

**“Azersu” Open Joint Stock Company**

**Consolidated financial statements**

*Year ended December 31, 2021  
together with independent auditor's report*

## Contents

### Independent Auditor's Report

### Consolidated financial statements

Consolidated statement of financial position.....	1
Consolidated statement of profit or loss and other comprehensive income .....	2
Consolidated statement of changes in equity .....	3
Consolidated statement of cash flows .....	4

### Notes to the consolidated financial statements

1. The Group's principal activity .....	5
2. Basis of preparation and significant accounting policies .....	5
3. Adoption of new or revised standards and interpretations .....	18
4. Critical accounting estimates and judgments .....	21
5. Property, plant and equipment .....	24
6. Right of use asset and lease liabilities .....	25
7. Taxes receivable.....	26
8. Inventories.....	27
9. Trade and other receivables .....	27
10. Cash and cash equivalents and restricted cash .....	28
11. Share capital .....	29
12. Government investments.....	29
13. Interest-bearing loans and borrowings .....	30
14. Provisions.....	32
15. Taxes and penalties payable other than income tax, net .....	33
16. Trade and other payables .....	33
17. Balances and transactions with related parties .....	33
18. Financial risk management .....	35
19. Sales revenue and deferred revenue .....	40
20. Other income.....	40
21. Expenses .....	41
22. Corporate income tax .....	43
23. Significant non-cash investing and financing activities .....	44
24. Contingences, commitments and operating risks .....	44
25. Events after the reporting date .....	46

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## **Independent auditor's report**

To management and those charged with governance of "Azersu" OJSC:

### **Opinion**

We have audited the consolidated financial statements of "Azersu" OJSC and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at December 31, 2021, and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at December 31, 2021 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

### **Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Responsibilities of management and those charged with governance for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, 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. In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.



### *Auditor's responsibilities for the audit of the consolidated financial statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

June 30, 2022  
Baku, Azerbaijan

RSM Azerbaijan

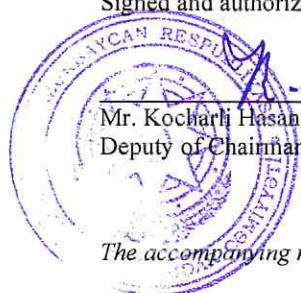


**Consolidated statement of financial position**

*(Amounts presented are in thousands of Azerbaijani manats)*

	Notes	December 31, 2021	December 31, 2020
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	5	953,771	942,733
Intangible assets	5	665	908
Right of use asset	6	609	702
Deferred tax assets	22	317	252
<b>Total non-current assets</b>		<b>955,362</b>	<b>944,595</b>
<b>Current assets</b>			
Inventories	8	16,584	13,177
Taxes receivable	7	15,033	18,545
Trade and other receivables	9	27,600	19,826
Prepayments		678	1,064
Cash and cash equivalents	10	5,906	2,863
Restricted cash	10	467	767
<b>Total current assets</b>		<b>66,268</b>	<b>56,242</b>
<b>Total assets</b>		<b>1,021,630</b>	<b>1,000,837</b>
<b>Equity and liabilities</b>			
<b>Equity</b>			
Share capital	11	400,000	400,000
Additional paid-in capital	11	7,092,817	6,820,384
Government investments	12	806,055	501,095
Accumulated losses		(7,855,686)	(7,303,456)
<b>Total equity</b>		<b>443,186</b>	<b>418,023</b>
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Interest-bearing loans and borrowings	13	248,103	243,072
Trade and other payables	16	347	6,904
Lease liabilities	6	411	453
Provisions	14	10,057	9,488
<b>Total non-current liabilities</b>		<b>258,918</b>	<b>259,917</b>
<b>Current liabilities</b>			
Interest-bearing loans and borrowings	13	11,994	21,689
Corporate income tax payable		2,414	2,262
Taxes and penalties payable other than corporate income tax, net	15	30,054	5,195
Trade and other payables	16	264,789	284,027
Lease liabilities	6	244	287
Deferred revenue	19	10,016	9,410
Provisions	14	15	27
<b>Total current liabilities</b>		<b>319,526</b>	<b>322,897</b>
<b>Total liabilities</b>		<b>578,444</b>	<b>582,814</b>
<b>Total equity and liabilities</b>		<b>1,021,630</b>	<b>1,000,837</b>

Signed and authorized for release on behalf of the Group on June 30, 2022.



Mr. Kocharli Hasanov  
Deputy of Chairman

Mr. Yashar Kalbiyev  
Head of Economics and Accounting Department

*The accompanying notes form an integral part of these consolidated financial statements.*

**Consolidated statement of profit or loss and other comprehensive income**

*(Amounts presented are in thousands of Azerbaijani manats)*

	Notes	Year ended December 31, 2021	Year ended December 31, 2020
Sales revenue	19	262,947	184,246
Cost of sales	21	(128,729)	(131,524)
<b>Gross profit</b>		<b>134,218</b>	<b>52,722</b>
Other income	20	32,236	7,846
Administrative expenses	21	(28,756)	(40,432)
Selling and distribution expenses	21	(146,607)	(117,024)
Other operating expenses	21	(549,528)	(207,855)
Foreign exchange gain/(loss)	21	10,315	(15,508)
<b>Operating loss</b>		<b>(548,122)</b>	<b>(320,251)</b>
Finance cost		(3,450)	(2,823)
Interest expense on lease liabilities		(60)	(63)
<b>Loss before tax</b>		<b>(551,632)</b>	<b>(323,137)</b>
Corporate income tax expense	22	(598)	(85)
<b>Loss for the year</b>		<b>(552,230)</b>	<b>(323,222)</b>
Other comprehensive income for the year		–	–
<b>Total comprehensive loss for the year</b>		<b>(552,230)</b>	<b>(323,222)</b>

*The accompanying notes form an integral part of these consolidated financial statements.*

**Consolidated statement of changes in equity**

*(Amounts presented are in thousands of Azerbaijani manats)*

	Notes	Share capital	Additional paid-in capital	Government investments	Accumulated loss	Total equity
<b>As at December 31, 2019</b>		<b>400,000</b>	<b>6,238,703</b>	<b>667,100</b>	<b>(6,980,234)</b>	<b>325,569</b>
Increase in Additional paid-in capital	11	–	581,681	–	–	581,681
Net decrease in Government investments	12	–	–	(166,005)	–	(166,005)
Loss for the year		–	–	–	(323,222)	(323,222)
<b>As at December 31, 2020</b>		<b>400,000</b>	<b>6,820,384</b>	<b>501,095</b>	<b>(7,303,456)</b>	<b>418,023</b>
	Notes	Share capital	Additional paid-in capital	Government investments	Accumulated loss	Total equity
<b>As at December 31, 2020</b>		<b>400,000</b>	<b>6,820,384</b>	<b>501,095</b>	<b>(7,303,456)</b>	<b>418,023</b>
Increase in Additional paid-in capital	11	–	272,433	–	–	272,433
Net increase in Government investments	12	–	–	304,960	–	304,960
Loss for the year		–	–	–	(552,230)	(552,230)
<b>As at December 31, 2021</b>		<b>400,000</b>	<b>7,092,817</b>	<b>806,055</b>	<b>(7,855,686)</b>	<b>443,186</b>

*The accompanying notes form an integral part of these consolidated financial statements.*



**Consolidated statement of cash flows**

*(Amounts presented are in thousands of Azerbaijani manats)*

	Notes	Year ended December, 31 2021	Year ended December, 31 2020
<b>Operating activities</b>			
Loss before tax		(551,632)	(323,137)
<b>Non-cash adjustments to reconcile loss before tax to net cash flows</b>			
Depreciation of property, plant and equipment and	21	42,408	21,357
Depreciation of right of use asset	21	272	223
Change in impairment of trade and other receivables	9	18,084	9,337
Change in provision	14	557	(1,560)
Gain on reversal of allowance for payments	20	-	(4,713)
Finance cost		3,450	2,823
Interest expense lease liabilities	6	60	63
Impairment of property, plant and equipment and intangible assets	21	549,528	207,855
Foreign exchange (gain)/loss	21	(10,347)	14,959
Loss on disposal of property, plant and equipment	21	81	275
		<b>52,461</b>	<b>(72,518)</b>
<b>Working capital adjustments</b>			
Inventories		(3,407)	2,326
Taxes receivable		3,512	1,814
Trade and other receivables		(25,858)	(5,119)
Deferred revenue		606	(245)
Trade and other payables		(43,469)	45,526
Prepayment		386	15,283
Taxes and penalties payable other than income tax		24,860	1,928
		<b>9,091</b>	<b>(11,005)</b>
Income tax paid		(512)	(131)
<b>Net cash flows used in operating activities</b>		<b>8,579</b>	<b>(11,136)</b>
<b>Investing activities</b>			
Purchase of property, plant and equipment		(5,085)	(3,420)
Purchase of intangible assets		(163)	(823)
<b>Net cash flows used in investing activities</b>		<b>(5,248)</b>	<b>(4,243)</b>
<b>Financing activities</b>			
Payment of lease liabilities	6	(320)	(270)
<b>Net cash flows used in financing activities</b>		<b>(320)</b>	<b>(270)</b>
Foreign exchange gain on cash and cash equivalents		32	549
<b>Net decrease in cash and cash equivalents</b>		<b>3,043</b>	<b>(15,100)</b>
<b>Cash and cash equivalents at the beginning of the year</b>	10	<b>2,863</b>	<b>17,963</b>
<b>Cash and cash equivalents at the end of the year</b>	10	<b>5,906</b>	<b>2,863</b>

*The accompanying notes form an integral part of these consolidated financial statements.*

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 1. The Group's principal activity

Azersu Open Joint Stock Company (“Azersu OJSC”) and its subsidiaries (the “Group”) were established by the Decree of President of Republic of Azerbaijan on June 11, 2004 in accordance with legislation and are domiciled in the Republic of Azerbaijan. The Group is 100% owned by the government of the Republic of Azerbaijan (the “Government”) and is a natural monopoly in charge of the implementation of the Government policy and strategy in the field of water supply, drinking water supply and sanitation services in the Republic of Azerbaijan. The Group's main functions pertain to extraction of water from sources followed by treatment as filtering and stabilization of water specification to make available to consumers' use, distribution and sale within the Republic of Azerbaijan.

