

**Southern Gas Corridor  
Closed Joint-Stock Company**

**Consolidated financial statements**

*For the year ended 31 December 2021  
with independent auditor's report*

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Independent auditor's report

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Ernst & Young Holdings (CIS) B.V.  
Port Baku Towers Business Centre  
South Tower, 9th floor,  
153, Neftçilar Ave.  
Baku, AZ1010, Azerbaijan  
Tel: +994 (12) 490 70 20  
Fax: +994 (12) 490 70 17  
www.ey.com/az

Ernst & Yanq Holdings (SiAyEs) Bi.Vi.  
Port Baku Towers Biznes Mərkəzi  
Cənub Qülləsi, 9-cu mərtəbə  
Neftçilər prospekti, 153  
Bakı, AZ1010, Azərbaycan  
Tel: +994 (12) 490 70 20  
Faks: +994 (12) 490 70 17

## Independent auditor's report

To Management and the Supervisory Board of the  
Southern Gas Corridor Closed Joint-Stock Company

### **Opinion**

We have audited the 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 2021, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2021, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

### **Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Key audit matters**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.



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We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

**Key audit matter**

**How our audit addressed the key audit matter**

***Revenue recognition***

We identified revenue recognition as one of the matters of most significance to our audit because the amount of revenue is significant to the consolidated financial statements. In addition, 2021 was the first year of full operation for the Group. The Group has different revenue streams represented by sales of natural gas and condensate as well as transportation of natural gas.

Information on revenue recognition is disclosed in Notes 2 and 17 to the consolidated financial statements.

We analysed the Group's accounting policy in respect of revenue recognition and obtained understating of the Group's revenue streams.

We analysed sales contracts terms in respect of transfer of control over natural gas and condensate. For condensate and natural gas sales, we recalculated revenue by multiplying volumes indicated in monthly bill of lading by prices indicated in respective invoices and agreed to the amount of revenue recognized by the Group.

We analysed natural gas transportation agreements' terms in respect of transfer of control over services rendered. For transportation services rendered, on a sample basis, we recalculated revenue by multiplying volumes of transported natural gas indicated in dispatch notes by transportation tariff rates indicated in natural gas transportation agreements and agreed to the amount of revenue recognized by the Group.

We compared monthly sales records of the current year against records of the prior year and analysed unusual fluctuations.

On a sample basis, we obtained confirmations of accounts receivable balances from customers.

We analyzed disclosure of revenue in the notes to the consolidated financial statements.



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**Key audit matter**

**How our audit addressed the key audit matter**

***Natural gas and condensate reserves estimates***

The estimation of natural gas and condensate reserves has a significant impact on depreciation, depletion and amortization charges, decommissioning provisions and impairment trigger analysis of oil and gas properties and related advance payments. Internationally recognized independent reserves engineers were involved to evaluate natural gas and condensate reserves of the field where the Group holds interest.

Information on natural gas and condensate reserve estimates is disclosed in Note 3 to the consolidated financial statements.

We compared the assumptions used by the reserves engineers with the Group's approved budget and historical data.

We analysed the underlying assumptions and compared estimates of reserves and resources provided by the reserves engineers to the amounts included in the calculation of depreciation, depletion and amortization charges, decommissioning provisions and impairment trigger analysis of oil and gas properties and related advance payments.

We obtained an understanding of professional qualifications, experience and reputation of reserves engineers to evaluate their competence, capability and expertise.

We analyzed disclosure of condensate and natural gas reserve estimates in the notes to the consolidated financial statements.

***Responsibilities of management and the Supervisory board for the consolidated financial statements***

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

The Supervisory board is responsible for overseeing the Group's financial reporting process.

***Auditor's responsibilities for the audit of the consolidated financial statements***

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.



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

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Supervisory board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Supervisory board with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.



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From the matters communicated with the Supervisory board, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The partner in charge of the audit resulting in this independent auditor's report is Azer Babayev.

*Ernst & Young Holdings (CIS) B.V.*

30 June 2022

Baku, Azerbaijan

**Consolidated statement of financial position****as at 31 December 2021***(Amounts presented are in thousands of US dollars)*

	Note	31 December 2021	31 December 2020
<b>Assets</b>			
<b>Non-current assets</b>			
Oil and gas properties	6	8,469,087	8,725,764
Advance payments	7	2,537,145	2,536,833
Investment in associate	8	264,574	249,448
Loan receivables	9	546,775	632,275
Right-of-use asset	10	20,180	26,399
Deferred tax assets		–	1,421
Other non-current assets		15,177	8,682
<b>Total non-current assets</b>		<b>11,852,938</b>	<b>12,180,822</b>
<b>Current assets</b>			
Cash and cash equivalents	11	235,481	57,955
Deposits	11	320,278	278,927
Accounts receivable	12	212,345	110,091
Inventories		38,167	34,704
Other current assets		13,513	14,172
<b>Total current assets</b>		<b>819,784</b>	<b>495,849</b>
<b>Total assets</b>		<b>12,672,722</b>	<b>12,676,671</b>
<b>Equity and liabilities</b>			
<b>Equity</b>			
Share capital	13	2,415,800	2,415,800
Additional paid-in capital	13	31,481	31,481
Other reserves	13	(47,886)	(73,363)
Cumulative translation differences		(15,296)	7,955
Accumulated losses		(147,495)	(603,501)
<b>Equity attributable to the equity holders of the Parent</b>		<b>2,236,604</b>	<b>1,778,372</b>
Non-controlling interests		1,788,614	1,449,223
<b>Total equity</b>		<b>4,025,218</b>	<b>3,227,595</b>
<b>Non-current liabilities</b>			
Long-term borrowings	14	6,925,827	7,525,892
Government grant	14	559,209	581,056
Decommissioning liabilities	15	199,458	183,052
Deferred tax liability	20	20,033	13,433
Lease liability	10	17,186	24,404
Other non-current liabilities		67,076	55,308
<b>Total non-current liabilities</b>		<b>7,788,789</b>	<b>8,383,145</b>
<b>Current liabilities</b>			
Trade and other payables	16	54,155	46,967
Short-term and current portion of long-term borrowings	14	750,205	960,050
Accrued liabilities	16	39,675	47,923
Income tax payable	20	8,842	6,878
Current portion of lease liability	10	5,838	4,113
<b>Total current liabilities</b>		<b>858,715</b>	<b>1,065,931</b>
<b>Total equity and liabilities</b>		<b>12,672,722</b>	<b>12,676,671</b>

**Signed and authorised on behalf of the Group**

Afgan Isayev, General Director

30 June 2022

Adil Pashayev, Finance Director

30 June 2022

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



**Consolidated statement of comprehensive income****for the year ended 31 December 2021***(Amounts presented are in thousands of US dollars)*

