owned by Partnership Fund JSC, a wholly state-owned company. The ultimate controlling party of the Group is the Government of Georgia. Related party transactions are disclosed in note 27.

2. Basis of accounting

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 29(h)(iii) – useful lives and residual values of property, plant and equipment;
- Note 22(b)(ii) – impairment allowances for trade and other receivables;
- Note 16 – classification of deposits with original maturities of more than three months as cash and cash equivalents;
- Note 17 (e) – fair value of the land plots transferred to the Government of Georgia.

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 11 (a) – recoverability of construction of Tbilisi Bypass project;
- Note 27(c) (iii) – recoverability of the loan issued to the state controlled entity.

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.

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

5. Operating segments

The Group has two 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 because they require different technology and marketing strategies. For each of the strategic business units, the Group's Management Board reviews internal management reports on at least a quarterly basis. The following summary describes the operations in each of the Group's reportable segments:

- *Freight transportation*. Includes transportation of goods and commodities and related services.
- *Passenger transportation*. Includes transportation of passengers and luggage.

There are no inter-segment charges.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before infrastructure costs, which are the cost of maintaining the rail network used by both reportable segments, central overheads, interest and income tax, as included in the internal management reports that are reviewed by the Group's Management Board. 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 Group's Management Board does not monitor segment liabilities.

(i) Information about reportable segments

	Freight transportation		**Passenger transportation**		**Total**	
'000 GEL	**2015**	**2014**	**2015**	**2014**	**2015**	**2014**
External revenues	552,298	489,592	15,487	18,317	567,785	507,909
Depreciation and amortization	(42,411)	(41,859)	(9,144)	(8,135)	(51,555)	(49,994)
Reportable segment profit/(loss) before infrastructure costs, net interest cost and income tax	378,494	311,551	(18,810)	(15,182)	359,684	296,369
Reportable segment assets	361,759	370,972	113,206	114,629	474,965	485,601
Capital expenditure and other additions to non-current assets	36,449	41,674	3,860	1,147	40,309	42,821

(ii) Reconciliations of reportable segment revenues, profit or loss, assets and other material items

'000 GEL	**2015**	**2014**
Revenues		
Total revenue for reportable segments	567,785	507,909
Other revenue	6,988	3,661
Consolidated revenue	**574,773**	**511,570**
Profit or loss		
Total profit or loss for reportable segments	359,684	296,369
Employee benefits expense – infrastructure and headquarters	(58,539)	(57,743)
Depreciation expenses – infrastructure and headquarters	(52,861)	(55,264)
Net finance costs	(294,423)	(99,603)
Other net unallocated expenses	(29,913)	(38,590)
Consolidated (loss)/ profit before income tax	**(76,052)**	**45,169**
Assets		
Total assets for reportable segments	474,965	485,601
Property, plant and equipment - infrastructure and headquarters	2,033,350	1,917,603
Other unallocated assets, principally cash and non-current assets	585,602	565,177
Consolidated total assets	**3,093,917**	**2,968,381**

(iii) Other material items 2015

'000 GEL	**Reportable segment totals**	**Infrastructure and headquarters**	**Consolidated totals**
Capital expenditure and other additions to non-current assets	40,309	154,049	194,358
Depreciation and amortization	51,555	52,861	104,416

(iv) Other material items 2014

'000 GEL	**Reportable segment totals**	**Infrastructure and headquarters**	**Consolidated totals**
Capital expenditure and other additions to non-current assets	42,821	75,874	118,695
Depreciation and amortization	49,994	55,264	105,258

(v) Geographical information

Approximately 90% (2014: 90%) of the Group's revenue is generated in Georgia with the remainder generated in CIS countries. The non-current assets of the Group are located in Georgia.

(vi) Major customer

In 2015 one customer of the Group's freight transportation segment represented approximately 22% of the Group's total revenue (GEL 125,727 thousand). In 2014 one customer of the Group's freight transportation segment represented approximately 18% of the Group's total revenue (GEL 92,499 thousand).

6. Revenue

'000 GEL	2015	2014
Freight traffic	528,037	451,781
Freight car rental	24,261	37,811
Passenger traffic	15,487	18,317
Other	6,988	3,661
	574,773	**511,570**

Railroad transportation in Georgia is a natural monopoly; however the prices are not subject to government regulation. According to clause 64 of the Railway Code of Georgia, which came into force on 1 July 2005, the Government of Georgia allowed the Group to set the prices for all services provided, including freight transportation, freight transportation-related additional services, and passenger and luggage transportation.

