

# **JSC PASHA Bank Georgia**

## **Financial Statements**

*Year ended 31 December 2015  
together with independent auditor's report*

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## Independent Auditors Report

To the shareholders and Boards of the Directors of JSC Pasha Bank Georgia

We have audited the accompanying financial statements of JSC Pasha Bank Georgia, which comprise the statement of financial position as at 31 December 2015, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year 2015, and a summary of significant accounting policies and other explanatory information.

### ***Audited entity's responsibility for the financial statements***

Management of the audited entity 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 the fairness of these financial statements based on our audit. We concluded our audit in accordance with International Financial Reporting Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing audit procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The audit procedures selected depend on our judgment, including the assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making these risk assessment of the auditor considers internal control relevant to the 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 of the audited entity, as well as evaluating the overall presentation of the financial statements.

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

**Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of JSC PASHA Bank Georgia as at 31 December 2015, and its financial performance and cash flows for the year 2015 in accordance with International Financial Reporting Standards.

*EY Georgia LLC*

15 March 2016



**STATEMENT OF FINANCIAL POSITION****As at 31 December 2015***(Amounts in tables are in thousands of Georgian lari)*

	<b>Notes</b>	<b>2015</b>	<b>2014</b>
<b>Assets</b>			
Cash and cash equivalents	5	22,282	7,100
Amounts due from credit institutions	6	21,152	13,700
Loans to customers	7	108,602	51,836
Investment securities	8	123,320	76,219
Property and equipment	9	2,689	4,047
Intangible assets	10	2,024	1,097
Deferred income tax assets	14	1,522	–
Other assets	11	719	1,208
<b>Total assets</b>		<b>282,310</b>	<b>155,207</b>
<b>Liabilities</b>			
Amounts due to credit institutions	12	161,929	52,982
Amounts due to customers	13	21,288	5,197
Deferred income tax liabilities	14	–	98
Provisions for guarantees and letters of credit		–	59
Other liabilities	11	912	386
<b>Total liabilities</b>		<b>184,129</b>	<b>58,722</b>
<b>Equity</b>			
Share capital	15	103,000	103,000
Accumulated deficit		(4,527)	(6,789)
Other reserves		(292)	274
<b>Total equity</b>		<b>98,181</b>	<b>96,485</b>
<b>Total equity and liabilities</b>		<b>282,310</b>	<b>155,207</b>

Signed on behalf of the Board of Directors of the Bank:

Shahin Mammadov

Chairman of the Board of Directors

Chingiz Abdullayev

Chief Financial Officer, Member of the Board of Directors



15 March 2016

The accompanying selected explanatory notes on pages 6 to 42 are an integral part of these financial statements

**STATEMENT OF COMPREHENSIVE INCOME****For the year ended 31 December 2015***(Amounts in tables are in thousands of Georgian lari)*

	<b>Notes</b>	<b>2015</b>	<b>2014</b>
<b>Interest income</b>			
Loans to customers		9,864	2,837
Investment securities		7,859	3,539
Amounts due from credit institutions		1,322	1,376
		<b>19,045</b>	<b>7,752</b>
<b>Interest expense</b>			
Amounts due to credit institutions		(5,741)	(808)
Amounts due to customers		(168)	(92)
		<b>(5,909)</b>	<b>(900)</b>
<b>Net interest income</b>		<b>13,136</b>	<b>6,852</b>
Provision for impairment losses on interest bearing assets	7	(3,541)	(295)
<b>Net interest income after impairment losses</b>		<b>9,595</b>	<b>6,557</b>
Net gains/(losses) from foreign currencies:			
- dealing		294	104
- translation differences		300	(116)
Net fee and commission income/(expense)	17	307	(11)
Other operating income		117	303
<b>Non-interest income</b>		<b>1,018</b>	<b>280</b>
Personnel expenses	18	(4,489)	(2,273)
General and administrative expenses	18	(3,721)	(2,891)
Depreciation and amortisation	9,10	(1,824)	(1,707)
Other operating expenses		–	(505)
Reversal/(provision) for impairment losses on guarantees and letters of credit		59	(59)
Loss on initial recognition of financial assets at fair value		–	(3,206)
<b>Non-interest expenses</b>		<b>(9,975)</b>	<b>(10,641)</b>
<b>Profit/(loss) before income tax benefit</b>		<b>638</b>	<b>(3,804)</b>
Income tax benefit	14	1,624	6
<b>Net profit/(loss) for the period</b>		<b>2,262</b>	<b>(3,798)</b>
<b>Other comprehensive income</b>			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent periods:</i>			
Net unrealized (loss)/gain on investments securities available for sale		(562)	280
Income tax effect on net (loss)/gain on investments available for sale	14	(4)	(6)
<b>Total comprehensive profit/(loss) for the year</b>		<b>1,696</b>	<b>(3,524)</b>

The accompanying selected explanatory notes on pages 6 to 42 are an integral part of these financial statements

**STATEMENT OF CHANGES IN EQUITY****For the year ended 31 December 2015***(Amounts in tables are in thousands of Georgian lari)*

	<i>Share capital</i>	<i>Accumulated deficit</i>	<i>Other Reserves</i>	<i>Total Equity</i>
<b>1 January 2014</b>	<b>35,000</b>	<b>(2,991)</b>	<b>–</b>	<b>32,009</b>
Loss for the year	–	(3,798)	–	(3,798)
Other comprehensive income for the year	–	–	274	274
<b>Total comprehensive loss for the year</b>	<b>–</b>	<b>(3,798)</b>	<b>274</b>	<b>(3,524)</b>
Issue of share capital (Note 15)	68,000	–	–	68,000
<b>31 December 2014</b>	<b>103,000</b>	<b>(6,789)</b>	<b>274</b>	<b>96,485</b>
Profit for the year	–	2,262	–	2,262
Other comprehensive loss for the year	–	–	(566)	(566)
<b>Total comprehensive income for the year</b>	<b>–</b>	<b>2,262</b>	<b>(566)</b>	<b>1,696</b>
<b>31 December 2015</b>	<b>103,000</b>	<b>(4,527)</b>	<b>(292)</b>	<b>98,181</b>

The accompanying selected explanatory notes on pages 6 to 42 are an integral part of these financial statements

**STATEMENT OF CASH FLOWS****For the year ended 31 December 2015***(Amounts in tables are in thousands of Georgian lari)*

	<b>Notes</b>	<b>2015</b>	<b>2014</b>
<b>Cash flows from operating activities</b>			
Interest received		18,975	4,830
Interest paid		(5,680)	(716)
Fees and commissions received		561	83
Fees and commissions paid		(134)	(109)
Realised gains less losses from dealing in foreign currencies		294	104
Personnel expenses paid		(3,782)	(2,432)
General and administrative expenses paid		(4,037)	(2,987)
Other income received		117	303
<b>Cash flows from/(used in) operating activities before changes in operating assets and liabilities</b>		<b>6,314</b>	<b>(924)</b>
<i>Net (increase)/decrease in operating assets</i>			
Amounts due from credit institutions		(2,470)	300
Loans to customers		(48,635)	(47,999)
<i>Net increase/(decrease) in operating liabilities</i>			
Amounts due to credit institutions		94,544	40,570
Amounts due to customers		14,837	4,684
Other liabilities		(204)	204
<b>Net cash from/(used in) operating activities</b>		<b>64,386</b>	<b>(3,165)</b>
<b>Cash flows from investing activities</b>			
Purchase of investment securities		(139,946)	(83,272)
Proceeds from redemption of investment securities		90,432	22,585
Purchase of property and equipment		(280)	(137)
Purchase of intangible assets		(466)	(1,300)
<b>Net cash used in investing activities</b>		<b>(50,260)</b>	<b>(62,124)</b>
<b>Cash flows from financing activities</b>			
Share capital contribution	15	–	68,000
<b>Net cash from financing activities</b>		<b>–</b>	<b>68,000</b>
Effect of exchange rates changes on cash and cash equivalents		1,056	(36)
<b>Net increase in cash and cash equivalents</b>		<b>15,182</b>	<b>2,675</b>
<b>Cash and cash equivalents, beginning</b>	5	<b>7,100</b>	<b>4,425</b>
<b>Cash and cash equivalents, ending</b>	5	<b>22,282</b>	<b>7,100</b>

*The accompanying selected explanatory notes on pages 6 to 42 are an integral part of these financial statements*



## **1. Principal activities**

JSC PASHA Bank Georgia (the "Bank") was formed on 17 December 2012 as a joint stock company under the laws of Georgia. The Bank operates under a general banking license issued by the National Bank of Georgia (the "NBG") on 17 January 2013.

