

Municipal Development Fund of Georgia

Sustainable Urban Transport Investment Program,
Tranche 3
Loan No. 3063-GEO

Special Purpose Project Financial Statements

For the Year Ended 31 December 2019

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Independent Auditors' Report on Special Purpose Project Financial Statement

To the management of the Municipal Development Fund of Georgia

Opinion

We have audited the accompanying special purpose project financial statements of the Sustainable Urban Transport Investment Program, Tranche 3 (the "Project"), implemented by Municipal Development Fund of Georgia (the "Fund"), which comprise the statement of financial position as of 31 December 2019, the statements of Project sources and uses of funds, the imprest accounts, the Government co-financing account for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information. The special purpose project financial statements have been prepared by management of the Fund based on the financial reporting provisions of Section 4.03 of the Loan Agreement №. 3063-GEO dated 19 December 2013 (the "Loan Agreement").

In our opinion, the special purpose project financial statements for the year ended 31 December 2019 are prepared, in all material respects, in accordance with the financial reporting provisions of Section 4.03 of the Loan Agreement.

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 *Auditors' Responsibilities for the Audit of the Special Purpose Project Financial Statements* section of our report. We are independent of the Fund in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) together with the ethical requirements that are relevant to our audit of the special purpose project financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the International Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Matter

Data included on pages 5 to 15 of the accompanying special purpose project financial statements that are marked as "*Unaudited*" have not been audited.

Emphasis of Matter - Basis of Accounting and Restriction on Use and Distribution

We draw attention to Note 2 to the special purpose project financial statements, which describes the basis of accounting. The special purpose project financial statements have been prepared for providing information to the Government of Georgia and the Asian Development Bank to assist them in evaluating the Project implementation. As a result, the special purpose project financial statements may not be suitable for another purpose. Our report is intended solely for the Fund, the Government of Georgia and the Asian Development Bank and should not be used by, or distributed to, other parties. Our opinion is not modified in respect of this matter.

Other Matter on which we are required to report

Pursuant to Section 3 of the Terms of Reference for the audit of the special purpose project financial statements of the Project dated 3 June 2016 we have audited the utilization of proceeds of the loan withdrawn from the Asian Development Bank. In our opinion, the Fund has utilized, in all material respects, the proceeds of the loan withdrawn from the Asian Development Bank only for purposes of the Project as agreed between the Asian Development Bank and the Fund, in accordance with the Loan Agreement №. 3063-GEO dated 19 December 2013 and no proceeds of the loan have been utilized for other purposes.



Responsibilities of Management and Those Charged with Governance for the Special Purpose Project Financial Statements

Management is responsible for the preparation of these special purpose project financial statements in accordance with the financial reporting provisions of Section 4.03 of the Loan Agreement, for determining the acceptability of the basis of accounting, and for such internal control as management determines is necessary to enable the preparation of special purpose project financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities for the Audit of the Special Purpose Project Financial Statements

Our objectives are to obtain reasonable assurance about whether the special purpose project financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' 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 special purpose project financial statements.

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

- Identify and assess the risks of material misstatement of the special purpose 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 Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Evaluate the overall presentation, structure and content of the special purpose project financial statements, including the disclosures, and whether the special purpose project financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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.

The engagement partner on the audit resulting in this independent auditors' report is:

Karen Safaryan



KPMG Georgia LLC
Tbilisi, Georgia
29 June 2020

Sustainable Urban Transport Investment Program, Tranche 3
 Statement of financial position as of and for the year ended December 31, 2019
 (in US Dollars)

	Note	As of December 31, 2019	As of December 31, 2018
Assets			
<i>Non-current assets</i>			
Accumulated Project expenses		49,303,338	41,176,916
		49,303,338	41,176,916
<i>Current assets</i>			
Advances and receivables	4	3,444,899	5,929,291
Bank balances		11,757,073	14,582,456
		15,201,972	20,511,747
Total assets		64,505,310	61,688,663
Funds and liabilities			
<i>Funds</i>			
Accumulated Project financing		63,617,610	61,118,277
Foreign exchange rate differences		(528,787)	(599,595)
		63,088,823	60,518,682
<i>Liabilities</i>			
Accounts payable	5	1,416,487	1,169,981
		1,416,487	1,169,981
Total funds and liabilities		64,505,310	61,688,663

The special purpose project financial statements were approved on June 29, 2020 by:


 George Shengelia
 Executive Director




 Levan Sharvadze
 Deputy Director, CFO

This statement of financial position is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 15.