Tariffs for freight transportation are based on the International Rail Transit Tariff. The Group is a co-signatory of the Tariff Agreement together with CIS countries, Latvia, Lithuania and Estonia. The parties to the Agreement hold annual conferences to determine the tariff policy for the following year: each party declares tariffs denominated in Swiss Francs (CHF) for railway transportation and states the general rules that apply to and modify tariffs. The agreed tariffs indicate the maximum level of tariffs applicable.

7. Electricity and materials used

'000 GEL	2015	2014
Electricity	20,424	20,091
Materials	19,276	19,280
Fuel	5,807	7,868
	45,507	**47,239**

8. Other expenses

'000 GEL	2015	2014
Taxes other than income tax	25,969	24,384
Repairs and maintenance	15,420	10,001
Freight car rental	11,210	19,992
Security	8,734	8,495
Write off of non-current assets	-	3,858
Other	27,292	14,750
	88,625	**81,480**

9. Finance income and finance costs

'000 GEL	**2015**	**2014**
Recognised in profit or loss		
Interest income on bank balances	20,932	11,666
Finance income	**20,932**	**11,666**
Impairment loss on trade receivables (note 22 (b)(ii))	(28,627)	(5,245)
Interest expense on financial liabilities	(59,891)	(44,891)
Net foreign exchange loss	(226,837)	(61,133)
Finance costs	**(315,355)**	**(111,269)**
Net finance costs recognised in profit or loss	**(294,423)**	**(99,603)**

10. Income tax expense

(a) Amounts recognized in profit or loss

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

'000 GEL	**2015**	**2014**
Current tax expense		
Current year	5,052	4,321
	5,052	**4,321**
Deferred tax (benefit)/expense		
Origination and reversal of temporary differences	(15,607)	1,562
	(10,555)	**5,883**

Reconciliation of effective tax rate:

	2015		2014	
	’000 GEL	%	’000 GEL	%
(Loss)/ profit before income tax	(76,052)	100	45,169	100
Income tax at applicable tax rate	(11,408)	15	6,775	15
Net non-deductible expenses/ (non-taxable income)	853	(1)	(892)	(2)
	(10,555)	**14**	**5,883**	**13**

(b) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
’000 GEL	**2015**	**2014**	**2015**	**2014**	**2015**	**2014**
Property, plant and equipment	-	-	(102,133)	(95,270)	(102,133)	(95,270)
Other non-current assets	-	46	(297)	-	(297)	46
Inventories	10,919	10,516	-	-	10,919	10,516
Trade and other receivables	21,136	15,688	-	-	21,136	15,688
Prepayments and other current assets	1,636	1,636	-	-	1,636	1,636
Loans and borrowings	6,277	4,966	-	-	6,277	4,966
Trade and other payables	120	673	-	-	120	673
Provisions	1,249	967	-	-	1,249	967
Other current liabilities	1,041	780	-	-	1,041	780
Tax loss carry-forwards	17,218	1,557	-	-	17,218	1,557
Tax assets/(liabilities)	**59,596**	**36,829**	**(102,430)**	**(95,270)**	**(42,834)**	**(58,441)**
Set off of tax	(58,502)	(35,272)	58,502	35,272	-	-
Net tax assets/(liabilities)	**1,094**	**1,557**	**(43,928)**	**(59,998)**	**(42,834)**	**(58,441)**

(c) Movement in temporary differences during the year

’000 GEL	1 January 2015	Recognised in profit or loss	31 December 2015
Property, plant and equipment	(95,270)	(6,863)	(102,133)
Other non-current assets	46	(343)	(297)
Inventories	10,516	403	10,919
Trade and other receivables	15,688	5,448	21,136
Prepayments and other current assets	1,636	-	1,636
Loans and borrowings	4,966	1,311	6,277
Trade and other payables	673	(553)	120
Provisions	967	282	1,249
Other current liabilities	780	261	1,041
Tax loss carry-forwards	1,557	15,661	17,218
	(58,441)	**15,607**	**(42,834)**

’000 GEL	1 January 2014	Recognised in profit or loss	31 December 2014
Property, plant and equipment	(94,141)	(1,129)	(95,270)
Other non-current assets	46	-	46
Inventories	12,948	(2,432)	10,516
Trade and other receivables	14,878	810	15,688
Prepayments and other current assets	1,637	(1)	1,636
Loans and borrowings	4,611	355	4,966
Trade and other payables	28	645	673
Provisions	923	44	967
Other current liabilities	634	146	780
Tax loss carry-forwards	1,557	-	1,557
	(56,879)	**(1,562)**	**(58,441)**

