# Project Financial Statements and Independent Auditor's Report

## Municipal Development Fund of Georgia

Sustainable Urban Transport Investment Program,
Project 1
Loan No. 2655-GEO(SF)
As of and for the year ended 31 December 2017

# Contents

Grant Thornton

# Independent auditor's report

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To the management of the Municipal Development Fund of Georgia

## *Opinion*

We have audited the accompanying project financial statements of the Sustainable Urban Transport Investment Program, Project 1 (the "Project"), financed by the Asian Development Bank (the "ADB") Loan No. 2655-GEO(SF), and implemented by the Municipality Development Fund of Georgia (the "MDF") which comprise the statement of financial position as of 31 December 2017, the statement of Project sources and uses of funds, the imprest account statement in US dollars, the imprest account statement in GEL and the government co-financing account statement as of and for the year ended 31 December 2017, the statement of expenditures ("SOEs") submitted to the ADB for the year ended 31 December 2017 in support of the Loan Agreement 2655-GEO (SF) withdrawals, and a summary of significant accounting policies and other explanatory information.

In our opinion,

- the aforementioned project financial statements and appended notes that were also the subject of the audit, present fairly, in all material respects, the financial position of the Sustainable Urban Transport Investment Program, Project 1 as of 31 December 2017 and the results of its operations for the year then ended, in conformity with the accrual basis of accounting, applied on a basis consistent in all material respects with that of the previous year, as explained in the note 2, the ADB guidelines and the relevant points of the Loan Agreement No. 2655-GEO(SF);
- the MDF has utilized all proceeds of the loan withdrawn from the ADB only for purposes of the Project as agreed between the ADB and Georgia, in accordance with the loan agreement; and no proceeds of the loan have been utilized for other purposes;
- As of the reporting dates the MDF was in compliance with all financial covenants of the Loan Agreement No. 2655-GEO (SF).

In addition:

(i) (a) with respect to the statements of expenditures, adequate supporting documentation has been maintained to support claims to the ADB for reimbursements of expenditures incurred; and (b) expenditures are eligible for financing under Loan Agreement No. 2655-GEO (SF).

(ii) (a) the Imprest accounts and the government co-financing account give a true and fair view of the receipts collected and payments made during the year ended 31 December 2017; and (b) these receipts and payments support Imprest accounts liquidations/replenishments during the year ended 31 December 2017.

## *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 Financial Statements section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in the Georgia, and we have fulfilled our other ethical responsibilities in accordance with those ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## *Emphasis of Matters*

We draw attention to note 2 to the project financial statements, which describes the basis of accounting. The project financial statements are prepared to assist the management of the MDF of Georgia to meet the requirements of the financial reporting of the ADB. As a result, the project financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

## *Management's Responsibility for the Project Financial Statements*

Management of the MDF is responsible for the preparation and fair presentation of these project financial statements in accordance with the accounting policies described in the note 2 to these project financial statements, the ADB guidelines and the financial covenants of the Loan Agreement No. 2655-GEO(SF), and for such internal control as management determines is necessary to enable the preparation of project financial statements that are free from material misstatement, whether due to fraud or error.

## *Auditor's Responsibilities for the Audit of the financial statements*

Our objectives are to obtain reasonable assurance about whether the project 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 ISAs 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 project 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 project 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 Company's internal control.

- Evaluate the appropriateness of accounting policies and the reasonableness of accounting estimates and related disclosures made by management.

- Evaluate the overall presentation, structure and content of the project financial statements, including the disclosures, and whether the project financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the management 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.