Sustainable Urban Transport Investment Program, Tranche 3
Statement of Project sources and uses of funds for the year ended December 31, 2019
(in US Dollars)

	Actual as at 31 December 2019		Planned as at 31 December 2019		Variance	
	Year to date	Cumulative to date	Year to date	Cumulative to date	Year to date	Cumulative to date
<i>Funds received by sources</i>						
			<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>
Asian Development Bank (ADB) funds (note 6)	1,296,556	45,511,787				
Government of Georgia (GoG) co-financing	<u>1,202,777</u>	<u>18,105,823</u>				
Total funds received	<u>2,499,333</u>	<u>63,617,610</u>				
Foreign exchange rate differences	<u>70,808</u>	<u>(528,787)</u>				
<i>Less: Project expenditures</i>						
ADB loan No 3063 - GEO (note 7.1)	6,958,140	31,233,449	3,550,000	34,783,449	3,408,140	(3,550,000)
Government co-financing (note 7.2)	<u>1,168,282</u>	<u>18,069,889</u>	<u>639,000</u>	<u>18,708,889</u>	<u>529,282</u>	<u>(639,000)</u>
Total Project expenditures	<u>8,126,422</u>	<u>49,303,338</u>	<u>4,189,000</u>	<u>53,492,338</u>	<u>3,937,422</u>	<u>(4,189,000)</u>
Net flows of funds (note 8)	<u>(5,556,281)</u>	<u>13,785,485</u>				

Statement of Project sources and uses of funds is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 15.

Sustainable Urban Transport Investment Program, Tranche 3
Imprest account statement (USD) as of and for the year ended December 31, 2019
(in US Dollars)

Opening balance as of January 1, 2019	14,582,456
<i>Add:</i>	
ADB loan replenishment during the year	-
Total inflow	-
<i>Less:</i>	
Transfer to GEL imprest account	2,825,383
Total outflow	2,825,383
Closing balance as of December 31, 2019	11,757,073

This Imprest account statement is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 15.

Sustainable Urban Transport Investment Program, Tranche 3
Imprest account statement (GEL) as of and for the year ended December 31, 2019
(in US Dollars)

Opening balance as of January 1, 2019	-
<hr/>	
<i>Add:</i>	
Transfer from the USD imprest account	2,825,383
Total inflow	2,825,383
<hr/>	
<i>Less:</i>	
Works	2,746,424
Consulting services	85,294
Total outflow	2,831,718
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Foreign exchange rate difference	6,335
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Closing balance as of December 31, 2019	-
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This Imprest account statement is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 15.

Sustainable Urban Transport Investment Program, Tranche 3
 Government co-financing account (GEL) statement as of and for the year ended December 31, 2019
 (in US Dollars)

Opening balance as of January 1, 2019	-
<hr/>	
<i>Add:</i>	
Government co-financing	1,202,777
Total inflow	1,202,777
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<i>Less:</i>	
Works	1,053,847
Consulting services	29,828
Resettlement expenses	29,142
Total outflow	1,112,817
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Foreign exchange rate difference	89,960
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Closing balance as of December 31, 2019	-
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This Government co-financing account statement is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 15.

1. Background

In accordance with the Loan Agreement No. 3063-GEO signed between Georgia and the Asian Development Bank (the “ADB”) on December 19, 2013 (the “Loan Agreement”), Georgia has received a loan in a total amount of USD 73,000,000 for the Sustainable Urban Transport Investment Program, Tranche 3 (the “Project”).

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

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

The objective of the Project is to improve efficiency, reliability and affordability of urban transport and services. As a part of the Investment Program, the Project aims to improve efficiency, reliability and affordability of urban transport infrastructure and services in the cities of Anaklia, Rustavi and Tbilisi.

The Project includes the following main components:

- a. construction of an approximately 6.8 kilometers 4-lane urban road link between the cities of Rustavi and Tbilisi, including a 2 kilometers urban boulevard and recreational areas;
- b. construction of an approximately 1.2 kilometers coastal protection structure in the city of Anaklia;
- c. project implementation support through financial audit and independent safeguards monitoring.

