Southern Gas Corridor
Closed Joint-Stock Company

Consolidated financial statements

31 December 2015

Southern Gas Corridor CJSC

Consolidated financial statements

31 December 2015

Contents

Building a better
working world

Ernst & Young Holdings (CIS) B.V.
Port Baku Towers Business Centre
South Tower, 9th floor
153, Neftchilar Ave.
Baku, AZ1010, Azerbaijan
Tel: +994 (12) 490 7020
Fax: +994 (12) 490 7017
www.ey.com/az

Ernst & Yanq Holdinqs (SiAyEs) Bi.Vi.
Port Baku Tauers Biznes Mərkəzi
Cənub Qülləsi, 9-cu mərtəbə
Neftçilər prospekti, 153
Bakı, AZ1010, Azərbaycan
Tel: +994 (12) 490 7020
Faks: +994 (12) 490 7017

Independent auditors' report

To the Board of Directors and shareholders of
the Southern Gas Corridor CJSC

We have audited the accompanying consolidated financial statements of the Southern Gas Corridor Closed Joint Stock Company (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2015 and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

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

Auditors' responsibility

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

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

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

Opinion

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

Ernst & Young Holdings (CIS) B.V.

13 June 2016

Southern Gas Corridor CJSC

Consolidated statement of financial position

(Amounts presented are in thousands of US dollars)

	Note	31 December 2015 Audited	31 December 2014 Audited
Assets			
Non-current assets			
Oil and gas properties	6	490,333	512,404
Construction in progress and development costs	7	2,564,393	988,117
Advance payments	8	1,636,491	943,134
Investments in associate	9	60,740	56,432
Loan receivables	10	137,497	44,334
Other non-current assets		2,003	2,335
Total non-current assets		**4,891,457**	**2,546,756**
Current assets			
Cash and cash equivalents	11	254,560	212,198
Deposits	11	–	33,246
Accounts receivable	12	19,004	36,820
Inventories	13	9,335	13,152
Accrued revenue	19	3,119	13,118
Other current assets	14	37,924	38,214
Total current assets		**323,942**	**346,748**
Total assets		**5,215,399**	**2,893,504**
Equity and liabilities			
Equity			
Share capital	15	1,444,900	100,000
Other reserves	15	(45,176)	–
Cumulative translation differences		(23,516)	(11,104)
Retained earnings		31,703	13,208
Equity attributable to the Group's equity holders		**1,407,911**	**102,104**
Non-controlling interest	15	339,995	–
Total equity		**1,747,906**	**102,104**
Non-current liabilities			
Long-term borrowings	16	2,191,873	1,854,301
Government grant	16	683,281	697,699
Decommissioning liabilities	17	52,066	37,063
Deferred revenue	19	5,283	7,662
Deferred tax liability	21	8,060	6,458
Other non-current liabilities		10,001	–
Total non-current liabilities		**2,950,564**	**2,603,183**
Current liabilities			
Trade and other payables	18	197,025	54,896
Accrued liabilities	18	318,759	131,945
Income tax payable		1,145	1,376
Total current liabilities		**516,929**	**188,217**
Total equity and liabilities		**5,215,399**	**2,893,504**

Signed and authorized on behalf of the Group

Afgan Isayev, General Director 13 June 2016

Ramil Babayev, Finance Director 13 June 2016

Azərbaycan Respublikası Qapalı Səhmdar Cəmiyyəti Cənub Qaz Dəhlizi Southern Gas Corridor Closed Joint Stock Company Azerbaijan Republic

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

Southern Gas Corridor CJSC

Consolidated statement of comprehensive income

(Amounts presented are in thousands of US dollars)

	Note	Year ended 31 December 2015 Audited	From 31 March 2014 (inception) to 31 December 2014 Audited
Revenue	19	151,473	76,894
Cost of sales	20	(69,944)	(28,433)
Gross profit		**81,529**	**48,461**
General and administrative expenses		(12,510)	(1,489)
Transportation tariffs		(4,613)	(1,594)
Other income		16,190	13,122
Operating profit		**80,596**	**58,500**
Interest income		4,895	3,338
Finance costs	10, 16, 17	(56,110)	(42,715)
Share of result of associates	9	(5,856)	(2,749)
Foreign exchange loss, net		(85)	(1,955)
Profit before income tax		**23,440**	**14,419**
Income tax expenses	21	(3,781)	(1,211)
Profit for the year/period		**19,659**	**13,208**
Other comprehensive loss			
Other comprehensive loss to be reclassified to profit or loss in subsequent period			
Exchange differences on translation of foreign operations		(6,411)	(5,354)
Exchange differences on translation of foreign associate	9	(6,001)	(5,750)
Other comprehensive loss for the year/period		**(12,412)**	**(11,104)**
Total comprehensive income for the year/period		**7,247**	**2,104**
Profit attributable to:			
Equity holders of the Group		18,495	13,208
Non-controlling interest		1,164	–
		19,659	**13,208**
Total comprehensive income attributable to:			
Equity holders of the Group		6,083	2,104
Non-controlling interest		1,164	–
		7,247	**2,104**

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

Southern Gas Corridor CJSC

Consolidated statement of cash flows

(Amounts presented are in thousands of US dollars)

	Note	Year ended 31 December 2015 Audited	From 31 March 2014 (inception) to 31 December 2014 Audited
Operating activities			
Profit before income tax		23,440	14,419
Non-cash adjustments to reconcile profit before tax to net cash flows			
Finance costs	10, 16,17	56,110	42,715
Depreciation and depletion	20	53,858	21,133
Share of result of associate	9	5,856	2,749
Other income		(16,190)	(13,122)
Interest income		(4,895)	(3,338)
Foreign exchange loss		(164)	817
Working capital adjustments			
Accounts receivable		12,638	(14,208)
Inventories		3,817	1,479
Accrued revenue		9,999	(8,844)
Other assets		622	(24,049)
Deferred revenue		(2,379)	(313)
Trade and other payables		(16,267)	(4,720)
Accrued liabilities		8,406	10,885
Cash generated from operations		**134,851**	**25,603**
Income tax paid		(2,497)	–
Interest received		4,895	2,823
Net cash flows from operating activities		**137,249**	**28,426**
Investing activities			
Acquisition of subsidiary, net of cash received		–	(165,219)
Acquisition of undivided interests in joint projects		–	(946,986)
Placement of deposits	11	(350,000)	(99,000)
Proceeds from withdrawal of deposits	11	383,246	65,754
Financing provided to third party	10	(27,950)	–
Financing provided to associate	10	(45,556)	–
Advance payments for acquisition of shares	8	(548,594)	(796,288)
Investments in oil and gas properties		(20,234)	(174,396)
Additions to construction in progress and development costs		(1,313,628)	(180,509)
Investment in associates	9	(17,500)	(8,260)
Other acquisitions		–	(2,003)
Net cash used in investing activities		**(1,940,216)**	**(2,306,907)**
Financing activities			
Contribution from shareholders	15	1,344,900	100,000
Proceeds from borrowings	16	234,780	2,522,996
Repayment of borrowings		–	(132,317)
Proceeds from sale of shares in subsidiary	15	265,649	–
Net cash flows from financing activities		**1,845,329**	**2,490,679**
Net increase in cash and cash equivalents		**42,362**	**212,198**
Cash and cash equivalents as at inception	11	212,198	–
Cash and cash equivalents at the end of the year	11	**254,560**	**212,198**
Non-cash operating activity			
Government grant on loan received for financing of projects	16	–	704,270

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

Southern Gas Corridor CJSC

Consolidated statement of changes in equity

(Amounts presented are in thousands of US dollars)

	Attributable to the equity holders of the parent						
	Share capital	**Other reserves**	**Cumulative translation differences**	**Retained earnings**	**Total**	**Non-controlling interest**	**Total equity**
At 31 March 2014 (inception)	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Profit for the period	–	–	–	13,208	**13,208**	–	**13,208**
Other comprehensive loss	–	–	(11,104)	–	**(11,104)**	–	**(11,104)**
Total comprehensive income/(loss)	**–**	**–**	**(11,104)**	**13,208**	**2,104**	**–**	**2,104**
Contribution from shareholders	100,000	–	–	–	**100,000**	–	**100,000**
At 31 December 2014	**100,000**	**–**	**(11,104)**	**13,208**	**102,104**	**–**	**102,104**
Profit for the year	–	–	–	18,495	**18,495**	1,164	**19,659**
Other comprehensive loss	–	–	(12,412)	–	**(12,412)**	–	**(12,412)**
Total comprehensive income/(loss)	**–**	**–**	**(12,412)**	**18,495**	**6,083**	**1,164**	**7,247**
Contribution from shareholders	1,344,900	–	–	–	**1,344,900**	–	**1,344,900**
Sale of share in subsidiary	–	(45,176)	–	–	**(45,176)**	338,831	**293,655**
At 31 December 2015	**1,444,900**	**(45,176)**	**(23,516)**	**31,703**	**1,407,911**	**339,995**	**1,747,906**

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

1. Corporate information

Southern Gas Corridor Closed Joint-Stock Company (the "Company" or "SGC CJSC") was established by the Presidential Decree No. 287 dated 25 February 2014. It was incorporated on 31 March 2014 in accordance with Azerbaijani legislation. 51% of the Company is owned by the Republic of Azerbaijan (the "State"), which is represented by the Ministry of Economy of the Republic of Azerbaijan ("ME"), whereas 49% belongs to the State Oil Company of Azerbaijan Republic ("SOCAR"). The Company is domiciled in the Republic of Azerbaijan. The registered address is located at 73 Neftchilar Avenue, Baku, AZ 1000, the Republic of Azerbaijan.

The Company was established for consolidating, managing and financing the State's interests in the full-field development of the Shah Deniz gas-condensate field, the expansion of the South Caucasus Pipeline ("SCP"), implementation of Trans-Anatolian Natural Gas Pipeline ("TANAP") and Trans Adriatic Pipeline ("TAP") projects (together the "Projects").

On 24 April 2014 the Company incorporated its 100% owned subsidiary, SGC Upstream LLC, for participating in the exploration and development of the Shah Deniz gas-condensate field in accordance with the Agreement on the Exploration, Development and Production Sharing for the Shah Deniz Prospective Area in the Azerbaijan Sector of the Caspian Sea ("SD PSA") dated 4 June 1996.

On 25 April 2014 the Company incorporated its 100% owned subsidiary, SGC Midstream LLC, to participate in the SCP project for the transportation of gas through gas export pipeline system from Azerbaijan through Georgia to the Georgian-Turkish border in accordance with, amongst other things, the Intergovernmental Agreement signed between the Government of Azerbaijan and the Government of Georgia.

On 31 July 2014 the Company, through its subsidiary, SGC Upstream LLC, acquired 6.67% participating interest in Shah Deniz project and 5.336% shares in Azerbaijan Gas Supply Company Limited ("AGSC") as well as 6.67% shares in South Caucasus Pipeline Company Limited ("SCPC"), through its subsidiary, SGC Midstream LLC, based on the Sale and Purchase Agreement ("SPA") signed on 29 April 2014 between the Company's respective subsidiaries (acting as the purchasers) and Azerbaijan (Shah Deniz) Limited ("AzSD") and Azerbaijan (South Caucasus Pipeline) Limited ("AzSCP") (acting as the sellers).

On 23 July 2014 the Company, acting through SGC Upstream LLC and SGC Midstream LLC signed the Deferred Sale and Purchase Agreement ("DSPA") for the acquisition of 10% participating interest in Shah Deniz project and 8% shares in AGSC from AzSD and 10% shares in SCPC from AzSCP, respectively. The closing of the agreement is expected to happen in March 2023, subject to fulfillment of all the conditions precedent.