11. Property, plant and equipment

’000 GEL	**Land**	**Buildings and constructions**	**Rail track infrastructure**	**Transport, machinery, equipment and other**	**Construction in progress**	**Total**
Cost or deemed cost						
Balance at 1 January 2014	541,816	131,239	845,820	853,590	585,939	2,958,404
Additions	3,343	2,137	53	23,495	114,548	143,576
Disposals and write offs	(60)	(749)	(6,629)	(12,194)	(7,036)	(26,668)
Transfers	(1,147)	1,800	32,436	22,503	(55,592)	-
Balance at 31 December 2014	**543,952**	**134,427**	**871,680**	**887,394**	**637,859**	**3,075,312**
Balance at 1 January 2015	543,952	134,427	871,680	887,394	637,859	3,075,312
Additions	401	1,792	-	23,520	186,624	212,337
Disposals and write offs	(122)	(6,984)	(14,485)	(36,278)	(47)	(57,916)
Transfers	1,240	768	46,357	27,589	(75,954)	-
Balance at 31 December 2015	**545,471**	**130,003**	**903,552**	**902,225**	**748,482**	**3,229,733**
Depreciation						
Balance at 1 January 2014	-	26,869	227,904	356,444	-	611,217
Depreciation for the year	-	3,827	43,405	57,655	-	104,887
Disposals and write offs	-	(521)	(6,418)	(12,081)	-	(19,020)
Balance at 31 December 2014	**-**	**30,175**	**264,891**	**402,018**	**-**	**697,084**
Balance at 1 January 2015	-	30,175	264,891	402,018	-	697,084
Depreciation for the year	-	4,062	40,910	59,396	-	104,368
Disposals and write offs	-	(5,034)	(14,365)	(35,713)	-	(55,112)
Balance at 31 December 2015	**-**	**29,203**	**291,436**	**425,701**	**-**	**746,340**
Carrying amounts						
At 1 January 2014	541,816	104,370	617,916	497,146	585,939	2,347,187
At 31 December 2014	**543,952**	**104,252**	**606,789**	**485,376**	**637,859**	**2,378,228**
At 31 December 2015	**545,471**	**100,800**	**612,116**	**476,524**	**748,482**	**2,483,393**

(a) During the year ended 31 December 2010 the Group started two large capital projects (included in construction in progress): the Main Line Modernization and the Tbilisi Bypass and started to incur expenditures for the projects in September 2010 and November 2010 respectively. To partly finance the projects the Group issued unsecured bonds in 2010. In 2012, the Group redeemed the bonds issued in 2010 by issuing new bonds for general corporate and liquidity management purposes (see note 19).

All the borrowing costs of the 2010 unsecured bonds allocated to each project on a 59%/41% basis were capitalized upon starting to incur expenditures for the projects. The interest on the bonds issued in 2012 was capitalized to the two projects in proportion to the costs incurred on the projects based on a capitalization rate of 8% (2014: 8%). Capitalised borrowing costs during 2015 related to the Main Line Modernization project amounted to GEL 33,310 thousand (2014: GEL 29,391 thousand).

In June 2013 the Group announced a decision to redesign the Tbilisi Bypass project. The Group held negotiations with the Government of Georgia and with the main third party construction companies to agree a plan for the conservation of the project for the period of redesigning. All construction works in progress were substantially completed by the end of October 2013 and further construction was suspended. No borrowing costs are capitalised after October 2013.

In March 2014, the Government of Georgia decided that the suspension of the construction of Tbilisi Bypass project will last for 18 months until the final modified project is presented. The modified project will be completed within an additional 18 months. The Group signed the amended construction contract with the main third party construction companies in accordance with the Government decision.

In January 2015, a comparative study for the existing and the bypass line was prepared by a third party consultant. The study analyzed different scenarios and concluded that the best option is maintaining only the current rail system on the existing main line (demolishing supporting railway infrastructure, such as depots and intermediate stations except the main terminal station) and constructing the Tbilisi Bypass line. Following this option the cargo directed from West to the East border will be transmitted via Tbilisi Main Line and the Cargo directed from the East to the West region- via new Tbilisi Bypass.