On 18 April 2016, Supervisory board of Municipal Development Fund of Georgia decided to cancel remaining coastal protection works.

The Ministry of Finance of Georgia sent an official letter # N 07-04/37453, dated April 8, 2019 to Mr. Werner Liepach, Director General of Central and West Asia Department, the Asian Development Bank, by which the Minister of Finance asks ADB for consideration to remove the remaining works under SUTIP-3 project for Phase 2 and Phase 3 of Tbilisi-Rustavi highway section 2.

On 31 July 2019, the Ministry of Finance of Georgia (MoF) requested ADB the partial loan cancellation of USD 27,000 thousand under loan 3063-GEO Sustainable Urban Transport Investment Program, Tranche 3. The request was approved by ADB on 5 September 2019 and is effective from the date the MoF’s request was received by ADB.

The financing of Loan Agreement No. 3063-GEO is implemented through the following categories:

Category	Total amount allocated for ADB financing (in USD)	Cancelled amount (in USD)	Revised allocation (in USD)	Basis for Withdrawal from the Loan Account
1 Works	62,123,000	(19,184,000)	42,939,000	100% of total expenditure claimed (*)
2 Consulting services	934,000	(250,000)	684,000	100% of total expenditure claimed (*)
3 Interest and commitment charges	2,377,000	-	2,377,000	100% of amounts due
4 Unallocated	7,566,000	(7,566,000)	-	
TOTAL	73,000,000	(27,000,000)	46,000,000	

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

2. Significant accounting policies

2.1 Statement of compliance

These special purpose project financial statements have been prepared in accordance with the accrual basis of accounting and the Loan Agreement, to the extent applicable to these special purpose project financial statements and as agreed by the Fund, the Government of Georgia and the Asian Development Bank.

2.2 Presentation currency

The national currency of Georgia is Georgian Lari (GEL). The special purpose project financial statements are presented in US dollar. All financial information presented in USD has been rounded to the nearest USD.

In preparing the special purpose project financial statements, transactions in currencies other than the presentation currency are recorded at the exchange rates defined by the National Bank of Georgia (the "NBG") prevailing on the dates of transactions. 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 2.8677 GEL for 1 US dollar as of December 31, 2019 (2.6766 GEL for 1 US dollar as of December 31, 2018). 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 accounts of the State Treasury of Georgia.

2.4 Advances and receivables

Advances are stated at nominal value. Advances include amounts paid to the contractor for works.

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 by the ADB 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 cost 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 Project expenses financed by Government of Georgia are recognized when the funds are available for those expenditures. The accumulated Project expenses are disclosed in the statement of financial position under non-current assets.

2.8 The ADB financing

To finance eligible expenses for the Loan Agreement, the ADB disburses proceeds from the Loan accounts 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 the Project was expected to be completed by June 30, 2018. The Ministry of Finance of Georgia sent an official letter # N 07-02/26298, dated February 23, 2018 to Mr. Werner Liepach, Director General of Central and West Asia Department, the Asian Development Bank, by which the Minister of Finance asked to extend the Project's completion date till July 18, 2020. The minister of finance received approval from ADB for extension of the loan closing date by 18 months, till 18 July 2020 (Note 13).

4. Advances and receivables

As at December 31, 2019 advances and receivables comprise of advances made to a construction company (Seza Insaat San. Ve Tic. Ltd STI (Turkey)) of USD 3,445 thousand (2018: USD 5,929 thousand).

5. Accounts payable

Retentions comprise amounts retained (5% of total contract price) and 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.

6. Asian Development Bank funds

<i>In US dollars</i>	For the year ended December 31, 2019	Cumulative as of December 31, 2019
<i>Loan No. 3063-GEO</i>		
Direct payments	586,558	6,959,395
Reimbursement procedure	-	2,298,904
Imprest account replenishment	926,187	20,202,675
Imprest account advance	(926,187)	13,673,813
Interest and commitment charge	709,998	2,377,000
	1,296,556	45,511,787