On 23 July 2014 the Company signed the agreement to get hold of 20% shares in Trans Adriatic Pipeline AG ("TAP AG") (Project Company of TAP) through the acquisition of 100% shares of AzTAP GmbH from SOCAR Energy Holdings AG, a subsidiary of SOCAR. TAP AG was established for planning, developing, financing, and operating TAP project, including the construction of TAP, for the transportation of natural gas to the European markets.

On 23 July 2014 the Company signed the agreement to acquire from SOCAR 100% shares of TANAP Doğalgaz Iletim A.Ş. (Project Company of TANAP), which was established for the implementation of TANAP project within the territory of the Republic of Turkey. The purpose of constructing TANAP is to distribute natural gas across the country and to transit gas through the territory of Turkey to European countries in accordance with the Intergovernmental Agreement signed between the Government of Azerbaijan and the Government of Turkey.

On 13 April 2015 the Company sold its 30% share in TANAP Doğalgaz İletim A.Ş. ("TANAP A.Ş.") to Boru Hatları ile Petrol Taşıma A.Ş. ("BOTAS"). On 16 April 2015 the Company sold further 12% share in TANAP A.Ş. to BP Pipelines (TANAP) Limited (BP). Further details are disclosed in Note 15.

On 28 October 2015, management of SOCAR Turkey Enerji A.Ş. ("STEAS") has sent official letter expressing its intention for acquiring 7% shares in TANAP A.Ş. from the Company. No acquisition has taken place as of issuance of these consolidated financial statements.

2. Significant accounting policies

Basis of preparation

These consolidated financial statements of the Company and its subsidiaries (collectively referred to as “the Group”) for the year ended 31 December 2015 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by International Accounting Standards Board (“IASB”). The principal accounting policies applied in the preparation of these consolidated financial statements are set out below.

Going concern

The going concern basis assumes that the Group will continue its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. As at 31 December 2015 the Group had net current liabilities in the amount of US dollars 192,987. In addition, as at 31 December 2015, the Group had certain commitments which would require significant cash outflows in foreseeable future (see Note 25).

The Group’s ability to continue as a going concern depends on the ability to generate sufficient cash inflows from financing provided by third parties and its shareholders.

As noted in Note 27, during the period subsequent to 31 December 2015 the Group has received cash contribution from its shareholders in the amount of US dollars 295,900 and issued government guaranteed Eurobonds in the amount of US dollars 1,000,000. In addition, the Group’s management expects to receive sufficient amount of funds from proceeds from hydrocarbons sales under current Shah Deniz Production Sharing Agreement, contributions from State Oil Fund of the Republic of Azerbaijan (“SOFAZ”) and capital injections by the shareholders as well as through funds raised by external debt. The Group management believes that the funds obtained from the above sources will be sufficient for meeting its financial commitments and the Group will be able to continue as a going concern for the foreseeable future.

Basis for consolidation

The consolidated financial statements comprise the financial statements of the Group as at 31 December 2015.

Subsidiaries are all entities (including structured entities) over which the Group has control. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if and only if the Group has:

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

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- the contractual arrangement with the other vote holders of the investee;
- rights arising from other contractual arrangements;
- the Group’s voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary.

2. Significant accounting policies (continued)

Basis for consolidation (continued)

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated but considered as an impairment indicator of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

Profit or loss and each component of other comprehensive income are attributed to the equity holders of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance.

Business combinations

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

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

Transactions with non-controlling interest

Changes in the Group's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions (i.e. transactions with owners in their capacity as owners). In such circumstances the carrying amounts of the controlling and non-controlling interests shall be adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the Group.

Business combinations with entities under common control

The Group applies pooling of interest method of accounting for business combinations with entities under the common control from the date when the combination took place.

The pooling of interests method includes the following:

The assets and liabilities of the combining entities are reflected at their carrying amounts. No adjustments are made to reflect fair values, or recognise any new assets or liabilities, at the date of the combination. The only adjustments that are made are to align accounting policies.

No "new" goodwill is recognised as a result of the combination. The only goodwill that is recognised is any existing goodwill relating to either of the combining entities. Any difference between the consideration paid/transferred and the net assets acquired is reflected within equity.

Total comprehensive income reflects the results of the combining entities from the period when the combination took place.

2. Significant accounting policies (continued)

Business combinations (continued)

Acquisition of an entity that is not a business

When the Group acquires an entity that is not a business, it allocates the cost of acquisition between the individual identifiable assets and liabilities of the acquired entity on the basis of their relative fair values as following:

- monetary assets and monetary liabilities are recognized at their fair value;
- the cost of acquisition remained after deduction of the fair value of monetary assets and monetary liabilities is allocated to non-monetary assets and non-monetary liabilities on the basis of their fair value at the date of acquisition.

Investment in associates

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

The Group's investment in its associate is accounted for using the equity method. Under the equity method, the investment in an associate is initially recognised at cost. The carrying amount of the investment is adjusted to recognise changes in the Group's share of net assets of the associate since the acquisition date. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The statement of profit or loss reflects the Group's share of the results of operations of the associate. Any change in other comprehensive income ("OCI") of those investees is presented as part of the Group's OCI. In addition, when there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

The aggregate of the Group's share of profit or loss of an associate is shown on the face of the statement of profit or loss outside operating profit and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate.

The financial statements of the associate are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognise an impairment loss on its investment in its associate. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value, and then recognises the loss as "Share of profit of an associate" in the statement of profit or loss.

Upon loss of significant influence over the associate, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss.

2. Significant accounting policies (continued)

Investments in SD PSA, SCP and AGSC

According to the terms of SD PSA, the Group owns the portion of project's assets and is liable for its portion of project's liabilities. At the same time the Group is entitled to its portion of expenses incurred and revenues earned by the whole project. Therefore, the Group accounts for its investment in SD PSA by recognizing its interest portion of underlying assets, liabilities, expenses incurred and income earned by the project.

Participating interest of the Group in the SCP Project is treated by the Group as undivided interest related to the investment in SCPC and accounted by recognizing its interest portion of underlying assets, liabilities, expenses incurred and income earned by the project.

The Group holds an interest in the AGSC, a company established together with other contractor parties of the Shah Deniz Project and Ministry of Energy of the Republic of Azerbaijan. AGSC is special structured entity established for marketing, accounting, billing, payment and reporting of other administrative activities related to the sales of Shah Deniz gas and operates on no gain, no loss basis.

Foreign currency translation

The consolidated financial statements are presented in US dollars ("USD") and all values are rounded to the nearest thousands, except when otherwise indicated.

The functional currency of the Company, subsidiaries and associate are the following:

SGC CJSC	USD
SGC Upstream LLC	USD
SGC Midstream LLC	USD
TANAP A.Ş.	USD
AzTAP GmbH	EUR
TAP AG	EUR

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

Monetary assets and liabilities not already measured in the functional currency of respective Group entity are translated into the functional currency of that entity at the appropriate exchange rates prevailing at the reporting date.

Foreign exchange gains and losses resulting from the re-measurement into the functional currencies of respective Group's entities are recognized in profit or loss.

The results and financial position of the Group entities which functional currency differ from the presentation currency of the Group and not already measured in the Group's presentation currency are translated into the presentation currency of the Group as follows:

(i) assets and liabilities for each statement of financial position are translated at the closing rate at the date of that statement of financial position;

(ii) income and expenses for each statement of profit or loss and other comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

(iii) all resulting exchange differences are recognized as a separate component of equity – currency translation difference.

At 31 December 2015 the principal rate of exchange used for translating foreign currency balances was USD 1.0931 per EUR 1 (31 December 2014: 1.2139).

2. Significant accounting policies (continued)

Financial instruments – key measurement terms

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

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible to by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Group 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 consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 – quoted (unadjusted) market prices in active markets for identical assets or liabilities;

Level 2 – valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;

Level 3 – valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

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

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

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

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

2. Significant accounting policies (continued)

Financial instruments – key measurement terms (continued)

The effective interest rate method is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

Financial assets

Initial recognition and measurement

Financial assets are classified, at initial recognition, as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. All financial assets are recognized initially at fair value.

The Group has not designated any financial assets upon initial recognition as at fair value through profit or loss, held-to-maturity investments, available-for-sale financial assets, or as derivatives.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification:

Loan and receivables

This category is most relevant to the Group. Loan and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortized cost using the effective interest rate method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the effective interest rate method.

The effective interest rate method amortization is included in finance income in the consolidated statement of comprehensive income. The losses arising from impairment are recognized in the consolidated statement of comprehensive income.

Cash and cash equivalents

Cash and cash equivalents comprise cash at banks and at hand and short-term deposits with an original maturity of three months or less.

Accounts receivable

Accounts receivables which generally have 30-90 days' terms, are recognized and carried at original invoice amount less an allowance for any uncollectible amounts.

2. Significant accounting policies (continued)

Financial assets (continued)

Derecognition

A financial asset (or, where applicable a part of a financial asset) is derecognized when:

the rights to receive cash flows from the asset have expired, or;

the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass through" arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Impairment of financial assets

The Group assesses at each statement of financial position 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 have occurred after the initial recognition of the asset (an incurred "loss event") and that loss event 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 debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization 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.

Financial assets carried at amortized cost

For financial assets carried at amortized cost, the Group 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 Group 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 risk 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 recognized, are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial assets original effective interest rate.

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognized initially at fair value and in the case of loans and borrowings, plus directly attributable transaction costs.

The Group has not designated any financial liabilities upon initial recognition as financial liabilities at fair value through profit or loss, or as derivatives designated as hedging instruments in an effective hedge.

2. Significant accounting policies (continued)

Financial liabilities (continued)

Subsequent measurement

The measurement of financial liabilities depends on their classification as follows:

Loans and borrowings

This category is most relevant to the Group. After initial recognition, interest bearing loans and borrowings which have a fixed contractual repayment schedule are subsequently measured at amortized cost using the effective interest rate method. Gains and losses are recognized in the consolidated statement of comprehensive income when the liabilities are derecognized as well as through the effective interest rate method amortization process.

Amortized cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the effective interest rate method. The effective interest rate method amortization is included in finance cost in the consolidated statement of comprehensive income.

Borrowings with no pre-defined contractual repayment schedules are measured in accordance with actual contractual terms.

Trade and other payables

Trade and other payables are accrued when the counterparty performed its obligations under the contract. Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

Derecognition

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

When 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 recognized in the consolidated statement of comprehensive income.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Oil and gas properties

Oil and gas properties are stated at cost, less accumulated depreciation and provision for impairment, where required. Such cost includes the cost of replacing part of the oil and gas properties and borrowing costs for long-term construction projects if the recognition criteria are met.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of oil and gas properties items are capitalised and the replaced part is retired.

2. Significant accounting policies (continued)

Oil and gas properties (continued)

At the end of each reporting period management assesses whether there is any indication of impairment of oil and gas properties. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in profit or loss for the year. An impairment loss recognised for an asset in prior years is reversed where appropriate if there are indicators that impairment loss may no longer exist or may have decreased.

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

Construction in progress

All costs directly or indirectly attributable to the projects to construction and expansion the capacity of the pipeline systems are capitalized as a construction in progress. The construction in progress is stated at a cost and not depreciated. The construction in progress is transferred to the property, plant and equipment upon completion.

Depreciation, depletion and amortization

Depreciation, depletion and amortization of capitalized costs of oil and gas properties is calculated using the units-of-production method based on proved reserves for the cost of property acquisitions and proved developed reserves for exploration and development costs.