The subsidiaries of the Group are disclosed in Note 11.

The registered address of the Group is 67, Moscow avenue, AZ1012, Baku, the Republic of Azerbaijan.

## 2. Basis of preparation and significant accounting policies

### Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented.

### Going concern

The going concern basis assumes that the Group will continue its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The Group's current liabilities exceeded its current assets by AZN 253,258 and AZN 266,655 as at December 31, 2021 and December 31, 2020, respectively, due to significant current investments in the infrastructure projects. The Group incurred a net loss of AZN 552,230 during the year ended December 31, 2021 (December 31 2020: AZN 323,222). The Group is part of the Government monopoly for supply of water and sewerage services and the Government keeps on investing to sustain the operations of the Group along with current investment projects.

The Group is actively involved in investing activities of construction of new water pipelines and sewerage systems in the Republic of Azerbaijan and receives subsidies from the Government on a regular basis. Historically the Group has had operating losses, negative cash flows from operations, and working capital deficit.

Management has developed a Master-Plan related to construction of new infrastructure projects as well as repair of existing facilities for future generation of cash inflows. Which will enable the Group to increase its subscribers, collection of receivables and reduce sales losses. Moreover by the Resolution No. 5 of the Tariff (Price) Council of the Republic of Azerbaijan dated January 30, 2021 the Decision No. 6 of the Tariff (Price) Council of the Republic of Azerbaijan dated May 13, 2016 “On approval of tariffs for water supply and wastewater disposal services” was amended. The decision came into force on February 1, 2021. Eventually this will lead to enhance the Group's financial position upon completion of the capital projects which are currently under construction. The Group continues to remain dependent on its ability to obtain sufficient funding from the Government to sustain operations and complete its current investment projects.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Going concern (continued)**

These conditions give rise to an uncertainty which may cast significant doubt about the Group’s ability to continue as a going concern. However, the Government as an ultimate shareholder of the Group has an incentive to continue to support financing the Group because of its social contribution and importance to the country. Management believes that appropriate measures are being taken for the Group to continue its operational existence in the foreseeable future. Accordingly, the Group applied going concern basis in preparing its consolidated financial statements.

### **Basis of consolidation**

The consolidated financial statements of the Group comprise the financial statements of “Azersu” OJSC and its subsidiaries as at December 31, 2021. Subsidiaries are all entities (including special-purpose entities) over which the Group has control, being the power to govern the financial and operating policies so as to obtain benefits from its activities, generally accompanying a shareholding of more than one half of the voting rights. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns.

The Group re-assesses whether or not it controls investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity, while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

### **Current versus non-current classification**

The Group presents assets and liabilities in the consolidated statement of financial position based on current/ non-current classification. An asset as current when it is:

- It is expected to be settled in normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within 12 months after the reporting period; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period

The Group classifies all other assets as non-current.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Current versus non-current classification (continued)**

A liability is current when:

- It is expected to be settled in normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within 12 months after the reporting period; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Group classifies all other liabilities as non-current.

Deferred income tax assets and liabilities are classified as non-current assets and liabilities.

### **Business combinations**

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses. When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

#### *Business combinations with entities under common control*

The Group applies acquisition method of accounting for business combinations with entities under the common control.

### **Foreign currency translation**

All amounts in these consolidated financial statements are presented in thousands of Azerbaijani manats (“AZN”), unless otherwise stated.

The functional currency of “Azersu” OJSC and its subsidiaries is AZN as the majority of the Group's revenues, costs, inventory purchased, and trade liabilities are either priced, incurred, payable or otherwise measured in AZN.

The transactions executed in foreign currencies are initially recorded in AZN by applying the appropriate rates of exchanges prevailing at the date of transaction.

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 2. Basis of preparation and significant accounting policies (continued)

### Foreign currency translation (continued)

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date.

Foreign exchange gains and losses resulting from the re-measurement of monetary assets into the functional currency are recognized in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of gain or loss on change in fair value in the item (i.e., the translation differences on items whose fair value gain or loss is recognized in other comprehensive income (“OCI”) or profit or loss are also recognized in OCI or profit or loss, respectively).

AZN is not a fully convertible currency outside the territory of the Republic of Azerbaijan. Within the Republic of Azerbaijan, official exchange rates are determined daily by the Central Bank of the Republic of Azerbaijan (“Central Bank”). Transactions denominated in foreign currencies are recorded at the official exchange rate on the date of the transaction.

The official rates of exchange used for translating foreign currency balances were as follow:

	December 31, 2021	December 31, 2020
1 USD / 1 AZN	1.7000	1.7000
1 EUR / 1 AZN	1.9265	2.0890
1 SDR / 1 AZN	2.3793	2.4485

### Financial instruments - key measurement terms

Depending on their classification financial instruments are carried at fair value or amortized cost as described below.

Fair value is 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. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Financial instruments - key measurement terms (continued)**

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 - quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 - valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- Level 3 - valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the consolidated financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

*Cost* is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes transaction costs. Measurement at cost is only applicable to investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured.

*Amortised cost (AC)* is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses ("ECL"). Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to the maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of the related items in the consolidated statement of financial position.

*The effective interest method (EI)* is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

### **Initial recognition of financial instruments**

Trading securities, derivatives and other financial instruments at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Group commits to deliver a financial asset. All other purchases are recognized when the entity becomes a party to the contractual provisions of the instrument.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Classification of financial instruments**

From January 1, 2018 on initial recognition, a financial asset is classified as measured at: amortized cost, fair value through other comprehensive income (“FVOCI”) or fair value through profit or loss (“FVPL”).

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give right on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated at FVPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give right on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortized cost or at FVOCI at FVPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

### **Reclassification of financial assets**

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model for managing financial assets. The reclassification has a prospective effect.

### **Financial assets impairment – credit loss allowance for Expected credit loss (ECL)**

The Group assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI and for the exposures arising from loan commitments and financial guarantee contracts. The Group measures ECL and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions and forecasts of future conditions.

Debt instruments measured at AC are presented in the consolidated statement of financial position net of the allowance for ECL. For loan commitments and financial guarantees, a separate provision for ECL is recognized as a liability in the consolidated statement of financial position. For debt instruments at FVOCI, changes in amortized cost, net of allowance for ECL, are recognized in profit or loss and other changes in carrying value are recognized in OCI as gains less losses on debt instruments at FVOCI.

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 2. Basis of preparation and significant accounting policies (continued)

### “Simplified approach” to impairment

IFRS 9 allows entities to apply a ‘simplified approach’ for trade receivables, contract assets and lease receivables. The simplified approach allows entities to recognize lifetime expected losses on all these assets without the need to identify significant increases in credit risk. Certain accounting policy choices apply:

- For trade receivables and contract assets that do not contain a significant financing component, it is a requirement to recognize a lifetime expected loss allowance (i.e. an entity must always apply the ‘simplified approach’).
- For other trade receivables, other contract assets, operating lease receivables and finance lease receivables it is an accounting policy choice that can be separately applied for each type of asset (but which applies to all assets of a particular type).

### Presentation of allowance for ECL in the consolidated statement of financial position

Loss allowances for ECL are presented in the consolidated statement of financial position as follows:

- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Group cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Group presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognized in the consolidated statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is recognized as part of fair value reserve.

### Financial assets – write-off

Financial assets are written-off, in whole or in part, when the Group exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event. The Group may write-off financial assets that are still subject to enforcement activity when the Group seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.

### Derecognition of financial assets

The Group derecognises financial assets when

- (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or
- (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Financial liabilities**

#### **Other financial liabilities**

Other financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

#### **Payables**

Payables are obligations paid by suppliers in exchange for goods or services. Accounts payable are classified as current liabilities if the repayment obligation is due for one year or less (or no longer than the whole working period).

Payables are stated at amortized cost using the effective interest rate.

#### **Interest bearing loans and borrowings**

All loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method. Gains and losses are recognized in the statement of comprehensive income when the liabilities are derecognized as well as through the amortization process.

#### **Derecognition of financial liabilities**

The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit and loss accounts.

#### **Offset of financial assets and liabilities**

Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to either settle on a net basis, or to realize the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) the event of default and (iii) the event of insolvency or bankruptcy.

#### **Cash and cash equivalents**

Cash and cash equivalents include cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 2. Basis of preparation and significant accounting policies (continued)

### Property, plant and equipment

Property, plant and equipment are stated at cost as described below, less accumulated depreciation and provision for impairment, where required.

The initial cost of an asset comprises its purchase price or construction cost, any cost directly attributable to bringing the asset into operation, the initial estimate of decommissioning obligation, if any, and for qualifying assets, borrowing costs. The assets held under finance lease are also included within property, plant and equipment.

#### *Development of tangible assets*

Expenditure on the construction, installation or completion of infrastructure facilities such as pipelines and transmission facilities are capitalized within tangible assets according to nature. All minor repair and maintenance costs are expensed as incurred. Cost of replacing major parts components of property, plant and equipment items are capitalized and replaced part is retired.

At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's or cash generating unit's fair value less costs to sell and its value in use. The carrying amount reduced to the recoverable amount and the impairment loss, if any, is recognized in the consolidated statement of profit or loss and other comprehensive income. An impairment loss recognized for an asset or cash generating unit in prior years is reversed if there are indicators that impairment loss may no longer exist or may have decreased.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount and are recognized in profit or loss.

#### *Depreciation*

Depreciation of property, plant and equipment are calculated using the straight-line method over their expected useful lives.

The estimated useful lives of the Group's property, plant and equipment are as follows:

Buildings and constructions	20 to 60 years
Facilities and transmission devices	3 to 40 years
Machinery and equipment	3 to 15 years
Vehicles	3 to 10 years
Office equipment	3 to 8 years

Land and assets under construction are not depreciated.

The expected useful lives of property, plant and equipment are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life unless scrap value is significant. The assets' residual values are reviewed, and adjusted if appropriate, at each consolidated statement of financial position date.

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **2. Basis of preparation and significant accounting policies (continued)**

### **Inventories**

Inventories are stated at the lower of cost and net realizable value. Cost is assigned by the FIFO method. Cost comprises direct purchase costs, cost of production, transportation and manufacturing expenses (based on normal operating capacity).