7. Project expenditures

a. From ADB funds

<i>In US dollars</i> <i>Loan No. 3063-GEO</i>	Actual as at 31 December 2019		Planned as at 31 December 2019		Variance	
	Year to date	Cumulative to date	Year to date	Cumulative to date	Year to date	Cumulative to date
			<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>
Works	6,162,848	28,509,157	3,500,000	32,009,157	2,662,848	(3,500,000)
Consulting services	85,294	347,292	50,000	397,292	35,294	(50,000)
Interest and commitment charge	709,998	2,377,000	-	2,377,000	709,998	-
Total	6,958,140	31,233,449	3,550,000	34,783,449	3,408,140	(3,550,000)

b. From Government co-financing funds

<i>In US dollars</i>	Actual as at 31 December 2019		Planned as at 31 December 2019		Variance	
	Year to date	Cumulative to date	Year to date	Cumulative to date	Year to date	Cumulative to date
			<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>	<i>Unaudited</i>
Works	1,109,312	5,135,564	630,000	5,765,564	479,312	(630,000)
Consulting services	29,828	204,914	9,000	213,914	20,828	(9,000)
Resettlement expenses	29,142	12,729,411	-	12,729,411	29,142	-
Total	1,168,282	18,069,889	639,000	18,708,889	529,282	(639,000)

8. Net flows of funds

<i>In US dollars</i>	For the year ended December 31, 2019	As of December 31, 2019
Decrease in bank balances	(2,825,383)	11,757,073
Decrease in advances	(2,484,392)	3,444,899
Increase in accounts payable	(246,506)	(1,416,487)
	(5,556,281)	13,785,485

9. Reconciliation between the amounts received by the Fund and disbursed by the Asian Development Bank

For the year ended December 31, 2019

Loan Agreement No. 3063-GEO

In US dollars

Category	W/Auth. No	The Fund	ADB	Difference
Works	19	335,714	335,714	-
	20	51,379	51,379	-
	801G	154,829	154,829	-
	801H	316,088	316,088	-
	801I	452,918	452,918	-
	21	199,465	199,465	-
			1,510,393	1,510,393
Consulting services	801J	2,352	2,352	-
		2,352	2,352	-
	9190	54,951	54,951	-
Interest and commitment charge	919A	655,047	655,047	-
		709,998	709,998	-
		2,222,743	2,222,743	-

10. Project implementation

As of December 31, 2019 only 67.90% (2018: 52.77%, Calculated from the revised allocation (Note 1)) of the Project has been implemented in the framework of the Loan Agreement. The Project expenses by categories (in percentages) are presented in the table below:

Category	Amounts disbursed in %
Works	66.39%
Consulting Services	50.77%
Interest and commitment charge	100.00%
Total Project	67.90%

11. Commitments and contingencies

The Fund is involved as a defendant in litigations, connected to the Project related works. The claimants, Georgian legal entities, reported that modernization of Tbilisi-Rustavi highway section 2 had negatively impacted their business operations, values of the properties was not assessed properly and requested additional amount which was caused due to late payment of the compensation. Claimants submitted claims of USD 2,113 thousand in total to Tbilisi court against the Fund. Currently the cases are under the review process of the court. According to legal department of the Fund, based on their knowledge of the case, the Fund has strong position with more than 50% probability to win those cases.

Management is not aware of any commitments and other contingencies which would have a material impact on this special purpose project financial statements as of December 31, 2019 and for the year then ended.

12. Georgian operating environment

The Fund's operations are located in Georgia. Consequently, the Fund is exposed to the economic and financial markets of Georgia, which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The special purpose project financial statements reflect management's assessment of the impact of the Georgian operating environment on the operations of the Fund. The future operating environment may differ from management's assessment.

13. Events subsequent to balance sheet date

The outbreak of COVID-19 in early 2020 and its rapid spread in the world, has caused substantial impact and changes to the business environment in all countries over the world, including Georgia, which resulted in announcement of the State of Emergency, on the basis of Decree of the President of Georgia dated 21 March 2020. As per the Decree the State of Emergency shall last until 21 April 2020; which is further prolonged till 22 May 2020.

Due to the unforeseeable effects of the COVID-19, restrictions imposed by the Government, border closure, cancelation of international flights, etc. contractors and consultant companies notified Minister of Finance of Georgia that they were not able to fulfill their contractual obligations in accordance with agreed schedules by the Project's closing date. On 8 May 2020 the Ministry of Finance of Georgia requested ADB for extension of Sustainable Urban Transport Investment Program Financing Agreement Availability Period and extension the Loan closing date until 31 December 2021 due to the COVID-19 outbreak. No official response has been received as of the date of these special purpose project financial statements..