The cost of an off-shore production platform, terminal and other development costs incurred in connection with a planned group of development wells is reduced for the portion of development costs related to wells which have not been drilled yet in determining the asset base subject to the unit-of-production amortization rate until the additional development wells are drilled. Similarly, in computing the depletion rate, those proved reserves that will be produced only after significant additional development costs are incurred are excluded from proved developed reserves.

Depreciation, depletion and amortization of capitalized costs of the pipeline systems are calculated using the straight line method for the period of useful life of pipelines. The estimated useful life of the SCP pipeline is thirty years from 25 November 2006 when the pipeline was officially put in use. The estimated useful life of the TANAP pipeline system will be the period from the date when the pipeline is officially put in use till the year 2061.

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Oil and natural gas development expenditure

The Group follows the successful efforts method of accounting for oil and natural gas development activities. Costs to acquire mineral interests, to determine the technical feasibility, assess commercial viability of an identified resource and to drill and equip exploratory wells that find proved reserves are capitalized within exploration and evaluation assets. Costs to drill exploratory wells that do not find proved reserves, geological and geophysical costs, and costs of carrying and retaining unproved properties are expensed.

When proved reserves of oil and natural gas are identified and development is sanctioned by management, the relevant capitalized expenditure is first assessed for impairment and (if required) any impairment loss is recognized, then the remaining balance is transferred to oil and gas properties. No amortization is charged during the exploration and evaluation phase.

2. Significant accounting policies (continued)

Oil and natural gas development expenditure (continued)

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, the drilling and equipment of development wells, including unsuccessful development or delineation wells, is capitalized within oil and gas properties. Oil and gas properties are stated at cost less accumulated depreciation and accumulated impairment losses.

Advance payments

Advance payments are recognized and carried at the original amount of payment less provision for any amount at risk of non-performance by the counterparty. Advance payments made for non-current assets as well as payments which will be settled during more than one-year period are non-current advance payments.

Borrowing costs

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

Impairment of oil and gas properties, construction in progress, development costs and other non-financial assets

The Group assesses at each statement of financial position date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash generating unit's ("CGU") fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

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

Inventories

Inventories are stated at the lower of cost and net realizable value. Cost of producing crude oil is accounted on weighted average basis. This cost includes all costs incurred in the normal course of business in bringing each product to its present location and condition. The cost of crude oil is the production cost, the appropriate proportion of depletion and depreciation charges and overheads. Net realizable value of crude oil is based on estimated selling price in the ordinary course of business less any costs expected to be incurred to completion and disposal.

2. Significant accounting policies (continued)

Decommissioning liabilities

Under the provisions of the SD PSA, the Contractor Parties to the SD PSA are obligated to finance the ultimate abandonment of oil and gas production properties employed in petroleum operations within the contract area. The maximum amounts of abandonment funds cannot exceed 10% of the capital costs in accordance with the SD PSA. The Group estimates its share of total decommissioning liabilities based on SD PSA provisions by applying the 10% limit to all capital costs incurred in petroleum operations in the contract area as at the year-end. The present value of the decommissioning liabilities is recorded by the Group as a liability at the time the assets are installed or placed in service. The amount of liability equals the present value of the future decommissioning liabilities discounted at pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability rate, which equals 5.95% at 31 December 2015 (31 December 2014: 5.77%). A corresponding tangible fixed asset of an amount equivalent to the liability is also created and included in the cost of oil and gas production properties. This amount is subsequently depreciated as part of the oil and gas production properties and charged against income using the unit-of-production method based on proved reserves. Changes in the estimated timing of decommissioning or decommissioning cost estimates are dealt with prospectively by recording an adjustment to the provision, and a corresponding adjustment to oil and gas production properties. The unwinding of the discount on the decommissioning provision is included as a finance cost.

According to the Host Government Agreement ("HGA") signed with the Georgian and Azerbaijan Governments, no later than 30 days after the termination of the HGA, SCPC must submit a decommissioning plan to these Governments addressing its obligations to retire the pipeline. The amount of asset retirement obligation is capitalized by shareholders of SCPC.

In accordance with HGA signed with the Government of Turkey, the Group shall comply with all its decommissioning obligations following the expiry of HGA (2061). The Group started construction works in March 2015. At the date of the consolidated financial statements, the Group had not performed works related to backfilling activities, placement of compressors and SCADAs, which would require decommissioning works.

Government grants

Government grants are recognized when there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant related to an asset, it is recognized as income in equal amounts over the expected useful life of the related asset.

The benefit of a governmental bond at a below market rate of interest is treated as a government grant. Such benefit is measured as the difference between the initial fair value of the issued bond and the proceeds received.

Income taxes

Income taxes have been provided for in the preliminary consolidated financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in profit or loss for the year unless it relates to transactions that are recognised, in the same or a different period, in other comprehensive income or directly in equity.

The Group is liable for financing of its 6.67% share in the tax liabilities of SCPC, namely Azerbaijani income tax, Georgian income tax and Georgian minimum tax liabilities.

According to the provisions of SD PSA, contractor parties are liable for profit taxes. However, according to the SD PSA, respective government entity of the Republic of Azerbaijan is liable for payment of profit taxes of each contractor party from the proceeds from sales of crude oil and natural gas. Accordingly, the Group recognizes profit taxes and related revenue in the consolidated statement of profit and loss.

2. Significant accounting policies (continued)

Income taxes (continued)

In accordance with HGA signed with the Government of Turkey and the Government of Azerbaijan, the Group will be subject to income tax in respect of TANAP project after the pipeline will be put in use. Accordingly, the Group is not subject to income tax during the construction phase.

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

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income taxes are provided in full on temporary differences arising on recognition and subsequent measurement of provision for asset retirement obligation and related adjustments to cost of property, plant and equipment.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision maker. Segments whose revenue, result or assets are ten percent or more of all the segments are reported separately.

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, or receivable, taking into account contractually defined terms of payment net of discounts, returns, value added taxes and other taxes or duty.

Revenues associated with sales of crude oil (condensate) and gas are recorded at the point when the significant risks and rewards of ownership are transferred, which is when title to the extracted oil and gas passes to the customer based on the terms of the SD PSA and based on the proportion of its share in total crude oil and gas entitlement. The actual volume of oil received by the Group may differ from the entitled volume resulting in an over/under lifting. Underlift is recognized as a sale of crude oil at the point of lifting by the underlifter to the overlifter. Overlift is recognized as a purchase of oil by the overlifter from the underlifter. The extent of underlift is reflected by the Group as an asset in the statement of financial position, and the extent of overlift is reflected as a liability. The initial measurement of the overlift liability or underlift asset is at the market price of crude oil at the date of lifting. Subsequent measurement of overlift/underlift liabilities and assets depends on the settlement terms of the related operating agreements. If such terms allow for a cash settlement of the overlift/underlift balances between the parties, the balances are remeasured at fair value at reporting dates subsequent to initial recognition. The overlift/underlift balances that are settled through delivery of physical quantities of crude oil are measured at the lower of carrying amount and fair value at reporting dates subsequent to initial recognition.

2. Significant accounting policies (continued)

Revenue recognition (continued)

BP Exploration Shah Deniz Limited, the Operator of the SD PSA (the “SD Operator”), provides the Contractor Parties of SD PSA on a quarterly basis with the Shah Deniz Petroleum Entitlement Report, that contains, inter alia, the final net back price figure which is applied when determining the final petroleum volume that each SD PSA party is entitled to receive. When the actual Shah Deniz Petroleum Entitlement Report is not available, the Group recognizes the revenue based on a provisional Shah Deniz Petroleum Entitlement Report issued by the SD Operator. The revenue recognized may be further revised in the event that actual net back price differs from the provisional net back price used for revenue calculation. The Group treats such revision of revenue, if any, as a change in estimate and reflects in the current year statement of comprehensive income.

Employee benefits

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

Transactions with related parties

For the purposes of these consolidated financial statements, 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. It is the nature of transactions with related parties that they cannot be presumed to be carried out on an arm’s length basis.

Contingencies

Contingent liabilities are not recognized in the consolidated financial statements unless it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made. A contingent asset is not recognized in the consolidated financial statements but disclosed when an inflow of economic benefits is probable.

New and amended standards and interpretations

The Group applied for the first time certain standards and amendments, which are effective for annual periods beginning on or after 1 January 2015. Although these new standards and amendments applied for the first time in 2015, they did not have a material impact on the consolidated financial statements of the Group.

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 effective for annual periods beginning on or after 1 July 2014. This amendment is not relevant to the Group, since none of the subsidiaries within the Group has defined benefit plans with contributions from employees or third parties.

2. Significant accounting policies (continued)

New and amended standards and interpretations (continued)

Annual improvements 2010-2012 cycle

These improvements are effective for accounting periods beginning on or after 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies that all contingent consideration arrangements classified as liabilities (or assets) arising from a business combination should be subsequently measured at fair value through profit or loss whether or not they fall within the scope of IFRS 9 (or IAS 39, as applicable). This is consistent with the Group's current accounting policy, and thus this amendment does not impact the Group's accounting policy.

IFRS 8 Operating Segments

The amendments are applied retrospectively and clarify that:

- an entity must disclose the judgements made by management in applying the aggregation criteria in paragraph 12 of IFRS 8, including a brief description of operating segments that have been aggregated and the economic characteristics (e.g., sales and gross margins) used to assess whether the segments are 'similar';
- the reconciliation of segment assets to total assets is only required to be disclosed if the reconciliation is reported to the chief operating decision maker, similar to the required disclosure for segment liabilities.

The Group has not applied the aggregation criteria in IFRS 8.12.

IFRS 13 Fair Value Measurement

The amendment 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 Group's current accounting policy, and thus this amendment does not impact the Group's accounting policy.

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 by either adjusting the gross carrying amount of the asset to market value or by determining the market value of the carrying value and adjusting the gross carrying amount proportionately so that the resulting carrying amount equals the market value. In addition, the accumulated depreciation or amortization is the difference between the gross and carrying amounts of the asset. The Group 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. The Group has applied these amendments for the first time in these consolidated financial statements.

2. Significant accounting policies (continued)

New and amended standards and interpretations (continued)

Annual improvements 2011-2013 cycle

These improvements are effective for accounting periods beginning on or after 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies for the scope exceptions within IFRS 3 that:

- joint arrangements, not just joint ventures, are outside the scope of IFRS 3;
- this scope exception applies only to the accounting in the financial statements of the joint arrangement itself.

The Group does not have investment in a joint arrangement, and thus this amendment is not relevant for the Group.

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 Group does not apply the portfolio exception in IFRS 13.

3. Significant accounting judgments, estimates and assumptions

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

On an on-going basis, management evaluates their estimates, including those related to revenue recognition and contingencies. Management bases their estimates on various market-specific assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making assumptions about the carrying values of assets that are not readily apparent from other sources. Actual results may differ significantly from these estimates using different assumptions or conditions.

The key assumptions concerning the future and other key sources of estimation uncertainty at the date of consolidated financial statements that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Reserve estimates

Estimates of recoverable quantities of proven and probable reserves reported include judgmental assumptions regarding commodity prices, exchange rates, discount rates and production and transportation costs for future cash flows. It also requires interpretation of complex geological and geophysical models in order to make an assessment of the size, shape, depth and quantity of reservoirs, and their anticipated recoveries. The economic, geological and technical factors used to estimate reserves may change from period to period; changes in reported reserves can impact provision of decommissioning liabilities due to changes in expected future cash flows. Reserves are integral to the amount of depreciation, depletion and amortization charges to the consolidated statement of comprehensive income.

