MUNICIPAL DEVELOPMENT FUND OF GEORGIA

Financial Statements

and

Independent Auditor's Report

For the year ended 31 December 2014

Content

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2014

The management of the Municipal Development Fund of Georgia (the MDF) is responsible for the preparation of the financial statements of the MDF that present fairly the financial position of the MDF as at 31 December 2014, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

In preparing the financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures that enable users to understand the impact of particular transactions, other events and conditions to the financial statements.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls;
- Maintaining adequate accounting records that are sufficient to show and explain the transactions and disclose with reasonable accuracy, and which enable to ensure that the financial statements comply with the basis of accounting adopted;
- Maintaining statutory accounting records in compliance with Georgian legislation;
- Taking such steps that are reasonably available to them to safeguard the assets of the MDF; and
- Preventing and detecting fraud and other errors.

The financial statements for the year ended 31 December 2014 were approved on 30 June 2015 by the Management.

On behalf of the Management:

Ilia Darchiashvili Executive Director	Natalie Godziashvili Head of Financial Management and Investments Unit

INDEPENDENT AUDITOR'S REPORT N 71

On the financial statements of
the Municipal Development Fund of Georgia
for the year ended 31 December 2014

To the management of Municipal Development Fund of Georgia

We have audited the accompanying financial statements of the Municipal Development Fund of Georgia (the MDF), which comprise the statement of financial position as of 31 December 2014, and the statement of profit or loss and other comprehensive income, statement of changes in reserves and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Municipal Development Fund of Georgia as of 31 December 2014, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

"SOS-Audit" LLC
30 June 2015

Manvel Ghazaryan
Director

Gnel Khachatryan, FCCA
Auditor

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Statement of financial position

	Note	As of 31 Dec 2014 Georgian Lari	As of 31 Dec 2013 Georgian Lari
Assets			
Non-current assets			
Property and equipment	4	1,121,672	1,013,366
Intangible assets		69,842	72,192
Loans to municipalities	5	22,765,213	31,668,743
Deferred income tax asset	8	112,925	103,425
		24,069,652	**32,857,726**
Current assets			
Receivables and advances	6	65,817,860	40,245,801
Current portion of loans to municipalities	5	10,302,245	8,327,650
Current income tax assets	15	303,259	267,307
Other current assets		54,412	102,962
Bank balances	7	120,318,804	83,913,384
		196,796,580	**132,857,104**
Total assets		**220,866,232**	**165,714,830**
Reserves and liabilities			
Restricted reserves			
Source of financing		141,776,533	76,940,859
Loan revolving fund		32,139,454	39,135,837
Unrestricted reserves			
Retained surplus		31,800,071	36,463,294
		205,716,058	**152,539,990**
Non-current liabilities			
Grants related to assets	9	104,186	132,896
		104,186	**132,896**
Current liabilities			
Accounts payable	10	15,045,988	10,641,666
Payables to government	11	-	2,400,278
		15,045,988	**13,041,944**
Total equity and liabilities		**220,866,232**	**165,714,830**

The financial statements were approved on 30 June 2015 by:

Ilia Darchiashvili
Executive Director

Natalie Godziashvili
Head of Financial Management
and Investments Unit

The statement of financial position is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 29.

Statement of profit or loss and other comprehensive income

	Note	Year ended 31 December 2014	Year ended 31 December 2013
		Georgian Lari	Georgian Lari
Income			
Income from loans to municipalities	12	4,459,036	5,414,045
Bank interest income		2,289,401	2,250,032
Other income	13	2,835,738	4,964,831
Gain from exchange rate differences		-	556,946
		9,584,175	**13,185,854**
Expenses			
Administrative expenses	14	(6,274,721)	(3,136,550)
Loss from exchange rate differences		(7,607,536)	-
		(13,882,257)	**(3,136,550)**
Result before tax		**(4,298,082)**	**10,049,304**
Income tax expense	15	(365,141)	(465,056)
Result for the year		**(4,663,223)**	**9,584,248**
Other comprehensive income for the year		-	-
Total comprehensive result for the year		**(4,663,223)**	**9,584,248**

The financial statements were approved on 30 June 2015 by:

Ilia Darchiashvili
Executive Director

Natalie Godziashvili
Head of Financial Management
and Investments Unit

The statement of gain and loss and other comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 29.