Gagik Gyulbudaghyan

Managing Partner

Emil Vassilyan, FCCA

Engagement Partner

27 June 2018

# Statement of financial position

| In US dollars | Note | As of 31 December 2017 | As of 31 December 2016 |
|---|---|---|---|
| Assets | | | |
| *Non-current assets* | | | |
| Accumulated Project expenses | | 87,532,074 | 66,678,840 |
| | | 87,532,074 | 66,678,840 |
| *Current assets* | | | |
| Advances and receivables | 4 | 631,016 | 9,593,523 |
| Bank balances | 5 | 3,401,849 | 5,075,803 |
| | | 4,032,865 | 14,669,326 |
| Total assets | | 91,564,939 | 81,348,166 |
| Funds and liabilities | | | |
| *Funds* | | | |
| Accumulated Project financing | | 94,927,399 | 82,479,315 |
| Foreign exchange rate differences | | (3,362,460) | (3,251,438) |
| | | 91,564,939 | 79,227,877 |
| *Liabilities* | | | |
| Accounts payable | 6 | - | 2,120,289 |
| | | - | 2,120,289 |
| Total funds and liabilities | | 91,564,939 | 81,348,166 |

The project financial statements were approved on 27 June 2018 by:

Juansher Burchuladze
Acting Executive Director

Natalie Godziashvili
Head of Financial Management and Investment Unit

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18.

# Statement of Project sources and uses of funds

*As of and for the year ended 31 December 2017*
*In US dollars*

| | Actual | | Planned | | Variance | |
|---|---|---|---|---|---|---|
| | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 |
| *Sources of funds* | | | | | | |
| ADB funds (note 7) | 11,339,137 | 73,027,828 | | | | |
| Government co-financing | 1,020,409 | 21,811,033 | | | | |
| Other income | 88,538 | 88,538 | | | | |
| | 12,448,084 | 94,927,399 | | | | |
| Foreign exchange rate differences | (111,022) | (3,362,460) | | | | |
| *Less: Project expenses* | | | | | | |
| ADB loan number 2655 - GEO(SF) (note 8.1) | 17,685,560 | 66,037,907 | 19,000,000 | 67,352,347 | (1,314,440) | (1,314,440) |
| Government co-financing (note 8.2) | 3,167,674 | 21,494,167 | 4,000,000 | 22,326,493 | (832,326) | (832,326) |
| Total | 20,853,234 | 87,532,074 | 23,000,000 | 89,678,840 | (2,146,766) | (2,146,766) |
| Net increase/(decrease) in working capital (note 9) | (8,516,172) | 4,032,865 | | | | |

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18.

# SOE withdrawal schedule

*For the year ended 31 December 2017*
*Loan Agreement No. 2655-GEO*
*In US dollars*

| Application No. | Category | Total | ADB percentage of financing | Eligible expense |
|---|---|---|---|---|
| ADB45 | Works and Goods | 1,973,724 | 100% | 1,973,724 |
| | Consulting Services and Incremental Administration | 559,933 | 100% | 559,933 |
| | | | | **2,533,657** |

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18.

# Imprest account statement (USD)

*As of and for the year ended 31 December 2017*
*Loan Agreement No. 2655-GEO*
*In US dollars*

| | |
|---|---|
| Opening balance as of 1 January 2017 | 5,075,803 |
| *Add:* | |
| ADB loan replenishment during the year | 2,169,918 |
| Total inflow | 2,169,918 |
| *Less:* | |
| Transfer to GEL imprest account | (3,843,872) |
| Total outflow | (3,843,872) |
| Closing balance as of 31 December 2017 | 3,401,849 |

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18

# Imprest account statement (GEL)

*As of and for the year ended 31 December 2017*
*Loan Agreement No. 2655-GEO*
*In US dollars*

| | |
|---|---|
| Opening balance as of 1 January 2017 | - |
| *Add:* | |
| Transfer from the USD imprest account | 3,843,872 |
| Total inflow | 3,843,872 |
| Foreign exchange rate differences | (18,217) |
| *Less:* | |
| Works and Goods | (2,153,527) |
| Consulting Services and Incremental Administration | (1,672,128) |
| Total outflow | (3,825,655) |
| Closing balance as of 31 December 2017 | - |

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18.

# Government co-financing account (GEL) statement

*As of and for the year ended 31 December 2017*
*In US dollars*

| | |
|---|---|
| Opening balance as of 1 January 2017 | - |
| *Add:* | |
| Government co-financing | 1,020,409 |
| Total inflow | 1,020,409 |
| *Less:* | |
| Works and Goods | (645,193) |
| Consulting Services and Incremental Administration | (375,216) |
| Total outflow | (1,020,409) |
| Closing balance as of 31 December 2017 | - |

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This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 12 to 18

# Notes to the Project financial statements

## 1 Nature of operations and general information

In accordance with the Loan Agreement No. 2655-GEO(SF) signed between Georgia and the Asian Development Bank (the "ADB") on 5 August 2010, Georgia has received a loan in a total amount of SDR 57,986,000 for the Sustainable Urban Transport Investment Program, Project 1 (the "Project").