3. Significant accounting judgments, estimates and assumptions (continued)

Reserve estimates (continued)

Natural gas and condensate reserves depend on price fluctuations as a result of change in production entitlement split between the State and contractor parties. Natural gas prices are calculated based on the long-term sales contracts provisions and depend on crude oil prices and other inputs. The current long-term Brent FOB oil price assumption used in the estimation of reserves is seventy two dollars thirty four cents per barrel (US dollars 72.34) as at the consolidated statement of financial position date.

The level of estimated commercial reserves is also a key determinant in assessing whether the carrying value of any of the Group's development and production assets has been impaired.

Decommissioning liabilities

As discussed in Note 2, under the terms of the SD PSA the Group will have to make contributions to the abandonment fund when seventy percent (70%) of petroleum reserves of the Shah Deniz field are recovered. Decommissioning liabilities are stated in the amount of expected contributions related to the currently employed assets discounted at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. This valuation requires the Group to make estimates about timing of expected future cash flows and adjustment to the discount rate, and hence they are subject to uncertainty. The estimation of the decommissioning liabilities is based on the assumption that contributions to the abandonment fund will start in 2029. Further details are disclosed in Note 17.

If the estimated discount rate used in the calculation had been 1% higher/lower than management's estimate, the carrying amount of the provision would have been US dollar 7,266 lower / US dollars 8,584 higher, respectively.

Deferred and accrued revenue

In the valuation of the Group's over-lift and under-lift position under the Shah Deniz PSA as at the year-end the Group uses thirty five dollars seventy four cents per barrel (US dollars 35.74) market price for crude oil as at 31 December 2015.

Recoverability of oil and gas assets

The Group assesses each asset or CGU every reporting period to determine whether any indication of impairment exists. Where an indicator of impairment exists, a formal estimate of the recoverable amount is made, which is considered to be the higher of the fair value less costs to sell and value in use. These assessments require the use of estimates and assumptions such as long-term oil prices, discount rates, operating costs, future capital requirements, decommissioning costs, exploration potential, reserves and operating performance (which includes production and sales volumes). These estimates and assumptions are subject to risk and uncertainty. Therefore, there is a possibility that changes in circumstances will impact these projections, which may impact the recoverable amount of assets and/or CGUs.

Given the nature of the Group's activities, information on the fair value of an asset or CGU is not practicable to identify. Consequently, the recoverable amount used in performing the impairment test described below is value-in-use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. The Group generally estimates value-in-use using a discounted cash flow model from financial budgets approved by management.

3. Significant accounting judgments, estimates and assumptions (continued)

Recoverability of oil and gas assets (continued)

Key assumptions used in value-in-use calculations

The calculation of value-in-use for oil fields is most sensitive to the following assumptions:

Identification of CGU

CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets of group of assets. The management assesses that SCP, TANAP and TAP projects are being constructed with the ultimate goal of the delivering Shah Deniz field natural gas to the Georgian, Turkish and European markets. Therefore, all these projects have been considered as one CGU and impairment test is performed on the level of the whole Group.

Capital expenditures

Capital expenditures necessary to maintain estimated production volumes are based on long-term development plans for particular field.

Commitments under DSPA

As disclosed in Note 25, the Group is committed to make progress payments under the terms of the DSPA. The parties to the DSPA have intention to revise progress payments which will result in decrease of cash outflows by the Group. The Group expects that the respective amendment to DSPA will be signed in 2016. Accordingly the Group used revised progress payments in calculation of undiscounted cash flows.

Crude oil price

Commodity prices used in the forecasts are publicly available.

If the forecasted prices used in the calculation had been five dollars (US dollars 5.0) lower than management's estimate, this would not result with any impairment loss.

Discount rate

The post-tax discount rate applied to the cash flow projections of CGU was 6%. The discount rate calculation is based on the specific circumstances of the Group and derived from its incremental borrowing rate adjusted to the specific risks associated with the asset's estimated cash flows. If the estimated discount rate used in the calculation had been 1% higher than management's estimate, this would not result in impairment loss.

Contingencies

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events.

4. New standards and amendments issued, but not yet effective

Standards issued, but not yet effective up to the date of issuance of the Group's consolidated financial statements are listed below. This listing of standards and interpretations issued are those that the Group reasonably expects to have an impact on disclosures, financial position or performance when applied at a future date. The Group intends to adopt these standards when they become effective.

4. New standards and amendments issued, but not yet effective (continued)

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. Except for hedge accounting, retrospective application is required, but comparative information is not compulsory. The Group plans to adopt the new standard on the required effective date. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets, but no impact on the classification and measurement of the Group's financial liabilities.

The Group's loan receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. The Group expects that these will continue to be measured at amortised cost under IFRS 9. However, the Group will analyse the contractual cash flow characteristics of those instruments in more detail before concluding whether all those instruments meet the criteria for amortised cost measurement under IFRS 9.

Amendments to IFRS 10 and IAS 28: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address the conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture, is recognised in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture. These amendments must be applied prospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value.

Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries. These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests

The amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business, must apply the relevant IFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained. In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.

The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are prospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

4. New standards and amendments issued, but not yet effective (continued)

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. Under IFRS 15 revenue is recognized 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 recognizing 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 2017 with early adoption permitted. The Group is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

Amendments to IAS 1 Disclosure Initiative

The amendments to IAS 1 *Presentation of Financial Statements* clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- the materiality requirements in IAS 1;
- that specific line items in the statement(s) of profit or loss and OCI and the statement of financial position may be disaggregated;
- that entities have flexibility as to the order in which they present the notes to financial statements;
- that the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and OCI. These amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

IAS 7 (Statement of Cash Flows): amendments resulting from the disclosure initiative

The amendments aim at clarifying IAS 7 to improve information provided to users of financial statements about an entity's financing activities. The Group has not yet considered any changes or amendments to be made to the financial reports (effective for annual periods beginning on or after 1 January 2017).

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 Group given that the Group has not used a revenue-based method to depreciate its non-current assets.

IFRS 16 Leases

IFRS 16 specifies how an IFRS reporter will recognise, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17 (effective for annual reporting periods beginning on or after 1 January 2019). These amendments are not expected to have any impact on the Group.

4. New standards and amendments issued, but not yet effective (continued)

Annual improvements 2012-2014 cycle

In the 2012-2014 annual improvements cycle, the IASB issued five amendments to four standards, summaries of which are provided below. The changes are effective from 1 January 2016. The Group did not early adopt any of the amendments.

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

Assets (or disposal groups) are generally disposed of either through sale or distribution to owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. The amendment must be applied prospectively.

IFRS 7 Financial Instruments: Disclosures

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 the arrangement against the guidance for continuing involvement in IFRS 7.B30 and IFRS 7.42C in order to assess whether the disclosures are required.

The assessment of which servicing contracts constitute continuing involvement must 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.

The amendment clarifies that the offsetting disclosure requirements do not apply to condensed interim financial statements, unless such disclosures provide a significant update to the information reported in the most recent annual report. The amendment must be applied retrospectively.

The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

IAS 19 Employee Benefits

The amendment clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. This amendment must be applied prospectively. These amendments are not expected to have any impact on the Group.

IAS 34 Interim Financial Reporting

The amendment clarifies 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 interim financial report (e.g., in the management commentary or risk report). 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. This amendment must be applied retrospectively. These amendments are not expected to have any impact on the Group.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

5. Segment information

Operating segments are components that engage in business activities that may earn revenues or incur expenses, whose operating results are regularly reviewed by the management of the Group and for which discrete financial information is available.

The Group is organised into business units based on their products and services and has two reportable segments as follows:

oil and gas – representing extraction of natural gas and gas condensate;

distribution – representing transportation of natural gas and gas condensate.

No operating segments have been aggregated to form the above reportable operating segments.

The Group's segments are strategic business units that focus on different customers. Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Transfer prices between operating segments are either on an arm's length basis or non-arm's length basis.

Information about reportable segment profit or loss, assets and liabilities

Segment information for the reportable segments for the year ended 31 December 2015 is set out below:

	Oil and gas	Distribution	Unallocated (*)	Eliminations (**)	Total
Revenues					
External customers	151,473	–	–	–	**151,473**
Inter-segment	–	20,046	–	(20,046)	**–**
Total revenue	**151,473**	**20,046**	**–**	**(20,046)**	**151,473**
Depreciation and depletion	(50,446)	(3,412)	–	–	**(53,858)**
Other costs	(12,932)	(3,968)	–	814	**(16,086)**
Transportation tariffs	(23,845)	–	–	19,232	**(4,613)**
General and administrative expenses	(7,976)	(2,796)	(1,738)	–	**(12,510)**
Other operating income	1,758	14	14,418	–	**16,190**
Interest income	–	2,241	38,577	(35,923)	**4,895**
Finance costs	(24,292)	(9,700)	(53,981)	31,863	**(56,110)**
Share of result of associates	–	(5,856)	–	–	**(5,856)**
Foreign exchange loss, net	(79)	(6,961)	(3,568)	10,523	**(85)**
Income tax expense	–	(3,781)	–	–	**(3,781)**
Net profit/(loss) for the year	**33,661**	**(14,173)**	**(6,292)**	**6,463**	**19,659**

(*) These numbers include unallocated transactions managed and recognized at the group level.

(**) Inter-segment revenues and expenses are eliminated on consolidation. Amounts shown as eliminations include intercompany transactions.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

5. Segment information (continued)

Information about reportable segment profit or loss, assets and liabilities (continued)

	Oil and gas	Distribution	Unallocated (*)	Eliminations (**)	Total
Investment in associates	–	60,740	–	–	**60,740**
Other reportable segment assets	2,241,496	2,584,868	3,537,638	(3,209,343)	**5,154,659**
Total reportable segment assets	**2,241,496**	**2,645,608**	**3,537,638**	**(3,209,343)**	**5,215,399**
Other reportable segment liabilities	(2,169,421)	(1,852,488)	(2,638,603)	3,193,019	**(3,467,493)**
Total reportable segment liabilities	**(2,169,421)**	**(1,852,488)**	**(2,638,603)**	**3,193,019**	**(3,467,493)**
Capital expenditure (***)					
Additions	352,157	1,255,842	64	–	**1,608,063**
Advance payments for acquisition of shares	432,610	115,984	–	–	**548,594**
Advance payments related to construction works	8,021	136,742	–	–	**144,763**
Total capital expenditures	**792,788**	**1,508,568**	**64**	**–**	**2,301,420**

(*) These numbers include unallocated assets and liabilities managed and recognized at the group level.

(**) Inter-segment balances are eliminated on consolidation. Amounts shown as eliminations include intercompany balances.

(***) Capital expenditure represents additions to non-current assets other than financial instruments and deferred tax assets.

Segment information for the reportable segments from 31 March 2014 (inception) to 31 December 2014 is set out below:

	Oil and gas	Distribution	Unallocated (*)	Eliminations (**)	Total
Revenues					
External customers	76,894	–	–	–	**76,894**
Inter-segment	–	9,561	–	(9,561)	**–**
Total revenue	**76,894**	**9,561**	**–**	**(9,561)**	**76,894**
Depreciation and depletion	(19,731)	(1,402)	–	–	**(21,133)**
Other costs	(5,501)	(2,464)	–	665	**(7,300)**
Transportation tariffs	(10,488)	(2)	–	8,896	**(1,594)**
General and administrative expenses	(766)	(391)	(332)	–	**(1,489)**
Other operating income	6,551	–	6,571	–	**13,122**
Interest income	25	2,184	21,342	(20,213)	**3,338**
Finance costs	(10,193)	(3,566)	(41,581)	12,625	**(42,715)**
Share of result of associates	–	(2,749)	–	–	**(2,749)**
Foreign exchange loss, net	–	–	(1,955)	–	**(1,955)**
Income tax expense	–	(1,211)	–	–	**(1,211)**
Net profit/(loss) for the period	**36,791**	**(40)**	**(15,955)**	**(7,588)**	**13,208**

(*) These numbers include unallocated transactions managed and recognized at the group level.