The Bank accepts deposits and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its commercial customers. The Bank has one service office in Georgia as of 31 December 2015. The Bank's registered legal address is 15 Rustaveli Avenue, Tbilisi, 0108, Georgia.

As at 31 December 2015 and 2014, the Bank's 100% owner was OJSC PASHA Bank (the "Parent"), the Republic of Azerbaijan. The Bank is ultimately owned by Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva, who exercise joint control over the Bank.

These financial statements have not yet been approved by the Parent at the General Meeting of Shareholders. The shareholders have the power and authority to amend the financial statements after the issuance.

## **2. Basis of preparation**

### **General**

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

These financial statements are presented in Georgian Lari ("GEL"), unless otherwise indicated.

## **3. Summary of accounting policies**

### **Changes in accounting policies**

The Bank has adopted the following amended IFRS and IFRIC which are effective for annual periods beginning on or after 1 January 2015:

#### *Amendments to IAS 19 Defined Benefit Plans: Employee Contributions*

IAS 19 requires an entity to consider contributions from employees or third parties when accounting for defined benefit plans. Where the contributions are linked to service, they should be attributed to periods of service as a negative benefit. These amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognise such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. This amendment is not relevant to the Bank, since the Bank does not have defined benefit plans with contributions from employees or third parties.

#### *Annual improvements 2010-2012 Cycle*

These improvements are effective from 1 July 2014 and the Bank has applied these amendments for the first time in these financial statements. They include:

#### *IFRS 13 Short-term Receivables and Payables – Amendments to IFRS 13*

This amendment to IFRS 13 clarifies in the Basis for Conclusions that short-term receivables and payables with no stated interest rates can be measured at invoice amounts when the effect of discounting is immaterial. This is consistent with the Bank's current accounting policy, and thus this amendment does not impact the Bank's accounting policy.



(Amounts in tables are in thousands of Georgian lari)

### 3 Summary of accounting policies (continued)

#### Changes in accounting policies (continued)

##### *IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets*

The amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortisation is the difference between the gross and carrying amounts of the asset. The Bank did not record any revaluation adjustments during the current period.

##### *IAS 24 Related Party Disclosures*

The amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services. This amendment is not relevant for the Bank as it does not receive any management services from other entities.

##### *Annual improvements 2011-2013 Cycle*

These improvements are effective from 1 July 2014 and the Bank has applied these amendments for the first time in these financial statements. They include:

##### *IFRS 13 Fair Value Measurement*

The amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IFRS 9 (or IAS 39, as applicable). The Bank does not apply the portfolio exception in IFRS 13.

##### *Meaning of effective IFRSs – Amendments to IFRS 1*

The amendment clarifies in the Basis for Conclusions that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first IFRS financial statements. This amendment to IFRS 1 had no impact on the Bank, since the Bank is an existing IFRS preparer.

#### **Fair value measurement**

The Bank measures financial instruments, such as available-for-sale securities at fair value at each reporting date. Fair values of financial instruments measured at amortised cost are disclosed in Note 20.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

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

(Amounts in tables are in thousands of Georgian lari)

### 3 Summary of accounting policies (continued)

#### Fair value measurement (continued)

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

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

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

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

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

#### Financial assets

##### *Initial recognition*

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. The Bank determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

##### *Date of recognition*

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Bank commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.



### **3 Summary of accounting policies (continued)**

#### **Financial assets (continued)**

##### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

##### *Measurement of loans and receivables originated through acquisition*

In the case of loans and receivables originated through acquisition the fair value at initial recognition is measured using discounting of future cash flows expected from the financial asset. The difference between the acquisition price and the fair value is recognized in the statement of comprehensive income as gain/(loss) on initial recognition. This policy is applied equally to transactions with third parties, related parties, entities under common control and shareholders.

These loans and receivables are also measured at amortized cost using the effective interest method. Any gain resulting from revision of estimates of the future cash flows is accounted in the statement of comprehensive income within interest income from loans to customers. Any loss resulting from impairment is accounted within the loan loss provision in the statement of comprehensive income.

##### *Available-for-sale financial assets*

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised in other comprehensive income until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is reclassified to the statement of profit or loss. However, interest calculated using the effective interest method is recognised in profit or loss.

#### **Reclassification of financial assets**

If a non-derivative financial asset classified as held for trading is no longer held for the purpose of selling in the near term, it may be reclassified out of the fair value through profit or loss category in one of the following cases:

- ▶ a financial asset that would have met the definition of loans and receivables above may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity;
- ▶ other financial assets may be reclassified to available for sale or held to maturity categories only in rare circumstances.

A financial asset classified as available for sale that would have met the definition of loans and receivables may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. Any gain or loss already recognized in profit or loss is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortised cost, as applicable.



### **3 Summary of accounting policies (continued)**

#### **Measurement of financial instruments at initial recognition**

When financial instruments are recognised initially, they are measured at fair value, adjusted, in the case of instruments not at fair value through profit or loss, for directly attributable fees and costs.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price. If the Bank determines that the fair value at initial recognition differs from the transaction price, then:

- ▶ if the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e., a Level 1 input) or based on a valuation technique that uses only data from observable markets, the Bank recognises the difference between the fair value at initial recognition and the transaction price as a gain or loss;
- ▶ in all other cases, the initial measurement of the financial instrument is adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Bank recognises that deferred difference as a gain or loss only when the inputs become observable, or when the instrument is derecognized.

#### **Offsetting of financial instruments**

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. The right of set-off must not be contingent on a future event and must be legally enforceable in all of the following circumstances:

- ▶ the normal course of business;
- ▶ the event of default; and
- ▶ the event of insolvency or bankruptcy of the entity and all of the counterparties.

These conditions are not generally met in master netting agreements, and the related assets and liabilities are presented gross in the statement of financial position.

#### **Impairment of financial assets**

The Bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.



### 3 Summary of accounting policies (continued)

#### Impairment of financial assets (continued)

*Amounts due from credit institutions, investment securities: loans and receivables and loans to customers*

For amounts due from credit institutions, investment securities: loans and receivables and loans to customers carried at amortised cost, the Bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is an objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the statement of profit or loss.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of industrial average of historical loss experience for assets with credit risk characteristics similar to those in the group, due to the reason that the Bank does not have sufficient statistical data.

#### *Available-for-sale financial investments*

For available-for-sale financial investments, the Bank assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in profit or loss. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the statement of profit or loss.



### **3 Summary of accounting policies (continued)**

#### **Derecognition of financial assets and liabilities**

##### *Financial assets*

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- ▶ the rights to receive cash flows from the asset have expired;
- ▶ the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a “pass-through” arrangement; and
- ▶ the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank’s continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank’s continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price

##### *Financial liabilities*

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

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

### **3 Summary of accounting policies (continued)**

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

Cash and cash equivalents consist of cash on hand, amounts due from the National Bank of Georgia, excluding mandatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

#### **Derivative financial instruments**

In the normal course of business, the Bank enters into derivative financial instruments such as currency swaps. These financial instruments are recorded at fair value and the fair values of currency swaps are estimated based on spot market prices, due to short term maturities of the financial instruments.

Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the statement of comprehensive income as net gains/(losses) from foreign currencies dealing.

#### **Mandatory reserve deposit with the NBG**

Mandatory reserve deposits with the NBG are carried at amortised cost and represent interest bearing mandatory reserve deposits which are not available to finance the Bank's day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows. Mandatory reserve is included in amounts due from credit institutions.

#### **Leases**

##### **Operating – Bank as lessee**

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

#### **Financial guarantees**

In the ordinary course of business, the Bank gives financial guarantees. Financial guarantees are initially recognised in the financial statements at fair value, in "Other liabilities", being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the statement of profit or loss. The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.



(Amounts in tables are in thousands of Georgian lari)

### 3. Summary of accounting policies (continued)

#### Taxation

The current income tax expense is calculated in accordance with the regulations of Georgia.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

Georgia also has various operating taxes that are assessed on the Bank's activities. These taxes are included as a component of other operating expenses.

#### Property and equipment

Property and equipment are carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Furniture and fixtures	4
Computers and equipment	4
Motor vehicles	4
Other equipment	5
Leasehold improvements	4

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalization.

### **3. Summary of accounting policies (continued)**

#### **Intangible assets**

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives of 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

#### **Contingencies**

Contingent liabilities are not recognised in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the statement of financial position but disclosed when an inflow of economic benefits is probable.