In 2015 the Group has presented the final project with various scenarios including the best option identified by the third party consultants to the Government of Georgia for approval. As at the date these consolidated financial statements were authorized for issue, the Group is in discussion with the Tbilisi City Hall and the Government of Georgia about various scenarios of completing the project. It is believed that the final decision will be agreed by June 2016 and that the execution of any of the possible scenarios will not cause any existing significant constructions to become redundant.

(b) The Government of Georgia contributes certain property, plant and equipment in the form of an increase in share capital. In 2015 and 2014 the share capital has been increased by the fair value of these assets of GEL 402 thousand and GEL 780 thousand respectively (see note 17 (a)).

12. Other non-current assets

’000 GEL	**2015**	**2014**
Prepayments for non-current assets	88,341	103,338
Construction materials	56,232	65,662
Goodwill	46	46
Other	3,379	1,144
	147,998	**170,190**

13. Inventories

’000 GEL	**2015**	**2014**
Materials	30,347	29,939
Rails	2,109	3,141
Fuel	2,086	3,110
Other	4,203	2,022
	38,745	38,212
Allowance for inventory obsolescence	(3,977)	(4,204)
	34,768	**34,008**
Reversal of previous write-down of inventories	227	57

14. Trade and other receivables

’000 GEL	**2015**	**2014**
Trade receivables	210,519	158,138
Impairment allowance on trade receivables	(140,846)	(104,463)
	69,673	**53,675**
Other receivables	972	269
	70,645	**53,944**

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

15. Prepayments and other current assets

’000 GEL	2015	2014
Taxes, other than on income	10,906	16,515
Advances paid to suppliers	995	2,032
	11,901	**18,547**

16. Cash and cash equivalents

’000 GEL	2015	2014
Current accounts in banks	142,953	88,169
Call deposits	151,770	212,710
Petty cash	61	104
Cash and cash equivalents in the consolidated statement of financial position and the consolidated statement of cash flows	**294,784**	**300,983**

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 any 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.

17. Equity and liabilities to the Government

(a) Share capital

Number of shares	**Ordinary shares**	
	2015	**2014**
In issue at 1 January	1,052,202,448	1,050,075,578
Issued for property, plant and equipment (see note 11 (b))	402,055	779,590
Withdrawal of property, plant and equipment	-	(9,520)
Issued for inventory	-	1,356,800
In issue at 31 December, fully paid	**1,052,604,503**	**1,052,202,448**
Authorised shares - par value	**1**	**1**

All ordinary shares rank equally with regard to the Company’s residual assets.

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) Non-cash owner contribution reserve

The difference between the nominal amount of registered share capital for non-cash assets contributed by the owner and the fair value of the contributed assets is recognised in the non-cash owner contribution reserve.

(c) Liabilities to the Government

Liabilities to the owners represent liabilities in the form of property, plant and equipment which are withdrawn as a reduction in share capital but not yet transferred formally to the owners. These liabilities are recorded at the carrying amount of assets to be transferred to the owner.

'000 GEL	**2015**	**2014**
Liabilities to the Government	**8,009**	**8,467**

(d) Dividends

In 2015, the Company declared and paid dividends of GEL 25,537 thousand (GEL 0.02 per issued share) and GEL 21,852 thousand, respectively (2014: declared and paid dividends of GEL 50,330 thousand in total or GEL 0.05 per issued share). The remaining amount of the dividends payable is gradually reduced by the costs incurred by the Company on the construction of Batumi Station infrastructure as declared by the Government.

(e) Advance received from the Government

In April 2012, the Company and the Government entered into the Bypass Project Memorandum. According to the Bypass Project Memorandum the Government is interested and aims to purchase from the Group approximately 70.1 hectares of land plots with attached constructions which will be freed up as a result of the removal of railway infrastructure from Tbilisi city center and construction of a new bypass railway route for the purposes of further development of the land plots. The Government agrees to pay to the Group CHF 138 million equivalents in national currency through the reduction in the amount of dividends payable to the Government.

In 2012, the Company declared dividends of GEL 231,592 thousand (CHF 138 million). Subsequently, the Company agreed with the Government that the declared dividend amount would represent a consideration due from the Government for the future sale of the land plots in accordance with the Bypass Project Memorandum. As a result, the dividend payable was classified as an advance received from the Government for the sale of land.