The Project is implemented by the Municipal Development Fund of Georgia (the "MDF"). The MDF has been established by the Presidential Decree # 294 dated 7 June 1997.

The legal address of MDF is 150, Aghmashenebeli Avenue, 0112, Tbilisi, Georgia.

During the reporting period the average number of the MDF staff was 146 (2016: 138).

The expected overall impact of the Project is to provide efficient, reliable and affordable urban transport infrastructure and services, thereby increasing economic growth potential and competitiveness of urban communities, improving livelihoods of over 1.5 million people. The Project also aims to: i) improve urban, environment and communities' access to economic opportunities and to public and social services; ii) promote efficient and sustainable urban transportation; and iii) generate income and employment opportunities.

The Project includes the following main components:

- a Urban Transport Infrastructure Improvement, including the following subprojects:
  - i Tbilisi urban environment improvement and Gorgasali road reconstruction;
  - ii Tbilisi metro extension (Vazha Pshavela avenue);
  - iii Kutaisi urban renewal and non-motorize transport facilities development; and
  - iv Road improvement in Mestia.
- b Institutional Capacity Development to strengthen organization, increase coordination, monitoring and financing of urban transport subsector; and
- c Project Management Facility and consulting services for subproject preparation, construction supervision, audit, social and environmental assessments, and institutional capacity development in the urban transport subsector.

The Project financing is implemented through the following categories:

| | Category | Total Amount Allocated for ADB Financing (in SDR) | ADB Financing Basis |
|---|---|---|---|
| 1 | Works and Goods | 42,920,533 | 100% of total expenditure claimed (*) |
| 2 | Consulting Services and Incremental Administration | 9,546,051 | 100% of total expenditure claimed (*) |
| 3 | Interest charge | 1,228,000 | 100% of amounts due |
| 4 | Unallocated | 4,291,416 | |
| | TOTAL | 57,986,000 | |

(*) Exclusive of taxes and duties imposed within the territory of Georgia.

# 2 Significant accounting policies

## 2.1 Statement of compliance

The MDF's policy is to prepare the accompanying project financial statements on the accrual basis of accounting and the Asian Development Bank guidelines, as well as the relevant points of the Loan Agreement No. 2655-GEO(SF).

## 2.2 Functional and presentation currency

The national currency of Georgia is Georgian lari (GEL). The project financial statements are presented in US dollar (presentation currency).

In preparing the project financial statements, transactions in currencies other than the presentation currency are recorded at the rates of exchange defined by the National Bank of Georgia (the "NBG") prevailing on the dates of transactions.

For direct payments denominated in the currencies other than the US dollar to the contractor/consultant from the ADB share, the exchange rate set out for the presentation of the operation in the system LFIS (lfis.adb.org) is used.

At each reporting date monetary items denominated in currencies other than the presentation currency are retranslated into US dollar at the rate defined by the NBG prevailing as at the reporting date, which is 2.5922 lari for 1 US dollar as of 31 December 2017 (2.6468 lari for 1 US dollar as of31 December 2016). Any exchange rate differences are recognized in the statement of Project sources and uses of funds and the accumulated figure of exchange rate difference is disclosed in the statement of financial position under "Funds".

## 2.3 Bank balances

Bank balances consist of cash amounts in the treasury accounts.

## 2.4 Advances

Advances are stated at nominal value. Advances include amounts paid to civil work and consulting service contractors.

## 2.5 Sources of funds

The ADB Loan and Government co-financing are recognized when earned, which is the date when the funds are received by the MDF or directly paid out to contractors. The accumulated Project financing is disclosed under "Funds" in the Statement of financial position. In addition, the current year funds received are disclosed in the Statement of Project sources and uses of funds, showing the sources of funds.