### **Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of the respective asset. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Borrowing costs for all eligible qualifying assets are capitalized.

### **Intangible assets**

Intangible assets are stated at cost, less accumulated amortization and accumulated impairment losses. Intangible assets include rights, licenses and computer software.

The useful lives of intangible assets are assessed as either finite or indefinite. Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the statement of profit or loss and other comprehensive income in the expense category consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

### **Impairment of intangible assets**

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's ("CGU") fair value less costs to sell and its value in use. It is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. 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. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators.



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## **2. Basis of preparation and significant accounting policies (continued)**

### **Impairment of intangible assets (continued)**

The Group bases its impairment calculation on detailed budgets and forecasts which are prepared separately for each of the Group's CGU to which the individual assets are allocated. These budgets and forecast calculations are generally covering a period of five years. For longer periods, a long-term growth rate is calculated and applied to project future cash flows after the fifth year.

Impairment losses of continuing operations, including impairment on inventories, are recognized in the consolidated income statement in those expense categories consistent with the function of the impaired asset, except for a property previously revalued where the revaluation was taken to other comprehensive income. In this case, the impairment is also recognized in other comprehensive income up to the amount of any previous revaluation.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the Group estimates the asset's or CGU's recoverable amount.

A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized.

The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the income statement unless the asset is carried at a revalued amount, in which case the reversal is treated as a revaluation increase.

### **Corporate income taxes**

Corporate income taxes have been provided for in consolidated financial statements in accordance with the applicable legislation enacted by the reporting date. The income tax charge comprises current tax and deferred tax and is reflected in the consolidated statement of profit or loss and other comprehensive income.

Current income tax is the amount expected to be paid to or recovered from the state budget through taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided in full, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.



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## **2. Basis of preparation and significant accounting policies (continued)**

### **Value-added tax**

The tax legislation allows the settlement of sales and purchases value-added tax (“VAT”) on a net basis.

The amount of VAT paid when purchasing goods (works, services) for VAT-charged transactions is reimbursed when the value of the transaction is paid to the bank account and the amount of VAT is paid to the VAT deposit account. The timing of the reimbursed VAT is regulated by the relevant legislation.

*VAT recoverable* relates to purchases which have not been settled at the statement of financial position date. VAT recoverable is reclaimable against VAT on sales upon payment for the purchases.

### **Provisions for liabilities and charges**

Provisions for liabilities and charges are liabilities of uncertain timing or amount. They are accrued when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

### **Government investments**

Government investments are made in the form of cash contributions, transfer of other state-owned entities or transfer of all or part of the Government’s share in other entities. Transfer of the state-owned entities to the Group is recognized as contribution through consolidated equity statement in the amount being the fair value of the transferred entity (in case of transfer by the Government of its share in other entities – the transferred share in the fair value of the respective entity).

### **Revenue recognition**

Revenue comprises the fair value of consideration received or receivable for the sale of goods and services in the ordinary course of the Group’s activities. Revenue is shown net of VAT, returns, discounts, and other sales-based taxes, if any, after eliminating sales within the Group.

Revenue from sales of water and sewerage services are recorded on the basis of regular water meter readings (monitored on a monthly basis) and estimates of customer usage from the last meter reading to the end of the reporting period. Water prices and waste water treatment tariffs to the final consumers in the Republic of Azerbaijan are regulated by the Tariff Council of the Republic of Azerbaijan.

Sales of services are recognized in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

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## **2. Basis of preparation and significant accounting policies (continued)**

### **Expenses**

Expenses are presented by function in consolidated statement of profit or loss and other comprehensive income. Categorization of the nature of expenses is based on operational functions of the Group's departments and subsidiaries.

### **Employee benefits**

Wages, salaries, contributions to the Social Protection Fund of the Republic of Azerbaijan, paid annual leave and sick leave, bonuses, and non-monetary benefits (e.g. health services) are accrued in the year in which the associated services are rendered by the employees of the Group.

### **Related parties**

Related parties are disclosed in accordance with IAS 24 *Related Party Disclosures*.

Governmental economic and social policies affect the Group's financial position, results of operations and cash flows. The Government imposed an obligation on the Group to provide an uninterrupted supply of water to customers in the Republic of Azerbaijan at government controlled prices.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be affected on the same terms, conditions and amounts as transactions between unrelated parties. It is the nature of transactions with related parties that they cannot be presumed to be carried out on an arms-length basis.

### **Lease agreements**

#### **Accounting for leases by the Group as a lessee**

The Group leases office premises. Leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is recognised at cost and depreciated over the shorter of the assets useful life and the lease term on a straight-line basis.

Liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- Fixed payments (including in-substance fixed payments), less any lease Incentives receivable;
- Variable lease payment that are based on an index or a rate;
- Amounts expected to be payable by the lessee under residual value guarantees;
- The exercise price of a purchase option If the lessee is reasonably certain to exercise that option;
- Payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be determined, the lessee's incremental borrowing rate is used, being the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions. Right-of-use assets are measured at cost comprising the following:



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## **2. Basis of preparation and significant accounting policies (continued)**

### **Lease agreements (continued)**

- The amount of the initial measurement of lease liability;
- Any lease payments made at or before the commencement date less any lease incentives received;
- Any initial direct costs; and
- Restoration costs.

In determining the lease term, management of the Group considers all facts and circumstances that create an economic incentive to exercise an extension option, or not exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated).

The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee.

### **Accounting for operating leases by the Group as a lessor**

When assets are leased out under an operating lease, the lease payments receivable are recognised as rental income on a straight-line basis over the lease term.

The accounting policy adopted in the preparation of the financial statements is the same as the accounting rules in the preparation of the consolidated financial statements of the Group for the year ended 31 December 2021. Several amendments came into force on 1 January 2022, but had no effect on the Group's consolidated financial statements.

## **3. Adoption of new or revised standards and interpretations**

### **Amendments to IAS 1: Classification of Liabilities as Current or Non-current**

In January 2020, the IASB issued amendments to paragraphs 69 to 76 of IAS 1 to specify the requirements for classifying liabilities as current or non-current. The amendments clarify:

- What is meant by a right to defer settlement;
- That a right to defer must exist at the end of the reporting period;
- That classification is unaffected by the likelihood that an entity will exercise its deferral right;
- That only if an embedded derivative in a convertible liability is itself an equity instrument would the terms of a liability not impact its classification.

These amendments shall enter into force for annual reporting periods beginning on or after 1 January 2023 and shall be applied retrospectively. The Group is currently assessing the impact of the amendments on its current practice and whether there is a need to revise existing loan agreement



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### **3. Adoption of new or revised standards and interpretations (continued)**

#### **Reference to the Conceptual Framework – Amendments to IFRS 3**

In May 2020, the IASB issued Amendments to IFRS 3 Business Combinations – Reference to the Conceptual Framework. The amendments are intended to replace a reference to the Framework for the Preparation and Presentation of Financial Statements, issued in 1989, with a reference to the Conceptual Framework for Financial Reporting issued in March 2018 without significantly changing its requirements.

The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential ‘day 2’ gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 Levies, if incurred separately. At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the Framework for the Preparation and Presentation of Financial Statements. The amendments are effective for annual reporting periods beginning on or after January 1, 2022 and apply prospectively. These amendments are not expected to have impact on the consolidated financial statements of the Group.

#### **Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16**

In May 2020, the IASB issued Property, Plant and Equipment – Proceeds before Intended Use, which prohibits entities deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognises the proceeds from selling such items, and the costs of producing those items, in profit or loss.

The amendment is effective for annual reporting periods beginning on or after January 1, 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Group.

#### **Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37**

In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making.

The amendments apply a “directly related cost approach”. The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

The Group will apply these amendments to contracts for which it has not yet fulfilled all its obligations at the beginning of the annual reporting period in which it first applies the amendments.

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### 3. Adoption of new or revised standards and interpretations (continued)

#### **IFRS 1 First-time Adoption of International Financial Reporting Standards – Subsidiary as a first-time adopter**

As part of its 2018-2020 annual improvements to IFRS standards process, the IASB issued an amendment to IFRS 1 First-time Adoption of International Financial Reporting Standards. The amendment permits a subsidiary that elects to apply paragraph D16(a) of IFRS 1 to measure cumulative translation differences using the amounts reported by the parent, based on the parent's date of transition to IFRS. This amendment is also applied to an associate or joint venture that elects to apply paragraph D16(a) of IFRS 1. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted.

These amendments are not expected to have impact on the consolidated financial statements of the Group.

#### **IFRS 9 Financial Instruments – Fees in the ‘10 per cent’ test for derecognition of financial liabilities**

As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted. The Group will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendments are not expected to have a material impact on the Group.

### 4. Critical accounting estimates and judgments

The preparation of the Group's consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumption and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Estimates and judgments are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group based its assumptions and estimates on parameters available when consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Group. Such changes are reflected in the assumptions when they occur. Management also makes certain judgments, apart from those involving estimations, in the process of applying the accounting policies.

Judgments that have the most significant effect on the amounts recognized in these consolidated financial statements and estimates that can cause a material adjustment to the carrying amount of assets and liabilities at reporting date include:



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#### **4. Critical accounting estimates and judgments (continued)**

##### **Environmental obligations**

The Group records a provision in respect of estimated costs of remediation of the damage historically caused to the natural environment by the activities of the Group. The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the respective consolidated statement of financial position date based on requirements of the Code of Administrative Offences of the Republic of Azerbaijan in effect and is also subject to changes because of modifications and revisions. Governmental authorities continuously consider applicable regulations and their enforcement.

Estimated liability for environmental remediation as of December 31, 2021 and December 31, 2020 amounted nil. Changes in any of these conditions may result in adjustments to provisions recorded by the Group.

##### **Useful lives of property, plant and equipment and intangible assets**

Management determines the estimated useful lives and related depreciation and amortization charges for its property, plant and equipment and intangible assets. This estimate is based on projected period over which the Group expects to consume economic benefits from the asset. Management will increase the depreciation charge where useful lives are less than previously estimated lives, or it will write-off or write-down technically obsolete assets that have been abandoned or sold. The useful lives are reviewed at least at each reporting date. Changes in any of the above conditions or estimates may result in adjustments to future depreciation rates.