In 2015 the Company transferred 3,266 square meter land plots with the carrying value of GEL 85 thousand to the Government within the framework of the Bypass Project Memorandum. The fair value of these land plots was determined by an independent appraiser at GEL 7,588 thousand based on market prices in recent transactions or adjusted ask prices for similar properties. The difference between the fair value and the carrying value of the transferred land plots of GEL 7,503 thousand was recognized as other income in the consolidated statement of profit or loss.

18. 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 the Group's revenues and profit, and long-term investment plans mainly financed by the Group's operating cash flows and unsecured bonds. With these measures the Group aims for steady profits growth.

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

19. 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	**2015**	**2014**
Non-current liabilities		
Unsecured bonds	1,193,301	929,373
Loans and borrowings	**1,193,301**	**929,373**
Current liabilities		
Current portion of unsecured bonds	44,855	87,330
Loans and borrowings	**44,855**	**87,330**

Terms and debt repayment schedule

Terms and conditions of outstanding loans and borrowings were as follows:

				31 December 2015		**31 December 2014**	
'000 GEL	**Currency**	**Nominal interest rate**	**Year of maturity**	**Face value**	**Carrying amount**	**Face value**	**Carrying amount**
Unsecured bonds	USD	7.8%	2022	1,238,156	1,238,156	963,253	963,253
Unsecured bonds	USD	9.9%	2015	-	-	53,450	53,450
Total interest-bearing liabilities				**1,238,156**	**1,238,156**	**1,016,703**	**1,016,703**

In July 2012 the Group carried out the issuance, placement and registration (listing) on the London Stock Exchange of unsecured bonds of USD 500 million and the early redemption of the unsecured bonds of USD 250 million due in 2015 issued by the Group in July 2010 (the 2010 Notes). As a result of the above transaction, the Group has issued USD 500 million 7.75% Notes due 2022 and redeemed 88.99% of the outstanding 2010 Notes with a face value of USD 222 million.

In July 2015 the Group has fully repaid 2010 Notes.

20. Trade and other payables

’000 GEL	**2015**	**2014**
Trade payables	73,064	57,448
Advances received from customers	16,194	21,032
	89,258	**78,480**

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

21. Provisions

’000 GEL	**2015**	**2014**
Balance as at 1 January	6,447	6,154
Provisions made during the year	1,878	608
Provisions used during the year	-	(315)
Balance as at 31 December	**8,325**	**6,447**

The Group recognised a provision for the estimated cash outflow required to settle legal cases against the Group existing as at 31 December 2015 as well as to settle the legal obligations towards the employees injured during the performance of their duties.

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 realizable in an immediate sale of the assets or transfer of liabilities.

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

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;
- liquidity risk;
- market risk.

(i) Risk management framework

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

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

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

(ii) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and 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	**2015**	**2014**
Cash and cash equivalents - Georgian banks (not impaired or past due)	294,723	300,879
Loan receivable	38,341	-
Trade receivables	69,673	53,675
	402,737	**354,554**

Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the factors that may influence the credit risk of the Group's customer base, including the default risk of the industry and country, in which customers operate, particularly in the currently deteriorating economic circumstances. Approximately 22% (2014: 18%) of the Group's revenue is attributable to sales transactions with a single customer.

Credit risk is managed by requesting prepayments from freight and passenger transportation customers. Accordingly the Group's trade receivables mainly consist of receivables from foreign railway companies. Credit risk related to receivables from foreign railway companies is managed through the monthly monitoring of receivable balances and requiring immediate repayment of a debt when the balance approaches specific limits set for each individual counterparty.

More than 90% of the Group's foreign railway customers have been transacting with the Group for several years, and losses have occurred infrequently. In monitoring customer credit risk, customers are grouped according to their credit characteristics, including aging profile, maturity and existence of previous financial difficulties.

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	**2015**	**2014**
CIS countries	54,544	46,321
Domestic	15,129	7,354
	69,673	**53,675**

The Group's two most significant customers account for GEL 41,143 thousand of the trade receivables carrying amount as at 31 December 2015 (2014: GEL 34,267 thousand).

Impairment losses

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

'000 GEL	**Gross 2015**	**Impairment 2015**	**Gross 2014**	**Impairment 2014**
Past due 0- 90 days	9,319	8,040	5,030	2,777
Past due 91-180 days	18,814	9,988	3,742	837
Past due 181-365 days	37,636	18,355	11,535	4,470
Past due more than one year	144,750	104,463	137,831	96,379
	210,519	**140,846**	**158,138**	**104,463**

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

'000 GEL	**2015**	**2014**
Balance at beginning of the year	104,463	96,379
Increase during the year	28,627	8,084
Net foreign exchange loss	7,756	-
Balance at end of the year	**140,846**	**104,463**

In 2015 the Group recognized impairment loss of approximately GEL 13 million for the trade receivables from one counterparty that were originated in 2015. The Group believes that, at the origination date, it was probable that the economic benefits would flow to the Group. The corresponding revenue is included in freight traffic revenue for 2015.