#### **Share capital**

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

#### **Recognition of income and expenses**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

##### *Interest and similar income and expense*

For all financial instruments measured at amortised cost and interest bearing securities classified as trading or available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the new carrying amount.



(Amounts in tables are in thousands of Georgian lari)

### 3. Summary of accounting policies (continued)

#### Recognition of income and expenses (continued)

##### *Fee and commission income*

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

► *Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

► *Fee income from providing transaction services*

Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

#### Foreign currency translation

The financial statements are presented in Georgian Lari ("GEL"), which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of profit or loss as gains less losses from foreign currencies – translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies. The official GEL exchange rates at 31 December 2015 and 2014 were 2.3949 GEL and 1.8636 GEL to 1 USD, respectively, 2.6169 GEL and 2.265 GEL to 1 EUR, respectively and 1.5374 GEL and 2.3758 GEL to 1 AZN, respectively.



(Amounts in tables are in thousands of Georgian lari)

### 3. Summary of accounting policies (continued)

#### Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank's financial statements which may have impact on the Bank's financial statements are disclosed below. The Bank intends to adopt this standard, when it becomes effective.

Management does not expect application of other new standards and interpretations to have significant impact on financial statements.

#### *IFRS 9 Financial Instruments*

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Bank's financial assets, but no impact on the classification and measurement of the Bank's financial liabilities. The Bank does not expect a significant impact on its equity due to adoption of IFRS 9 impairment requirements, but it will need to perform a more detailed analysis which considers all reasonable and supportable information, including forward-looking elements to determine the extent of the impact.

#### *IFRS 15 Revenue from Contracts with Customers*

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Revenue arising from lease contracts within the scope of IAS 17 *Leases*, insurance contracts within the scope of IFRS 4 *Insurance Contracts* and financial instruments and other contractual rights and obligations within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments*, if early adopted) is out of IFRS 15 scope and is dealt by respective standards.

Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue.

The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018 with early adoption permitted. The Bank is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

#### *Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation*

The amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are effective prospectively for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact to the Bank given that the Bank has not used a revenue-based method to depreciate its non-current assets.



(Amounts in tables are in thousands of Georgian lari)

### 3. Summary of accounting policies (continued)

#### Standards issued but not yet effective (continued)

##### *Annual improvements 2012-2014 Cycle*

These improvements are effective on or after 1 January 2016 and are not expected to have a material impact on the Bank. They include:

##### *IFRS 7 Financial Instruments: Disclosures – servicing contracts*

IFRS 7 requires an entity to provide disclosures for any continuing involvement in a transferred asset that is derecognised in its entirety. The Board was asked whether servicing contracts constitute continuing involvement for the purposes of applying these disclosure requirements. The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and arrangement against the guidance for continuing involvement in paragraphs IFRS 7.B30 and IFRS 7.42C in order to assess whether the disclosures are required. The amendment must be applied for annual periods beginning on or after 1 January 2016, with earlier application permitted. The amendment is to be applied such that the assessment of which servicing contracts constitute continuing involvement will need to be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.

##### *IFRS 7 Financial Instruments: Disclosures - applicability of the offsetting disclosures to condensed interim financial statements*

In December 2011, IFRS 7 was amended to add guidance on offsetting of financial assets and financial liabilities. In the effective date and transition for that amendment IFRS 7 states that “[A]n entity shall apply those amendments for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods. The interim disclosure standard, IAS 34, does not reflect this requirement, however, and it is not clear whether those disclosures are required in the condensed interim financial report.

The amendment removes the phrase ‘and interim periods within those annual periods’, clarifying that these IFRS 7 disclosures are not required in the condensed interim financial report. The amendment must be applied retrospectively for annual periods beginning on or after 1 January 2016, with earlier application permitted.

##### *IAS 34 Interim Financial Reporting – disclosure of information ‘elsewhere in the interim financial report’*

The amendment states that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report (e.g., in the management commentary or risk report). The Board specified that the other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time. If users do not have access to the other information in this manner, then the interim financial report is incomplete. The amendment should be applied retrospectively for annual periods beginning on or after 1 January 2016, with earlier application permitted.

(Amounts in tables are in thousands of Georgian lari)

#### **4. Significant accounting judgments and estimates**

##### **Judgments**

In the process of applying the Bank's accounting policies, management has made the following judgments, apart from those involving estimates, which have the most significant effect on the amounts recognised in the financial statements:

##### *Classification of investment securities*

The Bank changed the classification of its investment securities on 1 July 2015. It was the Bank's judgment that all of its securities classified as available-for-sale will be held until maturity and thus they qualify for reclassification into investment securities: loans and receivables or investment securities: held-to-maturity in line with the Bank's accounting policy (Note 8). The classification of investment securities significantly impacts the amounts reported in the financial statements. Note 20 discloses the difference between the carrying value and the fair value of investment securities.

##### **Estimation uncertainty**

In the process of applying the Bank's accounting policies, management has used its judgments and made estimates in determining the amounts recognised in the financial statements. The most significant use of judgments and estimates are as follows:

##### *Fair value of financial instruments*

Where the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Additional details are provided in Note 20.

##### *Allowance for loan impairment*

The Bank regularly reviews its loans and receivables to assess impairment. As at 31 December 2015 total loan portfolio was assessed on collective basis (Note 7). Due to inexistence of own historical loss experience for loans to customers, the Bank uses industry average loss ratios for collectively assessed loans.



*(Amounts in tables are in thousands of Georgian lari)***5. Cash and cash equivalents****Cash and cash equivalents comprise:**

	<b>2015</b>	<b>2014</b>
Cash on hand	406	487
Current accounts with the NBG	922	68
Current accounts with other credit institutions	2,159	666
Time deposits with credit institutions up to 90 days	18,795	5,879
<b>Cash and cash equivalents</b>	<b>22,282</b>	<b>7,100</b>

As at 31 December 2015, current accounts and time deposit accounts with credit institutions denominated in EUR represent 69.84% of total current and time deposit accounts (31 December 2014: 65.05%). The outstanding balance of current accounts and time deposits accounts, consist of interest bearing correspondent account balances with resident banks in the amount of GEL 987 thousand and GEL 18,795 thousand, respectively, (31 December 2014: GEL 129 and GEL 5,879 thousand respectively) and non-interest bearing correspondent account balances with resident and non-resident banks in the amounts of GEL 1,140 thousand and GEL 32 thousand, respectively (31 December 2014: GEL 150 thousand and GEL 387 thousand, respectively).

**6. Amounts due from credit institutions****Amounts due from credit institutions comprise:**

	<b>2015</b>	<b>2014</b>
Mandatory reserve with the NBG	12,610	2,595
Time deposits for more than 90 days	8,542	11,105
<b>Amounts due from credit institutions</b>	<b>21,152</b>	<b>13,700</b>

Time deposits comprise of deposits in USD placed with one local commercial bank with maturities in first quarter of 2016 and interest rates of 5.50% p.a. (31 December 2014: 5.50% p.a. to 10.00% p.a.).

Credit institutions are required to maintain a mandatory interest earning cash deposit with the NBG at the level of 10.00% and 15.00% of the average of funds attracted from customers by the credit institution for the appropriate two-week period in GEL and foreign currencies, respectively. The Bank's ability to withdraw such deposit is significantly restricted by the statutory legislation.

**7. Loans to customers****Loans to customers comprise:**

	<b>2015</b>	<b>2014</b>
Private entities	70,651	32,968
State controlled entities	36,347	19,267
Individuals	2,915	–
<b>Loans to customers</b>	<b>109,913</b>	<b>52,235</b>
Less – Allowance for impairment	(1,311)	(399)
<b>Loans to customers</b>	<b>108,602</b>	<b>51,836</b>

(Amounts in tables are in thousands of Georgian lari)

**7. Loans to customers (continued)**

As at 31 December 2014 included in loans to customers was a syndicated loan acquired from the Parent on 5 June 2014. GEL 15,731 thousand was the consideration paid to the Parent at the time of acquisition. The loan was initially recognized at fair value estimated to equal GEL 12,525 thousand. The loss on initial recognition of financial assets of GEL 3,206 thousand was recognized in the statement of comprehensive income for the year ended 31 December 2014. In August 2015 the management of the Bank negotiated and executed a deal to sell the loan at a discount.