## 2.6 Accounts payable

Accounts payable are stated at nominal amount and include outstanding retentions from progress payments against certificates of executed works, for the purpose of liquidation of post-completion faults and defects.

## 2.7 Project expenses

Project expenses are recognized on the accrual basis of accounting. The accumulated Project expenses are disclosed in the Statement of financial position under non-current assets. In addition, current year expenses are disclosed in the Statement of Project sources and uses of funds.

## 2.8 The ADB financing

To finance eligible expenses for the Loan Agreement, the ADB disburses proceeds from the Loan amount using one or more of the disbursement methods described below:

a Direct payment procedure, where ADB, at the borrower's request, pays a designated beneficiary directly;

b Commitment procedure, where ADB, at the borrower's request, provides an irrevocable undertaking to reimburse a commercial bank for payments made or to be made to a supplier against a Letter of Credit financed from the loan account;

c Reimbursement procedure, where ADB pays from the loan account to the borrower's account or to the project account for eligible expenditures, which have been incurred and paid for by the project out of its budget allocation or its own resources; and

d Imprest fund procedure, where ADB makes an advance disbursement from the loan account for deposit to an imprest account to be used exclusively for ADB's share of eligible expenditures.

# 3 Closing date of the Project

In accordance with the Schedule 1 of the Loan Agreement No. 2655-GEO(SF), the Project closing date is 30 September 2018. However, on 23 February 2018 the Ministry of Finance of Georgia applied to the Asian Development Bank for extending the Project closing date until 18 July 2020.

# 4 Advances and receivables

| In US dollars | As of 31 December 2017 | As of 31 December 2016 |
|---|---|---|
| Advances to constructors | 276,884 | 9,593,523 |
| Accounts receivable from MDF | 354,132 | - |
| | 631,016 | 9,593,523 |

Advances were paid to the Joint Venture of Cobra Instalaciones Y Servicios, S.A., with Assignia Infraestructuras, S.A. of US dollars 276,884 as of 31 December 2017 (31 December 2016: to the "Modern business group" Ltd of US dollars 448,623 and the Joint Venture of Cobra Instalaciones Y Servicios, S.A., with Assignia Infraestructuras, S.A. of US dollars 9,144,900).

During 2017 the MDF and the "Modern business group" Ltd agreed to breach contractual obligations and the "Modern business group" Ltd returned the unused advance at the amount of GEL 917,982 (equivalent to US dollars 354,132) to the commercial bank account of the MDF. As of 31 December 2017 this amount was not transferred from the commercial bank account of the MDF into treasury account of the Project.

# 5 Bank balances

| In US dollars | As of 31 December 2017 | As of 31 December 2016 |
|---|---|---|
| Imprest account (USD) | 3,401,849 | 5,075,803 |
| | 3,401,849 | 5,075,803 |

## 6 Accounts payable

| In US dollars | As of 31 December 2017 | As of 31 December 2016 |
|---|---|---|
| Retentions | - | 2,120,289 |
| | | 2,120,289 |

Retentions comprise amounts retained (5% of total contract price) and to be paid out to the contractor at the expiration of the faults and defects period, as defined in civil works contracts. Amounts are retained from each progress payment made to civil works contractors against presented acceptance acts for executed works.

## 7 ADB funds

| In US dollars | For the year ended 31 December 2017 | As of 31 December 2017 |
|---|---|---|
| SOE procedures | 2,533,657 | 39,929,703 |
| Direct payments | 9,025,149 | 23,178,738 |
| Interest charge | 144,070 | 1,783,126 |
| Imprest account advance | (363,739) | 8,136,261 |
| | 11,339,137 | 73,027,828 |

## 8 Project expenses

### 8.1 From ADB funds

| In US dollars | Actual | | Planned | | Variance | |
|---|---|---|---|---|---|---|
| *Loan number 2655-GEO (SF)* | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 |
| Works and Goods | 15,503,932 | 49,976,685 | 16,500,000 | 50,972,753 | (996,068) | (996,068) |
| Consulting Services and Incremental Administration | 2,037,558 | 14,278,096 | 2,500,000 | 14,740,538 | (462,442) | (462,442) |
| Interest charge | 144,070 | 1,783,126 | - | 1,639,056 | 144,070 | 144,070 |
| Total | 17,685,560 | 66,037,907 | 19,000,000 | 67,352,347 | (1,314,440) | (1,314,440) |