	Note	Year ended 31 December 2021	Year ended 31 December 2020
Revenue	17	1,763,092	861,551
Cost of sales	18	(328,717)	(295,534)
<b>Gross profit</b>		<b>1,434,375</b>	<b>566,017</b>
General and administrative expenses		(265,620)	(212,832)
Transportation tariffs		(64,338)	(18,169)
Other income	14	26,293	28,722
<b>Operating profit</b>		<b>1,130,710</b>	<b>363,738</b>
Interest income	19	34,001	37,358
Finance costs	10, 14, 15	(417,343)	(395,505)
Share of result of associate	8	68,380	17,265
Foreign exchange loss, net		(2,718)	(1,649)
<b>Profit before income tax</b>		<b>813,030</b>	<b>21,207</b>
Income tax expenses	20	(17,633)	(8,135)
<b>Profit for the year</b>		<b>795,397</b>	<b>13,072</b>
<b>Other comprehensive income</b>			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent period</i>			
Exchange differences on translation of foreign associate	8	(23,251)	24,048
Net profit/(loss) on cash flow hedge reserve of associate	8, 13	25,477	(18,381)
<b>Other comprehensive income for the year, net of tax</b>		<b>2,226</b>	<b>5,667</b>
<b>Total comprehensive income for the year</b>		<b>797,623</b>	<b>18,739</b>
<b>Profit attributable to:</b>			
Equity holders of the Parent		456,006	(65,032)
Non-controlling interests		339,391	78,104
		<b>795,397</b>	<b>13,072</b>
<b>Total comprehensive income attributable to:</b>			
Equity holders of the Parent		458,232	(59,365)
Non-controlling interests		339,391	78,104
		<b>797,623</b>	<b>18,739</b>

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

**Consolidated statement of cash flows****for the year ended 31 December 2021***(Amounts presented are in thousands of US dollars)*

	Note	Year ended 31 December 2021	Year ended 31 December 2020
<b>Operating activities</b>			
Profit before income tax		813,030	21,207
<i>Non-cash adjustments to reconcile profit before tax to net cash flows</i>			
Finance costs	10, 14, 15	417,343	395,505
Depreciation and depletion of property, plant and equipment and right-of-use assets	6, 10	319,231	291,549
Share of result of associate	8	(68,380)	(17,265)
Expected credit loss		3,364	8,943
Other income	14	(26,293)	(28,721)
Interest income	19	(34,001)	(37,358)
<i>Working capital adjustments</i>			
Accounts receivable		(102,254)	(66,323)
Inventories		(3,463)	(22,881)
Other assets		(14,384)	(10,807)
Trade and other payables		31,820	8,787
Accrued liabilities		(8,248)	(632)
<b>Cash generated from operations</b>		<b>1,327,765</b>	<b>542,004</b>
Income tax paid		(7,648)	(5,036)
Interest received		5,549	3,708
<b>Net cash flows from operating activities</b>		<b>1,325,666</b>	<b>540,676</b>
<b>Investing activities</b>			
Placement of deposits	11	(330,000)	(180,000)
Deposits withdrawal	11	289,128	70,000
Proceeds from repayment of loans given to related parties	9	84,551	42,350
Proceeds of interest from loans given to related parties	9	5,871	3,850
Return of advance payments for acquisition of shares		–	3,053
Investments in oil and gas properties		(66,050)	(76,173)
Additions to construction in progress and development costs		–	(12,470)
Divestment from / (investment in) associate	8	55,480	(16,576)
<b>Net cash flows / (used in) investing activities</b>		<b>38,980</b>	<b>(165,966)</b>
<b>Financing activities</b>			
Proceeds from borrowings		–	455,000
Repayment of borrowings	14	(75,663)	(356,612)
Payment of principal portion of lease liabilities	10	(5,493)	(5,784)
Proceeds of deferred consideration from disposal of non-controlling interests in a subsidiary	9	31,018	–
Interest paid		(1,136,982)	(504,567)
<b>Net cash used in financing activities</b>		<b>(1,187,120)</b>	<b>(411,963)</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>177,526</b>	<b>(37,253)</b>
Cash and cash equivalents at the beginning of the year	11	57,955	95,208
<b>Cash and cash equivalents at the end of the year</b>	11	<b>235,481</b>	<b>57,955</b>

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

**Consolidated statement of changes in equity**  
**for the year ended 31 December 2021**

*(Amounts presented are in thousands of US dollars)*

	Share capital	Additional paid-in capital	Other reserves (Note 13)	Cumulative translation differences	Retained earnings	Total	Non-controlling interests	Total equity
<b>At 1 January 2020</b>	<b>2,415,800</b>	<b>31,481</b>	<b>(54,982)</b>	<b>(16,093)</b>	<b>(538,469)</b>	<b>1,837,737</b>	<b>1,371,119</b>	<b>3,208,856</b>
(Loss)/profit for the year	–	–	–	–	(65,032)	<b>(65,032)</b>	78,104	<b>13,072</b>
Other comprehensive (loss)/profit	–	–	(18,381)	24,048	–	<b>5,667</b>	–	<b>5,667</b>
<b>Total comprehensive (loss)/profit</b>	<b>–</b>	<b>–</b>	<b>(18,381)</b>	<b>24,048</b>	<b>(65,032)</b>	<b>(59,365)</b>	<b>78,104</b>	<b>18,739</b>
<b>At 31 December 2020</b>	<b>2,415,800</b>	<b>31,481</b>	<b>(73,363)</b>	<b>7,955</b>	<b>(603,501)</b>	<b>1,778,372</b>	<b>1,449,223</b>	<b>3,227,595</b>
Profit for the year	–	–	–	–	456,006	<b>456,006</b>	339,391	<b>795,397</b>
Other comprehensive profit/(loss)	–	–	25,477	(23,251)	–	<b>2,226</b>	–	<b>2,226</b>
<b>Total comprehensive profit/(loss)</b>	<b>–</b>	<b>–</b>	<b>25,477</b>	<b>(23,251)</b>	<b>456,006</b>	<b>458,232</b>	<b>339,391</b>	<b>797,623</b>
<b>At 31 December 2021</b>	<b>2,415,800</b>	<b>31,481</b>	<b>(47,886)</b>	<b>(15,296)</b>	<b>(147,495)</b>	<b>2,236,604</b>	<b>1,788,614</b>	<b>4,025,218</b>

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

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

## 1. Corporate information

Southern Gas Corridor Closed Joint-Stock Company (the "Company", the Parent 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 ("SD") 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"). The Company has the following subsidiaries:

Name	Country of incorporation	% equity interest	
		31 December 2021	31 December 2020
SGC Upstream LLC	Azerbaijan	100%	100%
SGC Midstream LLC	Azerbaijan	100%	100%
TANAP Doğalgaz İletim A.Ş. ("TANAP A.Ş.")	Turkey	51%	51%
AzTAP GmbH	Switzerland	100%	100%

The Company holds 20% share in Trans Adriatic Pipeline AG ("TAP AG"), through AzTAP GmbH.

## 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 2021 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 realise its assets and discharge its liabilities and commitments in the normal course of business. As at 31 December 2021, the Group's current liabilities exceeded current assets as significant portion of current liabilities were represented by current portion of long-term borrowing. In addition, as at 31 December 2021, the Group had capital and operating commitments (see Note 23) and long-term loan agreements (see Note 14) which would require significant cash outflows in foreseeable future.