The movement in allowance for impairment losses for loans to customers was as follows:

<b>2015</b>			
	<b>Private legal entities</b>	<b>Individuals</b>	<b>Total</b>
<b>At 1 January 2015</b>	<b>399</b>	<b>–</b>	<b>399</b>
Charge for the year	3,483	58	3,541
Write-off	(2,629)	–	(2,629)
<b>At 31 December 2015</b>	<b>1,253</b>	<b>58</b>	<b>1,311</b>
Collective impairment	1,253	58	1,311

  

<b>2014</b>			
	<b>Private legal entities</b>	<b>Individuals</b>	<b>Total</b>
<b>At 1 January 2014</b>	<b>104</b>	<b>–</b>	<b>104</b>
Charge for the year	295	–	295
<b>At 31 December 2014</b>	<b>399</b>	<b>–</b>	<b>399</b>
Collective impairment	399	–	399

**Collateral and other credit enhancements**

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters. The main types of collateral obtained are charges over real estate properties and guarantees from the Parent. The Bank also obtains guarantees from parent companies for loans to their subsidiaries.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for loan impairment.

**Concentration of loans to customers**

As at 31 December 2015, the Bank had a concentration of loans due from three major group of borrowers in the total exposure of GEL 63,039 thousand that represented 57.35% of the total gross loan portfolio (31 December 2014: three loans of GEL 39,116 thousand with 74.88% of the gross loan portfolio). As at 31 December 2015 an allowance of GEL 374 thousand (31 December 2014: nil) was recognised against these loans.



*(Amounts in tables are in thousands of Georgian lari)***7. Loans to customers (continued)**

Loans are made in the following industry sectors:

	<b>2015</b>	<b>2014</b>
Trade and services	61,775	17,431
Energy	24,833	16,510
Non-banking credit organizations	13,214	3,093
Construction	7,176	–
Individuals	2,915	–
Transport and telecommunications	–	13,000
Manufacturing	–	333
Other	–	1,868
	<b>109,913</b>	<b>52,235</b>

**8. Investment securities**

As at 31 December 2015, investment securities mainly comprised of debt securities of the Ministry of Finance of Georgia, debt securities of the National Bank of Georgia and debt securities of companies and commercial banks registered in Georgia and Azerbaijan.

Investment securities comprise:

	<b>2015</b>	<b>2014</b>
<b>Investment securities: loans and receivables</b>		
Treasury bonds of the Ministry of Finance of Georgia	38,718	–
Treasury bills of the Ministry of Finance of Georgia	23,528	–
Bonds of financial institutions	24,652	–
Certificates of deposit of the NBG	15,326	–
Certificates of deposit of financial institutions	12,204	–
Corporate bonds	8,892	–
<b>Total investment securities: loans and receivables</b>	<b>123,320</b>	<b>–</b>
<b>Investment securities: available-for-sale</b>		
Treasury bills of the Ministry of Finance of Georgia	–	53,392
Treasury bonds of the Ministry of Finance of Georgia	–	8,163
Bonds of financial institutions	–	6,197
Corporate bonds	–	4,652
Certificates of deposit of financial institutions	–	3,815
<b>Total investment securities: available-for-sale</b>	<b>–</b>	<b>76,219</b>
<b>Total investment securities</b>	<b>123,320</b>	<b>76,219</b>

On 1 July 2015 the Bank's Asset and Liability Committee (ALCO) decided to reclassify all of the Bank's investment securities from the available-for-sale category into category of loans and receivables. The Bank has no history of sale of any of its securities before maturity. The Bank assessed that based on the changing market conditions it is not intending to sell the securities in future and will hold them till their contractual maturities. The fair value of available-for-sale securities at the date of reclassification was GEL 94,516 thousand.

(Amounts in tables are in thousands of Georgian lari)

**9. Property and equipment**

The movements in property and equipment were as follows:

	<i>Furniture and fixtures</i>	<i>Computers and equipment</i>	<i>Motor vehicles</i>	<i>Other equipment</i>	<i>Leasehold improve- ments</i>	<i>Total</i>
<b>Cost</b>						
<b>31 December 2013</b>	<b>1,767</b>	<b>2,209</b>	<b>116</b>	<b>431</b>	<b>1,908</b>	<b>6,431</b>
Additions	51	70	–	16	–	137
<b>31 December 2014</b>	<b>1,818</b>	<b>2,279</b>	<b>116</b>	<b>447</b>	<b>1,908</b>	<b>6,568</b>
Additions	22	111	131	12	4	280
<b>31 December 2015</b>	<b>1,840</b>	<b>2,390</b>	<b>247</b>	<b>459</b>	<b>1,912</b>	<b>6,848</b>
<b>Accumulated depreciation:</b>						
<b>31 December 2013</b>	<b>(269)</b>	<b>(324)</b>	<b>(20)</b>	<b>(54)</b>	<b>(283)</b>	<b>(950)</b>
Depreciation charge	(449)	(548)	(29)	(87)	(458)	(1,571)
<b>31 December 2014</b>	<b>(718)</b>	<b>(872)</b>	<b>(49)</b>	<b>(141)</b>	<b>(741)</b>	<b>(2,521)</b>
Depreciation charge	(455)	(575)	(59)	(91)	(458)	(1,638)
<b>31 December 2015</b>	<b>(1,173)</b>	<b>(1,447)</b>	<b>(108)</b>	<b>(232)</b>	<b>(1,199)</b>	<b>(4,159)</b>
<b>Net book value:</b>						
<b>31 December 2013</b>	<b>1,498</b>	<b>1,885</b>	<b>96</b>	<b>377</b>	<b>1,625</b>	<b>5,481</b>
<b>31 December 2014</b>	<b>1,100</b>	<b>1,407</b>	<b>67</b>	<b>306</b>	<b>1,167</b>	<b>4,047</b>
<b>31 December 2015</b>	<b>667</b>	<b>943</b>	<b>139</b>	<b>227</b>	<b>713</b>	<b>2,689</b>

**10. Intangible assets**

The movements in intangible assets were as follows:

	<i>Licenses</i>	<i>Computer software</i>	<i>Total</i>
<b>Cost</b>			
<b>31 December 2013</b>	<b>876</b>	<b>232</b>	<b>1,108</b>
Additions	152	551	703
Disposals and write offs	(592)	(15)	(607)
<b>31 December 2014</b>	<b>436</b>	<b>768</b>	<b>1,204</b>
Additions	54	1,061	1,115
Disposals and write offs	(2)	–	(2)
<b>31 December 2015</b>	<b>488</b>	<b>1,829</b>	<b>2,317</b>
<b>Accumulated amortization</b>			
<b>31 December 2013</b>	<b>(58)</b>	<b>(15)</b>	<b>(73)</b>
Amortization charge	(101)	(35)	(136)
Disposal and write offs	100	2	102
<b>31 December 2014</b>	<b>(59)</b>	<b>(48)</b>	<b>(107)</b>
Amortisation charge	(49)	(137)	(186)
<b>31 December 2015</b>	<b>(108)</b>	<b>(185)</b>	<b>(293)</b>
<b>Net book value:</b>			
<b>31 December 2013</b>	<b>818</b>	<b>217</b>	<b>1,035</b>
<b>31 December 2014</b>	<b>377</b>	<b>720</b>	<b>1,097</b>
<b>31 December 2015</b>	<b>380</b>	<b>1,644</b>	<b>2,024</b>



(Amounts in tables are in thousands of Georgian lari)

**11. Other assets and liabilities**

Other assets comprise:

	2015	2014
<b>Other non-financial assets</b>		
Prepaid expenses	432	284
Prepayments for operating lease	150	150
Prepayments for acquisition of intangible assets	106	752
Prepaid taxes other than income tax	20	15
Other	11	7
<b>Other assets</b>	<b>719</b>	<b>1,208</b>

Other liabilities comprise:

	2015	2014
<b>Other financial liabilities</b>		
Other financial liabilities	95	65
Derivative liabilities	–	204
	<b>95</b>	<b>269</b>
<b>Other non-financial liabilities</b>		
Payable to employees	780	73
Deferred income	35	24
Taxes other than income tax	2	20
	<b>817</b>	<b>117</b>
<b>Other liabilities</b>	<b>912</b>	<b>386</b>

The table below shows the fair values of derivative financial instruments, recorded as liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset or liability and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk. There are no derivatives as of 31 December 2015.