Statement of changes in reserves

	Restricted reserves		Unrestricted reserves	Total
	Sources of financing	**Loan revolving fund**	**Retained surplus**	
	Georgian Lari	Georgian Lari	Georgian Lari	Georgian Lari
As of 1 January 2013	**57,770,865**	**46,382,820**	**26,879,046**	**131,032,731**
Result for the year	-	-	9,584,248	9,584,248
Decrease in loan revolving fund	-	(7,246,983)	-	(7,246,983)
Net financing of implemented projects	19,169,994	-	-	19,169,994
As of 31 December 2013	**76,940,859**	**39,135,837**	**36,463,294**	**152,539,990**
Result for the year	-	-	(4,663,223)	(4,663,223)
Decrease in loan revolving fund	-	(6,996,383)	-	(6,996,383)
Net financing of implemented projects	64,835,674	-	-	64,835,674
As of 31 December 2014	**141,776,533**	**32,139,454**	**31,800,071**	**205,716,058**

The financial statements were approved on 30 June 2015 by:

Ilia Darchiashvili
Executive Director

Natalie Godziashvili
Head of Financial Management
and Investments Unit

The statement of changes in reserves is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 29.

Statement of cash flows

	Year ended 31 December 2014	Year ended 31 December 2013
	Georgian Lari	Georgian Lari
Cash flows from operating activities		
Result for the year	(4,663,223)	9,584,248
Adjustments for:		
Depreciation and amortization	427,722	494,340
Income from grants related to assets	(28,710)	(82,321)
Interest income	(6,748,437)	(7,664,077)
Income tax expense	365,141	465,056
Foreign exchange (gain)/loss	7,607,536	(556,946)
Provision for doubtful receivables	995,472	-
Operating gain/(loss) before working capital changes	***(2,044,499)***	***2,240,300***
Change in receivables and advances	(26,567,531)	(22,866,229)
Change in other current assets	48,550	(77,825)
Change in payables	4,404,322	4,486,093
Payables to government	(2,400,278)	-
Cash used in operations	***(26,559,436)***	***(16,217,661)***
Income tax paid	(410,593)	(788,000)
Net cash used in operating activities	***(26,970,029)***	***(17,005,661)***
Cash flows from investing activities		
Acquisition of property and equipment and intangible assets	(522,267)	(200,693)
Proceeds from disposal of property and equipment	17,299	225,383
Interest received from municipalities and banks	13,648,662	4,640,672
Net cash from investing activities	***13,143,694***	***4,665,362***
Cash flows from financing activities		
Projects financing	64,835,674	19,169,994
Proceeds from repayment of issued loans, net	(6,996,383)	(7,246,983)
Net cash from financing activities	***57,839,291***	***11,923,011***
Net (decrease)/increase in cash and bank balances	**44,012,956**	**(417,288)**
Foreign exchange effect on cash	(7,607,536)	556,946
Bank balances at the beginning of the year	83,913,384	83,773,726
Bank balances at the end of the year	**120,318,804**	**83,913,384**

The financial statements were approved on 30 June 2015 by:

Ilia Darchiashvili
Executive Director

Natalie Godziashvili
Head of Financial Management
and Investments Unit

The statement of cash flows is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 29.

Notes to the financial statements

1 Nature of operations and general information

The Municipal Development Fund of Georgia (the "MDF") was established on June 7, 1997 by the Presidential Decree No. 294 "On Management of Funds Designated for the Development of the Municipal Sector in Georgia" as a legal entity under the public law, the objective of which is to support strengthening institutional and financial capacity of local government units, investing financial resources in local infrastructure and servicing and improving on a sustainable basis the primary economic and social services for the local population (communities). The founder and the governing body of the MDF is the Government of Georgia in the person of Prime-Minister of Georgia.

2 Basis of preparation

2.1 Statement of compliance

The financial statements have been prepared based on the accounting records maintained under the requirements of the Georgian legislation and presented in accordance with International Financial Reporting Standards ("IFRS").

Currently, IFRS do not contain specific guidance for non-profit organizations and non-governmental organizations concerning the accounting treatment and the presentation of financial statements. Where IFRS is silent or does not give guidance on how to treat transactions specific to the non-for-profit sector, accounting policies have been based on the general principles of IFRS, as detailed in the IASB Framework for Preparation and Presentation of Financial Statements.

2.2 Basis of measurement

The financial statements have been prepared on the historical cost basis.

2.3 Functional and presentation currency

The national currency of Georgia is the Georgian lari("Lari"), which is the MDF's functional currency, since this currency best reflects the economic substance of the underlying events and transactions of the MDF.

These financial statements are presented in Georgian lari, since management believes that this currency is more useful for the users of these financial statements. All financial information presented in Georgian lari has been rounded to the nearest lari.

2.4 Use of estimates and judgment

The preparation of financial statements in conformity with IFRS requires management to make critical accounting estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although management has made the best possible estimates in the given circumstances, the fair values can materially differ from those estimates.

2.5 Adoption of new and revised standards

In the current year MDF has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the "IASB") and International Financial Reporting Interpretations Committee (the "IFRIC") of the IASB that are relevant to its operations and effective for annual reporting periods beginning on 1 January 2014.