The Group's management expects to receive sufficient amount of proceeds from hydrocarbons sales under current Shah Deniz Production Sharing Agreement and proceeds from transportation of natural gas through SCP, TANAP and TAP pipelines (see Note 17). The Group's 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 Company and its subsidiaries as at 31 December 2021.

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

## 2. Significant accounting policies (continued)

### Basis for consolidation (continued)

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.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised 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 ("NCIs"), even if this results in the NCIs 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 ("NCI")*

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 NCIs shall be adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the NCIs 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.

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

## **2. Significant accounting policies (continued)**

### **Business combinations (continued)**

#### *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 interest 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.

#### *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 as following:

- ▶ For any identifiable asset or liability initially measured at an amount other than cost, an entity initially measures that asset or liability at the amount specified in the applicable IFRS;
- ▶ The Group deducts from the transaction price of the group the amounts allocated to the assets and liabilities initially measured at an amount other than cost, and then allocates the residual transaction price to the remaining identifiable assets and liabilities based on their relative fair values at the date of the acquisition.

### **Investment in associate**

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 comprehensive income 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 comprehensive income outside operating profit and represents profit or loss after tax and NCIs 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.

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

## 2. Significant accounting policies (continued)

### Investment in associate (continued)

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 within "Share of profit of an associate" in the statement of comprehensive income.

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.

### Investments in the SD PSA, SCP and AGSC

According to the terms of Shah Deniz Production Sharing Agreement ("SD PSA"), the Group owns the portion of the SD project's assets and is liable for its portion of the SD 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 the SD PSA by recognising 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 South Caucasus Pipeline Company Limited ("SCPC") and accounted by recognising its portion of underlying assets, liabilities, expenses incurred and income earned by the project.

The Group holds an interest in the Azerbaijan Gas Supply Company Limited ("AGSC"), a company established together with the other Contractor Parties of the SD Project and the Ministry of Energy of the Republic of Azerbaijan. AGSC is a special structured entity established for marketing, accounting, billing, payment and reporting of other administrative activities related to the sales of SD gas and operates on a 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 is 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 recognised in profit or loss.

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

## 2. Significant accounting policies (continued)

### Foreign currency translation (continued)

The results and financial position of the Group entities which functional currency differ from the presentation currency of the Group 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 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 recognised as a separate component of equity – currency translation difference.

At 31 December 2021 the principal rate of exchange used for translating foreign currency balances was USD 1.1332 per EUR 1 (31 December 2020: USD 1.2288 per EUR 1), USD 0.0782 per TRY 1 (31 December 2020: USD 0.1356 per TRY 1) and USD 1.0920 per CHF 1 (31 December 2020: USD 1.1341 per CHF 1).

### Current versus non-current classification

The Group presents assets and liabilities in the statement of financial position based on current/non-current classification. An asset is current when it is:

- ▶ Expected to be realised or intended to be sold or consumed in the normal operating cycle;
- ▶ Held primarily for the purpose of trading;
- ▶ Expected to be realised within twelve months after the reporting period; or
- ▶ Cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

A liability is current when:

- ▶ It is expected to be settled in the normal operating cycle;
- ▶ It is held primarily for the purpose of trading;
- ▶ It is due to be settled within twelve months after the reporting period; or
- ▶ There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Group classifies all other assets and liabilities as non-current.

### Fair value measurement of financial instruments

Depending on their classification financial instruments are carried at fair value 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 best economic interest.

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



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

## 2. Significant accounting policies (continued)

### Fair value measurement of financial instruments (continued)

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.

*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 allowance for expected credit losses (“ECL”). 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.

*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 subsequently measured at amortised cost, fair value through other comprehensive income (“FVOCI”), and fair value through profit or loss (“FVPL”).

The classification of financial assets at initial recognition depends on the financial asset’s contractual cash flow characteristics and the Group’s business model for managing them. With the exception of trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient, the Group initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs. Trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient are measured at the transaction price determined under IFRS 15.

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

## **2. Significant accounting policies (continued)**

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

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

The Group's business model for managing financial assets refers to how it manages its financial assets to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both. Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the marketplace (regular way trades) are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the asset.

### **Subsequent measurement**

For purposes of subsequent measurement, financial assets are classified in four categories:

- ▶ Financial assets at amortised cost (debt instruments);
- ▶ Financial assets at FVOCI with recycling of cumulative gains and losses (debt instruments);
- ▶ Financial assets designated at FVOCI with no recycling of cumulative gains and losses upon derecognition (equity instruments);
- ▶ Financial assets at FVPL.

#### *Financial assets at amortised cost (debt instruments)*

This category is the most relevant to the Group. The Group measures financial assets at amortised cost if both of the following conditions are met:

- ▶ The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows; and
- ▶ The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired as well as through amortization process.

The Group's financial assets at amortised cost includes trade receivables, loan receivables and other non-current financial assets.

### **Derecognition**

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group's consolidated statement of financial position) 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 recognises an allowance for ECLs for all debt instruments not held at FVPL. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate.

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

## 2. Significant accounting policies (continued)

### Financial assets (continued)

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

The Group considers a financial asset to be in default when internal or external information indicates that the Group is unlikely to receive the outstanding contractual amounts in full before taking into account any credit enhancements held by the Group. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

### 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 recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

#### *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 measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the consolidated statement of comprehensive income when the liabilities are derecognised as well as through the effective interest rate method amortisation process.

Amortised 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 amortisation is included in finance cost in the consolidated statement of comprehensive income.

##### *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 derecognised 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 the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the profit or loss 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 consolidated statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

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

## 2. Significant accounting policies (continued)

### Derivative financial instruments and hedge accounting

#### *Initial recognition and subsequent measurement*

The Group's associate uses derivative financial instruments, such as interest rate swap contracts, to hedge its foreign currency risks and interest rate risks. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

For the purpose of hedge accounting, hedges are classified as:

- ▶ Fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment;
- ▶ Cash flow hedges when hedging the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction or the foreign currency risk in an unrecognised firm commitment.

At the inception of a hedge relationship, the Group's associate formally designates and documents the hedge relationship to which it wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge.

The documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the Group's associate will assess whether the hedging relationship meets the hedge effectiveness requirements (including the analysis of sources of hedge ineffectiveness and how the hedge ratio is determined). A hedging relationship qualifies for hedge accounting if it meets all of the following effectiveness requirements:

- ▶ There is 'an economic relationship' between the hedged item and the hedging instrument;
- ▶ The effect of credit risk does not 'dominate the value changes' that result from that economic relationship;
- ▶ The hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group's associate actually uses to hedge that quantity of hedged item.

Hedges that meet all the qualifying criteria for hedge accounting are accounted for, as described below:

#### *Cash flow hedges*

The effective portion of the gain or loss on the hedging instrument is recognised in OCI in the cash flow hedge reserve, while any ineffective portion is recognised immediately in the statement of comprehensive income. The cash flow hedge reserve is adjusted to the lower of the cumulative gain or loss on the hedging instrument and the cumulative change in fair value of the hedged item.

### 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 is capitalised and the replaced part is retired.

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.