	2014	
	Notional amount	Fair Value liability
<b>Foreign exchange contracts</b>		
SWAPS – domestic	22,927	204
<b>Total derivative liabilities</b>	<b>22,927</b>	<b>204</b>

*(Amounts in tables are in thousands of Georgian lari)***12. Amounts due to credit institutions**

Amounts due to credit institutions comprise:

	<b>2015</b>	<b>2014</b>
Short-term loan from the NBG	69,700	–
Time deposits of the Parent	64,086	43,222
Time deposits of resident commercial banks	15,706	9,318
Overdraft from the Parent	6,397	–
Time deposits of non-resident commercial banks	4,793	–
Current accounts of the Parent	1,247	442
<b>Amounts due to credit institutions</b>	<b>161,929</b>	<b>52,982</b>

The time deposits placed by four resident commercial banks denominated in GEL and a single non-resident bank denominated in USD, outstanding at 31 December 2015, matured in January 2016.

The loan from the NBG was obtained on 31 December 2015 and matured in January 2016.

Time deposits placed by the Parent are denominated in EUR, AZN and USD. Time deposits of GEL 44,304 thousand mature during 2016 and GEL 19,782 thousand matures in June 2017.

**13. Amounts due to customers**

The amounts due to customers include the following:

	<b>2015</b>	<b>2014</b>
Time deposits of customers	11,149	3,980
Current accounts of customers	10,139	1,217
<b>Amounts due to customers</b>	<b>21,288</b>	<b>5,197</b>

Held as security against guarantees (Note 16)	10,497	–
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As at 31 December 2015, amounts due to customers included balances with three major customers of GEL 13,984 thousand that constituted 65.69% of the total of customer accounts (31 December 2014: GEL 4,819 thousand constituting 92.72% of the total amounts due to customers).

An analysis of customer accounts by economic sector follows:

	<b>2015</b>	<b>2014</b>
Construction	10,893	3,813
Non-banking credit organizations	5,511	–
Trade and services	4,569	1,218
Energy	235	–
Individuals	23	–
Other	57	166
<b>Amounts due to customers</b>	<b>21,288</b>	<b>5,197</b>



(Amounts in tables are in thousands of Georgian lari)

**14. Taxation**

The corporate income tax benefit for the year ended 31 December 2015 comprises of deferred tax benefit of GEL 1,624 thousand (31 December 2014: GEL 6 thousand).

The income tax rate applicable to the Bank's income is 15%. The effective income tax rate differs from the statutory income tax rate. A reconciliation of the income tax benefit expense on statutory rates with actual is as follows:

	<b>2015</b>	<b>2014</b>
<b>Profit/(loss) before income tax</b>	638	(3,804)
Statutory tax rate	15%	15%
<b>Theoretical income tax benefit at the statutory rate</b>	<b>(96)</b>	<b>571</b>
Tax exempt income	334	453
Non-deductible expenses	(53)	(108)
Utilised tax losses carried forward, not recognized previously	335	–
Change in unrecognized deferred tax asset	1,104	(910)
<b>Income tax benefit</b>	<b>1,624</b>	<b>6</b>

Deferred tax assets and liabilities as at 31 December 2015 and 31 December 2014 and their movements for the respective period:

	<b>2013</b>	<i>Through statement of profit and loss</i>	<i>Through statement of OCI</i>	<b>2014</b>	<i>Through statement of profit and loss</i>	<i>Through statement of OCI</i>	<b>2015</b>
<b>Tax effect of deductible temporary differences</b>							
Tax losses carried forward	561	1,624	–	2,185	(367)	–	1,818
Other liabilities	19	(5)	–	14	54	–	68
<b>Gross deferred tax asset</b>	<b>580</b>	<b>1,619</b>	<b>–</b>	<b>2,199</b>	<b>(313)</b>	<b>–</b>	<b>1,886</b>
Unrecognised deferred tax asset	(561)	(910)	–	(1,471)	1,471	–	–
<b>Deferred tax asset</b>	<b>19</b>	<b>709</b>	<b>–</b>	<b>728</b>	<b>1,158</b>	<b>–</b>	<b>1,886</b>
<b>Tax effect of taxable temporary differences</b>							
Property and equipment	(100)	64	–	(36)	109	–	73
Intangible assets	(17)	(5)	–	(22)	(27)	–	(49)
Loans to customers	–	(762)	–	(762)	368	–	(394)
Investment securities	–	–	(6)	(6)	16	(4)	6
<b>Deferred tax liability</b>	<b>(117)</b>	<b>(703)</b>	<b>(6)</b>	<b>(826)</b>	<b>466</b>	<b>(4)</b>	<b>(364)</b>
<b>Deferred tax asset/(liability)</b>	<b>(98)</b>	<b>6</b>	<b>(6)</b>	<b>(98)</b>	<b>1,624</b>	<b>(4)</b>	<b>1,522</b>

The Bank incurred tax losses of GEL 10,915 thousand and GEL 3,440 thousand for 2014 and 2013 which, can be carried for 5 years and will expire in 2018 and 2019 respectively if not utilized. During 2015 the Bank utilized GEL 2,233 thousand from the tax losses of 2013. Management evaluated and concluded that it is probable that deferred tax assets on past tax losses will be recovered, since the Bank started to generate taxable profits in 2015, thus the deferred tax asset on tax losses carried forward has been recognized in full as at 31 December 2015.

(Amounts in tables are in thousands of Georgian lari)

## 15. Equity

The share capital of the Bank was contributed by the Parent in GEL and they entitle to dividends and any capital distribution in GEL.

On 14 February 2014, the Parent of the Bank decided to increase the Bank's share capital by GEL 68,000 thousand. Increase of capital was paid on 17 March 2014.

As at 31 December 2015 and 2014, the Bank's authorized, issued and fully paid capital amounted to GEL 103,000 thousand comprising of 103,000,000 common shares with nominal value of GEL 1.00. Each share entitles one vote to the shareholder.

In accordance with Georgian legislation, dividends may only be declared by the Bank's Parent from the net income as shown in the Bank's financial statements prepared in compliance with the NBG requirements. The Bank is obliged to officially inform the NBG of any dividends declared and the NBG reserves the right to suspend or restrict the disbursement of dividends should the Bank be in breach of the NBG regulations.

No dividends were declared or paid during the year ended 31 December 2015 (2014: nil).

### Nature and purpose of other reserves

Unrealised fair value changes on available-for-sale investments are recorded as other reserves in the equity.

## 16. Commitments and contingencies

### Taxation

Georgian tax legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by the relevant tax authorities. It is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation as at 31 December 2015 is appropriate and that the Bank's tax, currency and customs positions will be sustained.

### Commitments and contingencies

As at 31 December 2015 and 2014, the Bank's commitments and contingencies comprised the following:

	2015	2014
<b>Credit related commitments</b>		
Guarantees issued	22,326	2,902
Unused credit lines	443	463
Letters of credit	359	559
	<b>23,128</b>	<b>3,924</b>
<b>Operating lease commitments</b>		
Not later than 1 year	1,525	1,112
More than 1 year but less than 5 years	625	1,633
	<b>2,150</b>	<b>2,745</b>
<b>Capital commitments</b>		
Less: deposits held as security against guarantees issued (Note 13)	–	108
	(10,497)	–
<b>Commitments and contingencies</b>	<b>14,781</b>	<b>6,777</b>



*(Amounts in tables are in thousands of Georgian lari)***17. Net fee and commission income/(expense)**

Net fee and commission income/(expense) comprise:

	2015	2014
Guarantees	299	11
Brokerage operations	163	–
Settlements operations	72	51
Cash operations	13	3
Currency conversion operations	–	29
<b>Fee and commission income</b>	<b>547</b>	<b>94</b>
Settlements operations	(119)	(98)
Plastic cards	(56)	–
Guarantees	(45)	–
Cash operations	(19)	(7)
Brokerage operations	(1)	–
<b>Fee and commission expense</b>	<b>(240)</b>	<b>(105)</b>
<b>Net fee and commission income/(expense)</b>	<b>307</b>	<b>(11)</b>

**18. Personnel, general and administrative expenses**

Personnel, general and administrative expenses comprise:

	2015	2014
Salaries	3,160	2,038
Bonuses and other employee benefits	1,329	235
<b>Personnel expenses</b>	<b>4,489</b>	<b>2,273</b>
Operating leases	1,341	1,005
Professional services	912	696
Advertising costs	412	337
Personnel training	190	84
Corporate hospitality and entertainment	155	105
Transportation and business trip expenses	122	120
Utilities	117	99
Security expenses	69	58
Communication	62	124
Maintenance and exploitation	38	7
Insurance	35	32
Taxes other than income tax	34	48
Membership fees	26	25
Other	208	151
<b>General and administrative expenses</b>	<b>3,721</b>	<b>2,891</b>

(Amounts in tables are in thousands of Georgian lari)

## 19. Risk management

### Introduction

The process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. Regardless of the sophistication of the measures, bank distinguishes between expected and unexpected losses. Expected losses are typically reserved for as described in credit risk policy. For unexpected losses Bank relies on its capital as a buffer to absorb such losses. The Bank is exposed to financial risk, being subdivided into credit and liquidity risk, operational risk and market risk, being subdivided into trading and non-trading risks.