Standards and Interpretations in issue but not yet adopted

IFRS 9 Financial Instruments (2014)

The IASB recently released IFRS 9 Financial Instruments (2014), representing the completion of its project to replace IAS 39 Financial Instruments: Recognition and Measurement. The new standard introduces extensive changes to IAS 39's guidance on the classification and measurement of financial assets and introduces a new "expected credit loss" model for the impairment of financial assets. IFRS 9 also provides new guidance on the application of hedge accounting.

MDF's management have yet to assess the impact of this new standard on the MDF's financial statements. The new standard is required to be applied for annual reporting periods beginning on or after January 1, 2018.

3 Significant accounting policies

3.1 Foreign currencies

Foreign currency transactions

In preparing the financial statements, transactions in currencies other than the functional currency are recorded at the rates of exchange defined by the National Bank of Georgia prevailing on the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated at the rates defined by the National Bank of Georgia prevailing on the reporting date, which is 1.8636 Lari for 1 US dollar as of December 31, 2014 (December 31, 2013: 1.7363 Lari for 1 US dollar).

Exchange differences arising on the settlement and retranslation of monetary items, are included in profit or loss for the period.

3.2 Property and equipment

Property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. Cost comprises purchase price including import duties and non-refundable purchase taxes and other directly attributable costs. When an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Buildings that are leasehold property are also included in property and equipment if they are held under a finance lease. Such assets are depreciated over their expected useful lives (determined by reference to comparable owned assets) or over the term of the lease, if shorter.

The gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

Expenditure to replace a component of an item of property and equipment, that is accounted for separately, is capitalized with the carrying amount of the component being written off. Other subsequent expenditure is capitalized if future economic benefits will arise from the expenditure. All other expenditure, including repair and maintenance, is recognized in the statement of other comprehensive income as incurred.

Depreciation is charged to the statement of comprehensive income on a straight line basis over the estimated useful lives of the individual assets. Depreciation commences when assets are available for use. The estimated useful lives are as follows:

• Equipment furniture and others	3 - 5 years
• Motor vehicles	5 - 7 years
• Leasehold improvement	20 year.

3.3 Intangible assets

Intangible assets, which are acquired by the MDF and which have finite useful lives, are stated at cost less accumulated amortization and impairment losses.

Amortization is charged to the statement of comprehensive income on a straight line basis over the estimated useful lives of the intangible assets.

3.4 Financial instruments

Financial assets and financial liabilities are recognized when the MDF becomes a part to the contractual provisions of the financial instrument.

Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred.

Financial liabilities are derecognized when they are extinguished, discharged, cancelled or expire.

Financial assets and financial liabilities are measured initially at fair value plus transaction costs, except for financial assets and financial liabilities carried at fair value through profit or loss, which are measured initially at fair value.

Financial assets and financial liabilities are measured subsequently as described below.

Financial assets

Financial assets other than hedging instruments are divided into the following categories:

- loans and receivables
- financial assets at fair value through profit or loss
- available-for-sale financial assets
- held-to-maturity investment.

Financial assets are assigned to the different categories on initial recognition, depending on the characteristics of the instrument and its purpose. A financial instrument's category is relevant for the way it is measured and whether any resulting income and expenses are recognized in profit or loss or directly in other comprehensive income and credited to the equity. See note 16.2 for a summary of the MDF's financial assets by category.

Generally, the MDF recognizes all financial assets using settlement date accounting. An assessment of whether a financial asset is impaired is made at least at each reporting date. All income and expense relating to financial assets are recognized in the Statement of comprehensive income line item "finance costs" or "finance income", respectively.

i Loans and receivables

Loans to municipalities

Current accounts receivable are initially recognized at fair value. Subsequently they are measured at amortized cost less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the MDF will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor and default and delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of the estimated future cash flows, discounted at the original effective interest rate.

The balance of the allowance is adjusted by recording a charge or income to the statement of comprehensive income of the reporting period. Any amount written-off with respect to customer account balances is charged against the existing allowance for doubtful accounts. All accounts receivable for which collection is not considered probable are written-off.

Bank balances

The MDF's cash and bank balances comprise cash in commercial bank accounts and cash in treasury account.

Financial liabilities

The MDF's financial liabilities include borrowings, trade and other payables, which are measured at amortized cost using the effective interest rate method. A summary of MDF's financial liabilities by category is given in note 16.2.

ii Accounts payable

Accounts payable are stated at fair value and subsequently stated at amortized cost.

3.5 Impairment

Impairment of property and equipment and intangible assets

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

Recoverable amount is the higher of net selling price and value in use. If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. Impairment losses are recognized as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss recognized for the asset or cash-generating unit in prior years. A reversal of an impairment loss is recognized as income immediately, unless the relevant asset is carried at a revalued amount, in which case any reversal of impairment loss is treated as a revaluation increase.