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

## **2. Significant accounting policies (continued)**

### **Oil and gas properties (continued)**

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

### **Construction in progress**

All costs directly or indirectly attributable to the projects of construction and expansion the capacity of the pipeline systems are capitalised as a construction in progress. The construction in progress is stated at a cost and not depreciated but tested for impairment if indicators exist. The construction in progress is transferred to the oil and gas properties upon completion.

### **Depreciation, depletion and amortisation**

Depreciation, depletion and amortisation of capitalised 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 amortisation 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 amortisation of capitalised 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, the date when the pipeline was officially ready and put in use. The estimated useful life of the TANAP pipeline system is expected to last until the year 2062.

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 capitalised 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 capitalised expenditure is first assessed for impairment and (if required) any impairment loss is recognised, then the remaining balance is transferred to oil and gas properties. No amortisation is charged during the exploration and evaluation phase.

### **Leases**

The Group assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

#### **Group as a lessee**

The Group applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Group recognises lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

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

## 2. Significant accounting policies (continued)

### Leases (continued)

#### *Right-of-use assets*

The Group recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, lease payments made at or before the commencement date and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received. Unless the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right-of-use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term, as follows:

- ▶ Buildings and construction assets 6 years;
- ▶ Vehicles 2 years.

If the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term the recognised right-of-use asset is depreciated over estimated useful lives of the respective underlying asset. Right-of-use assets are subject to impairment.

#### *Lease liabilities*

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be payable by the lessee under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating a lease, if the lease term reflects the Group exercising the option to terminate. The variable lease payments that do not depend on an index or a rate are recognised as expense in the period on which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset. When the lease liability is remeasured as described above, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded as gain or loss in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero. When there is a modification of a lease that decreases the scope of the lease, the Group also recognises gain or loss in the profit or loss equal to the difference between carrying amounts of portions of lease liability and right-of-use asset derecognised.

#### *Incremental borrowing rate (IBR)*

The Group uses incremental borrowing rate as the discount rate as interest rate implicit in the lease is not readily determinable. In determining the incremental borrowing rate, the lessee considers borrowings with a similar term and security to the right-of-use asset, not the underlying asset. Lessee's incremental borrowing rate reflects the rate of interest that a lessee would have to pay, among others, in a similar economic environment. If the contract requires lease payments to be made in a currency other than the functional currency of the lessee, the incremental borrowing rate should be determined based on a borrowing of a similar amount in that foreign currency.

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

## **2. Significant accounting policies (continued)**

### **Leases (continued)**

#### *Short-term leases and leases of low-value assets*

The Group applies the short-term lease recognition exemption to its short-term leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option. The Group also assesses the value of an underlying asset based on the value of the asset when it is new, regardless of the age of the asset being leased and treats the underlying assets as low-value when a new one has a value of USD 5,000 or less. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

#### *Significant judgement in determining the lease term of contracts with renewal options*

The Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

The Group applies judgement in evaluating whether it is reasonably certain to exercise the option to renew. That is, it considers all relevant factors that create an economic incentive for it to exercise the renewal. After the commencement date, the Group reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not to exercise) the option to renew (e.g., a change in business strategy).

#### **Group as a lessor**

Leases in which the Group does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of comprehensive income due to its operating nature. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Variable lease payments are recognised as revenue in the period in which they are earned.

#### **Advance payments**

Advance payments are recognised 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 are recognised in the consolidated statement of comprehensive income in expense categories consistent with the function of the impaired asset.

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

## **2. Significant accounting policies (continued)**

### **Inventories**

Inventories are stated at the lower of cost and net realisable 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 realisable 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.

### **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 the 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, which equals 4.08% at 31 December 2021 (31 December 2020: 4.10%). A corresponding tangible fixed asset of an amount equivalent to the liability is also created. This amount is subsequently depreciated 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 in finance costs.

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 capitalised by shareholders of SCPC. The Group recognises underlying asset retirement obligation in respect of its participating interest in SCPC. A corresponding tangible fixed asset of an amount equivalent to the liability is also created. This amount is subsequently depreciated and charged against income. 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, which equals 8% at 31 December 2021 (31 December 2020: 8%).

In accordance with HGA signed with the Government of Turkey, the Group shall comply with all its decommissioning obligations following the expiry of HGA (2062). The Group recognised decommissioning liability, which represents the management’s best estimate of the expenditures required to settle the present obligation at the reporting date. A corresponding tangible fixed asset of an amount equivalent to the liability is also created. This amount is subsequently depreciated and charged against income. 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, which equals 6.7% at 31 December 2021 (31 December 2020: 6%).

### **Revenue recognition**

The Group’s revenue is generated from sales of natural gas and crude oil produced in Azerbaijan and sold to customers in Azerbaijan, Georgia, Turkey and Europe. The Group also recognises revenue from transportation of natural gas to relevant delivery points in Azerbaijan, Georgia and Turkey. Revenue is recognised when control of the services or goods are transferred to the customer at an amount that reflects the consideration to which the Group expects to be entitled in exchange for those services or goods.



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

## **2. Significant accounting policies (continued)**

### **Revenue recognition (continued)**

#### *Sale of natural gas and crude oil*

For contracts with customers in which the sale of goods is generally expected to be the only performance obligation, the Group recognises revenue from sale of natural gas and crude oil at the point in time when control of the asset is transferred to a customer.

#### *Transportation of natural gas*

The Group's contracts with customers for transportation of natural gas include deliver the natural gas to the exit points under respective natural gas transportation agreements. The Group recognises revenue only when it satisfies an identified performance obligation by transferring a promised service to a customer.

#### *Accounting for over/underlift crude oil*

The Group operates in the SD PSA arrangement for production of oil and gas products. The Group recognises revenue based on actually sold volume of crude oil with no adjustments made in respect of production imbalances resulted in any variance between actual share of production volume sold to date and the share of production which the party has been entitled to sell to date. The cost of sales is adjusted for production imbalances in order to align with the volumes actually sold. The Group applies cost method for measurement of underlift asset and overlift liability at initial recognition.

### **Government grants**

Government grants are recognised 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 recognised as income over the expected useful life of the related asset on a basis consistent with the depreciation policy.

The benefit of a bond issued to the government (or to state-owned entity) 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 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 the 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 recognises profit taxes and related revenue in the consolidated statement of comprehensive income.

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 realised or the deferred income tax liability is settled. The Company's corporate income tax rate for the year ended 31 December 2021 and 2020 was 20 per cent.

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

## 2. Significant accounting policies (continued)

### Income taxes (continued)

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 recognised 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 liability 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 tax assets are recognised for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised, except:

- ▶ When the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss;
- ▶ In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint arrangements, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

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 and plant and equipment. The same approach is applied for right of use assets and lease liabilities.

### Operating tax of TANAP A.Ş.

As per the HGA between the Republic of Turkey and TANAP A.Ş., it was determined that the corporate income tax of TANAP A.Ş. will only be based on the amount of natural gas transmitted from the pipeline after the pipeline is put in use. According to tax ruling received on 7 April 2017 TANAP A.Ş. is not subject to corporate tax. TANAP A.Ş. is required to pay tax of US dollars 6.31 per thousand cubic metrics of gas measured at entry point (2020: US dollars 6.19 per thousand cubic metrics of gas).