#### *Risk management structure*

##### *Board of Directors*

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles. The Board of Directors is ultimately responsible for identifying and controlling risks and different departments and committees which are responsible for managing and monitoring risks.

##### *Risk management*

The Risk Management Department is responsible for determining, implementing and maintaining risk management framework.

##### *Asset and Liability Committee*

*Asset and Liability Committee* (ALCO) is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding, liquidity, interest rate, and capital adequacy risks of the Bank.

##### *Internal Audit*

Risk management processes throughout the Bank are audited by the internal audit function on a constant basis, which examines the adequacy of the procedures, their design and operational effectiveness, and the Bank's compliance both with the regulatory requirements and internal procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

##### *Audit Committee*

Audit committee functions are undertaken by the relevant audit committee members of the Parent. The Audit Committee is responsible for the fundamental risk issues and manages and monitors relevant risk decisions and performance of control functions by other departments in the Bank pertaining to general control environment, manual, IT dependent or application controls, intentional or unintentional misstatement risks, risk of fraud or misappropriation of assets, information security, anti-money laundering, etc.



(Amounts in tables are in thousands of Georgian lari)

## **19. Risk management (continued)**

### **Introduction (continued)**

#### *Risk measurement and reporting systems*

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept. The main body to which the risks are reported is ALCO. The respective meetings are held once a month.

#### *Excessive risk concentration*

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

### **Credit risk**

Credit risk is the risk that the Bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Actual exposure per borrower against limits is monitored on loans granted. The Credit Committee may initiate a change in the limits. Where appropriate, the Bank obtains collateral and corporate guarantees. The credit risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

#### *Credit-related commitments risks*

The Bank makes available to its customers guarantees which may require that the Bank make payments on their behalf. Such payments are collected from customers based on the terms of guarantee. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

(Amounts in tables are in thousands of Georgian lari)

**19. Risk management (continued)****Credit risk (continued)***Credit quality per class of financial assets*

The credit quality of financial assets is managed by the Bank internal credit review process.

Loans to customers of High grade are those for which the principal and interest are paid in a timely manner and are supported by the sound capital and paying capability of the borrower. This classification is proper when the borrower is financially strong and has sufficient capital to cushion unforeseen adverse impacts, is within its profit targets and produces cash flows sufficient to satisfy a liability on time, including the subject asset.

Standard grade is assigned to loans when they are adequately protected but potentially weak because while there was to be stable financial condition and paying capability of the borrower at the time of the loan's origination, some deficiencies or trends are now apparent which, if not corrected, might cause concern about the borrower's ability to continue to serve the loan in a timely manner.

Loans are classified as Sub-standard if they are inadequately protected by the capital and paying capability of the borrower or by the value of any supporting collateral. Sub-standard loan has such weaknesses or problems which jeopardize payments of the indebtedness or makes full repayment questionable.

	<i>Notes</i>	<i>Neither past due nor impaired</i>		<i>Total 2015</i>
		<i>High grade 2015</i>	<i>Standard grade 2015</i>	
Amounts due from credit institutions	6	21,152	–	21,152
Loans to customers, gross	7	109,913	–	109,913
Investment securities	8	117,105	6,215	123,320
<b>Total</b>		<b>248,170</b>	<b>6,215</b>	<b>254,385</b>

	<i>Notes</i>	<i>Neither past due nor impaired</i>		<i>Total 2014</i>
		<i>High grade 2014</i>	<i>Sub-standard grade 2014</i>	
Amounts due from credit institutions	6	13,700	–	13,700
Loans to customers, gross	7	39,235	13,000	52,235
Investment securities	8	76,219	–	76,219
<b>Total</b>		<b>129,154</b>	<b>13,000</b>	<b>142,154</b>



(Amounts in tables are in thousands of Georgian lari)

## 19. Risk management (continued)

### Credit risk (continued)

#### *Impairment assessment*

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 30 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

#### *Individually assessed allowances*

The Bank determines the allowances appropriate for each individually significant loan on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

#### *Collectively assessed allowances*

Allowances are assessed collectively for losses on loans to customers that are not individually significant and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review. Zero collective assessment rates is applied for the loan exposures towards legal entities owned by high credit rated foreign government.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Due to the reason that the Bank does not possess own statistical data impairment losses are calculated based on industrial average.

Financial guarantees are assessed and provision made in a similar manner as for loans to customers.

(Amounts in tables are in thousands of Georgian lari)

**19. Risk management (continued)****Credit risk (continued)**

The geographical concentration of Bank's financial assets and liabilities is set out below:

	2015				2014			
	Georgia	OECD	Other Non-OECD	Total	Georgia	OECD	Other Non-OECD	Total
<b>Assets</b>								
Cash and cash equivalents	22,250	3	29	22,282	6,713	185	202	7,100
Amounts due from credit institutions	21,152	–	–	21,152	4,636	–	9,064	13,700
Loans to customers	108,602	–	–	108,602	51,836	–	–	51,836
Investment securities	117,105	–	6,215	123,320	65,369	–	10,850	76,219
	<u>269,109</u>	<u>3</u>	<u>6,244</u>	<u>275,356</u>	<u>128,554</u>	<u>185</u>	<u>20,116</u>	<u>148,855</u>
<b>Liabilities</b>								
Amounts due to credit institutions	85,407	2	76,520	161,929	9,318	–	43,664	52,982
Amounts due to customers	21,288	–	–	21,288	5,197	–	–	5,197
Other liabilities	91	4	–	95	266	3	–	269
	<u>106,786</u>	<u>6</u>	<u>76,520</u>	<u>183,312</u>	<u>14,781</u>	<u>3</u>	<u>43,664</u>	<u>58,448</u>
<b>Net assets/(liabilities)</b>	<u>162,323</u>	<u>(3)</u>	<u>(70,276)</u>	<u>92,044</u>	<u>113,773</u>	<u>182</u>	<u>(23,548)</u>	<u>90,407</u>

**Liquidity risk and funding management**

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. Funds attracted from the Parent provide sufficient sources for the Bank's operations in the foreseeable future. The Bank manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of state securities that can be pledged to the NBG in the event of an unforeseen interruption of cash flow. In addition, the Bank maintains a cash deposit (obligatory reserve) with the NBG, the amount of which depends on the level of customer funds attracted. The liquidity position is assessed and managed by the Bank primarily on a standalone basis, based on certain liquidity ratios established by the NBG. As at 31 December, these ratios were as follows:

	2015 %	2014 %
LK "Average Liquidity Ratio" (Average volume of liquid assets / Average volume of liabilities)	34.12	102.66



(Amounts in tables are in thousands of Georgian lari)

**19. Risk management (continued)****Liquidity risk and funding management (continued)***Analysis of financial liabilities by remaining contractual maturities*

The tables below summarize the maturity profile of the Bank's financial liabilities at 31 December based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

<b>As at 31 December 2015</b>	<b><i>Less than 3 months</i></b>	<b><i>3 to 12 months</i></b>	<b><i>1 to 5 years</i></b>	<b><i>Over 5 years</i></b>	<b><i>Total</i></b>
<b>Financial liabilities</b>					
Amounts due to credit institutions	141,430	987	21,214	–	<b>163,631</b>
Amounts due to customers	20,636	2,919	–	–	<b>23,555</b>
Other financial liabilities	95	–	–	–	<b>95</b>
<b>Total undiscounted financial liabilities</b>	<b>162,161</b>	<b>3,906</b>	<b>21,214</b>	<b>–</b>	<b>187,281</b>

  

<b>As at 31 December 2014</b>	<b><i>Less than 3 months</i></b>	<b><i>3 to 12 months</i></b>	<b><i>1 to 5 years</i></b>	<b><i>Over 5 years</i></b>	<b><i>Total</i></b>
<b>Financial liabilities</b>					
Amounts due to credit institutions	38,215	15,092	–	–	<b>53,307</b>
Amounts due to customers	4,864	347	–	–	<b>5,211</b>
Other financial liabilities	269	–	–	–	<b>269</b>
<b>Total undiscounted financial liabilities</b>	<b>43,348</b>	<b>15,439</b>	<b>–</b>	<b>–</b>	<b>58,787</b>

The table below shows the contractual expiry by maturity of the Bank's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

	<b><i>Less than 3 months</i></b>	<b><i>3 to 12 months</i></b>	<b><i>1 to 5 years</i></b>	<b><i>Over 5 years</i></b>	<b><i>Total</i></b>
2015	22,769	359	–	–	<b>23,128</b>

  

	<b><i>Less than 3 months</i></b>	<b><i>3 to 12 months</i></b>	<b><i>1 to 5 years</i></b>	<b><i>Over 5 years</i></b>	<b><i>Total</i></b>
2014	3,091	833	–	–	<b>3,924</b>

The Bank expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments. The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables above. These balances are included in amounts due in less than three months in the tables above.