##### **Depreciation and amortization method of property, plant and equipment and intangible assets**

Management determines the method of depreciation and amortization of property, plant and equipment and intangible assets. These estimates are based on the Group's fair presentation of those assets. As at January 1, 2021, the management of the Group reviewed and re-estimated the depreciation method for machinery and equipment and vehicles and changed depreciation method from reducing balance method to the straight-line method prospectively. As a result of the change, the Group's depreciation expenses were AZN 53,435 less.

##### **Deferred income tax asset recognition**

The net deferred tax asset represents income taxes recoverable through future deductions from taxable profits and is recorded on the consolidated statement of financial position. Deferred income tax assets are recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimation based on last three years results and expectations of future income that are believed to be reasonable under the circumstances.

##### **Current taxes**

Azerbaijani tax, currency and customs legislation is subject to varying interpretations and changes occurring frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group may be assessed additional taxes, penalties and interest, which can be significant.

The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As at December 31, 2021 and December 31, 2020 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

#### 4. Critical accounting estimates and judgments (continued)

##### **Impairment of non-financial assets**

Management assesses whether there are any indicators of possible impairment of all non-financial assets at each reporting date based on events or circumstances that indicate the carrying value of assets may not be recoverable. Goodwill and other indefinite life intangibles are tested for impairment annually and at other times when impairment indicators exist. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable.

Given the nature of the Group's activities, information on the fair value of an asset is usually difficult to obtain unless negotiations with potential purchasers are taking place. Consequently, unless indicated otherwise, the recoverable amount used in assessing the impairment charges described below is value-in-use.

When value in use calculations is undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

The Group has been considered as one CGU and impairment was determined on the level of the whole Group. The value of the CGU was calculated by discounting the future cash flows at the rate of 11.84% (December 31, 2020: 9.21%) on pre-tax base and impairment charge of AZN 549,528 (December 31, 2020: AZN 207,855) has been recognized in consolidated statement of profit or loss and other comprehensive income to write-down the book value of certain property, plant and equipment with regard to the functional use of these assets.

The discount rate calculation is based on the specific circumstances of the Group and its operating segments and derived from its weighted average cost of capital ("WACC").

In calculating WACC the cost of equity was estimated using peer group data and the cost of debt is based on interest bearing borrowings, the Group is obliged to service. Specific risks are incorporated by applying individual beta factors, market risk and size of the Group. The beta factors are evaluated annually based on publicly available market data. If the estimated WACC used in the calculation had been 1% higher / lower than management's estimate, the aggregate amount of impairment loss would have been AZN 110,658 higher / AZN 152,529 lower (December 31, 2020: AZN 149,612 higher / AZN 230,171 lower, respectively).

##### **Impairment provision for trade receivables**

The impairment provision for trade receivables is based on management's assessment of the probability of collection of major individual consumers' accounts receivable. Significant financial difficulties of the consumers, probability that the contract parties will suffer bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the receivable is potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates. Additionally, a large number of minor receivables are grouped into homogenous groups and assessed for impairment collectively. Trade receivables outstanding more than 12 months are generally written off against respective impairment provision.

When there is no expectation of recovering additional cash for an amount receivable, amount receivable is written off against associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

#### **4. Critical accounting estimates and judgments (continued)**

##### **Provision for unused vacation**

The Group has a policy to settle total amount of payable to individual employee accrued for several years for unused vacations only when the vacation option is utilized by the employee and no reliable basis for estimation of timing of payment is available.

##### **Determining lease term**

The application of IFRS 16 requires to make judgements of right-of-use assets and lease liabilities. In determining the lease term, the Group considers all facts and circumstances that create an economic incentive to exercise renewal options (or not to exercise termination options). Assessing whether a contract include a lease also requires judgement. Estimates are required to determine the appropriate discount rate used to measure lease liabilities.

##### **Going concern**

Management prepared these financial statements on a going concern basis. In making this judgement management considered the Group's financial position, current intentions, profitability of operations and access to financial resources, and analysed the impact of the recent financial crisis on future operations of the Group.

According to management's estimates and measures, it is considered the Group would be able to adjust the needs of liquidity over the next twelve months and therefore current financial statements have been prepared on a going concern basis.

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

## 5. Property, plant and equipment

Movements in the carrying amount of property, plant and equipment (“PPE”) were as follows:

Cost	Land	Buildings and constructions	Facilities	Transmission devices	Machinery and equipment	Vehicles	Stationary and office equipment	Construction in progress	Intangible assets	Total
<b>At January 1, 2020</b>	21,663	46,822	45,319	361,762	81,112	37,127	5,172	5,106,415	5,229	5,710,621
Additions	–	–	99	1	2,876	48	109	329,571	–	332,704
Granted assets	–	1,135	2,149	8,360	1,081	27	139	–	–	12,891
Transfers	–	4,088	6,927	54,535	6,534	515	6	(73,428)	823	–
Disposals	–	–	(1)	–	(269)	–	–	(5)	–	(275)
<b>At December 31, 2020</b>	21,663	52,045	54,493	424,658	91,334	37,717	5,426	5,362,553	6,052	6,055,941
Additions	–	–	7	42	2,675	2,211	149	200,233	–	205,317
Granted assets	41	41,381	28,575	259,210	68,198	36	54	–	–	397,495
Transfers	–	5,437	2,535	155,330	16,119	–	11	(179,595)	163	–
Disposals	–	–	(1)	(16)	(5)	–	–	(59)	–	(81)
<b>At December 31, 2021</b>	21,704	98,863	85,609	839,224	178,321	39,964	5,640	5,383,132	6,215	6,658,672
<b>Depreciation and impairment</b>										
<b>At January 1, 2020</b>	(15,524)	(38,188)	(38,643)	(296,183)	(75,835)	(36,840)	(4,929)	(4,372,148)	(4,799)	(4,883,089)
Depreciation charge	–	(730)	(952)	(6,641)	(12,031)	(764)	(105)	–	(133)	(21,356)
Impairment charge	(1,427)	(2,678)	(3,027)	(24,801)	(397)	–	(46)	(175,267)	(212)	(207,855)
<b>At December 31, 2020</b>	(16,951)	(41,596)	(42,622)	(327,625)	(88,263)	(37,604)	(5,080)	(4,547,415)	(5,144)	(5,112,300)
Depreciation charge	–	(2,335)	(2,970)	(24,813)	(11,771)	(261)	(134)	–	(124)	(42,408)
Impairment charge	–	(19,409)	(13,545)	(175,442)	(27,657)	(10)	(110)	(313,073)	(282)	(549,528)
<b>At December 31, 2021</b>	(16,951)	(63,340)	(59,137)	(527,880)	(127,691)	(37,875)	(5,324)	(4,860,488)	(5,550)	(5,704,236)
<b>Net book value</b>										
<b>At December 31, 2020</b>	4,712	10,449	11,871	97,033	3,071	113	346	815,138	908	943,641
<b>At December 31, 2021</b>	4,753	35,523	26,472	311,344	50,630	2,089	316	522,644	665	954,436

As of December 31, 2021, the residual value of property, plant and equipment with historical cost of AZN 1,122,128 is zero (2020: AZN 314,388)



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 5. Property, plant and equipment (continued)

### Granted assets

During the years ended December 31, 2021 and December 31, 2020 certain assets (transmission devices and other infrastructures, land, buildings, etc.) were contributed to the Group by various governmental organizations. The Group engaged an independent appraiser to determine the fair value of granted assets as of December 31, 2021 and December 31, 2020. Fair value of granted assets was determined in the amount of AZN 397,496 for the year ended December 31, 2020 (December 31, 2020: AZN 12,891) and comprised of government organizations' assets of AZN 397,460 (2020: AZN 12,864) and AZN 36 of commercial organizations' assets (2020: AZN 27). Assets received from governmental organizations were recognized as Government investments in the consolidated financial statements (see Note 12).

### Prepayments

Included in construction in progress are prepayments made for construction activities and services that have not been provided yet. The net amounts of such prepayments are AZN 25,545 and AZN 25,994 as at December 31, 2021 and December 31, 2020, respectively.

### Capitalization of borrowings costs

Since 2005, the Group inceptioned several construction projects for building of new water pipelines and reservoirs as well as waste management and sewerage system in Baku city and other regions of the Republic of Azerbaijan. The projects are financed through government investments and loans from international financial organizations. During 2021, the Group did not have borrowing costs capitalized on construction property (December 31, 2020: AZN 2,284).

## 6. Right of use asset and lease liabilities

The Group leases offices. Rental contracts are typically made for forced periods of 2-10 years but may have extension options.

Contracts may contain both lease and non-lease components. The Group elected not to separate lease and non-lease components and instead accounts for these as a single lease component. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions.

The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes. Extension and termination options are included in a number of leases across the Group. These are used to maximize operational flexibility in terms of managing the assets used in the Group's operations. The majority of extension and termination options held are exercisable by both the Group and the respective lessors.

From January 1, 2019, leases are recognized as a right-of-use asset and a corresponding liability from the date when the leased asset becomes available for use by the Group.

The right-of-use assets by class of underlying items is analyzed as follows:

	Office spaces	Total
<b>December 31, 2020</b>	<b>702</b>	<b>702</b>
Additions for the year	303	303
Modification	(88)	(87)
Termination	(37)	(37)
Depreciation of right-of-use asset	(271)	(271)
<b>December 31, 2021</b>	<b>609</b>	<b>609</b>

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

## 6. Right-of-use assets and lease liabilities (continued)

The reconciliation of the opening and closing amounts of lease liabilities with relevant cash and non-cash changes from financing activities is stated below:

	Lease liabilities
<b>December 31, 2020</b>	<b>740</b>
Additions for the year	303
Modification	(87)
Termination	(41)
Interest expense on lease liabilities	60
Payment of interest expense on lease liabilities	(60)
Payment of principal amount on lease liabilities	(260)
<b>December 31, 2021</b>	<b>655</b>

Future minimum lease payments as at December 31, 2021:

	Up to 1 year	More than 1 year	Total
Future minimum payments	293	517	810
Finance cost	(49)	(106)	(155)
<b>Net carrying value</b>	<b>244</b>	<b>411</b>	<b>655</b>

Future minimum lease payments as at December 31, 2020:

	Up to 1 year	More than 1 year	Total
Future minimum payments	340	565	905
Finance cost	(53)	(112)	(165)
<b>Net carrying value</b>	<b>287</b>	<b>453</b>	<b>740</b>

The recognized lease liabilities classified as follows:

	December 31, 2021	December 31, 2020
Current portion	244	287
Non-current portion	411	453
<b>Total lease liabilities</b>	<b>655</b>	<b>740</b>

## 7. Taxes receivable

In December 31, 2021 and December 31, 2020 taxes receivable mainly comprised VAT recoverable in the amount of AZN 15,033 (December 31, 2020: AZN 18,545) related to purchases which have not been settled at the end of the year, and thus not claimed in tax declarations and prepayment on construction works which can be claimed only after the vendor performs the associated services.