### 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.

### 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 to 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.

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

## **2. Significant accounting policies (continued)**

### **Transactions with related parties (continued)**

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be 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 recognised 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 recognised in the consolidated financial statements but disclosed when an inflow of economic benefits is probable.

## **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 amortisation charges to the consolidated statement of comprehensive income.

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 which are either fixed or variable depending on crude oil prices and other inputs.

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. Latest forecasts issued by internationally recognised independent reserves engineers were dated as of 31 December 2021.

### **ECL measurement**

The Group estimates probability of default for all instruments based on external rating migration matrices. The Probability of default estimates is calibrated from through-the-cycle to point-in-time and adjusted for forward-looking information. Integration of forward-looking information is performed by probability of default calibration with the forward-looking coefficient which is conservatively calculated to reflect the current situation.

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

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

#### **ECL measurement (continued)**

The assessment of the correlation between historical observed default rates, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and of forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future.

#### **Leases – estimating the incremental borrowing rate**

The Group cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (IBR) to measure lease liabilities. The IBR is the rate of interest that the Group would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Group 'would have to pay', which requires estimation when no observable rates are available.

#### **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 SD 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 2027 (Note 15). 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 dollars 13,682 lower / US dollars 15,264 higher, respectively.

#### **Recoverability of oil and gas assets**

The Group assesses each 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, 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.

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 post-tax discount rate of the Group as at 31 December 2021 was 6.55% (2020: 8.12%). The Group generally estimates value-in-use using a discounted cash flow model from financial budgets approved by management. As at 31 December 2021 the Group performed impairment trigger analysis and did not identify any impairment trigger.

#### **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.

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

## 4. New and amended standards and interpretations

### 4.1 Change in the Group's accounting policies

The Group applied for the first-time certain amendments to the standards, which are effective for annual periods beginning on or after 1 January 2021. The Group also early adopted Amendments to IFRS 16 *Covid-19 Related Rent Concessions*. No other standards, interpretations or amendments that have been issued but are not yet effective, were early adopted. The nature and the impact of each amendment is described below:

#### *Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform – Phase 2*

The amendments provide temporary reliefs which address the financial reporting effects when an interbank offered rate (IBOR) is replaced with an alternative nearly risk-free interest rate (RFR). The amendments include the following practical expedients:

- ▶ A practical expedient to require contractual changes, or changes to cash flows that are directly required by the reform, to be treated as changes to a floating interest rate, equivalent to a movement in a market rate of interest;
- ▶ Permit changes required by IBOR reform to be made to hedge designations and hedge documentation without the hedging relationship being discontinued;
- ▶ Provide temporary relief to entities from having to meet the separately identifiable requirement when an RFR instrument is designated as a hedge of a risk component.

These amendments had no impact on the consolidated financial statements of the Group. The Group intends to use the practical expedients in future periods if they become applicable. The Group continues to monitor the development of Interest Rate Benchmark Reform and to assess the impact of reform on the Group's hedging relationships and borrowings. The Group conducts discussions with lenders.

#### *Amendments to IFRS 16 Covid-19-Related Rent Concessions*

On 28 May 2020, the IASB issued Covid-19-Related Rent Concessions – amendment to IFRS 16 Leases. The amendments provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions arising as a direct consequence of the Covid-19 pandemic. As a practical expedient, a lessee may elect not to assess whether a Covid-19 related rent concession from a lessor is a lease modification. A lessee that makes this election accounts for any change in lease payments resulting from the Covid-19 related rent concession the same way it would account for the change under IFRS 16, if the change were not a lease modification. The amendment was intended to apply until 30 June 2021, but as the impact of the Covid-19 pandemic is continuing, on 31 March 2021, the IASB extended the period of application of the practical expedient to 30 June 2022. The amendment applies to annual reporting periods beginning on or after 1 April 2021. The Group applied this amendment early in these consolidated financial statements. However, the Group has not received Covid-19-related rent concessions, therefore, these amendments had no impact on the consolidated financial statements of the Group.

### 4.2 Standards issued but not yet effective

#### *IFRS 17 Insurance Contracts*

In May 2017, the IASB issued IFRS 17 *Insurance Contracts* (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 *Insurance Contracts* (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features.

IFRS 17 is effective for reporting periods beginning on or after 1 January 2023, with comparative figures required. Early application is permitted, provided the entity also applies IFRS 9 and IFRS 15 on or before the date it first applies IFRS 17. This standard is not applicable to the Group as it did not have any insurance contracts.

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

#### 4. New and amended standards and interpretations (continued)

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

###### *Amendments to IAS 1: Classification of Liabilities as Current or Non-current*

In January 2020, the IASB issued amendments to paragraphs 69 to 76 of IAS 1 to specify the requirements for classifying liabilities as current or non-current. The amendments clarify:

- ▶ What is meant by a right to defer settlement;
- ▶ That a right to defer must exist at the end of the reporting period;
- ▶ That classification is unaffected by the likelihood that an entity will exercise its deferral right;
- ▶ That only if an embedded derivative in a convertible liability is itself an equity instrument would the terms of a liability not impact its classification.

The amendments are effective for annual reporting periods beginning on or after 1 January 2023 and must be applied retrospectively. The Group is currently assessing the impact the amendments will have on current practice and whether existing loan agreements may require renegotiation.

###### *Reference to the Conceptual Framework – Amendments to IFRS 3*

In May 2020, the IASB issued Amendments to IFRS 3 *Business Combinations – Reference to the Conceptual Framework*. The amendments are intended to replace a reference to the *Framework for the Preparation and Presentation of Financial Statements*, issued in 1989, with a reference to the *Conceptual Framework for Financial Reporting* issued in March 2018 without significantly changing its requirements. The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential 'day 2' gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 *Levies*, if incurred separately.

At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the *Framework for the Preparation and Presentation of Financial Statements*. The amendments are effective for annual reporting periods beginning on or after 1 January 2022 and apply prospectively. These amendments are not expected to have impact on the consolidated financial statements of the Group.

###### *Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16*

In May 2020, the IASB issued *Property, Plant and Equipment – Proceeds before Intended Use*, which prohibits entities deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognises the proceeds from selling such items, and the costs of producing those items, in profit or loss.

The amendment is effective for annual reporting periods beginning on or after 1 January 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Group.

###### *Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37*

In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making. The amendments apply a "directly related cost approach". The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract.

The amendments are effective for annual reporting periods beginning on or after 1 January 2022. The Group will apply these amendments to contracts for which it has not yet fulfilled all its obligations at the beginning of the annual reporting period in which it first applies the amendments.

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

#### **4. New and amended standards and interpretations (continued)**

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

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

In December 2015, the IASB decided to defer the effective date of the amendments until such time as it has finalised any amendments that result from its research project on the equity method. Early application of the amendments is still permitted. The amendments address the conflict between IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* 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 a full gain or loss is recognised when a transfer to an associate or joint venture involves a business as defined in IFRS 3. Any gain or loss resulting from the sale or contribution of assets that does not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture. The amendments must be applied prospectively. Early application is permitted and must be disclosed. The Group did not expect significant effect of these amendments on its consolidated financial statements.