Most of the impairment loss at 31 December 2015 relates to several customers that have indicated that they are not expecting to be able to pay their outstanding balances either because of economic circumstances or as a result of bankruptcy. The Group believes that the unimpaired amounts that are past due are still collectible, based on historic payment behaviour and analyses on the underlying customers' credit ratings, when available. In addition, receivables of GEL 42,024 thousand (2014: GEL 38,663 thousand) relate to freight car rental customers with which the Group incurs freight car rental expense and related payables. These receivables and payables are periodically net settled.

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

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

Cash and cash equivalents and term deposits

To mitigate the credit risk of cash and bank balances, the Group holds the majority of its funds with five largest Georgian banks with short-term default rating of B, rated by Fitch Ratings. The Group does not expect any counterparty to fail to meet its obligations.

Loan receivable

The loan is receivable from a state controlled entity (see note 27 (c) (iii)). Management believes that as at 31 December 2015 the Group is not significantly exposed to credit risk from the loan receivable, as the loan is not overdue and, if required, the Government of Georgia, represented by the Ministry of Energy, will provide support to the extent permitted by the Georgian legislation to the state controlled entity to enable it to repay the loan to the Group.

(iii) Liquidity risk

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

The Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of three months, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

The Group maintains an unsecured GEL 43,975 thousand unused overdraft facility. Interest on this facility is payable at the rate of 12%-14.5%.

The Group has significant contractual commitments to purchase property, plant and equipment (see note 25) for the Main Line Modernization and Tbilisi Bypass projects expected to be completed by the end of 2019 and 2020, respectively. Management believes that the cash and cash equivalents held by the Group and the future cash flows from operating activities will be sufficient to finance these two projects.

Exposure to liquidity risk

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements. It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

2015

'000 GEL	Carrying amount	Contractual cash flows	0-6 months	6-12 months	1-2 years	2-5 years	Over 5 years
Unsecured bonds	1,238,156	1,847,066	46,401	46,401	92,802	278,407	1,383,055
Trade payables	73,116	73,116	73,064	-	-	52	-
Other current liabilities	10,429	10,429	10,429	-	-	-	-
	1,321,701	**1,930,611**	**129,894**	**46,401**	**92,802**	**278,459**	**1,383,055**

2014

'000 GEL	Carrying amount	Contractual cash flows	0-6 months	6-12 months	1-2 years	2-5 years	Over 5 years
Unsecured bonds	1,016,703	1,565,867	38,640	89,926	72,215	216,644	1,148,442
Trade payables	57,500	57,500	57,448	-	-	52	-
Other current liabilities	6,106	6,106	6,106	-	-	-	-
	1,080,309	**1,629,473**	**102,194**	**89,926**	**72,215**	**216,696**	**1,148,442**

(iv) Market risk

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

Currency risk

The Group is exposed to currency risk to the extent that there is a mismatch between currencies in which sales, purchases and borrowings are denominated and the respective functional currencies of Group entities. The functional currencies of Group companies are the Georgian Lari (GEL). The currencies in which these transactions are primarily denominated and settled are U.S. Dollars (USD) and Swiss Francs (CHF).

Borrowings and related interest are denominated in currencies that match the cash flows generated by the underlying operations of the Group. This provides an economic hedge without a need to enter into derivatives contracts.

Exposure to currency risk

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

’000 GEL	USD - denominated 2015	CHF - denominated 2015	USD - denominated 2014	CHF - denominated 2014
Cash and cash equivalents	142,233	324	175,479	3,297
Loan receivable	38,341	-	-	-
Trade receivables	494	54,544	1	46,319
Unsecured bonds	(1,238,156)	-	(1,016,703)	-
Trade and other payables	(5,717)	-	(4,625)	-
Net exposure	**(1,062,805)**	**54,868**	**(845,848)**	**49,616**

The following significant exchange rates applied during the year:

in GEL	Average rate		Reporting date spot rate	
	2015	**2014**	**2015**	**2014**
USD 1	2.27	1.77	2.39	1.86
CHF 1	2.36	1.93	2.42	1.88