(Amounts in tables are in thousands of Georgian lari)

**19. Risk management (continued)****Market risk**

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. Except for the concentrations within foreign currency, the Bank has no significant concentration of market risk.

*Currency risk*

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank has set limits on positions by currency based on the NBG regulations. Positions are monitored on a daily basis.

<i>Currency</i>	<i>change in currency rate 2015</i>	<i>Effect on profit before tax 2015</i>	<i>change in currency rate 2014</i>	<i>Effect on profit before tax 2014</i>
USD	15%/(15%)	105/(105)	1%/(1%)	(107)/107
AZN	15%/(15%)	15/(15)	1%/(1%)	108/(108)

*Prepayment risk*

Prepayment risk is the risk that the Bank will incur a financial loss because its customers and counterparties repay or request repayment earlier or later than expected.

The effect on profit before tax for one year assuming 10% of repayable financial instruments were to prepay at the beginning of the year, with all other variables held constant, is as follows:

	<i>Decrease of net interest income</i>
2015	1,303
2014	589

**Operational risk**

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls should include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.



(Amounts in tables are in thousands of Georgian lari)

**20. Fair value measurements****Fair value hierarchy**

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- ▶ Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- ▶ Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- ▶ Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

<i>Fair value measurement using</i>				
<i>At 31 December 2015</i>	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
<b>Assets for which fair values are disclosed</b>				
Cash and cash equivalents	22,282	–	–	<b>22,282</b>
Amounts due from credit institutions	–	–	21,152	<b>21,152</b>
Loans to customers	–	–	108,602	<b>108,602</b>
Investment securities	–	6,215	117,105	<b>123,320</b>
<i>Fair value measurement using</i>				
<i>At 31 December 2015</i>	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
<b>Liabilities for which fair values are disclosed</b>				
Amounts due to credit institutions	–	–	161,929	<b>161,929</b>
Amounts due to customers	–	–	21,288	<b>21,288</b>
<i>Fair value measurement using</i>				
<i>At 31 December 2014</i>	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
<b>Assets measured at fair value</b>				
Investment securities	10,849	–	65,370	<b>76,219</b>
<b>Assets for which fair values are disclosed</b>				
Cash and cash equivalents	7,100	–	–	<b>7,100</b>
Amounts due from credit institutions	–	–	13,700	<b>13,700</b>
Loans to customers	–	–	51,836	<b>51,836</b>
<i>Fair value measurement using</i>				
<i>At 31 December 2014</i>	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
<b>Liabilities measured at fair value</b>				
Other liabilities - derivative financial liabilities	–	204	–	<b>204</b>
<b>Liabilities for which fair values are disclosed</b>				
Amounts due to credit institutions	–	–	52,982	<b>52,982</b>
Amounts due to customers	–	–	5,197	<b>5,197</b>

(Amounts in tables are in thousands of Georgian lari)

**20. Fair value measurements (continued)****Fair value of financial assets and liabilities not carried at fair value**

Set out below is a comparison by class of the carrying amounts and fair values of the Bank's financial instruments that are not carried at fair value in the statement of financial position. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying value 2015</i>	<i>Fair value 2015</i>	<i>Unrecog- nised gain/(loss) 2015</i>	<i>Carrying value 2014</i>	<i>Fair value 2014</i>	<i>Unrecog- nised gain/(loss) 2014</i>
<b>Financial assets</b>						
Cash and cash equivalents	22,282	22,282	–	7,100	7,100	–
Amounts due from credit institutions	21,152	21,152	–	13,700	13,700	–
Loans to customers	108,602	108,602	–	51,836	51,836	–
Investment securities	123,320	121,500	(1,820)	–	–	–
<b>Financial liabilities</b>						
Amounts due to credit institutions	161,929	161,929	–	52,982	52,982	–
Amounts due to customers	21,288	21,288	–	5,197	5,197	–
<b>Total unrecognised change in fair value</b>			<b>(1,820)</b>			<b>–</b>

**Valuation techniques and assumptions**

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

*Assets for which fair value approximates carrying value*

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. All of the Bank's financial assets excluding loans to customers (i.e. cash and cash equivalents and amounts due from credit institutions) and financial liabilities (amounts due to customers) are either liquid or are maturing within 3 months from the reporting date.

The fair value of loans to customers is estimated by comparing market interest rates when they were first recognized with current market rates offered for similar financial assets. The majority of loans to customers outstanding as at 31 December were issued within 12 months period ended 31 December 2015 at market interest rates, while the contractual interest rates of those loans issued in 2014 approximate market interest rates as at 31 December 2015. Hence their carrying value approximates their fair value.

*Investment securities*

As at 31 December 2015 investment securities represent fixed and floating rated financial assets carried at amortized cost (31 December 2014: investment securities available for sale, measured at fair value). The fair value for investment securities loans and receivables is derived by discounting the future cash flows using current market rates for similar financial assets.



(Amounts in tables are in thousands of Georgian lari)

**20. Fair value measurements (continued)****Movements in level 3 assets at fair value**

The following table shows a reconciliation of the opening and closing amount of Level 3 assets which are recorded at fair value:

	1 January 2015	Purchases	Interest income	Loss recorded in OCI	Settlements	Reclassifica- tions (Note 8)	At 31 December 2015
<b>Assets</b>							
Investment securities available-for-sale	65,370	77,525	3,104	(779)	(60,543)	(84,677)	–
	<u>65,370</u>	<u>77,525</u>	<u>3,104</u>	<u>(779)</u>	<u>(60,543)</u>	<u>(84,677)</u>	<u>–</u>

  

	At 1 January 2014	Purchases	Interest income	Gain recorded in OCI	Settlements	At 31 December 2014
<b>Assets</b>						
Investment securities available-for-sale	12,220	72,670	3,366	245	(23,131)	65,370
	<u>12,220</u>	<u>72,670</u>	<u>3,366</u>	<u>245</u>	<u>(23,131)</u>	<u>65,370</u>

The following table shows the quantitative information about significant unobservable inputs used in the fair value measurement categorized within Level 3 of the fair value hierarchy:

31 December 2014	Carrying amount	Valuation techniques	Unobservable input	Range of discount rate
<b>Investment securities available-for-sale</b>				
Treasury bills of the Ministry of Finance of Georgia	53,392	Discounted cash flow	Discount rate	4.59% - 5.34%
Treasury bonds of the Ministry of Finance of Georgia	8,163	Discounted cash flow	Discount rate	6.47%
Certificates of deposit of financial institutions	3,815	Discounted cash flow	Discount rate	5.25%

In order to determine reasonably possible alternative assumptions the Bank adjusted the above key unobservable model inputs by increasing and decreasing the discount rate by 10%. The effect on carrying amount of investment securities available for sale was immaterial.

(Amounts in tables are in thousands of Georgian lari)

**21. Maturity analysis of assets and liabilities**

The table below shows an analysis of assets and liabilities according to when they are expected to be recovered or settled. See Note 19 "Risk management" for the Bank's contractual undiscounted repayment obligations.