###### *IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities*

As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendment is effective for annual reporting periods beginning on or after 1 January 2022 with earlier adoption permitted. The Group will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendments are not expected to have a material impact on the Group.

###### *Amendments to IAS 12 Income Taxes: Deferred Tax related to Assets and Liabilities arising from a Single Transaction*

The IASB has amended IAS 12, *Income Taxes*, to require companies to recognise deferred tax on particular transactions that, on initial recognition, give rise to equal amounts of taxable and deductible temporary differences. The proposed amendments will typically apply to transactions such as leases for the lessee and decommissioning obligations.

According to the amended IAS 12, a temporary difference that arises on initial recognition of an asset or liability is not subject to the initial recognition exemption if that transaction gave rise to equal amounts of taxable and deductible temporary differences.

These amendments might have a significant impact on the preparation of financial statements by companies that have substantial balances of right-of-use assets, lease liabilities, decommissioning, restoration and similar liabilities. The impact for those affected would be the recognition of additional deferred tax assets and liabilities.

The amendments should be applied for annual periods beginning on or after 1 January 2023. Earlier application is permitted. The amendments should be applied to transactions that occur on or after the beginning of the earliest comparative period presented in the financial statements for annual period in which they are applied. The amendments are not expected to have a material 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.

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 2021 is set out below:

	Oil and gas	Distribution	Unallocated (* )	Eliminations and adjustments (** )	Total
<b>Revenues</b>					
External customers	517,933	1,245,159	–	–	1,763,092
Inter-segment	–	121,329	–	(121,329)	–
<b>Total revenue</b>	<b>517,933</b>	<b>1,366,488</b>	<b>–</b>	<b>(121,329)</b>	<b>1,763,092</b>
Depreciation and depletion of PPE	(130,738)	(182,274)	–	–	(313,012)
Other costs	(15,705)	(2,122)	–	2,122	(15,705)
Transportation tariffs	(183,545)	–	–	119,207	(64,338)
General and administrative expenses	(2,693)	(255,808)	(7,119)	–	(265,620)
Other income	1,070	3,376	21,847	–	26,293
Interest income	–	547	180,764	(147,310)	34,001
Finance costs	(51,125)	(203,904)	(309,624)	147,310	(417,343)
Share of result of associates	–	68,380	–	–	68,380
Foreign exchange loss, net	(1)	(2,717)	–	–	(2,718)
Income tax expense	–	(17,633)	–	–	(17,633)
<b>Net profit/(loss) for the year</b>	<b>135,196</b>	<b>774,333</b>	<b>(114,132)</b>	<b>–</b>	<b>795,397</b>

(\*) These numbers include unallocated transactions managed and recognised 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 and adjustments (**)	Total
Investment in associate	–	264,574	–	–	264,574
Other reportable segment assets	3,601,573	7,630,526	7,667,991	(6,491,942)	12,408,148
<b>Total reportable segment assets</b>	<b>3,601,573</b>	<b>7,895,100</b>	<b>7,667,991</b>	<b>(6,491,942)</b>	<b>12,672,722</b>
Other reportable segment liabilities	(3,692,307)	(4,219,177)	(6,875,309)	6,139,289	(8,647,504)
<b>Total reportable segment liabilities</b>	<b>(3,692,307)</b>	<b>(4,219,177)</b>	<b>(6,875,309)</b>	<b>6,139,289</b>	<b>(8,647,504)</b>
<b>Capital expenditure (***)</b>					
Additions	53,359	2,976	–	–	56,335
<b>Total capital expenditures</b>	<b>53,359</b>	<b>2,976</b>	<b>–</b>	<b>–</b>	<b>56,335</b>

*(\*) These numbers include unallocated assets and liabilities managed and recognised 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 for the year ended 31 December 2020 is set out below:

	Oil and gas	Distribution	Unallocated (*)	Eliminations and adjustments (**)	Total
<b>Revenues</b>					
External customers	193,077	668,474	–	–	861,551
Inter-segment	–	61,674	–	(61,674)	–
<b>Total revenue</b>	<b>193,077</b>	<b>730,148</b>	<b>–</b>	<b>(61,674)</b>	<b>861,551</b>
Depreciation and depletion of PPE	(136,265)	(148,807)	–	–	(285,072)
Other costs	(10,462)	(1,573)	–	1,573	(10,462)
Transportation tariffs	(78,270)	–	–	60,101	(18,169)
General and administrative expenses	(2,785)	(198,787)	(2,316)	–	(203,888)
Other income	884	1,463	17,431	–	19,778
Interest income	–	390	250,004	(213,036)	37,358
Finance costs	(82,078)	(221,028)	(283,003)	190,604	(395,505)
Share of result of associates	–	17,265	–	–	17,265
Foreign exchange loss, net	(2)	(1,647)	–	–	(1,649)
Income tax expense	–	(8,135)	–	–	(8,135)
<b>Net (loss)/profit for the year</b>	<b>(115,901)</b>	<b>169,289</b>	<b>(17,884)</b>	<b>(22,432)</b>	<b>13,072</b>

*(\*) These numbers include unallocated transactions managed and recognised 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 and adjustments (**)	Total
Investment in associate	–	249,448	–	–	249,448
Other reportable segment assets	3,522,295	7,743,252	8,213,133	(7,051,457)	12,427,223
<b>Total reportable segment assets</b>	<b>3,522,295</b>	<b>7,992,700</b>	<b>8,213,133</b>	<b>(7,051,457)</b>	<b>12,676,671</b>
Other reportable segment liabilities	(3,748,223)	(5,108,904)	(7,295,734)	6,703,785	(9,449,076)
<b>Total reportable segment liabilities</b>	<b>(3,748,223)</b>	<b>(5,108,904)</b>	<b>(7,295,734)</b>	<b>6,703,785</b>	<b>(9,449,076)</b>
<b>Capital expenditure (***)</b>					
Additions	90,312	73,115	–	(22,432)	140,995
Additions – investment in associate	–	16,576	–	–	16,576
<b>Total capital expenditures</b>	<b>90,312</b>	<b>89,691</b>	<b>–</b>	<b>(22,432)</b>	<b>157,571</b>

(\*) *These numbers include unallocated assets and liabilities managed and recognised 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**

The Group's revenue is generated from sales of natural gas and crude oil produced in Azerbaijan and sold to customers in Azerbaijan, Georgia, Turkey and Europe. The Group also recognises revenue from transportation of natural gas to relevant delivery points in Azerbaijan, Georgia and Turkey.