Sensitivity analysis

A reasonably possible strengthening (weakening) of the GEL, as indicated below, against all other currencies at 31 December would have affected the measurement of financial instruments denominated in a foreign currency and 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
2015	
USD (30% weakening)	(271,015)
CHF (30% weakening)	13,991
2014	
USD (30% weakening)	(215,691)
CHF (30% weakening)	12,652

A strengthening of the GEL against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

(v) 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	**2015**	**2014**
Fixed rate instruments		
Financial assets	190,111	212,710
Financial liabilities	(1,238,156)	(1,016,703)
	(1,048,045)	**(803,933)**

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. Subsidiaries

			2015	2014
Subsidiary	**Country of incorporation**	**Principal activities**	**Ownership/ voting**	**Ownership/ voting**
Georgian Railway Property Management LLC	Georgia	Property management and development	100%	100%
Trans Caucasus Terminals LLC (former Georgian Railway Transcontainer LLC)	Georgia	Container transportation	100%	100%
Georgian Railway Construction JSC	Georgia	Construction and other projects	100%	100%
Borjomi Bakuriani Railway LLC	Georgia	Passenger transportation	100%	100%
Georgia Transit LLC	Georgia	Transportation services	100%	100%
GR Transit Line LLC	Georgia	Transportation services	100%	100%
GR Trans Shipment LLC (established in 2015)	Georgia	Transportation services	100%	-
Georgian Transit LLC (established in 2015)	Georgia	Transportation services	100%	-

24. Operating leases

Non-cancellable operating lease rentals are receivable as follows:

’000 GEL	**2015**	**2014**
Less than one year	4,832	3,028
Between one and five years	5,686	5,883
More than five years	17,754	16,103
	28,272	**25,014**

Operating leases relate to rent of other buildings, containers, locomotives and fittings owned by the Group with lease terms of mainly between 10 to 50 years. Lessees do not have an option to purchase the property at the end of the lease term.

25. Capital commitments

As at 31 December 2015 the Group had entered into contracts for the construction or purchase of property, plant and equipment of GEL 628,928 thousand (2014: GEL 561,489 thousand) mainly relating to the Main Line Modernization project of GEL 406,595 thousand (2014: GEL 385,660 thousand) and Tbilisi Bypass project of GEL 216,421 thousand (2014: GEL 156,155 thousand).

26. Contingencies

(a) Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group does not have full coverage for its property, 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) 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 four 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.

(c) Litigation

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

27. Related parties

(a) Parent and ultimate controlling party

At 31 December 2015 and 2014 the immediate and ultimate parent of the Group is Partnership Fund JSC. The ultimate controlling party of the Group is the Government of Georgia. Partnership Fund JSC produces publicly available consolidated 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 employee benefits expenses:

'000 GEL	**2015**	**2014**
Salaries and bonuses	**1,132**	**1,138**

(c) Other related party transactions

(i) Transactions with the government

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.

The Group's other related party transactions are disclosed below.

(ii) Revenue, purchases and expenses

The Group purchases electricity from a State-owned operator which amounted to GEL 1,376 thousand for 2015 (2014: GEL 1,864 thousand). The Group also purchases security services from a state agency which amounted to GEL 8,741 thousand for 2015 (2014: GEL 8,437 thousand). The Group usually does not have significant balances for these purchases.

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

(iii) Loan issued to a state controlled entity

In December 2015 the Group issued loan of USD 16 million to a state controlled entity with the purpose to guarantee the contractual obligations of the counterparty in a form of a restricted bank deposit. The loan together with the accrued interest matures in July 2016, when it is expected that the state controlled entity will receive the financing from the international financial institution to settle the contractual obligations and release the restriction on the funds received from the Group. The loan is not secured and bears a contractual interest rate of 10.5% per annum.

As at 31 December 2015 the loan is not overdue. Management believes, that if required, the Government of Georgia, represented by the Ministry of Energy, will provide support to the extent permitted by the Georgian legislation to the state controlled entity to enable it to repay the loan to the Group.

The Group's exposure to currency risk related to the loan issued to the state controlled entity is disclosed in note 22.

28. Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that property, plant and equipment was revalued to determine deemed cost as part of the adoption of IFRSs.

29. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

(a) Basis of consolidation

(i) Business combination

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group.