3.6 Reserves

3.6.1 Restricted reserves

Reserves are restricted if the related funds are restricted by the donors for implementation of specific projects. In the statement of changes in reserves the restricted reserves are composed of the sources of financing and the loan revolving fund.

Sources of financing

Sources of financing represent the difference between financing received during the reporting year and the expenses incurred for the implementation of projects for which the financing was provided. Sources of financing are recognized as the financing is received, net of project expenses incurred. If the expenses of implemented projects accrued during the current year exceed the related financing received, then the difference included in the statement of changes in reserves is a negative figure.

Loan revolving fund

Loan revolving fund represents donor funding received for the purposes of providing loan financing to municipalities, and is recognized at nominal value, when received. In the statement of changes in reserves increases or decreases of the loan revolving fund are presented net.

3.6.2 Unrestricted reserves

Reserves are unrestricted if their use is not restricted by donors. These include the MDF's retained earnings from its own operations.

3.7 Income tax

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

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

3.8 Income

Interest and other income

Interest income on loans to municipalities is recognized on an accrual basis of accounting using the effective interest rate method. Income earned on cash balances held at bank accounts is shown separately on the face of the statement of comprehensive income and are recognized on an accrual basis.

4 Property and equipment

In Georgian Lari

	Land	Leasehold improvement	Equipment and machinery	Motor vehicles	Furniture and other	Total
Cost						
as of January 1, 2013	-	**1,153,747**	**1,436,317**	**1,438,596**	**182,755**	**4,211,415**
Additions	-	9,905	185,883	354,830	1,840	552,458
Disposals	-	-	(449,194)	(450,977)	(24,660)	(924,831)
Reclassification	-	-	(49,532)	-	49,532	-
as of December 31, 2013	-	**1,163,652**	**1,123,474**	**1,342,449**	**209,467**	**3,839,042**
Additions	69,209	-	109,526	291,217	70,045	539,997
Disposals	-	-	(3,875)	(177,073)	(277)	(181,225)
as of December 31, 2014	**69,209**	**1,163,652**	**1,229,125**	**1,456,593**	**279,235**	**4,197,814**
Accumulated depreciation						
as of January 1, 2013	-	**825,075**	**1,223,758**	**813,429**	**182,079**	**3,044,341**
Charge for the year	-	232,730	86,457	158,912	2,684	480,783
Eliminated on disposal	-	-	(449,194)	(225,594)	(24,660)	(699,448)
Reclassification	-	-	(43,126)	-	43,126	-
as of December 31, 2013	-	**1,057,805**	**817,895**	**746,747**	**203,229**	**2,825,676**
Charge for the year	-	50,499	112,826	240,848	10,219	414,392
Eliminated on disposal	-	-	(1,508)	(162,250)	(168)	(163,926)
as of December 31, 2014	-	**1,108,304**	**929,213**	**825,345**	**213,280**	**3,076,142**
Carrying amount						
as of December 31, 2013	-	**105,847**	**305,579**	**595,702**	**6,238**	**1,013,366**
as of December 31, 2014	**69,209**	**55,348**	**299,912**	**631,248**	**65,955**	**1,121,672**

As of December 31, 2014 the cost of property and equipment with a carrying amount of nil is Lari 2,265,103 (December 31, 2013: Lari 2,443,839).

In accordance with the Order No. 1-1/1419 of the Ministry of Economy of Georgia dated September 20, 2007, the MDF received the area on three floors of the administrative building situated at 150 Aghmashenebeli Avenue, Tbilisi, Georgia, and the respective portion of the land on which the building is constructed, under the terms of "usufruct". Under the mentioned legal arrangement, MDF may use the building and receive any economic benefits arising from its use, while the ownership title and disposal rights over the building remain with the Ministryof Economy.

In 2014 and 2013 depreciation charge has been allocated totally to the administrative expenses.

5 Loans to municipalities

Loans issued to municipalities represent loans issued by the MDF to municipalities within the scope of the Municipal Services Development Project and Municipal Services Development Project – Phase II implemented by the MDF under the loan agreements signed between the Government of Georgia and Asian Development Bank. These projects foresee issuing of loans and grants to municipalities for subprojects for rehabilitation, construction and repair of existing municipal infrastructures. Both projects include financing windows, as follows:

- Window 1 – combination of sub-loans and grants, for subprojects above USD 500,000, with minimum beneficiary contribution of 20% of total subproject costs,
- Window 2 – grants for subprojects above USD 100,000, with minimum beneficiary contribution of 15% of total subproject costs.