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

	2021	2020
Azerbaijan	4,454,142	4,544,235
Turkey	6,120,651	6,282,247
Georgia	466,137	470,571
Switzerland	264,574	249,448
<b>Total</b>	<b>11,305,504</b>	<b>11,546,501</b>

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:

	<b>Oil and gas production properties</b>	<b>Pipeline assets</b>	<b>Decommis- sioning costs</b>	<b>Total</b>
<b>Cost</b>				
<b>At 31 December 2019</b>	<b>2,055,239</b>	<b>4,783,240</b>	<b>114,825</b>	<b>6,953,304</b>
Additions	69,834	18,862	17,303	<b>105,999</b>
Transfers from development costs and construction in progress	–	2,482,561	18,984	<b>2,501,545</b>
<b>At 31 December 2020</b>	<b>2,125,073</b>	<b>7,284,663</b>	<b>151,112</b>	<b>9,560,848</b>
Additions	45,642	2,976	7,717	<b>56,335</b>
<b>At 31 December 2021</b>	<b>2,170,715</b>	<b>7,287,639</b>	<b>158,829</b>	<b>9,617,183</b>
<b>Accumulated depletion and depreciation</b>				
<b>At 31 December 2019</b>	<b>(346,065)</b>	<b>(186,312)</b>	<b>(17,635)</b>	<b>(550,012)</b>
Charge for the year	(124,575)	(148,236)	(12,261)	<b>(285,072)</b>
<b>At 31 December 2020</b>	<b>(470,640)</b>	<b>(334,548)</b>	<b>(29,896)</b>	<b>(835,084)</b>
Charge for the year	(121,027)	(182,274)	(9,711)	<b>(313,012)</b>
<b>At 31 December 2021</b>	<b>(591,667)</b>	<b>(516,822)</b>	<b>(39,607)</b>	<b>(1,148,096)</b>
<b>Net book value</b>				
<b>At 31 December 2021</b>	<b>1,579,048</b>	<b>6,770,817</b>	<b>119,222</b>	<b>8,469,087</b>
<b>At 31 December 2020</b>	<b>1,654,433</b>	<b>6,950,115</b>	<b>121,216</b>	<b>8,725,764</b>

**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 the SD project.

**Pipeline assets**

The pipeline cost represents the Group's 6.67% share in cost of construction of SCP pipeline and cost of construction of TANAP pipeline.

Construction of TANAP pipeline consisted of two phases: Phase 0 and Phase 1. Construction of the Phase 0, the pipeline's section for gas delivery to BOTAS from the Georgia/Turkey border to Eskishehir, was completed on 30 June 2018. The Phase 1, the construction, as well as testing and commissioning, of the pipeline section from Eskishehir to Turkey/Greece border, was completed by 30 June 2020 and respective accumulated costs amounting to US dollars 2,482,561 were transferred from construction in progress to pipeline assets.

**Decommissioning costs**

The capitalised decommissioning costs are represented by the Group's 6.67% share in costs related to decommissioning of assets employed for the purposes of the SD project and the SCP project and costs related to decommissioning of assets of the TANAP project (Note 15).

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

## 7. Advance payments

Advance payments consisted of the following at 31 December:

	<b>2021</b>	<b>2020</b>
Advance payments for acquisition of shares	2,533,903	2,533,903
Other payments related to construction works	3,242	2,930
	<b>2,537,145</b>	<b>2,536,833</b>

### Advance payments for acquisition of shares

In July 2014 the Group signed the Deferred Sale and Purchase Agreement (“DSPA”) for the acquisition of additional 10% participating interest in the SD project and additional 8% shares in AGSC from Azerbaijan (Shah Deniz) Limited (“AzSD”) and 10% shares in the SCP project from Azerbaijan (South Caucasus Pipeline) Limited (“AzSCP”). The agreement was subsequently amended by the 1st Addendum to the DSPA dated 20 December 2017 and 2nd Addendum to the DSPA dated 31 May 2019. According to the terms of this agreement the Group had to 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. The Group had fulfilled all of its financial obligations before AzSD and AzSCP under the DSPA by the end of 2020 and the management expects no further cash outflows in connection with the DSPA.

Advance payments for acquisition of shares represents advances paid in the amount of US dollars 1,855 million (31 December 2020: US dollars 1,855 million) to AzSD and US dollars 679 million (31 December 2020: US dollars 679 million) to AzSCP.

## 8. Investment in associate

At 31 December 2021 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 SD natural gas to European countries. On 15 November 2020, TAP AG announced the start of commercial operations of the TAP pipeline, following which the commercial deliveries of SD natural gas to Europe commenced on 31 December 2020.

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.

The table below summarises the movements in the carrying amount of the Group’s investment in TAP AG:

	<b>2021</b>	<b>2020</b>
<b>Opening carrying amount at 1 January</b>	<b>249,448</b>	<b>211,330</b>
Additions to investment in associate	–	16,576
Divestment from associate	(55,480)	–
Share of after-tax profit or loss of associate	68,380	17,265
Share of after-tax other comprehensive income/(loss) of associate	25,477	(18,381)
Exchange differences	(23,251)	22,658
<b>Closing carrying amount at 31 December</b>	<b>264,574</b>	<b>249,448</b>

During 2021 the Board of Directors of TAP AG unanimously approved a reduction of the share capital by US dollars 277,400 (Euro 238,200 thousand) by way of cancellation of 260,294,200 registered shares of TAP AG with a nominal value of Swiss franc 1 each which was used to pay back the nominal value of each cancelled share to the respective shareholder in accordance with their shareholding percentage. The Group’s portion of reduction is US dollars 55,480 (Euro 47,640 thousand).

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***8. Investment in associate (continued)**

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

	<b>2021</b>	<b>2020</b>
Current assets	604,198	339,735
Non-current assets	5,029,563	5,660,275
Current liabilities	(461,132)	(396,992)
Non-current liabilities	(3,934,516)	(4,455,473)
<b>Net assets</b>	<b>1,238,113</b>	<b>1,147,545</b>
<b>Group's interest in net assets (20%)</b>	<b>247,623</b>	<b>229,509</b>
Goodwill recognised upon acquisition	18,872	18,872
Exchange differences on translation of goodwill	(1,921)	1,067
<b>Carrying value</b>	<b>264,574</b>	<b>249,448</b>

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

	<b>2021</b>	<b>2020</b>
Revenue	900,755	192,338
Operating expenses	(493,195)	(90,694)
<b>Profit before tax</b>	<b>407,560</b>	<b>101,644</b>
Income tax expense	(65,662)	(15,317)
<b>Net profit for the year</b>	<b>341,898</b>	<b>86,327</b>
<b>Group's share of net profit (20%)</b>	<b>68,380</b>	<b>17,265</b>
<b>Other comprehensive income/(loss) for the year, net of tax (20%)</b>	<b>127,384</b>	<b>(91,905)</b>
<b>Group's share of total comprehensive income/(loss) (Note 13)</b>	<b>25,477</b>	<b>(18,381)</b>

**9. Loan receivables**

As at 31 December 2021 the Group had loan receivables from Boru Hatları İle Petrol Taşıma A.Ş. ("BOTAS") and SOCAR Turkey Enerji A.Ş. ("STEAS") in the amount of US dollars 204,783 and US dollars 341,992, respectively (31 December 2020: US dollars 243,162 and US dollars 389,113, respectively).

Receivables from BOTAS represent deferred consideration in the amount of US dollars 9,790 (31 December 2020: US dollars 15,730) and loan receivable in the amount of US dollars 194,993 (31 December 2020: US dollars 227,432).

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 which does not bear interest. 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 2021 was US dollars 440 (2020: US dollars 1,716) and it was recognised within interest income.