Taxes receivable is recoverable by means of an offset against tax liabilities or as a direct cash refund from the tax authorities.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 8. Inventories

Inventories comprised the following as at:

	December 31, 2021	December 31, 2020
Materials	6,714	6,103
Goods	3,686	2,796
Goods for sale	4,335	2,680
Spare parts	1,281	1,000
Raw materials	520	542
Fuel and lubricants	48	56
<b>Total inventories</b>	<b>16,584</b>	<b>13,177</b>

## 9. Trade and other receivables

Trade and other receivables comprised the following as at:

	December 31, 2021	December 31, 2020
Receivables from sale of water	120,460	94,653
Less impairment loss provision	(94,364)	(76,280)
<b>Total trade receivables</b>	<b>26,096</b>	<b>18,373</b>
Other receivables	1,504	1,453
<b>Total trade and other receivables</b>	<b>27,600</b>	<b>19,826</b>

As of December 31, 2021 trade receivables are mainly represented by receivables for sale of water to non-population and population in the amount of AZN 55,411 and AZN 65,049 respectively (December 31, 2020: AZN 49,912 and AZN 44,741, respectively). General credit terms on sales of water include 30 days settlement requirement after the billing date. Tariffs on sales of water are subject to state regulations and are governed by the Tariff Council of the Republic of Azerbaijan.

Movements on the provision for impairment of trade receivables were as follows:

	2021	2020
<b>At January 1</b>	<b>76,280</b>	<b>66,943</b>
Receivables written off during the year as uncollectible net of recovery	—	—
Net change in provision (Note 21)	18,084	9,337
<b>At December 31</b>	<b>94,364</b>	<b>76,280</b>

The ageing analysis of trade and other receivables is as follows:

	Total	<30 days	Past due but not impaired collectively	Individually and impaired
December 31, 2020	96,106	19,826	—	76,280
December 31, 2021	121,964	27,600	—	94,364

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

# **10. Cash and cash equivalents and restricted cash**

Cash and cash equivalents comprised the following as at:

	December 31, 2021	December 31, 2020
Cash in transit	2,795	2,079
Correspondent and settlement accounts	3,109	777
Cash on hand	–	5
Other cash equivalents	2	2
<b>Total cash and cash equivalents</b>	<b>5,906</b>	<b>2,863</b>

Cash and cash equivalents in original currency comprised the following as at:

	December 31, 2021	December 31, 2020
AZN dominated bank balances	5,883	2,755
USD dominated bank balances	4	82
EUR dominated bank balances	19	21
Cash on hand	–	5
<b>Total cash and cash equivalents</b>	<b>5,906</b>	<b>2,863</b>

The balances of cash and cash equivalents are included in Stage 1 in ECL assessment.

Restricted cash comprised the following as at:

	December 31, 2021	December 31, 2020
VAT deposit account	467	581
Designated accounts	–	186
<b>Total restricted cash</b>	<b>467</b>	<b>767</b>

Account at the State Treasury was originated based on signed order by the Government and is held at the State Treasury of the Republic of Azerbaijan. The Group has no direct control over the account which is mainly used for financing of the Group’s construction projects and funded by the Government based on authorized requests placed at the State Treasury. Subject to the State Treasury approval appropriated funds are directly transferred to the vendor’s account. The Group treats these contributions as a Government Investment within the Group’s equity.

The Government has also established Designated Accounts at commercial banks acceptable to the international financing institutions in accordance with the terms of respective loan agreements for use of funds provided under these loan agreements. Designated Accounts are established, managed, replenished and liquidated in accordance with manuals introduced by the international financing institutions. The Designated Accounts are maintained in foreign currencies and the Group has no direct control over these accounts.

Effective January 1, 2008 the state tax authorities introduced VAT deposit accounts and enforced payments of input and output VAT via these accounts. In order to comply with new tax regulation, the Group has opened a VAT deposit account.



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## 11. Share capital

Share capital of the Group comprised the following as at:

	December 31, 2021		December 31, 2020	
	Number of shares	Share capital	Number of shares	Share capital
“Azersu” OJSC	20,000,000	400,000	20,000,000	400,000
<b>Subsidiaries</b>				
“Sutikinti” Division	100	1,423	100	1,423
“Sukanal” Scientific Research and Design Institute	–	131	–	131
“Ganja Sukanal” SJSC	383,640	7,673	383,640	7,673
“Aghdash Sukanal” SJSC	–	–	–	–
“Goychay Sukanal” SJSC	–	–	–	–
“Sheki Sukanal” SJSC	95,663	1,914	95,663	1,914
“Birleshmish Sukanal” LLC	4,173,128	83,463	4,173,128	83,463

Parent company of the Group, Azersu OJSC, has a legal status of a state enterprise. The Group includes 6 separate legal entities (2020: 6) each possessing their own share capital. As at December 31, 2021 and December 31, 2020 Azersu OJSC had authorized and issued 20,000,000 shares at par AZN 0.02. Azersu OJSC has ultimate control and 100% interest in all of its subsidiaries.

During 2021 the Group recorded additional paid-in capital in the amount of AZN 283,433 (December 31, 2020: AZN 581,681) based on value of the completed investment projects accepted by the Government.

## 12. Government investments

Government investments comprised the following as at:

	December 31, 2021	December 31, 2020
Non-financial asset investments	411,608	14,148
Investments financed from the State Budget of the Republic of Azerbaijan	237,821	354,885
Investments financed from international financial organizations under the state guarantee	156,626	132,062
<b>Total government investments</b>	<b>806,055</b>	<b>501,095</b>

The balance of Government investments comprised funding made from the State Budget to finance various capital and other expenditures of the Group, Government borrowings from international financial institutions and non-financial assets granted to the Group by the Government.

As discussed in Note 5, fair value of non-financial assets granted from the various budget organizations at the date of transition amounted to AZN 397,460 during 2021 (December 31, 2020: AZN 12,864).

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

### 13. Interest-bearing loans and borrowings

Interest-bearing loans and borrowings comprised the following:

	December 31, 2021	December 31, 2020
Government loans financed by international financial institutions	111,593	136,255
Loans from the Ministry of Finance of the Republic of Azerbaijan	148,504	128,433
Loans from local banks	–	73
<b>Total interest-bearing loans and borrowings</b>	<b>260,097</b>	<b>264,761</b>

Current portion of loans of the Group were represented by the following financial institutions:

Financial institution	Contractual interest rate	Original currency	Maturity date	December 31, 2021	December 31, 2020
World Bank (IDA)	0.75%	SDR	May 2030	3,297	8,588
World Bank (IDA)	0.75%	SDR	November 2037	546	1,184
KfW	0.75%	EUR	June 2040	927	1,006
KfW	0.75%	EUR	December 2045	1,718	1,860
Natixis	2.45%	EUR	September 2030	4,214	4,570
ADB	2.5%	SDR	November 2036	1,292	4,408
International Bank of Azerbaijan	1%	AZN	July 2025	–	73
<b>Total short-term loans and current portion of long- term loans</b>				<b>11,994</b>	<b>21,689</b>

Non-current portion of loans of the Group were represented by the following financial institutions:

Financial institution	Contractual interest rate	Original currency	Maturity date	December 31, 2021	December 31, 2020
World Bank (IDA)	0.75%	SDR	May 2030	–	4,338
World Bank (IDA)	0.75%	SDR	November 2037	–	566
KfW	0.75%	EUR	June 2040	16,485	18,776
KfW	0.75%	EUR	December 2045	39,571	44,662
Natixis	2.45%	EUR	September 2030	28,282	34,215
ADB	2.5%	SDR	November 2036	15,261	12,082
The Ministry of Finance	0%	AZN	December 2027	11,453	11,340
The Ministry of Finance	0%	USD	March 2028	28,269	27,989
The Ministry of Finance	0%	USD	August 2028	18,110	17,931
The Ministry of Finance	0%	USD	August 2030	17,907	17,730
The Ministry of Finance	0%	USD	August 2031	17,903	17,726
The Ministry of Finance	0%	USD	August 2027	17,925	17,748
The Ministry of Finance	0%	USD	August 2028	18,149	17,969
The Ministry of Finance	1%	USD	November 2031	10,686	–
The Ministry of Finance	1%	EUR	November 2031	8,102	–
<b>Total long-term loans</b>				<b>248,103</b>	<b>243,072</b>

Reconciliation of loans of the Group was represented as the following:

	December 31, 2020	Non-cash reconciliation			December 31, 2021
		Cash Reconciliation	Paid by Government	Forex and others	
Interest-bearing loans and borrowings	264,761	–	(19,002)	14,338	260,097
<b>Total loans</b>	<b>264,761</b>	<b>–</b>	<b>(19,002)</b>	<b>14,338</b>	<b>260,097</b>



(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

### 13. Interest-bearing loans and borrowings (continued)

	December 31, 2019	Cash reconciliation	Non-cash reconciliation		December 31, 2020
			Paid by Government	Forex and others	
Interest-bearing loans and borrowings	247,110	–	(19,050)	36,701	264,761
<b>Total loans</b>	<b>247,110</b>	<b>–</b>	<b>(19,050)</b>	<b>36,701</b>	<b>264,761</b>

#### Government loans financed by international financial institutions

Loans from international financial institutions represent lending for the financing of projects related to development and improvement of water supply system of the Republic of Azerbaijan lent directly to the Government. The Government in its turn transferred related rights and obligations on these loans to the Group by means of re-financing agreement between the Government and the Group under the similar terms and conditions.