Aforementioned loans carry interest rate of 12% and have maturity of 8 year for Japanese Government loans and 10 years for others, including grace period from 1to 1.5 years.

Loans to municipalities mature in 2014-2020 and bear a weighted average interest rate of 13.85% annually (2013: 12.79% annually). Loans to municipalities are stated in Georgian Lari and are not secured.

Loans to municipalities are presented below:

In Georgian Lari	**As of December 31, 2014**	**As of December 31, 2013**
Long-term loans to municipalities	22,765,213	31,668,743
Short-term loans to municipalities	10,302,245	8,327,650
	33,067,458	**39,996,393**

Short-term loans to municipalities are comprised of the following items:

In Georgian Lari	**As of December 31, 2014**	**As of December 31, 2013**
Principal amount receivable	9,374,241	7,467,094
Interest receivable	918,751	819,287
Penalties receivable	9,253	41,269
	10,302,245	**8,327,650**

The gross amount of loans to municipalities is detailed below:

In Georgian Lari

2014 Municipality	Current portion	Non-current portion	Total
Tbilisi	1,646,454	903,830	2,550,284
Kutaisi	684,797	61,860	746,657
Batumi	434,853	672,415	1,107,268
Ozurgeti	350,538	60,652	411,190
Rustavi	685,277	3,444,164	4,129,441
Gori	215,364	26,210	241,574
Poti	3,179,545	589,223	3,768,768
Zugdidi	577,664	3,039,484	3,617,148
Zestafoni	126,823	485,312	612,135
Telavi	265,811	1,545,189	1,811,000
Borjomi	107,294	301,805	409,099
Dusheti	243,485	1,141,234	1,384,719
Akhalqalaqi	122,773	672,569	795,342
Khobi	111,005	642,621	753,626
Akhaltsikhe	12,359	28,196	40,555
Marneuli	140,969	776,701	917,670
Mtskheta	233,974	1,207,276	1,441,250
Oni	12,315	28,185	40,500
Sagarejo	12,148	29,079	41,227
Tsalenjikha	15,223	30,027	45,250
Kaspi	12,088	29,013	41,101
Bolnisi	239,330	1,310,289	1,549,619
Gardabani	77,500	465,222	542,722
Gurjaani	315,231	1,786,291	2,101,522
Lagodekhi	110,453	638,455	748,908
Lentekhi	11,899	31,169	43,068
Sighnaghi	12,642	30,371	43,013
Kobuleti	344,431	2,788,371	3,132,802
	10,302,245	**22,765,213**	**33,067,458**

In Georgian Lari

2013 Municipality	Current portion	Non-current portion	Total
Tbilisi	1,890,260	2,550,284	4,440,544
Kutaisi	699,993	746,657	1,446,650
Batumi	609,966	1,107,267	1,717,233
Ozurgeti	302,300	411,190	713,490
Rustavi	694,910	4,129,440	4,824,350
Gori	186,598	241,534	428,132
Poti	859,213	2,989,617	3,848,830
Zugdidi	449,808	3,009,600	3,459,408
Zestafoni	126,211	612,135	738,346
Telavi	613,411	1,802,324	2,415,735
Borjomi	95,217	409,099	504,316
Dusheti	216,081	1,384,719	1,600,800
Akhalqalaqi	108,956	795,342	904,298
Khobi	98,512	753,627	852,139
Akhaltsikhe	10,968	40,553	51,521
Marneuli	125,103	917,670	1,042,773
Mtskheta	207,619	1,441,224	1,648,843
Oni	10,929	40,500	51,429
Sagarejo	10,778	41,227	52,005
Tsalenjikha	13,700	41,987	55,687
Kaspi	10,727	41,101	51,828
Bolnisi	212,392	1,549,619	1,762,011
Gardabani	68,778	542,722	611,500
Gurjaani	279,753	2,101,522	2,381,275
Lagodekhi	98,021	748,908	846,929
Lentekhi	10,562	43,068	53,630
Sighnaghi	11,220	43,013	54,233
Kobuleti	305,664	3,132,794	3,438,458
	8,327,650	**31,668,743**	**39,996,393**

The right to borrow from the MDF under the programme funded by the World Bank and the Asian Development Bank is granted to the Municipality by the Governmental Decree, signed by the Prime Minister or Georgia. Prior to signing each loan agreement between the Ministry of Finance and donors, the MDF conducts the analysis creditworthiness of the municipalities. Information regarding the municipalities' solvency positions is provided by the Ministry of Finance.

Management is of the opinion that no provisions need to be made for loans to municipalities since there are no loans payments overdue.

All loans are denominated in Georgian Lari.

Refer to note 0 for more information about the MDF's interest rate risks.