(**) Inter-segment revenues and expenses are eliminated on consolidation. Amounts shown as eliminations include intercompany transactions.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

5. Segment information (continued)

Information about reportable segment profit or loss, assets and liabilities (continued)

	Oil and gas	Distribution	Unallocated (*)	Eliminations (**)	Total
Investment in associates	–	56,432	–	–	**56,432**
Other reportable segment assets	1,553,889	1,256,612	2,025,999	(1,999,428)	**2,837,072**
Total reportable segment assets	**1,553,889**	**1,313,044**	**2,025,999**	**(1,999,428)**	**2,893,504**
Other reportable segment liabilities	(1,516,041)	(711,259)	(2,552,348)	1,988,248	**(2,791,400)**
Total reportable segment liabilities	**(1,516,041)**	**(711,259)**	**(2,552,348)**	**1,988,248**	**(2,791,400)**
Capital expenditure (***)					
Additions	125,323	148,595	60	–	**273,978**
Acquisitions of shares in projects	911,710	335,966	–	–	**1,247,676**
Advance payments for acquisition of shares	454,662	341,626	–	–	**796,288**
Advance payments related to construction works	–	146,846	–	–	**146,846**
Total capital expenditures	**1,491,695**	**973,033**	**60**	**–**	**2,464,788**

(*) These numbers include unallocated assets and liabilities managed and recognized at the group level.

(**) Inter-segment balances are eliminated on consolidation. Amounts shown as eliminations include intercompany balances.

(***) Capital expenditure represents additions to non-current assets other than financial instruments and deferred tax assets.

Geographical information

All revenue is generated from sales of natural gas and gas condensate produced in Azerbaijan.

Non-current assets other than financial instruments and deferred tax assets for each individual country for which it is material is reported separately as follows:

	2015	2014
Azerbaijan	2,594,078	1,704,621
Turkey	1,756,526	468,918
Georgia	342,616	272,451
Switzerland	60,740	56,432
Total	**4,753,960**	**2,502,422**

The analysis is based on location of assets.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

6. Oil and gas properties

Movements in the carrying amount of oil and gas properties consisted of the following:

	Oil and gas production properties	Pipeline assets	Decommis-sioning costs	Total
Cost				
At 31 March 2014	–	–	–	–
Acquisition of undivided interest in joint projects	430,079	74,207	14,273	**518,559**
Additions	12,619	266	2,093	**14,978**
At 31 December 2014	**442,698**	**74,473**	**16,366**	**533,537**
Additions	29,858	845	1,084	**31,787**
At 31 December 2015	**472,556**	**75,318**	**17,450**	**565,324**
Accumulated depletion and depreciation				
At 31 March 2014	–	–	–	–
Charge for the period	(19,182)	(1,402)	(549)	**(21,133)**
At 31 December 2014	**(19,182)**	**(1,402)**	**(549)**	**(21,133)**
Charge for the year	(49,226)	(3,398)	(1,234)	**(53,858)**
At 31 December 2015	**(68,408)**	**(4,800)**	**(1,783)**	**(74,991)**
Net book value				
At 31 December 2015	**404,148**	**70,518**	**15,667**	**490,333**
At 31 December 2014	**423,516**	**73,071**	**15,817**	**512,404**

Oil and gas production properties

Oil and gas production properties are represented by the Group's 6.67% share in oil and gas production properties of Shah Deniz ("SD") project.

Pipeline assets

The pipeline cost represents the Group's 6.67% share in cost of construction and capitalized maintenance expenses on SCP pipeline.

Decommissioning costs

The capitalized decommissioning costs are represented by the Group's 6.67% share in costs related to decommissioning of assets employed for the purposes of SD and SCP projects. Refer to Note 17 for details.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

7. Construction in progress and development costs

Movements in the carrying amount of oil and gas properties consisted of the following:

	Development costs	Construction in progress	Decommis-sioning costs	Total
At 31 March 2014	**–**	**–**	**–**	**–**
Acquisition of undivided interest in joint projects	449,630	54,534	18,125	**522,289**
Acquisition of subsidiary	–	206,828	–	**206,828**
Additions	108,223	148,205	2,572	**259,000**
At 31 December 2014	**557,853**	**409,567**	**20,697**	**988,117**
Additions	309,783	1,254,682	11,811	**1,576,276**
At 31 December 2015	**867,636**	**1,664,249**	**32,508**	**2,564,393**
Net book value				
At 31 December 2015	**867,636**	**1,664,249**	**32,508**	**2,564,393**
At 31 December 2014	**557,853**	**409,567**	**20,697**	**988,117**

Development costs

Development costs are represented by costs incurred in respect of Shah Deniz Stage 2 Development project.

Construction in progress

As at 31 December 2015 this amount includes cost directly related to the construction of TANAP and expansion of SCP pipeline system in the amount of US dollars 1,501,908 (31 December 2014: US dollars 322,080) and US dollars 162,341 (31 December 2014: US dollars 87,487), respectively. The amount related to construction of TANAP includes costs for project management services, early work expenses, land acquisition costs, personnel expenses and other costs directly attributable to the construction of pipeline.

Capitalized borrowing cost

As at 31 December 2015 the Group capitalized borrowing cost in the amount of US dollars 54,003 as part of construction in progress and development costs (2014: nil). Refer to Note 16 for further details.

8. Advance payments

Advance payments consisted of the following at 31 December:

	2015	2014
Advance payments for acquisition of shares	1,344,882	796,288
Other payments related to construction works	291,609	146,846
	1,636,491	**943,134**

Advance payments for acquisition of shares

Advance payments for acquisition of shares represents advances paid in the amount of US dollars 887 million (31 December 2014: US dollars 454 million) to AzSD and US dollars 458 million (31 December 2014: US dollars 342 million) to AzSCP for acquisition of their 10% interests in the SD PSA and SCP projects, respectively, and treated as non-financial assets. Refer to Note 25 for further details.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

9. Investments in associate

At 31 December 2015 the Group held twenty percent (20%) interest in TAP AG. TAP AG is responsible for the development and operation of the gas transportation infrastructure from the Greece/Turkey border to Southern Italy in order to deliver Shah Deniz natural gas to European countries. The Group exercises significant influence over the entity by participating in its financial and operating decisions.

The Group acquired investment in TAP AG through acquisition of 100% shares of AzTAP GmbH in 2014 (Note 23).

The table below summarizes the movements in the carrying amount of the Group's investment in TAP AG:

	2015	2014
Opening carrying amount	**56,432**	**–**
Acquisition of investment in associate	–	56,671
Additions to investment in associate	17,500	8,260
Share of after tax results of associate	(5,856)	(2,749)
Other	(1,335)	–
Exchange differences	(6,001)	(5,750)
Closing carrying amount	**60,740**	**56,432**

The following table illustrates summarized financial information of the Group's investment in TAP AG at 31 December:

	2015	2014
Current assets	160,736	49,600
Non-current assets	604,796	390,633
Current liabilities	(109,262)	(23,033)
Non-current liabilities	(434,211)	(221,665)
Net assets	**222,059**	**195,535**
Group's interest in net assets	**44,412**	**39,107**
Goodwill recognized upon acquisition	18,872	18,872
Exchange differences on translation of goodwill	(1,209)	(1,547)
Other	(1,335)	–
Carrying value	**60,740**	**56,432**

Share of associate's results for the period ended 31 December:

	2015	2014
Revenue	–	–
Operating expenses	36,391	16,100
Other income	(592)	(829)
Loss before tax	**35,799**	**15,271**
Income tax benefit	(6,517)	(1,526)
Net loss for the period since acquisition of associate	**29,282**	**13,745**
Group's share of net loss	**5,856**	**2,749**

(Amounts presented are in thousands of US dollars, unless otherwise stated)

10. Loan receivables

Loan receivables consisted of receivable from TAP AG in the amount of US dollars 84,977 (31 December 2014: US dollars 44,334) and receivables from BOTAS in the amount of US dollars 52,520. The loan to TAP bears interest at the rate of EUR rate for cross border shareholders loans as published by the Swiss federal tax authorities plus 1% margin and was equal to 2% in 2015 (2014: 3%). The loan matures in July 2043. Interest income earned during the year ended 31 December 2015 was US dollars 1,335 (31 December 2014: US dollars 580).

Receivables from BOTAS represent deferred consideration in the amount of US dollars 28,987 and loan receivable in the amount of US dollars 23,533. As discussed in Note 1, in accordance with the sale and purchase agreement, on 13 April 2015 the Group sold its 30% shares in TANAP A.Ş. to BOTAS for cash consideration of US dollars 168,226 and deferred consideration of US dollars 33,645. The deferred consideration does not bear interest and is expected to be repaid during 2020-2021. At initial recognition fair value of the deferred consideration was calculated as the present value using the market borrowing rate for similar financial instruments (3.5%) in the amount of US dollars 28,006. Income earned in respect of the deferred consideration from BOTAS during the year ended 31 December 2015 was US dollars 981 and was recognized within interest income.

As discussed in Note 25, according to the Funding Agreement, following the sale of 30% shares of TANAP A.Ş., the Group financed cash call requirements of BOTAS equivalent to 5% shares in TANAP A.Ş. in the amount of US dollars 27,950. The loan does not bear interest and is expected to be repaid in 2021. At initial recognition, the present value was calculated using the market borrowing rate for similar financial instruments (3.5%) in the amount of US dollars 22,737 and the difference between the fair value and carrying amount of loan in the amount of US dollars 5,213 was recognized in profit and loss. Interest income earned in respect of the loan receivable from BOTAS during the year ended 31 December 2015 was US dollars 796 (2014: nil).

11. Cash and cash equivalents, deposits

Cash and cash equivalents consisted of the following at 31 December:

	2015	**2014**
Cash at bank, USD	254,228	202,472
Cash at bank, EUR	332	9,726
Total cash and cash equivalents	**254,560**	**212,198**

Cash at bank includes time deposits in the amount of US dollars 535 (31 December 2014: US dollars 194,832) with maturity of up to one month and bearing effective interest rate of 1.95% (31 December 2014: 1.6-2.5%).

Deposits

During 2015, the Group placed time deposit in the amount of US dollars 350 million with the maturity period of one year. The whole balance of deposit was fully utilized as at 31 December 2015.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

12. Accounts receivable

Accounts receivable consisted of the following at 31 December:

	2015	2014
Receivable from AzSD	–	21,554
Receivable from AGSC	9,760	5,178
Receivable from the SD Operator	4,401	5,127
Receivable from SOCAR MO	3,606	–
Other receivables	1,237	4,961
Total accounts receivable	**19,004**	**36,820**

Receivables from the SD Operator represent the inception-to-date excess of cash calls paid by the Group to the SD Operator over the actual expenditures reported by the SD Operator.