The Group measures goodwill at the acquisition date as:

- The fair value of the consideration transferred; plus
- The recognised amount of any non-controlling interests in the acquiree; plus
- If the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquire; less
- The net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.
The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

(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) 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) Transportation activities

Revenue from freight and passenger transportation is measured at the fair value of the consideration received or receivable. Freight and passenger transportation revenue is recognized in profit or loss according to the percentage of completed service method based on transit time of freight and passengers moving from the original location to the final destination.

Revenue from services rendered in stations is recognised in profit or loss when the service is rendered.

(ii) Commissions

When the Group acts in the capacity of an agent rather than as the principal in a transaction, the revenue recognised is the net amount of commission made by the Group.

(iii) Rental income

Rental income from investment property or other assets rented is recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

(c) Other expense

(i) Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

(ii) Social expenditure

To the extent that the Group’s contributions to social programs benefit the community at large and are not restricted to the Group’s employees, they are recognised in profit or loss as incurred.

(d) Finance income and costs

The Group’s finance income and finance costs include:

- interest income on bank deposits;
- interest expense on financial liabilities;
- Impairment loss on trade receivables;
- the foreign currency gain or loss on financial assets and financial liabilities.

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.

(e) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions.

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

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

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

(f) Income tax

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

(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, associates 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; and
- taxable temporary differences arising on the initial recognition of goodwill.

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.

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 impairment losses. The cost of property, plant and equipment at 1 January 2007, the date of transition to IFRS, was determined by reference to its fair value at that date.

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

When parts of an item of property, 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 recognised net within other income/other expenses in profit or loss.

(ii) Subsequent costs

The cost of replacing a component of an item of property, 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.

Maintenance and repair expenses are recognised as follows:

- Rolling stock:
  - current maintenance expenses during the useful life of equipment (repair work and replacement of unusable and missing parts) are recognised as operating expenses in profit or loss as incurred;
  - expenses under multi-year major overhaul programmes are capitalised as a separate overhaul component and depreciated separately from the main asset;
  - overhauls performed near the end of the useful life of an asset, together with refurbishment, are capitalised when they extend the useful life of the underlying asset.

- Fixed installations:
  - current maintenance and repair expenses (technical inspections, maintenance contracts, etc.) are recognised as operating expenses in profit or loss as incurred;
  - labour, materials and other costs (associated with the installation of rails, sleepers and ballast) under multi-year major building or infrastructure maintenance programmes are capitalised through the partial or total replacement of each component concerned;
  - costs associated with infrastructure improvements are capitalized to the extent that they increase the functionality (traffic working speed) of the asset.

(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. Land is not depreciated.

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

- buildings and constructions 44 years;
- rail track infrastructure 23 years;
- transport, machinery, equipment and other 12 years.

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

(i) Financial instruments

The Group classifies non-derivative financial assets into the following categories: loans and receivables and cash and cash equivalents.

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

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

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

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

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. The Group 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 Group and all counterparties.

Loans and receivables

Loans and receivables are a category of financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses (see note 29(j)(i)).

Loans and receivables category comprise loans given, trade and other receivables 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. 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.

(ii) Non-derivative financial liabilities-measurement

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised 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, trade payables and other current liabilities.

(iii) 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.

Increase of share capital

Share capital increase is affected through the 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 a fair value adjustment reserve for non-cash owner contributions.

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.

(j) 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 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.

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 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 recognised in profit or loss and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

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

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

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

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

(k) 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.

(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) 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 Management Board to make decisions about resources to be allocated to the segment and assess its performance.

Segment results that are reported to the Management Board include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly railway infrastructure, corporate assets (primarily the Group's headquarters), head office expenses, financial income and expenses, tax expenses and tax assets and liabilities. Items related to infrastructure are not allocated as the Group has not implemented systems for such allocations. The Group's Management Board does not monitor segment liabilities.

Segment capital expenditure is the total cost incurred during the year to acquire property, plant and equipment, and intangible assets.

30. 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 2015, 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, published in July 2014, replaces the existing guidance in IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 9.
- IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*. The core principle of the new standard is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard results in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively and improves guidance for multiple-element arrangements. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 15.
- IFRS 16 replaces the existing lease accounting guidance in IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a lease,* SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. It eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, there is a single, on-balance sheet accounting model that is similar to current finance lease accounting. Lessor accounting remains similar to current practice – i.e. lessors continue to classify leases as finance and operating leases. IFRS 16 is effective for annual reporting periods beginning on or after 1 January 2019, early adoption is permitted if IFRS 15 Revenue from Contracts with Customers is also adopted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 16.