	2015			2014		
	Within one year	More than one year	Total	Within one year	More than one year	Total
Cash and cash equivalents	22,282	–	22,282	7,100	–	7,100
Amounts due from credit institutions	21,152	–	21,152	13,700	–	13,700
Loans to customers	26,130	82,472	108,602	24,883	26,953	51,836
Investment securities	62,282	61,038	123,320	58,394	17,825	76,219
Property and equipment	–	2,689	2,689	–	4,047	4,047
Intangible assets	–	2,024	2,024	–	1,097	1,097
Deferred income tax assets	–	1,522	1,522	–	–	–
Other assets	604	115	719	1,189	19	1,208
<b>Total</b>	<b>132,450</b>	<b>149,860</b>	<b>282,310</b>	<b>105,266</b>	<b>49,941</b>	<b>155,207</b>
Amounts due to credit institutions	142,147	19,782	161,929	52,982	–	52,982
Amounts due to customers	21,288	–	21,288	5,197	–	5,197
Deferred income tax liabilities	–	–	–	–	98	98
Other liabilities	912	–	912	364	22	386
Provisions for guarantees and letters of credit	–	–	–	18	41	59
<b>Total</b>	<b>164,347</b>	<b>19,782</b>	<b>184,129</b>	<b>58,561</b>	<b>161</b>	<b>58,722</b>
<b>Net</b>	<b>(31,897)</b>	<b>130,078</b>	<b>98,181</b>	<b>46,705</b>	<b>49,780</b>	<b>96,485</b>

Negative net current position is mainly caused by the short-term nature of the funding obtained from the Parent and other credit institutions.

Included in amounts due to credit institutions are term deposits in amount of GEL 44,304 thousand obtained from the Parent that are maturing during 2016, including GEL 43,337 thousand that already matured as of the date of issuance of these financial statements.

All matured deposits were replaced by new term deposits of the Parent. The Bank has intention to continue using the short-term financing facilities from the Parent.

The Bank has obtained a letter from the Parent dated 25 February 2016, stating that the Parent intends and has the ability to continue financing of the Bank and prolong the maturities of the term deposits and not to demand repayment if it harms the financial stability of the Bank. The Bank's net current position is positive GEL 11,440 thousand if term deposits from the Parent that have been replaced by the date of these financial statements are not considered.

According to the NBG regulation monthly average liquidity ratio should not be less than 30%. The Bank was compliant with the NBG prudential ratio requirements in respect of liquidity during 2015 and 2014. Average liquidity ratio of the Bank for 2015 was 34.12%. For more details please refer to Note 19, Liquidity risk and funding management caption.

The Bank is also regulated by the NBG to maintain appropriate level of mandatory reserves in GEL and foreign currencies against its liabilities to other credit institutions and customers. The Bank has been in full compliance with the NBG's mandatory reserve requirements during the reporting period ending 31 December 2015 and 2014.



(Amounts in tables are in thousands of Georgian lari)

**22. Related party disclosures**

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The outstanding balances of related party transactions are as follows:

	2015			2014	
	<i>The Parent</i>	<i>Key management personnel</i>	<i>Entities under common control</i>	<i>The Parent</i>	<i>Key management personnel</i>
Cash and cash equivalents	29	–	–	202	–
Amounts due to credit institutions	(71,730)	–	–	(43,664)	–
Amounts due to customers	–	(1)	(42)	–	–
Other liabilities	–	–	–	(7)	(3)

The income and expense arising from related party transactions are as follows:

	2015	2014
	<i>The Parent</i>	<i>The Parent</i>
Fee and commission income	44	8
Fee and commission expense	53	23
Interest expense on amounts due to credit institutions	2,178	526
Professional fees	5	–

Compensation of key management personnel was comprised of the following:

	2015	2014
Salaries and other short-term benefits	1,029	407

Key management personnel as at 31 December 2015 and 2014, comprised of 3 members of the Supervisory Board and 3 members of the Board of Directors of the Bank.

**23. Capital adequacy**

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the ratios established by the NBG in supervising the Bank.

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements set by the NBG to safeguard the Bank's ability to continue as a going concern and to maintain sufficient capital base to achieve a capital adequacy ratio of at least 11.4% during 2015 (2014: 12%). Compliance with capital adequacy ratios set by the NBG is monitored monthly with reports outlining their calculation reviewed and signed by the Chief Accountant and submitted to the NBG.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities.

(Amounts in tables are in thousands of Georgian lari)

**23. Capital adequacy (continued)****NBG capital adequacy ratio**

The NBG requires banks to maintain a capital adequacy ratio of 11.4% of risk-weighted assets (2014: 12%) and Tier 1 Capital adequacy ratio of 7.6% (2014: 8%). As at 31 December 2015 and as at 31 December 2014, the Bank's capital adequacy ratios on this basis were as follows:

	<i>Notes</i>	<i>31 December 2015</i>	<i>Adjustments</i>	<i>31 December 2015 Per the NBG</i>
Share capital	15	103,000	–	103,000
Prior years accumulated deficit		(6,789)	(5,063)	(11,852)
Less: Intangible assets, net	10	(2,024)	–	(2,024)
<b>Main capital</b>		<b>94,187</b>	<b>(5,063)</b>	<b>89,124</b>
Current year income		2,262	431	2,693
General reserves	7	1,311	1,131	2,442
<b>Additional capital</b>		<b>3,573</b>	<b>1,562</b>	<b>5,135</b>
Less: deductions from capital		–	–	–
<b>Total capital</b>		<b>97,760</b>	<b>(3,501)</b>	<b>94,259</b>
<b>Risk weighted assets</b>				<b>215,933</b>
Capital adequacy ratio				43.65%
Tier 1 Capital adequacy ratio				41.27%

	<i>Notes</i>	<i>31 December 2014</i>	<i>Adjustments</i>	<i>31 December 2014 Per the NBG</i>
Share capital	15	103,000	–	103,000
Prior years accumulated deficit		(2,991)	94	(2,897)
Less: Intangible assets, net	10	(1,097)	–	(1,097)
<b>Main capital</b>		<b>98,912</b>	<b>94</b>	<b>99,006</b>
Current year loss		(3,798)	(5,157)	(8,955)
General reserves		458	394	852
<b>Additional capital</b>		<b>(3,340)</b>	<b>(4,763)</b>	<b>(8,103)</b>
Less: deductions from capital		–	–	–
<b>Total capital</b>		<b>95,572</b>	<b>(4,669)</b>	<b>90,903</b>
<b>Risk weighted assets</b>				<b>139,366</b>
Capital adequacy ratio				65.23%
Tier 1 Capital adequacy ratio				71.04%

Regulatory capital consists of main capital, which comprises share capital and retained earnings including current year profit. Certain adjustments are made to IFRS-based results and reserves, as prescribed by the NBG. The other component of regulatory capital is Additional capital, which includes subordinated debt and revaluation reserve.



(Amounts in tables are in thousands of Georgian lari)

**23. Capital adequacy (continued)****NBG capital adequacy ratio (continued)**

Starting from 30 June 2014 the NBG requires that all banks comply with Basel II regulations in their capital adequacy assessment. This implies the minimum ratio of 10.50% for total regulatory capital coefficient, minimum 7.00% of the core Tier 1 capital coefficient and minimum 8.50 % for Tier 1 capital coefficient. As at 31 December 2015, the Bank's capital adequacy ratios on the Basel II basis were as follows:

	Notes	31 December 2015	Adjustments	31 December 2015 Per the NBG
Additional tier 1 capital	15	103,000	–	103,000
Prior years accumulated deficit		(6,789)	(5,063)	(11,852)
Less: Intangible assets, net	10	(2,024)	–	(2,024)
Current year income		2,262	431	2,693
<b>Core tier 1 capital</b>		<b>96,449</b>	<b>(4,632)</b>	<b>91,817</b>
<b>Tier 1 capital</b>		<b>96,449</b>	<b>(4,632)</b>	<b>91,817</b>
Supplementary capital		1,311	1,131	2,442
<b>Total regulatory capital</b>		<b>97,760</b>	<b>(3,501)</b>	<b>94,259</b>
<b>Risk weighted assets</b>				<b>239,946</b>
Capital adequacy ratio				39.28%
Core Tier 1 capital/Tier 1 capital adequacy ratio				38.27%

	Notes	31 December 2014	Adjustments	31 December 2014 Per the NBG
Additional tier 1 capital	15	103,000	–	103,000
Prior years accumulated deficit		(2,991)	94	(2,897)
Less: Intangible assets, net	10	(1,097)	–	(1,097)
Current year loss		(3,798)	(5,157)	(8,955)
<b>Core tier 1 capital</b>		<b>95,114</b>	<b>(5,063)</b>	<b>90,051</b>
<b>Tier 1 capital</b>		<b>95,114</b>	<b>(5,063)</b>	<b>90,051</b>
Supplementary capital		458	394	852
<b>Total regulatory capital</b>		<b>95,572</b>	<b>(4,669)</b>	<b>90,903</b>
<b>Risk weighted assets</b>				<b>127,699</b>
Capital adequacy ratio				71.19%
Core Tier 1 capital/Tier 1 capital adequacy ratio				70.52%