According to the crude oil sales agency agreement, the Group appointed SOCAR MO, a subsidiary of SOCAR, as its trading and marketing agent in respect of Shah Deniz PSA petroleum. SOCAR MO charges the Group commission fees for agency and marketing services at 0.5% (value added tax ("VAT") inclusive) of the value of crude oil sold. Receivables from SOCAR MO represent a petroleum sold to a third party, for which no consideration was transferred to the Group as at 31 December 2015.

13. Inventories

As at 31 December 2015 and 2014 inventories are represented by the Group's share of inventories reported by the SD Operator.

14. Other current assets

Other current assets represent the following at 31 December:

	2015	2014
VAT receivable	31,637	25,966
Other assets	6,287	12,248
Total other current assets	**37,924**	**38,214**

15. Share capital and other reserves

Share capital

During the year ended 31 December 2015 the Group received additional contribution in share capital in the amount of US dollars 1,344,900. As at 31 December 2015 and 2014 the Company had authorized, issued and fully paid 100 ordinary shares at par USD 14,449 and USD 1,000, respectively. Each share entitles one vote to the shareholder.

Other reserves

As discussed in Note 1, on 13 April 2015 the Group sold its 30% shares in TANAP A.Ş. to BOTAS. Total consideration comprised of cash consideration paid by BOTAS in the amount of US dollars 168,226 and fair value of deferred consideration in the amount of US dollars 28,006 (Note 10). In addition, on 16 April 2015 the Group sold its 12% shares in TANAP A.Ş. to BP for cash consideration of US dollars 97,423. The difference between the net book value of shares sold (US dollars 338,831) and the fair value of considerations received from BOTAS and BP was recognized as loss on sale of share in subsidiary in other reserves in the amount of US dollars 45,176.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

16. Long-term borrowings and Government grant

Bonds issued to SOFAZ

In accordance with the Presidential Decree dated 25 February 2014 SOFAZ, a governmental fund established for funding of important socio-economic projects, was assigned to finance the Group's acquisitions of interests in the projects described in Note 1. Following this Decree, in 2014 the Group issued bonds to SOFAZ in the aggregate amount of US dollars 2,516,996 with maturity period of 10 years. Interest rate implicit in bond prospectus is 1% + 6 months LIBOR. The repayment of interest shall be made in semiannual installments effective from 2021 till 2024.

At initial recognition, the Group calculated the fair value of the bond using market rate for similar financial instruments (4.5% + 6 months LIBOR) and recognized US dollars 704,270 of difference between fair value and nominal amount of the bond as government grant in its consolidated statements of financial position.

Total interest accrued during the year ended 31 December 2015 was US dollars 99,641 (31 December 2014: US dollars 42,715). The Group capitalized US dollar 50,852 of borrowing cost as part of construction in progress and development costs during the year ended 31 December 2015 (2014: nil).

During the year ended 31 December 2015 the Group recognized income from government grant in the amount of US dollars 14,418 which was recognized within other income (31 December 2014: US dollars 6,571).

Loan from BOTAS and BP

In accordance with Term Loan Facility Agreement signed in 2015, shareholders of TANAP A.Ş undertake to make available a loan facility for financing of their shares of the capital expenditures relating to the TANAP project. During the year ended 31 December 2015, total amount of loans from BOTAS and BP were US dollars 167,700 and US dollars 67,080, respectively. The loans bear interest at the rate of 5.5% + 1 month LIBOR. Total interest charges incurred during the year ended 31 December 2015 amounted US dollars 3,151 which were capitalized as part of cost of asset.

17. Decommissioning liabilities

The Group has a legal and constructive obligation with respect to decommissioning of oil and gas production and pipeline assets. Movements in provisions for the related asset retirement obligations are as follows:

	31 December 2015	31 December 2014
Opening carrying amount	**37,063**	**–**
Acquisition of undivided interest in joint projects	–	32,398
Additional liability during the period	14,336	4,665
Unwinding of present value discount	2,108	–
Effect of discount rate revision	(1,441)	–
Closing carrying amount	**52,066**	**37,063**

Under the provisions of the SD PSA and SCP Host Government Agreements ("HGA") all Contractor Parties will have to make contributions to an abandonment fund, which will be used to finance the decommissioning and dismantling of constructed assets after the maturity of the SD PSA and SCP.

The maximum amount of decommissioning fund cannot exceed 10% of the capital costs in accordance with SD PSA. Decommissioning liability is estimated based on capital expenditures incurred in respect of assets already employed as at the end of each financial year. The Group share of the estimated undiscounted cost to abandon the production facilities employed in SD PSA was US dollar 132,759 as at 31 December 2015 (31 December 2014: US dollars 101,619).

(Amounts presented are in thousands of US dollars, unless otherwise stated)

17. Decommissioning liabilities (continued)

The Group's share of expected undiscounted cost to decommission the SCP pipeline facilities at 31 December 2015 was US dollars 10,301 (31 December 2014: US dollars 7,643). The Group used a 2.5% (31 December 2014: 2%) inflation rate in its estimate of the retirement obligation upon termination of HGA and used a pre-tax rate that reflects current market assessments of the time value of money to discount the obligation.

18. Trade and other payables, accrued liabilities

Trade and other payables and accrued liabilities mainly consist of payables related to Shah Deniz Stage 2 development, expansion of SCP and construction of TANAP pipeline systems as at 31 December 2015 and 31 December 2014.

19. Revenue, accrued revenue and deferred revenue

The Group's revenue consisted of the following for the year ended 31 December:

	2015	2014
Revenue from sale of gas	95,847	47,503
Revenue from sale of crude oil	55,626	29,391
	151,473	**76,894**

According to the provisions of the SD PSA the profit oil and gas is shared between the Government and the Contractor Parties depending on cumulative after-tax real rate of return achieved as at the end of each calendar quarter by the Contractor Parties. During 2014 and three quarters of 2015 the profit oil and gas was shared at a ratio of 55% to 45% in favor of the Government. In the fourth quarter of 2015 the split was 55% to 45% in favor of the Contractor Parties.

Accrued revenue

Accrued revenue balance of US dollars 3,119 at 31 December 2015 (31 December 2014: US dollars 13,118) represents the Group's underlift of crude oil resulted from a difference between the volumes lifted and entitled at Ceyhan terminal.

Deferred revenue

Deferred revenue balance of US dollars 5,283 at 31 December 2015 (31 December 2014: US dollars 7,662) represents the Group's overlift of crude oil resulted from a difference between the volumes lifted and entitled at Baku-Tbilisi-Ceyhan route ("BTC").

20. Cost of sales

The Group's cost of sales consisted of the following for the year ended 31 December:

	Note	2015	2014
Depreciation and depletion	6	53,858	21,133
Other costs		16,086	7,300
		69,944	**28,433**

21. Taxation

Taxation under the Shah Deniz Project

According to the provisions of SD PSA, the contractor parties are liable to pay income taxes related to the operations under the SD Project. According to the same provisions the respective state body of the Republic of Azerbaijan remits to the State Budget income taxes of each contractor party and reimburses the respective amount from condensate and natural gas attributable to the State. Accordingly, as a contractor party to SD PSA, the Group is liable for Azerbaijani income taxes and at the same time is entitled to additional profit petroleum. During the year ended 31 December 2015 and 2014 the Group had no income taxes from the activities in SD PSA.

The Group is exempt from certain ordinary operational taxes including Azerbaijani value added taxes in accordance with provision of SD PSA.

Taxation under the SCP project

SGC Midstream LLC elected SCPC to represent it in all tax issues before the tax authorities, so that the Group is a non-tax electing shareholder in accordance with the terms of Azerbaijani HGA. SCPC is liable for Azerbaijani income tax and Georgian minimum tax with respect to the income and deductions of, and natural gas transported by, SCPC, which are allocable to non-tax electing shareholders, including the Group.

The following taxes have been enacted:

Azerbaijani income tax at a fixed rate of 27%;

Georgian income tax at a fixed rate of 25%;

Georgian minimum tax (the “GMT”) at a fixed rate of US dollars 2.50 per thousand of cubic meters of gas delivered to Georgian-Turkey border.

Georgian income tax and minimum tax

According to Georgian HGA, SCPC is liable for the income tax at a fixed rate of 25% for income generated from operations in Georgia. In case SCPC does not generate taxable income during a fiscal year, it shall be liable for GMT. The GMT for the preceding periods can be carried forward without limitation and credited against future income tax liability of SCPC in Georgia. The Group estimates that the GMT will exceed the income tax under Georgian HGA.

The provision for income taxes mainly comprised of the Group’s share in Azerbaijan income tax expense, Georgian minimum tax expense and deferred tax expense of SCPC for the year ended 31 December 2015.

Deferred tax liabilities of SCPC are calculated on the temporary differences arising from the differences in accounting under IFRS and HGA (accrual versus cash basis).

(Amounts presented are in thousands of US dollars, unless otherwise stated)

22. Transactions with related parties

Transactions with related parties consisted of the following:

	As at 31 December 2015				For the year ended 31 December 2015	
Related party	**Long-term borrowings**	**Share capital**	**Advance payments**	**Accounts receivable**	**Receipts from related parties**	**Settlements with related parties**
SOFAZ (Note 16)	1,953,942	–	–	–	–	–
SOCAR	–	708,001	–	–	659,001	–
ME	–	736,899	–	–	685,899	–
AzSD	–	–	887,272	–	21,554	432,611
AzSCP	–	–	457,610	–	–	115,983
SOCAR MO	–	–	–	3,606	–	253
AGSC	–	–	–	9,760	69,851	–
Total	**1,953,942**	**1,444,900**	**1,344,882**	**13,366**	**1,436,305**	**548,847**
Total category	**2,191,873**	**1,444,900**	**1,636,491**	**19,004**		

	As at 31 December 2014				From 31 March 2014 (inception) to 31 December 2014	
Related party	**Long-term borrowings**	**Share capital**	**Advance payments**	**Accounts receivable**	**Receipts from related parties**	**Settlements with related parties**
SOFAZ (Note 16)	1,854,301	–	–	–	–	2,516,996
SOCAR	–	49,000	–	–	49,000	273,258
ME	–	51,000	–	–	51,000	–
AzSD	–	–	454,661	21,554	–	1,318,967
AzSCP	–	–	341,627	–	–	439,277
AGSC	–	–	–	5,178	40,249	–
Total	**1,854,301**	**100,000**	**796,288**	**26,732**	**140,249**	**4,548,498**
Total category	**1,854,301**	**100,000**	**943,134**	**36,820**		

AzSD

Settlements with AzSD (a subsidiary of SOCAR) for the year ended 31 December 2015 are represented by US dollars 432,611 advances paid for acquisition of 10% share in SD PSA and 8% share in AGSC under the DSPA. Settlements with AzSD during the period from 31 March 2014 (inception) to 31 December 2014 are represented by consideration paid for acquisition of 6.67% share in SD PSA and 5.336% share AGSC in the amount of US dollars 851,339, advances paid for acquisition of 10% share in SD PSA and 8% share in AGSC under DSPA in the amount of US dollars 454,661 and other advances. Refer to Note 25.

AzSCP

Settlements with AzSCP (a subsidiary of SOCAR) for the year ended 31 December 2015 are represented by US dollars 115,983 advances paid for acquisition of 10% shares in SCPC under the DSPA. Settlements with AzSCP during the period from 31 March 2014 (inception) to 31 December 2014 are represented by consideration paid for acquisition of 6.67% share in SCPC in the amount of US dollars 97,650 and advances paid for acquisition of 10% shares in SCPC under DSPA in the amount of US dollars 341,627. Refer to Note 25.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

22. Transactions with related parties (continued)

AGSC

AGSC is a company established by the contractor parties of the SD PSA for marketing, accounting, billing, payment and reporting of other administrative activities related to the sales of Shah Deniz gas. Receipts from AGSC represent cash received in the amount of US dollars 69,851 (31 December 2014: US dollars 40,249) from sale of gas to AGSC.