##### Loans from World Bank (IDA)

On 6 July 1995 the Government entered into loan agreement with International Development Association (“IDA”) that is included in the World Bank group, for the amount of SDR 38,800 thousand (AZN 92,317). On 30 June 2003 the Government signed another loan agreement with IDA for the amount of SDR 9,673 thousand (AZN 23,015). The annual effective interest rate under these loan agreements is 0.75% and they are repayable until 2030 and 2037, respectively. These loans were lent for the financing of the project “Greater Baku Water Supply Rehabilitation Project”.

##### Loans from KfW

On 25 September 2006 two loans were lent to the Government by Kreditanstalt für Wiederaufbau (“KfW”) German government-owned development bank, in the amount of EUR 14,827 thousand (AZN 28,564) and EUR 26,559 thousand (AZN 51,166), at 0.75% and 0.75% annual effective interest rate and repayable until 2040 and 2045, respectively. The loans were lent for the financing of the project “Open Program Municipal infrastructure”.

##### Loan from Natixis

On 30 September 2006 the loan was lent to the Government by the Natixis, a French corporate and investment bank on behalf of the Government of the Republic of France, in the amount of EUR 35,000 thousand (AZN 67,428) at 2.45% annual effective interest rate and repayable until 2030. The loan was lent for the financing of the project “Reconstruction of Hovsan waste management system, Zygh pump station”.

##### Loan from Asian Development Bank

On 29 November 2005 the loan was lent to the Government by the Asian Development Bank (“ADB”), in the amount of SDR 5,428 thousand (AZN 12,915) at 2.5% annual effective interest rate and repayable until 2036. The loan was lent for the financing of the project “Urban Water Supply and Sanitation Project”.

##### Loans from the Ministry of Finance of the Republic of Azerbaijan

On November 29, 2016 the Group received two interest free loans from the Ministry of Finance in amount of USD 17,382 thousand (AZN 29,549) and AZN 11,943. According to the contracts repayment of loans will start in 2024 in 8 equal instalments twice a year till December 2027

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

### 13. Interest-bearing loans and borrowings (continued)

#### Loans from the Ministry of Finance of the Republic of Azerbaijan (continued)

On June 7, 2017 the Group received interest free loan from the Ministry of Finance in amount of USD 11,183 thousand (AZN 19,011). According to the contract repayment of loans will start in February 2025 in 8 equal instalments twice a year till August 2028.

At the end of 2017 the Ministry of Finance has granted interest free loan to the Group in amount of USD 11,280 thousand (AZN 19,176). According to the contract repayment of loans will start in February 2027 in 8 equal instalments twice a year till August 2030.

At the end of 2018 the Ministry of Finance has granted interest free loan to the Group in amount of USD 11,390 thousand (AZN 19,363). According to the contract repayment of loans will start in February 2028 in 8 equal instalments twice a year till August 2031.

At the end of 2019 the Group received two interest free loans from the Ministry of Finance in amount of USD 10,959 thousand (AZN 18,630). According to the contracts repayment of loans will start in February 2024 in 8 equal instalments twice a year till August 2027.

At the end of 2020 the Group received two interest free loans from the Ministry of Finance in amount of USD 11,206 thousand (AZN 19,050). According to the contracts repayment of loans will start in February 2025 in 8 equal instalments twice a year till August 2028.

At the end of 2021, the Group received a loan from the Ministry of Finance in the amount of USD 6,286 thousand (AZN 10,686) and EUR 4,208 thousand (AZN 8,101) with an annual effective interest rate of 1%. According to the contracts repayment of loans will start in May 2027 in 8 equal instalments twice a year till November 2031.

#### Loan from International Bank of Azerbaijan

On July 15, 2016 the Group has signed a loan agreement with International Bank of Azerbaijan under the government guarantee in the amount of AZN 239,720. As of December 31, 2016, the Group utilized full loan amount for financing of the ongoing infrastructure projects. The interest rate under the loan agreement was 1% per annum. As at December 31, 2021 there is no unpaid accrued interest on the loan (December 31, 2020: AZN 73)

### 14. Provisions

Provisions comprised the following as at:

	December 31, 2021	December 31, 2020
Unused vacation	9,300	8,783
Provision for court cases	695	609
Other	77	123
<b>Total provisions</b>	<b>10,072</b>	<b>9,515</b>

#### Provision for court cases

Provision for court cases represents factual and probable estimated claims against the Group which were given rise due to ongoing construction projects mainly.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

# **15. Taxes and penalties payable other than corporate income tax, net**

Taxes and penalties payable other than income tax, net comprised the following as at:

	December 31, 2021	December 31, 2020
Property tax	5,753	4,672
VAT	13,879	3,339
Undeclared VAT	15,844	-
Withholding tax	283	131
Economic and financial sanctions	(980)	(67)
Land tax	(858)	(798)
Personal income tax	(3,867)	(2,082)
<b>Total taxes and penalties other than corporate income tax, net</b>	<b>30,054</b>	<b>5,195</b>

Economic and financial sanctions comprised fines and penalties for delayed submission of statutory financial reports, mistakes during statutory reporting and other sanctions.

# **16. Trade and other payables**

Trade and other payables comprised the following as at:

	December 31, 2021	December 31, 2020
Construction related payables	179,175	173,266
Trade payables	57,861	88,246
Other payables	11,539	11,123
<b>Total financial payables</b>	<b>248,575</b>	<b>272,635</b>
Payable to Social Security Fund	8,967	10,547
Payable to employees	7,594	7,749
<b>Total trade and other payables</b>	<b>265,136</b>	<b>290,931</b>

The Group’s total payables mainly represented by payables for construction services and payables for material, transportation, water-supply, energy and utilities provided by vendors to the Group.

# **17. Balances and transactions with related parties**

## **Key management compensation**

Key management of the Group includes the Chairman of the Group and its six deputies. The Chairman is appointed by the President of the Republic of Azerbaijan, deputies are appointed by the Chairman and approved by Deputy Prime Minister of the Republic of Azerbaijan. Key management individuals are entitled to salaries and benefits provided by the Group in accordance with the approved payroll matrix. During 2021 compensation of key management personnel totaled to AZN 437 (December 31, 2020: AZN 390).

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

# 17. Balances and transactions with related parties (continued)

## Significant transactions

All transactions with the Government are disclosed in Note 11, Note 12, Note 13 and Note 23.

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions or had significant balances outstanding are detailed below.

The Group had the following outstanding balances with related parties:

	Note	Government and entities under government control	
		December 31, 2021	December 31, 2020
Gross amounts of trade receivables		44,677	41,122
Impairment provisions for trade receivables		(27,083)	(25,802)
Other receivables		374	191
Taxes receivables	7	15,033	18,545
Cash and cash equivalents		1,628	331
Restricted cash	10	467	767
Long-term borrowings	13	(248,103)	(243,072)
Short-term borrowings		(11,994)	(21,689)
Trade and other payables		(152,314)	(125,224)
Taxes payables		(16,675)	(7,457)
Advances received		(5,038)	(2,823)
Deferred revenue		(184)	(276)

The transactions with related parties for the year ended December 31, 2021 and December 31, 2020 were as follows:

	Note	Government and entities under government control	
		Year ended December 31, 2021	Year ended December 31, 2020
Sales revenue		33,333	37,435
Energy costs	21	(44,433)	(49,719)
Security costs	21	(6,353)	(6,471)
Water purchase		(39)	(38)
Other expenses		(2,515)	(2,542)
Communication expenses		(61)	(65)

The sales to and purchases from related parties are made at terms equivalent to those that prevail in arm's length transactions except for Government loans lent at a below market rate. Outstanding balances at the yearend are unsecured and interest free except for borrowings. There have been no guarantees provided or received for any related party receivables or payables.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 18. Financial risk management

### Financial risk factors

In the ordinary course of business, the Group is exposed to credit, liquidity and market risks. Market risks arise from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial position. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position. Although there are no structured formal management procedures, management of the Group identifies and evaluates financial risks with reference to the current market position.

### Currency risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

The following tables demonstrate the sensitivity to a reasonably possible change in the USD, EUR, SDR exchange rates, with all other variables held constant, of the Group's post-tax profit. There is no material impact on the Group's equity:

<b>December 31, 2021</b>	<b>Change in rates</b>	<b>Effect on post-tax profit</b>
USD/AZN	10%/(-10%)	(10,316)/10,316
EUR/AZN	10%/(-10%)	(7,946)/7,946
SDR/AZN	1%/(-1%)	(163)/163

<b>December 31, 2020</b>	<b>Change in rates</b>	<b>Effect on post-tax profit</b>
USD/AZN	10%/(-10%)	(9,548)/9,548
EUR/AZN	10%/(-10%)	(8,779)/8,779
SDR/AZN	1%/(-1%)	(249)/249

The Group's exposure to foreign currency changes for all other currencies is not material.

### Credit risk and concentration of credit risk

Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if counterparty defaults on its contractual obligations.

The Group's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and trade and other receivables.

The Group's maximum exposure to credit risk is represented by carrying amounts of financial assets and is presented by class of assets as shown in the table below:

	<b>December 31, 2021</b>	<b>December 31, 2020</b>
Cash and cash equivalents	5,906	2,858
Trade and other receivables	27,600	19,826
<b>Total maximum exposure to credit risk</b>	<b>33,506</b>	<b>22,684</b>

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 18. Financial risk management (continued)

### Credit risk and concentration of credit risk (continued)

The Group places its cash with reputable financial institutions in the Republic of Azerbaijan. The Group continually monitors the status of the banks where its accounts are maintained. The Group's credit risk arising from its trade receivables balance with private sector and other third-party unrelated customers is mitigated by continuous monitoring of their creditworthiness. The requirement for an impairment is analyzed at each reporting date on an individual basis for major clients. Additionally, a large number of minor receivables are grouped into homogenous groups and assessed for impairment collectively. The calculation is based on actual incurred historical data. The maximum exposure to credit risk at the reporting date is the carrying value of each class of financial assets. The Group does not hold collateral as security. Management of the Group believes that the Group is not exposed to high credit risk as the impairment provision has already been accrued in the accompanying consolidated financial statements for all debtors which are not expected to be recovered in a future.

### Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure 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. In managing liquidity risk, the Group should maintain adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows.

Prudent liquidity risk management includes maintaining sufficient working capital and the ability to close out market positions. As discussed in Note 2 the Group continues to remain dependent on its ability to obtain sufficient funding from the Government to sustain operations and complete its current investment projects. Refer to the respective note for management's action points.

All of the Group's financial liabilities represent non-derivative financial instruments. The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period from the statement of financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

The maturity analysis of financial liabilities is as follows:

<b>At December 31, 2021</b>	<b>Less than 3 months</b>	<b>3-12 months</b>	<b>1-5 years</b>	<b>More than 5 years</b>	<b>Total</b>
Trade and other financial payables	248,228	–	347	–	248,575
Interest-bearing loans and borrowings	717	12,799	37,094	195,654	246,264
Lease liabilities	76	217	386	131	810
<b>Total undiscounted financial liabilities</b>	<b>249,021</b>	<b>13,016</b>	<b>37,827</b>	<b>195,785</b>	<b>495,649</b>

<b>At December 31, 2020</b>	<b>Less than 3 months</b>	<b>3-12 months</b>	<b>1-5 years</b>	<b>More than 5 years</b>	<b>Total</b>
Trade and other financial payables	265,731	–	6,904	–	272,635
Interest-bearing loans and borrowings	4,034	19,415	44,703	208,334	276,486
Lease liabilities	86	254	385	180	905
<b>Total undiscounted financial liabilities</b>	<b>269,851</b>	<b>19,669</b>	<b>51,992</b>	<b>208,514</b>	<b>550,026</b>



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 18. Financial risk management (continued)

### Capital management

The primary objective of the Group’s capital management policy is to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain government, investor and creditor confidence to support its business activities.

The Group is 100% owned by the Government of Azerbaijan Republic and periodically receives funds in form of Government investment for implementation of construction projects. Having considered that contributions and additions in capital depend on government decisions and there are no requirements and limits set on level of the capital, no specific capital risk management policies were developed by the Group.

### Fair value of financial instruments

The fair value of the financial assets and liabilities is included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. Management has used all available market information in estimating the fair value of the financial instruments.

Set out below is a comparison by class of the carrying amounts and fair value of the Group’s financial instruments that are carried in the consolidated financial statements.

	Carrying value	Fair value
<b>As at December 31, 2021</b>		
Cash and cash equivalents	5,906	5,906
Trade and other financial receivables	27,600	27,600
Long-term trade and other financial payables	(347)	(347)
Short-term trade and other financial payables	(248,228)	(248,228)
Long-term bank loans	(232,748)	(253,037)
Short-term bank loans	(13,516)	(23,449)
Long-term lease liabilities	(517)	(452)
Short-term lease liabilities	(293)	(288)
	Carrying value	Fair value
<b>As at December 31, 2020</b>		
Cash and cash equivalents	2,858	2,858
Trade and other financial receivables	19,826	19,826
Long-term trade and other financial payables	(6,904)	(6,904)
Short-term trade and other financial payables	(284,027)	(284,027)
Long-term bank loans	(243,072)	(243,072)
Short-term bank loans	(21,689)	(21,689)
Long-term lease liabilities	(453)	(453)
Short-term lease liabilities	(287)	(287)

The following methods and assumptions were used to estimate the fair values:

- Short-term financial assets and liabilities approximate their carrying amounts largely due to the short-term maturities of these instruments.
- Long-term borrowings are evaluated by the Group based on parameters such as interest rates, specific country risk factors, individual creditworthiness of customers and the risk characteristics of the financed project.

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

# 18. Financial risk management (continued)

## Fair value of financial instruments

The following table sets out the fair values of financial instruments not measured at fair value by the end of December 31, 2021 and analyzes them by the level in the fair value hierarchy into which each fair value measurement is categorized below:

		Fair value measurement using				
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
<b>Assets for which fair values are disclosed</b>						
Cash and cash equivalents	Amortized cost	December 31, 2021	5,906	—	—	5,906
Trade and other receivables	Amortized cost	December 31, 2021	—	—	27,600	27,600
<b>Liabilities for which fair values are disclosed</b>						
Long-term trade and other financial payables	Amortized cost	December 31, 2021	—	—	(347)	(347)
Short-term trade and other financial payables	Amortized cost	December 31, 2021	—	—	(248,228)	(248,228)
Long-term bank loans	Amortized cost	December 31, 2021	—	—	(232,748)	(232,748)
Short-term bank loans	Amortized cost	December 31, 2021	—	—	(13,516)	(13,516)
Long-term lease liabilities	Amortized cost	December 31, 2021	—	—	(517)	(517)
Short-term lease liabilities	Amortized cost	December 31, 2021	—	—	(293)	(293)



(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

# 18. Financial risk management (continued)

## Fair value of financial instruments (continued)

The following table sets out the fair values of financial instruments not measured at fair value by the end of December 31, 2020 and analyzes them by the level in the fair value hierarchy into which each fair value measurement is categorized below:

Fair value measurement using						
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
<b>Assets for which fair values are disclosed</b>						
Cash and cash equivalents	Amortized cost	December 31, 2020	2,863	—	—	<b>2,863</b>
Trade and other receivables	Amortized cost	December 31, 2020	—	—	19,826	<b>19,826</b>
<b>Liabilities for which fair values are disclosed</b>						
Long-term trade and other financial payables	Amortized cost	December 31, 2020	—	—	(6,904)	<b>(6,904)</b>
Short-term trade and other financial payables	Amortized cost	December 31, 2020	—	—	(284,027)	<b>(284,027)</b>
Long-term bank loans	Amortized cost	December 31, 2020	—	—	(243,072)	<b>(243,072)</b>
Short-term bank loans	Amortized cost	December 31, 2020	—	—	(21,689)	<b>(21,689)</b>
Long-term lease liability	Amortized cost	December 31, 2020	—	—	(453)	<b>(453)</b>
Short-term lease liability	Amortized cost	December 31, 2020	—	—	(287)	<b>(287)</b>

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 19. Sales revenue and deferred revenue

Sales revenue comprised the following:

	Year ended December 31, 2021	Year ended December 31, 2020
Sales of water	182,504	125,474
Sewerage services	70,498	51,790
Other sales revenue	9,945	6,982
<b>Total sales revenue</b>	<b>262,947</b>	<b>184,246</b>

Revenue from other sales mainly comprised the sales of water-meters and scientific research and design projects.

Deferred revenue is mainly comprised of advances received from customers for provision of water and sewerage services in the amount of AZN 8,777 as of December 31, 2021 (December 31, 2020: AZN 7,964). Moreover, this deferred revenue balance includes advance payments received for technical terms to be provided to the customers and amounted to AZN 1,240 as at December 31, 2021 (December 31, 2020: AZN 1,447).

## 20. Other income

Other income comprised the following:

	Year ended December 31, 2021	Year ended December 31, 2020
Gain on written-off for payables	30,906	25
Gain on reversal of allowance for prepayments	–	4,713
Gain on reversal of provision for court cases	–	691
Other	1,330	2,417
<b>Total other income</b>	<b>32,236</b>	<b>7,846</b>



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 21. Expenses

For the year ended December 31, 2021 cost of sales, administrative expenses, selling and distribution expenses and other operating expenses comprised the following:

2021	Cost of sales	Administrative expenses	Selling and distribution expenses	Other operating expenses	Total
Impairment of property, plant and equipment	—	—	—	(549,246)	(549,246)
Impairment of intangible assets	—	—	—	(282)	(282)
Wages, salaries and social security costs	(56,426)	(12,649)	(71,191)	—	(140,226)
Depreciation of property, plant and equipment	(7,832)	(88)	(34,363)	—	(42,283)
Amortization of intangible assets	(44)	(81)	—	—	(125)
Energy expense	(35,108)	(172)	(9,154)	—	(44,434)
Training, education and business development costs	—	—	—	—	—
Raw materials and consumables used	(10,908)	(139)	(1,183)	—	(12,230)
Taxes other than income tax	(4,968)	(172)	(3,885)	—	(9,025)
Repairs and maintenance expenses	(2,488)	(103)	(3,840)	—	(6,431)
Security expenses	(5,558)	(213)	(582)	—	(6,353)
Impairment of trade and other receivables	—	—	(18,085)	—	(18,085)
Change in other provisions and liabilities	(137)	(86)	(381)	—	(604)
Fuel expenses	(2,727)	—	(298)	—	(3,025)
Bank and collecting expenses	(92)	(3,471)	(275)	—	(3,838)
Economic sanctions and other penalties	(97)	(7,918)	(377)	—	(8,392)
Business trip expenses	(1,114)	(211)	(517)	—	(1,842)
Rent expenses	(184)	—	(276)	—	(460)
Insurance expenses	(591)	(1,231)	(845)	—	(2,667)
Communication expenses	(32)	(262)	(222)	—	(516)
Depreciation of right of use asset	—	—	(271)	—	(271)
Loss on disposal property, plant and equipment	(31)	—	(50)	—	(81)
Court and law expense	—	(10)	(2)	—	(12)
Other expenses	(392)	(1,950)	(810)	—	(3,151)
<b>Total expenses</b>	<b>(128,729)</b>	<b>(28,756)</b>	<b>(146,607)</b>	<b>(549,528)</b>	<b>(853,620)</b>

(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

## 21. Expenses (continued)

For the year ended December 31, 2020 cost of sales, administrative expenses, selling and distribution expenses and other operating expenses comprised the following:

2020	Cost of sales	Administrative expenses	Selling and distribution expenses	Other operating expenses	Total
Impairment of property, plant and equipment	—	—	—	(207,643)	(207,643)
Impairment of intangible assets	—	—	—	(212)	(212)
Wages, salaries and social security costs	(55,569)	(11,350)	(69,065)	—	(135,984)
Depreciation of property, plant and equipment	(10,176)	(835)	(10,213)	—	(21,224)
Amortization of intangible assets	(54)	(79)	—	—	(133)
Energy expense	(40,559)	(81)	(9,079)	—	(49,719)
Training, education and business development costs	—	(418)	—	—	(418)
Raw materials and consumables used	(8,008)	(262)	(2,108)	—	(10,378)
Taxes other than income tax	(4,937)	(315)	(2,686)	—	(7,938)
Repairs and maintenance expenses	(2,599)	(90)	(3,253)	—	(5,942)
Security expenses	(5,525)	(213)	(733)	—	(6,471)
Impairment of trade and other receivables	—	—	(9,337)	—	(9,337)
Change in other provisions and liabilities	(6)	—	(36)	—	(42)
Fuel expenses	(2,057)	—	(202)	—	(2,259)
Bank and collecting expenses	(44)	(2,339)	(204)	—	(2,587)
Economic sanctions and other penalties	(234)	(1,492)	(33)	—	(1,759)
Business trip expenses	(592)	(174)	(197)	—	(963)
Rent expenses	(206)	—	(614)	—	(820)
Insurance expenses	(590)	(9)	(712)	—	(1,311)
Communication expenses	(38)	(231)	(216)	—	(485)
Depreciation of right of use asset	—	—	(223)	—	(223)
Loss on disposal property, plant and equipment	(87)	(5)	(183)	—	(275)
Loss on disposal of intangible assets	—	(16,556)	(1)	—	(16,557)
Other expenses	(243)	(5,983)	(7,929)	—	(14,155)
<b>Total expenses</b>	<b>(131,524)</b>	<b>(40,432)</b>	<b>(117,024)</b>	<b>(207,855)</b>	<b>(496,835)</b>

During 2021 the Group incurred net foreign exchange gain in the amount of AZN 10,315 (2020 net foreign exchange loss in the amount of AZN 15,508) due to change of Azerbaijani manat against US dollar and other major currencies.



(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)

## 22. Corporate income tax

Income tax expense comprised the following:

	Year ended December 31, 2021	Year ended December 31, 2020
Current income tax expense	(663)	(144)
Change in deferred tax	65	59
<b>Corporate income tax expense for the year</b>	<b>(598)</b>	<b>(85)</b>

Differences between IFRS and applicable domestic tax regulations give rise to the temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of these temporary differences is detailed below:

	December 31, 2019	In the statement of profit or loss and other comprehensive income	December 31, 2020	In the statement of profit or loss and other comprehensive income	December 31, 2021
<b>Deductible temporary differences</b>					
Property, plant and equipment	174	57	231	65	296
Inventories	21	(3)	18	1	19
Trade and other receivable	(2)	2	—	—	—
Trade and other payables	(5)	3	(2)	—	(2)
Provisions	5	—	5	(1)	4
<b>Deferred income tax asset</b>	<b>193</b>	<b>59</b>	<b>252</b>	<b>65</b>	<b>317</b>

At December 31, 2021 cumulative balance of unrecognized deferred tax asset from carry forward losses and other temporary differences amounted 1,332,962 (December 31, 2020: AZN 1,272,301).

A reconciliation between tax expense and the product of accounting loss multiplied by the Group's domestic tax rate for the year ended December 31, 2021 and December 31, 2020 is as follows:

	Year ended December 31, 2021	Year ended December 31, 2020
<b>Loss before tax</b>	<b>(551,632)</b>	<b>(323,137)</b>
<b>Theoretical tax benefit at statutory rate of 20 per cent</b>	<b>110,326</b>	<b>64,627</b>
Tax effect of non-deductible expenses	(29)	(66)
Unrecognized deferred tax asset	(110,895)	(64,646)
<b>Corporate income tax expense for the year</b>	<b>(598)</b>	<b>(85)</b>

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## 22. Corporate income tax (continued)

The Group does not file a consolidated tax return. In the context of the Group's current structure, tax losses and current tax assets of different Group companies may not be offset against current tax liabilities and taxable profits of other Group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

The Group's several subsidiaries have tax losses, which in accordance with Azerbaijani tax legislation, can be carried forward for five years. However, as these losses relate to subsidiaries that have a history of losses, deferred tax assets have not been recognized as these losses may not be used to offset taxable profits elsewhere in the Group. The Group evaluated and concluded that it is not probable that deferred tax assets on balances of loss-making subsidiaries will be recovered in foreseeable future and recognized full allowance for deferred tax asset on these entities.

## 23. Significant non-cash investing and financing activities

Investing and financing transactions that did not require the use of cash and cash equivalents and were excluded from the consolidated cash flows statement are as follows:

	2021	2020
Construction works financed by the Government	177,638	211,260
Repayment of Group's loans by the Ministry of Finance	19,002	19,050
Property, plant and equipment granted to the Group by the Government (Note 5)	397,460	12,864

As discussed in Note 10 the Group's account at the State Treasury is restricted by financing of the Group's construction activities by the Government. The total amount of funds appropriated by the Government for the payment of the Group's construction activities during the years ended December 31, 2021 and December 31, 2020 amounted AZN 177,638 and AZN 211,260 respectively.

## 24. Contingences, commitments and operating risks

### Operating environment

Azerbaijani oil has shown an upward trend in oil exchanges in 2021. The price for Azeri Light crude oil increased to \$ 82.07 per barrel. The share of the non-oil and gas sector in the structure of industry in Azerbaijan is growing faster. Azerbaijan is developing in accordance with the requirements of the fourth industrial revolution. In the second half of the year, there was panic in Europe. The price of natural gas began to rise and broke historical records several times. The last highest score was reached on December 21. At that time, the exchange price of "blue fuel" in Europe reached \$ 2,150 per thousand cubic meters. Against the background of these events, the attention of energy market participants is focused on Azerbaijan. Although the country initially planned to export up to 5 billion cubic meters of gas to Europe this year, the actual volume of exports in January-November 2021 amounted to 7.3 billion cubic mete

Despite the deep socio-economic crisis in the world in 2021, the pace of development in many key areas has been maintained. In 2021, at the same time, large-scale reconstruction work began in the liberated territories, the 500 millionth ton of oil was exported via the Baku-Tbilisi-Ceyhan pipeline, Azerbaijan and Turkmenistan agreed on joint development of the Dostlug field, non-oil exports hit a record high. reached. This year was the second "year of the coronavirus" for the world. If the shock effect of 2020 had a serious impact on the global economy, in 2021 the world will gradually recover. The crisis management period began in March 2020 and ended in April 2021. Under the leadership of President Ilham Aliyev, the Azerbaijani state simultaneously set an example of pandemic, drought, low oil prices and crisis management against Armenia's military provocations.



*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **24. Contingences, commitments and operating risks (continued)**

### **Operating environment (continued)**

By mid-2021, the recession had stopped and economic growth had resumed. Azerbaijan has made a global contribution to the results of the fight against the pandemic, as well as to a leading position in terms of vaccination policy.

The Ministry of Economy forecasts GDP growth of 5.1 % in 2021. At the same time, the World Bank forecasts economic growth in Azerbaijan in 2021 from 2.9% to 5%. According to forecasts, the growth of the non-oil sector in 2021 will be 7.1 percent due to the growth of services, agriculture and industry

On January 29, 2021, the Board of the Central Bank of the Republic of Azerbaijan decided to keep the discount rate unchanged at 6.25%. The lower limit of the interest rate corridor was maintained at 5.75% and the upper limit at 6.75%. The increase in inflation is mainly explained by external supply and cost shocks, such as rising world commodity prices and problems in the global supply chain. The surplus balance of payments and the adopted macroeconomic platform have the potential to neutralize risk factors in the medium term. The increase in oil transfers in the state budget adopted in 2022 compared to the previous year will support the stability of the national currency. On the other hand, anti-inflationary monetary policy will serve to maintain a balanced level of domestic demand for monetary factors. As the effects of temporary external and internal cost factors on prices are neutralized, the reducing effects of balancing factors on inflation will intensify.

In connection with the implementation of the Order of the President of the Republic of Azerbaijan No. 2965 dated October 16, 2021, the amount of the minimum monthly salary shall be set at 300 AZN from January 1, 2022. In January-November 2021, the average monthly nominal wage of employees increased by 2.9 percent compared to the corresponding period of 2020 and amounted to AZN 724.. From January 1, 2021. Compulsory health insurance has been introduced. Until January 1, 2022, a 50 percent discount is applied to the amount of insurance premiums paid by employers and employees working in the non-state and non-oil sector from the part of the monthly salary fund up to AZN 8,000. This means that until January 1, 2022, employers and employees working in the non-governmental and non-oil sectors will receive compulsory health insurance in the amount of 1% of the monthly salary fund up to AZN 8,000 and 0.5% of the monthly salary over AZN 8,000. fee will be charged.

From 2022, employers and employees in the sector will be required to pay a mandatory health insurance fee of 2% of the monthly salary fund of up to AZN 8,000.

### **Legal proceedings**

From time to time and in the normal course of business, claims against the Group are received. On the basis of its own estimates internal professional advice management is of the opinion that no material losses will be incurred in respect of claims in excess of provisions that have been made in these consolidated financial statements.

### **Tax legislation**

Azerbaijani tax, currency and customs legislation is subject to varying interpretations, and changes, which may occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant authorities. Fiscal periods remain open to review by the tax authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances such reviews may cover longer periods.

*(Amounts presented are in thousands of Azerbaijani manats, unless otherwise stated)*

## **24. Contingences, commitments and operating risks (continued)**

### **Environmental matters**

The enforcement of environmental regulation in the Azerbaijan Republic is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group 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 liabilities for environmental damage.

## **25. Events after the reporting date**

Following significant events took place subsequent to December 31, 2021:

According to the Order No: 3143 of the President of the Republic of Azerbaijan dated February 10, 2022, the funds of AZN 138,960 from the budget of 2022 are considered to be allocated to the Group for improving the public supply of drinking water, reconstruction of water supply and sewerage system, construction of meters and improvement of the ecological situation in the state.

According to the Order of the President of the Republic of Azerbaijan No. 3166 dated March 1, 2022, the funds of AZN 18,900 from the budget for 2022 are considered to be allocated for the restoration of drinking water supply, reconstruction, construction of water supply and sewerage systems, installation of meters and improvement of the ecological situation of regions liberated from occupation.