6 Receivables and advances

In Georgian Lari	As of December 31, 2014	As of December 31, 2013
Advances to contractors	63,668,629	35,315,105
Receivable from terminated contracts	2,800,257	4,676,379
Other	344,446	254,317
Allowances for doubtful trade receivables	(995,472)	-
Net receivables and advances	**65,817,860**	**40,245,801**

Advances to contractors were paid in accordance with contracts signed within the framework of approved projects. Advances to contractors comprise advances paid to construction companies for construction and rehabilitation of water supply systems, municipal roads, public schools, houses for refugees amounting to lari 61,183,345 as of December 31, 2014 (as of December 31,2013: lari 32,332,417), advances paid for acquisition of certain goods amounting to lari 903,674 (as of December 31, 2013: lari 175,199), for supervision of construction works amounting to lari 1,477,900 (as of December 31, 2013: lari 2,807,489) and for other services Georgian lari 103,710 (as of December 31, 2013 nill). Advances to contractors are redeemed proportionately to performance of works and services. According to contractual terms advances given to contractors are to be fully redeemed at the point of 93% of completion of construction works and services provided.

No interest is charged on receivables and advances. The MDF has provided fully for all receivables over 365 days because historical experience is that receivables that are past due beyond 365 days are generally not recoverable. During 2014 year prepayments made to a constructor who has serious financial difficulties was fully provisioned with amount of Georgian lari 995,472 (as of December 31, 2013 nill).

7 Bank balances

In Georgian Lari	As of December 31, 2014	As of December 31, 2013
Commercial bank accounts	45,621,522	38,056,024
State treasury accounts	74,697,282	45,857,360
	120,318,804	**83,913,384**

8 Deferred income taxes

The movement of deferred income taxes is disclosed below:

In Georgian Lari	2014	2013
Balance at the beginning of year	103,425	86,064
Debited to profit or loss (refer to note 15)	9,500	17,361
Balance at the end of year	**112,925**	**103,425**

Deferred income taxes for the year ended December 31, 2014 can be summarized as follows:

In Georgian Lari	As of January 1, 2014	Recognized in profit or loss	As of December 31, 2014
Deferred income tax assets/(liability)			
Property and equipment	102,393	9,500	111,893
Intangible assets	1,032	-	9,500
Net position – deferred income tax asset/(liability)	**103,425**	**9,500**	**112,925**

Deferred income taxes for the year ended December 31, 2013 can be summarized as follows:

In Georgian Lari	As of January 1, 2013	Recognized in profit or loss	As of December 31, 2013
Deferred income tax assets/(liability)			
Property and equipment	86,608	15,785	102,393
Intangible assets	(544)	1,576	1,032
Net position – deferred income tax asset/(liability)	**86,064**	**17,361**	**103,425**

9 Grants related to assets

In Georgian Lari	2014	2013
Balance at the beginning of the year	132,896	415,562
Credited to profit and loss (refer to note 13)	(28,710)	(82,321)
Received during the year	-	173,000
Disposed during the year	-	(373,345)
Balance at the end of the year	**104,186**	**132,896**

10 Accounts payable

In Georgian Lari	As of December 31, 2014	As of December 31, 2013
Retentions payable to contractors	9,165,844	7,178,137
Payable to contractors and suppliers	4,765,058	1,909,100
Other advances received from municipalities	795,341	1,374,821
Tax payable	25,407	14,953
Other payables	294,338	164,655
	15,045,988	**10,641,666**

The MDF retains 5% of the invoice amounts under the category of "Construction works" in the framework of implemented project expenditures for possible future losses. Those amounts are subject to payment to constructors one year after the construction works are completed.

11 Payables to Government

In the year ended 31 December 2012 the Fund received a guarantee payment from a bank amounting to GEL 2,400,278. The guarantee were related to the Projects that were not realized. The management recognized this amount as a liability to the Government of Georgia. During 2014 year this amount was paid to Government.

12 Income from loans to municipalities

In Georgian Lari	Year ended December 31, 2014	Year ended December 31, 2013
Interest income	4,458,301	5,376,192
Income from penalties	735	37,853
	4,459,036	5,414,045

Interest income from loans to municipalities is detailed below:

In Georgian Lari **Municipality**	**Year ended December 31, 2014**	**Year ended December 31, 2013**
Tbilisi	488,494	781,866
Kutaisi	167,247	263,655
Batumi	192,083	273,954
Ozurgeti	85,360	126,950
Rustavi	546,511	633,319
Gori	49,106	74,006
Poti	377,695	406,480
Zugdidi	423,949	441,548
Zestafoni	83,009	98,065
Samtredia	-	2,476
Telavi	231,381	257,065
Borjomi	55,395	66,108
Dusheti	180,471	204,789
Akhalqalaqi	102,652	114,914
Khobi	96,955	108,043
Akhaltsikhe	5,593	6,826
Marneuli	118,401	132,481
Mtskheta	186,689	210,056
Oni	5,583	6,813
Sagarejo	5,662	6,873
Tsalenjikha	5,742	6,937
Kaspi	5,641	6,848
Bolnisi	200,012	222,909
Gardabani	69,678	77,421
Gurjaani	270,699	293,608
Lagodekhi	96,355	107,390
Lentekhi	5,866	7,058
Sighnaghi	5,904	7,167
Kobuleti	396,168	430,567
	4,458,301	5,376,192