Key management personnel

The senior management group consisted of the Group's General Director, Deputy General Director and three department directors as at 31 December 2015 (31 December 2014: General Director and Finance Director). The aggregate remuneration of members of the senior management group and the number of managers determined on a full-time equivalent basis receiving remuneration within this category was:

	31 December 2015	31 December 2014
Aggregate remuneration	121	63
Number of persons	5	2

The Group also incurred expenses for management services provided by SOCAR Upstream Management International LLC and SOCAR Midstream Operations LLC in the total amount of US dollars 3,193 during the year ended 31 December 2015 under the Operator Services Agreement signed in December 2014.

23. Business combination and acquisition of an entity that is not a business

Acquisition of TANAP

As discussed in the Note 1, in July 2014 the Group acquired 100% shares of TANAP A.Ş. from SOCAR. This transaction was accounted by the Group as acquisition of an entity under the common control and the assets and liabilities of the combining entity were recognized at their carrying amounts under pooling of interest method from the date when the combination took place.

Carrying values of identifiable assets and liabilities of TANAP at acquisition were as follows:

	Carrying value on acquisition
Assets	
Cash and cash equivalents	623
Accounts receivable	301
Other current assets	744
Oil and gas properties, net	206,828
Advance payments	11,604
	220,100
Liabilities	
Trade and other payables	(18,680)
Accrued liabilities	(16,501)
Short-term borrowings	(19,000)
	(54,181)
Total identifiable net assets at carrying value	**165,919**
Distribution to equity	–
Consideration, settled in cash	**165,919**

During 2015 TANAP contributed US dollars 1,465 net profit to the Group (31 December 2014: US dollars 1,412).

(Amounts presented are in thousands of US dollars, unless otherwise stated)

23. Business combination and acquisition of an entity that is not a business (continued)

Acquisition of AzTAP

As discussed in Note 1, in July 2014 the Group acquired 100% shares of AzTAP from SOCAR Energy Holdings AG for the amount US dollars 22 (CHF 20 thousand). AzTAP was established by SOCAR exclusively to exercise the option right to become shareholder of TAP AG. The Group recognized this purchase as acquisition of an entity that is not a business and allocated the cost of acquisition between the individual identifiable assets and liabilities of AzTAP on the basis of their relative fair values.

At the date of obtaining control over AzTAP, allocation of cost of acquisition to the identifiable assets and liabilities of AzTAP was as follows:

	Allocated cost
Cash and cash equivalents	99
Other current assets	65
Loan to associate	48,549
Investments in associates	56,671
Long-term borrowings	(105,362)
Net assets of subsidiary	**22**
Consideration, settled in cash	**22**

24. Financial risk management objectives and policies

Financial risk factors

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

(i) Foreign exchange risk

Foreign exchange risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates. Foreign exchange risk arises primarily from future commercial transactions, recognised assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency. The Group does not have any formal procedures on managing foreign exchange risk, however, management is quite well informed on the tendencies in the economy and has undertaken steps to minimise its foreign exchange risks. Management does not hedge the Group's foreign exchange risk.

The major financial instruments in a foreign currency comprise loan receivable and certain cash and cash equivalents that are denominated in EUR.

The following table demonstrates the sensitivity to a reasonably possible change in EUR of the Group's profit before tax. A negative amount in the table reflects a potential net reduction in the profit before tax, while a positive amount reflects a net potential increase.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

24. Financial risk management objectives and policies (continued)

Financial risk factors (continued)

(i) Foreign exchange risk (continued)

The Group's exposure to change in EUR are the following:

	Change in USD/EUR rate	Effect on profit before tax
2015	12.50%	10,664
	(12.50%)	(10,664)

	Change in USD/EUR rate	Effect on profit before tax
2014	6.23%	3,368
	(6.23%)	(3,368)

(ii) Interest rate risk

The Group holds significant interest bearing assets and liabilities as described in Note 10 and Note 16. Interest rates on existing loan agreements are fixed in respective agreements and depend on fluctuations in LIBOR and EUR rate for cross border shareholders loans published by the Swiss federal tax authorities (ESTV).

The table below summarizes effect on profit before tax of the following shift in LIBOR and EUR rate per ESTV as at 31 December 2015 and 31 December 2014:

	Change in floating variable		Effect on profit before tax	
2015	**Increase**	**Decrease**	**After increase**	**After decrease**
LIBOR	+0.5	-0.12	(9,900)	2,400
EUR rate per ESTV	+0.5	-0.5	297	(297)

	Change in floating variable		Effect on profit before tax	
2014	**Increase**	**Decrease**	**After increase**	**After decrease**
LIBOR	+0.2	-0.2	(1,802)	1,802
EUR rate per ESTV	+0.5	-0.5	192	(192)

(iii) Credit risk

Financial instruments involve, to varying degrees, credit risks. The Group is subject to credit risk from its portfolio of loan receivable, cash and cash equivalents, deposits and accounts receivable and would be exposed to losses in the event of non-performance by counterparties.

The Group's exposure to credit risks arises from default of the counterparty, with a maximum exposure of US dollars 406,660 and 321,471 as at 31 December 2015 and 31 December 2014, respectively.

The Group places its cash with high credit quality financial institutions. The Group trades only with recognized, creditworthy third parties. It is the Group's policy that all customers who wish to trade for condensate on credit terms are subject to credit verification procedures. Gas sales are made through AGSC to entities with strong financial position.

(iv) Liquidity risk

The Group monitors its risk to a shortage of funds by reviewing its net financial debt indicator on a regular basis. The net financial debt represents the difference between total financial liabilities and cash and cash equivalents. The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of loans.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

24. Financial risk management objectives and policies (continued)

Financial risk factors (continued)

The tables below summarize the maturity profile of the Group's financial liabilities at 31 December 2015 and 31 December 2014 based on contractual undiscounted payments:

2015	On demand	3 to 12 months	1 to 5 years	>5 years	Total
Trade and other payables	–	197,025	–	–	**197,025**
Accrued liabilities	–	318,759	–	–	**318,759**
Long-term borrowings	–	–	–	3,225,522	**3,225,522**
	–	**515,784**	**–**	**3,225,522**	**3,741,306**

2014	On demand	3 to 12 months	1 to 5 years	>5 years	Total
Trade and other payables	–	54,896	–	–	**54,896**
Accrued liabilities	–	131,945	–	–	**131,945**
Long-term borrowings	–	–	–	2,860,020	**2,860,020**
	–	**186,841**	**–**	**2,860,020**	**3,046,861**

(v) Capital management

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

The Group considers total capital under management to be as follows:

	31 December 2015	31 December 2014
Long-term borrowings (Note 16)	2,191,873	1,854,301
Less: cash and cash equivalents (Note 11)	(254,560)	(212,198)
Net debt	**1,937,313**	**1,642,103**
Equity	1,407,911	102,104
Capital and net debt	**3,345,224**	**1,744,207**
Gearing ratio	**58%**	**94%**

(vi) Fair value of financial instruments

The fair value of the financial assets and liabilities is included in the amount 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 estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. Management has used all available market information in estimating the fair value of financial instruments.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

24. Financial risk management objectives and policies (continued)

Financial risk factors (continued)

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

	31 December 2015	
	Carrying amounts	Fair values
Cash and cash equivalents (Note 11)	254,560	254,560
Accounts receivables (Note 12)	14,603	14,603
Loan receivables (Note 10)	137,497	137,497
Total financial assets	**406,660**	**406,660**
Trade and other payables (Note 18)	(197,025)	(197,025)
Accrued liabilities (Note 18)	(318,759)	(318,759)
Long-term borrowings (Note 16)	(2,191,873)	(2,197,326)
Total financial liabilities	**(2,707,657)**	**(2,713,110)**

	31 December 2014	
	Carrying amounts	Fair values
Cash and cash equivalents (Note 11)	212,198	212,198
Deposits (Note 11)	33,246	33,246
Accounts receivables (Note 12)	31,693	31,693
Loan receivables (Note 10)	44,334	44,334
Total financial assets	**321,471**	**321,471**
Trade and other payables (Note 18)	(54,896)	(54,896)
Accrued liabilities (Note 18)	(131,945)	(131,945)
Long-term borrowings (Note 16)	(1,854,301)	(1,854,301)
Total financial liabilities	**(2,041,142)**	**(2,041,142)**

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

(i) Current financial assets and liabilities approximate their carrying amounts largely due to the current maturities of these instruments;

(ii) Long-term fixed-rate and variable-rate receivables/borrowings are evaluated by the Group using Level 3 inputs based on parameters such as interest rates, specific country risk factors, individual creditworthiness of customers and the risk characteristics of the financed project.

25. Commitments and contingencies

Commitments related to participating interest in Shah Deniz PSA

On 17 December 2013 Shah Deniz consortium announced the final investment decision for Stage 2 development of Shah Deniz gas field in the Azerbaijan Sector of the Caspian Sea and signed Sixth, Seventh and Eighth Addendums to Shah Deniz PSA. The Group is committed to finance expenditures related to Shah Deniz project based on its share of interest.

(Amounts presented are in thousands of US dollars, unless otherwise stated)

25. Commitments and contingencies (continued)

Commitments related to participating interest in Shah Deniz PSA (continued)

As of 31 December 2015 the Shah Deniz PSA operator has entered into a number of capital commitments and operating leases. The Group estimated its 6.67% share of these capital commitments and operating leases in the amount of US dollars 966,064 and US dollars 21,727, respectively (31 December 2014: US dollars 1,255,780 and US dollars 13,775, respectively). The total of future minimum lease payments under non-cancellable operating leases for each of the following periods is as follows:

Operating leases	31 December 2015	31 December 2014
Not later than one year	6,852	6,848
Later than one year and not later than five years	14,175	6,875
Later than five years	700	52
	21,727	**13,775**

Commitment related to SCP Expansion

Shah Deniz PSA Contractor Parties made the final investment decision on SCP Expansion project on 17 December 2013. SCP Expansion project objective is to expand the existing SCP pipeline system capacity. Due to SCP expansion additional facilities will be constructed in Georgia for the purposes of interconnection with TANAP. The Group has the commitment to fund the SCP Expansion project equivalent to its 6.67% shares throughout the construction and initial operational phase. The remaining budget for SCP Expansion is estimated in the amount of US dollars 2,799,000 (the Group's share: US dollars 186,693).

Commitment related to TANAP

Construction of TANAP

At the financial statement date, the Group has capital commitment to fund the construction of TANAP pipeline system. The remaining budget for construction of TANAP system is estimated in the amount of US dollars 8,111,736 (31 December 2014: US dollars 9,269,920).

Commitment related to TAP

Construction of TAP

The Group has the commitment to fund construction of TAP pipeline system. The remaining budget for construction of the TAP system is estimated in the amount of US dollars 4,337,700 (31 December 2014: US dollars 4,781,552). The Group's share of commitment at the financial statement date was US dollars 867,540 (31 December 2014: US dollars 956,310).

Commitments related to participating interest in AGSC, TANAP, TAP and SCPC

BOTAS gas contract

AGSC is obliged under the gas contract signed with BOTAS to make available a maximum of approximately 6.6 bcm of gas annually from 2016 till 2019 at a price calculated based on a formula established by the gas contract.