## 8.2 From government co-financing amounts

| In US dollars | Actual | | Planned | | Variance | |
|---|---|---|---|---|---|---|
| *Loan number 2655-GEO (SF)* | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 | For the year | As of 31 December 2017 |
| Works and Goods | 2,790,708 | 9,087,001 | 3,000,000 | 9,296,293 | (209,292) | (209,292) |
| Consulting Services and Incremental Administration | 376,966 | 2,990,358 | 1,000,000 | 3,613,392 | (623,034) | (623,034) |
| Resettlement expenses | | 9,416,808 | - | 9,416,808 | - | - |
| Total | 3,167,674 | 21,494,167 | 4,000,000 | 22,326,493 | (832,326) | (832,326) |

# 9 Net increase/(decrease) in working capital

| In US dollars | For the year ended 31 December 2017 | As of 31 December 2017 |
|---|---|---|
| Increase/(decrease) in bank balances | (1,673,954) | 3,401,849 |
| Increase/(decrease) in advances | (8,962,507) | 631,016 |
| Decrease in accounts payable | 2,120,289 | - |
| | (8,516,172) | 4,032,865 |

# 10 Fixed assets

Fixed assets of the Project include acquisitions for the needs of Project implementation. The cost of fixed assets includes purchase price and other related acquisition costs.

The fixed assets are recognized in the project financial statements as expense. The accounting of fixed assets is made in the inventory registers. Taking into consideration the non-commercial status of the Project, depreciation is not charged.

The following table presents breakdown of fixed assets acquired with ADB financing as of and for the year ended 31 December 2017.

| In US dollars | For the year ended 31 December 2017 | As of 31 December 2017 |
|---|---|---|
| Office equipment | - | 9,331 |
| Furniture and other equipment | - | 1,873 |
| | - | 11,204 |

# 11 Reconciliation between the amounts received by the MDF and disbursed by the Asian Development Bank

*For the year ended 31 December 2017*
*In US dollars*

| Category | Appl. | MDF | ADB | Difference |
|---|---|---|---|---|
| Work and Goods | ADB45 | 1,973,724 | 1,973,724 | - |
| | ADB49 | 1,273,490 | 1,273,490 | - |
| | ADB50 | 635,471 | 635,471 | - |
| | ADB51 | 290,155 | 290,155 | - |
| | ADB52 | 1,032,309 | 1,032,309 | - |
| | ADB54 | 344,112 | 344,112 | - |
| | ADB55 | 316,389 | 316,389 | - |
| | ADB56 | 236,050 | 236,050 | - |
| | ADB57 | 96,702 | 96,702 | - |
| | ADB59 | 2,786,758 | 2,786,758 | - |
| | ADB60 | 1,333,825 | 1,333,825 | - |
| | ADB61 | 192,588 | 192,588 | - |
| | ADB62 | 97,837 | 97,837 | - |
| | | 10,609,410 | 10,609,410 | - |
| Consulting Services and Incremental Administration | ADB45 | 559,933 | 559,933 | - |
| | ADB63 | 179,287 | 179,287 | - |
| | ADB64 | 210,176 | 210,176 | - |
| | | 949,396 | 949,396 | - |
| Interest charge | CAP | 144,070 | 144,070 | - |
| | | 144,070 | 144,070 | - |
| Advance redemption | ADB45 | (363,739) | (363,739) | - |
| | | (363,739) | (363,739) | - |
| | | **11,339,137** | **11,339,137** | **-** |

## 12 Project implementation

As of 31 December 2017 only 78% of the Project has been implemented in the framework of the Loan Agreement No. 2655-GEO (SF). The Project expenses by categories (in percentages) are presented in the table below:

| Category | Amounts disbursed in % |
|---|---|
| Works and Goods | 80% |
| Consulting Services and Incremental Administration | 100% |
| Interest charge | 100% |
| Total | **78%** |