13 Other income

In Georgian Lari	**Year ended December 31, 2014**	**Year ended December 31, 2013**
Income from grants related to assets (refer to note 9)	28,710	82,321
Income from penalties related to projects	2,609,969	4,850,753
Other	197,059	31,757
	2,835,738	**4,964,831**

Income from penalties includes accrued penalties for contractors.

14 Administrative expenses

In Georgian Lari	Year ended December 31, 2014	Year ended December 31, 2013
Employee benefits	3,053,950	1,794,221
Depreciation and amortization	427,722	494,340
Office expenses	165,796	137,816
Trips, transportation, advertising and representation expenses	803,856	238,419
Communication costs	68,272	53,971
Insurance expenses	37,579	-
Audit and consulting	48,286	37,319
Non-reimbursable taxes	162,665	30,208
Representative expenses	8,559	58,507
Provision for doubtful receivables	995,472	-
Other	502,564	291,749
	6,274,721	**3,136,550**

15 Income tax expense

In Georgian Lari	Year ended December 31, 2014	Year ended December 31, 2013
Current tax	374,641	482,417
Deferred tax (refer to note 8)	(9,500)	(17,361)
	365,141	**465,056**

Reconciliation of effective tax rate is as follows:

	Year ended December 31, 2014		Year ended December 31, 2013	
	Georgian Lari	Effective tax rate (%)	Georgian Lari	Effective tax rate (%)
Profit before taxation (under IFRS)	(4,298,082)		10,049,304	
Tax calculated at the tax rate of 15% (2013: 15%)	(644,712)	15.00	1,507,396	15.00
(Non-taxable)/ non-deductible items, net	279,571	(6.50)	(1,972,452)	(19.63)
Income tax expense	**(365,141)**	**8.50**	**(465,056)**	**(4.63)**

Current income tax payable/(advance)

In Georgian Lari	Year ended December 31, 2014	Year ended December 31, 2013
Opening balance	**(267,307)**	**38,276**
Current tax	374,641	482,417
Paid	(410,593)	(788,000)
Closing balance	**(303,259)**	**(267,307)**

16 Financial instruments

16.1 Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition and the basis on which income and expenses are recognized, in respect of each class of financial asset, financial liability and equity instrument are disclosed in the "Financial Procedures" which is part of "Operational Manual" of the MDF. Mentioned documents are adopted by Supervisory Board of the MDF.

16.2 Categories of financial instruments

Financial assets

In Georgian Lari	As of December 31, 2014	As of December 31, 2013
Loans and receivables	35,867,715	80,035,502
Bank balances	120,318,804	83,913,384
	156,186,519	**163,948,886**

Financial liabilities

In Georgian Lari	As of December 31, 2014	As of December 31, 2013
Liabilities at amortized cost	13,930,902	10,641,666
	13,930,902	**10,641,666**

17 Financial risk management objectives

Exposure to market risk (including currency risk and interest rate risk), credit risk and liquidity risk arises in the normal course of the MDF's business. All loans issued by the MDF are preliminary reviewed and approved by the Supervisory Board. Based on the World Bank consultant's market risk report the Supervisory Board reviews the MDF's forecasts and operational budget for its further activity. The MDF strongly follows the approved budget. Any changes in the budget or unexpected activities are subject of discussion and additional approval by the Supervisory Board.

17.1 Market risk

The MDF's activities expose it primarily to the financial risks of changes in foreign currency exchange rates, interest rates and credit risk (see below).

17.2 Foreign currency risk management

The MDF undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise, but such fluctuations are related only with the World Bank financed projects, where exchange rate fluctuations primarily are reflected on the financing of mentioned projects:

a) An increase of SDR exchange rate against US dollar respectively increases financing from the World Bank;

b) An increase or decrease of Georgian lari exchange rate against US dollar respectively reflects on the value of expenditures incurred in the framework of implemented projects.

During 2014 the US dollar has appreciated in value against the Georgian lari for approximately 15% (opening ex-rate US dollars to lari as of December 31, 2014 was 1.8636, while closing ex-rate US dollars to lari as of December 31, 2013 was 1.7363). MDF has gained from exchange rate fluctuation since it has significant bank balances denominated in US dollars, which are received as financing from the Word Bank, Asian Development Bank and other international donors.