25. Commitments and contingencies (continued)

Commitments related to participating interest in AGSC, TANAP, TAP and SCPC (continued)

Stage 2 gas contract

On 25 October 2011, SOCAR and BOTAS executed a gas sale and purchase agreement ("Stage 2 SPA") with respect to the sale by SOCAR to BOTAS of certain volumes of Shah Deniz Stage 2 gas (2 bcm first delivery year, 4 bcm second delivery year, 6 bcm plateau period). In December 2012 SOCAR transferred and assigned the rights and obligations under the Stage 2 SPA to AGSC. The anticipated commencement of first gas delivery under Stage 2 BOTAS SPA is July 2018.

BOTAS contract for BTC fuel gas

AGSC is obliged under the agreement with BOTAS to make available 0.15 bcm of gas annually from 2016 till 2019 at a price which is calculated based on formula established in the contract.

Azerbaijan gas obligation

AGSC is obliged under the agreement signed with SOCAR to make available a minimum of approximately 1.5 bcm of gas in 2016 and onwards at a price calculated based on the formula established in the agreement.

Georgian gas obligation

AGSC is obliged under the agreement signed with Georgian Oil and Gas Corporation ("GOGC") and the government of Georgia to make available 0.5 bcm of gas in 2016 and onwards, at a price which is calculated based on a formula established in the contract.

Sale and purchase agreement with OptionCo

AGSC is obliged under the agreement signed with OptionCo to make available 0.29 bcm of gas during the contract year starting on 1 October 2015 and ending 1 September 2016. Thereafter, AGSC is obliged to deliver during the next contract year, which starts on 1 October 2016 and ends 30 September 2017, a maximum of five percent of the volumes transported by AGSC through Georgia via the SCP in the previous contract year, at a price which is calculated based on a formula established in the contract.

Shah Deniz Stage 2 EU Long term Gas Sales Agreements ("GSAs")

In September 2013 ten EU GSAs were signed by SOCAR with nine EU Buyers and in December 2013 the GSAs were assigned to AGSC until Shah Deniz PSA expiry with re-assignment to SOCAR as Shah Deniz Production declines. The commencement date will be firmed up through funnelling mechanism within a 1-year window between 1 January 2020 and 1 January 2021 for DEPA, Shell, Axpo (PSV) and E.On; 1 July 2020 and 1 July 2021 for Axpo (WTB), GDF Suez, Gas Natural Fenosa, Enel, Hera and Bulgargaz. The GSAs assume 3 year build-up period, as defined in the contracts, with the following peak annual delivery obligations: AXPO (PSV) 0.48 bcm, GDF Suez 2.64 bcm, Gas Natural Fenosa 0.99 bcm, E.On 1.45 bcm, Shell 0.95 bcm, Hera 0.3 bcm, Enel 0.48 bcm, AXPO (WTB) 0.96 bcm, Bulgargaz 0.94 bcm, DEPA 1 bcm.

Trans Anatolian Pipeline Gas Transportation Agreement (TANAP GTA)

AGSC is a party to TANAP GTA with annual reserved capacity during the build-up period, as defined in the contract, of 6.1 bcm, 6.2 bcm, 7.2 bcm and plateau of 10.5 bcm after 18 months with 100% ship or pay on the capacity reservation. The start date will be set through a funnelling mechanism inside the first window period between 1 July 2019 and 1 July 2021.

25. Commitments and contingencies (continued)

Commitments related to participating interest in AGSC, TANAP, TAP and SCPC (continued)

Trans Adriatic Pipeline GTA (TAP GTA)

AGSC is a party to TAP GTA with annual capacity of 9.08 bcm and additional annual regulated capacity of 0.46 bcm booked under TAP First Booking Phase ("FBP"). The planned commencement date is inside the second window period between 1 January 2020 and 31 December 2020.

TAP Deferral Gas Sales Agreement

AGSC is obliged under the agreement signed with SOCAR to make available gas during the period 1 May 2019 – 31 December 2020 (or until an earlier termination of the agreement in accordance with provisions of the agreement) in the volume of maximum 3.66 bcm in 2019 and 6.4 bcm in 2020, at a price which is stipulated in the contract.

Sale and purchase agreement with Baku-Tbilisi-Ceyhan Pipeline Company ("BTC Co")

AGSC is obliged under an agreement signed with BTC Co to make available 0.16 bcm during the following years until the termination of the contract subject to the right of BTC Co to reduce annual off-take, at a price which is calculated based on the formula established in the contract.

Debottlenecking SPA

AGSC is obliged under the agreement signed with SOCAR to make available gas during the period 1 January 2016 – 30 June 2018 as follows: 1.3 bcm per annum for the years 2016-2017 and 0.64 bcm in 2018, at a price which is stipulated in the contract.

BOTAS Gas Transportation Agreement (BOTAS GTA)

TANAP is a party to BOTAS GTA and with annual reserved capacity during the build-up period, as defined in the contract, of 1.9 bcm (12 month period commencing on start date), 3.8 bcm (next 12 month period) and plateau of 5.7 bcm 24 months after the start date. The start date will be within the period from and including 1 May 2018 to and including 30 June 2018.

SOCAR Gas Transportation Agreement (SOCAR GTA)

Based on this GTA, from and including the start date (6 March 2036) SOCAR shall pay to TAP AG the amount of actual monthly charge in relation of each booking of reserved capacity at each entry point and exit point at a price which is calculated based on the formula established in the contract. TAP AG shall make available to SOCAR for transportation of natural gas at the applicable entry point and exit point(s) as described below, a reserved capacity equal to the following maximum flow rates expressed in kilowatt-hours (kWh) per gas day: Entry point at Kipoi – 287,318,605 kWh per gas day; Exit point at SRG – 242,999,147 kWh per gas day; Exit point at Komotini – 44,319,458 kWh per gas day.

Framework agreement

On 17 December 2013, AGSC executed a Term Sheet for GSA Novation and Capacity Transfer Framework Agreement with SOCAR ("Term Sheet"). A fully-termed Framework Agreement was negotiated with SOCAR to give effect to the Term Sheet. Framework Agreement relates to novation of long-term GSAs and transfer of GTA capacity from AGSC to SOCAR after 2036. The Framework Agreement was executed on 19 October 2015.

25. Commitments and contingencies (continued)

Commitment under the Deferred Sale and Purchase Agreement ("DSPA")

In July 2014 the Group signed the DSPA for the acquisition of 10% participating interest in Shah Deniz project and 8% shares in AGSC from AzSD and 10% shares in SCPC from AzSCP. According to the terms of this agreement the Group shall make advance payments for these acquisitions to AzSD and AzSCP, while control will pass to the Group in March 2023, provided that certain conditions precedent are satisfied. As of 31 December 2015, the Group had commitments for payments in the amount of US dollars 536,087 (31 December 2014: US dollars 559,754) to AzSD and has to make progress payments equaled to Shah Deniz Stage 2 Development cash call requirements of AzSD till 31 December 2020. In addition, the Group has to make progress payments equaled to SCP Expansion project related cash calls requirements of AzSCP till 31 December 2020.

Commitment under the funding agreement with BOTAS (the "Funding Agreement")

On 26 May 2014 SOCAR and BOTAS signed Funding Agreement for financing BOTAS's 5% shares in TANAP A.Ş., upon acquisition of shares in TANAP A.Ş. by BOTAS. On 13 March 2015, the Group signed novation agreement with SOCAR and BOTAS, where all rights and obligations under the Funding Agreement were transferred from SOCAR to the Group. According to agreement with BOTAS, the Group has commitment for providing interest free loan to BOTAS for financing its 5% share in TANAP A.Ş.'s future cash call requirements till TANAP becomes operational.

Contingencies related to the SPA in respect of share in Shah Deniz PSA and AGSC

In July 2014 the Group acquired 6.67% participating interest in Shah Deniz project and 5.336% shares in AGSC and 6.67% shares in SCPC based on the sale and purchase agreement signed on 29 April 2014 with AzSD and AzSCP. These interest and shares were acquired by AzSD and AzSCP from Statoil Shah Deniz A.S. and Statoil Azerbaijan A.S., respectively based on the Sale and Purchase Agreement signed between the parties thereto. At 31 December 2015 AzSD had dispute with Statoil Shah Deniz A.S. ("Statoil") in the amount of US dollars 29 million related to the purchase consideration determination. The parties agreed to involve an independent expert to resolve the dispute as required under the provisions of the sale and purchase agreement. On 17 February 2016 the independent expert concluded that the purchase consideration must be adjusted by approximately US dollars 15 million (out of total US dollars 29 million initially requested) in favor of Statoil. The expert's decision is binding for AzSD and Statoil and the parties cannot challenge the expert's opinion in relation to the consideration adjustment, unless (i) there has been a manifest error or fraud; (ii) there is a material interest or duty prejudicing his decision; or (iii) the expert decided a matter outside of the scope. However, AzSD and AzSCP has made a counter claim against Statoil in the amount of US dollars 19 million under the leakage and indemnity provision of the SPA, which, AzSD and AzSCP believe, did not fall within the jurisdiction of independent expert. If the dispute is ultimately resolved in favor of Statoil, AzSD will make payment of US dollars 15 million to Statoil and the Group will reimburse this amount to AzSD. Management believes that the resolution of the issue will not result in any additional liability to the Group, therefore, liability of approximately US dollars 15 million is not recognized in these consolidated financial statements.

26. Current business environment

Azerbaijan economy

The Group's operations are mainly conducted in the Republic of Azerbaijan and the Republic of Turkey. As an emerging market, at the present time the Republic of Azerbaijan is developing business and regulatory infrastructure that would generally exist in a more mature market economy.

The Republic of Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks as required by the market economy. The future stability of the Republic of Azerbaijan economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

26. Current business environment (continued)

Azerbaijan economy (continued)

As a result of significant drop in crude oil prices, on 21 February 2015, Azerbaijani Manat was devalued against US dollar and other major currencies by 34%. The exchange rates before and after devaluation were AZN 0.786 and AZN 1.050 to US dollar 1, respectively. On 21 December 2015 Azerbaijani Manat devalued against major currencies by a further 47%. Following the second devaluation, the Central Bank of Republic of Azerbaijan announced the move to a floating exchange rate.

There continues to be uncertainty regarding economic growth, access to capital and cost of capital which could adversely affect the Company's future results and financial position and business prospects in a manner not currently determinable. During subsequent period, crude oil prices were subject to significant volatility. Any further significant drop in crude oil prices could negatively affect the Company's future liquidity position, results of operations and might result in an impairment loss on oil and gas assets.

Azerbaijani government announced plans to accelerate reforms and support to economic environment in response to current challenges.

The Company's Management is monitoring these developments in the current environment and taking precautionary measures it considered necessary in order to support the sustainability and development of the Company's business in the foreseeable future.

Turkish economy

The strong performance of the Turkish economy, as clearly demonstrated in economic indicators of previous years, was impacted to some degree by the sluggish European markets that Turkey is most dependent on. The Turkish government began to implement new policies and measures to revive domestic demand in order to compensate for the slowdown in foreign markets.

While management believes it is taking appropriate measures to support the sustainability of Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

These consolidated financial statements do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the period when they become known and estimable.

27. Events after the reporting date

Increase in share capital

ME and SOCAR have increased the Company's share capital in the total amount of US dollars 295,900 subsequent to year end.

Eurobond Emission

In March 2016 the Company issued US dollars 1 billion senior unsecured notes guaranteed by the Republic of Azerbaijan ("Notes"). The Notes bear interest rate of 6.875 per cent per annum payable semi-annually in arrears on 24 March and 24 September in each year until maturity. The Notes mature on 24 March 2026 and are listed on the Irish Stock Exchange.