The exposure of the MDF's financial assets and liabilities to the foreign currency risk is as follows:

Item	**Freely convertible currencies**
2014	
Financial assets	
Loans and receivables	-
Bank balances	82,608,854
	82,608,854
Financial liabilities	
Accounts payable	-
	-
Net position	**82,608,854**

Item	**Freely convertible currencies**
2013	
Financial assets	
Loans and receivables	-
Bank balances	48,172,171
	48,172,171
Financial liabilities	
Accounts payable	-
Net position	**48,172,171**

17.3 Interest rate risk management

MDF is exposed to interest rate risk as it issues loans to municipalities at the fixed interest rates. Interest rate for loans to municipalities is regulated by DCA, signed between Donor and Georgian Government.

The following table reconciles the average contractual and effective interest rates:

2014	**Average interest rate**	
	Contractual	**Effective**
Assets		
Current bank accounts		
Georgian lari	6.56%	6.56%
US dollar	5.00%	5.00%
	4.50%	4.50%
Loans to municipalities		
Georgian lari	13.85%	13.85%

2013	**Average interest rate**	
	Contractual	**Effective**
Assets		
Current bank accounts		
Georgian lari	12.80%	13.58%
US dollar	7.98%	8.28%
Loans to municipalities		
Georgian lari	12.79%	13.58%

17.4 Credit risk management

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the MDF. The MDF has adopted a policy of only dealing with creditworthy counterparties as a means of mitigating risk of financial loss from default.

As described in note 6 the MDF has made provision as of December 31, 2014 in the amount of 995,472 Lari (December 31, 2013: no provision) for a receivable on a constructor who has serious financial difficulties. Besides the risk on receivables, the maximum exposure to credit risk is represented by the carrying amount of each financial asset in the statement of financial position.

17.5 Liquidity risk management

The MDF's policy is to run a prudent liquidity management policy by means of holding sufficient cash and cash equivalents, as well as highly liquid assets for making all operational and debt service related payments when those become due.

17.6 Fair values

Management believes that the carrying amount of financial assets and financial liabilities recorded at amortized cost in the financial statements approximates their fair values.

Due to the lack of liquidity and published "indicator interest rates" in the Georgian market, and the fact that part of the MDF's transactions are with related parties and are of specialized nature, it has not been practicable to determine the fair values of receivables from and payables to related parties.

18 Contingencies

18.1 Operating environment

Georgia continues to undergo political and economic changes. As an emerging market, Georgia does not possess a regulatory infrastructure that generally exists in a more mature free market economy. Consequently, operations carried out in Georgia involve certain risks that are not typically associated with those in developed countries.

The MDF could be affected, for the foreseeable future, by these risks and their consequences. Financial statements of the MDF do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the MDF's financial statements in the period when they become known and estimable.

In addition, economic conditions continue to limit the volume of activity in the financial markets. Market quotations in generally illiquid markets may not be reflective of the values for financial instruments, which would be determined in an efficient, active market involving many willing buyers and willing sellers.

18.2 Insurance

The Georgian insurance industry is in its development stage and many forms of insurance protection common in other parts of the world are not yet generally available in Georgia. MDF does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on the MDF property or relating to the MDF operations. Until the MDF obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets or environmental damage could have a materially adverse affect on the MDF's operations and financial position.

18.3 Taxes

The taxation system in Georgia is relatively new and is characterized by frequently changing legislation, which is often subject to interpretation. Often differing interpretations exist among various taxation authorities and jurisdictions. Taxes are subject to review and investigations by tax authorities, which are enabled by law to impose severe fines and penalties.

These facts may create tax risks in Georgia substantially more than in other developed countries. Management believes that it has adequately provided for tax liabilities based on its interpretation of tax legislation. However, the relevant authorities may have differing interpretations and the effects could be significant.

18.4 Environmental matters

Management is of the opinion that the MDF has met the Government's requirements concerning environmental matters and, therefore, believes that the MDF does not have any current material environmental liabilities. However, environmental legislation in Georgia is in process of development and potential changes in the legislation and its interpretation may give rise to material liabilities in the future.

19 Related party transactions

The MDF's related parties include Government of Georgia, all ministries and governmental agencies, key management and others as described below.

During 2014 and 2013, the MDF received co-financing from the Government of Georgia for Projects implementations.

19.1 Transactions with management and close family members

Directors of the MDF and their close family members as of December 31, 2014 and December 31, 2013 had no significant shares in MDF.

Key management received the following remuneration during the year, which is included in payroll, employee and other benefits.

In Georgian lari	**Year ended December31, 2014**	**Year ended December31, 2013**
Salaries and bonuses	652,315	514,743
	652,315	**514,743**