According to the Funding Agreement, following the sale of 30% shares of TANAP A.Ş., the Company financed cash call requirements of BOTAS relating to 5% share in TANAP A.Ş. As at 31 December 2020 the Company has fulfilled all of its outstanding financial obligations under the Funding Agreement and the management expect no further cash outflows in connection with the Funding Agreement. The loan is expected to be repaid by 31 December 2025. Interest income earned in respect of the loan receivable from BOTAS during the year ended 31 December 2021 was US dollars 9,957 (2020: US dollars 9,524). At 31 December 2021 ECL recognised by the Group on loan receivable from BOTAS was US dollars 8,517 (31 December 2020: US dollars 10,341).

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

## 9. Loan receivables (continued)

During 2021 the Company received US dollars 50,600 (2020: US dollars 19,250) in respect of total receivables from BOTAS.

Loan receivables from STEAS represent only deferred consideration in the amount of US dollars 341,992 (31 December 2020: US dollars 344,543) as other loan receivable as of 31 December 2021 in respect of Cash Call Obligation (as defined below) was nil (31 December 2020: US dollars 44,570).

On 9 February 2018 the Company entered into sale and purchase agreement ("TANAP SPA") with STEAS to sell 7% shares in TANAP A.Ş. Pursuant to the TANAP SPA, the Company sold 7% of its loan receivables from as well as 7% equity in TANAP A.Ş. to STEAS. Fair value of total consideration amounted to US dollars 392,633 out of which US dollars 95,000 was paid on 22 February 2018. Remaining consideration in the amount of US dollars 297,633 was recognised as an interest-bearing deferred consideration at the rate of 5.74% per annum. During the year ended 31 December 2021 the Company received US dollars 24,638 from STEAS in respect of accrued interest of deferred consideration (2020: US dollars 2,700) and remaining outstanding amount is expected to be repaid by 31 December 2026. Income earned in respect of the deferred consideration from STEAS during the year ended 31 December 2021 was US dollars 20,388 (2020: US dollars 19,789) and was recognised within interest income. At 31 December 2021 ECL recognised by the Group deferred consideration from STEAS was US dollars 1,890 (31 December 2020: US dollars 3,589).

According to TANAP SPA, following the sale of 7% shares in TANAP A.Ş., the Company financed cash call requirements of STEAS relating to 7% interest in TANAP A.Ş. until 1 January 2020 ("Cash Call Obligation"). During the year ended 31 December 2021 the Company received final repayment in the amount of US dollars 46,202 from STEAS in respect of Cash Call Obligation. Interest income earned in respect of the Cash Call Obligation from STEAS during the year ended 31 December 2021 was US dollars 1,632 (2020: US dollars 3,888).

## 10. Right-of-use asset and lease liabilities

The Group has lease agreements for rent of buildings and construction assets and vehicles used in its operations with lease terms of 6 years and 2 years, respectively. The Group's obligations under its leases are secured by the lessor's title to the leased assets. Generally, the Group is restricted from assigning and subleasing the leased assets.

The Group also has certain lease agreements with lease terms of 12 months or less and leases with low value. The Group applies the 'short-term lease' and 'lease of low-value assets' recognition exemptions for these leases.

Set out below are the carrying amounts of the Group's right-of-use assets recognised and the movements during the period:

	<b>Buildings and construction</b>	<b>Vehicles</b>	<b>Total</b>
<b>As at 1 January 2020</b>	<b>31,710</b>	<b>1,166</b>	<b>32,876</b>
Depreciation charge for the year	(5,765)	(712)	<b>(6,477)</b>
<b>As at 31 December 2020</b>	<b>25,945</b>	<b>454</b>	<b>26,399</b>
Depreciation charge for the year	(5,765)	(454)	<b>(6,219)</b>
<b>As at 31 December 2021</b>	<b>20,180</b>	<b>–</b>	<b>20,180</b>

Set out below are the carrying amounts of lease liabilities and the movements during the period:

	<b>2021</b>	<b>2020</b>
<b>As at 1 January</b>	<b>28,517</b>	<b>34,301</b>
Interest expense	1,688	2,070
Payments	(7,181)	(7,854)
<b>As at 31 December</b>	<b>23,024</b>	<b>28,517</b>

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***10. Right-of-use asset and lease liabilities (continued)**

The Group presents its lease liabilities as non-current and current which were as follows at reporting date:

Balances of non-current and current lease liabilities were as follows:

	<b>31 December 2021</b>	<b>31 December 2020</b>
Non-current lease liabilities	17,186	24,404
Current lease liabilities	5,838	4,113
<b>Total liabilities from leasing activities</b>	<b>23,024</b>	<b>28,517</b>

Current portion of lease liabilities is the present value of future leases payments payable in one-year period after reporting date. The maturity analysis for lease liabilities is described in Note 22.

**11. Cash and cash equivalents, deposits**

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

	<b>2021</b>	<b>2020</b>
Cash at bank, USD	208,807	57,236
Cash at bank, CHF	25,123	415
Cash at bank, TRY	1,322	259
Cash at bank, other	229	45
<b>Total cash and cash equivalents</b>	<b>235,481</b>	<b>57,955</b>

**Deposits**

As at 31 December 2020 the Group had deposit balance US dollars 278,927. During 2021, the Group placed to the deposit balance US dollars 330,000 and made withdrawal in the amount of US dollars 289,128. Income earned in respect of deposit balance with average interest rate 0.19% (2020: 0.61%) in the amount of US dollars 480 (2020: US dollars 1,079) was recognized within interest income. As at 31 December 2021 the Group recognised ECL on deposit in the amount of US dollars 4 (31 December 2020: US dollars 3) and the Group's deposit as at 31 December 2021 was US dollars 320,278.

**12. Accounts receivable**

Accounts receivable consisted of the following at 31 December:

	<b>2021</b>	<b>2020</b>
Receivable from AGSC	149,532	54,704
Receivable from BOTAS	36,799	36,526
Receivable from the SD Operator	12,985	11,704
Receivable from crude oil sales to third parties	13,029	7,157
<b>Total accounts receivable</b>	<b>212,345</b>	<b>110,091</b>

**Receivable from BOTAS**

The ownership of gas in TANAP pipeline system belongs to BOTAS and AGSC, and TANAP A.Ş. is obliged to deliver the gas to the exit points under respective Gas Transportation Agreements. During the year ended 31 December 2021 the Group recognised revenue from BOTAS in the amount of US dollars 430,461 (2020: US dollars 364,325) and as at 31 December 2021 account receivable from BOTAS amounted to US dollars 36,799 (31 December 2020: US dollars 36,526).

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

## 12. Accounts receivable (continued)

### Receivable from AGSC

During the year ended 31 December 2021 the Group recognised revenue from AGSC in the amount of US dollars 808,113 (2020: US dollars 296,861) and as at 31 December 2021 receivable from AGSC for transportation of gas through TANAP pipeline was US dollars 81,746 (2020: US dollars 49,098). In addition, the Group recognised receivable from AGSC in the amount of US dollars 67,786 as at 31 December 2021 (31 December 2020: US dollars 5,606) for SD natural gas sold to the parties under relevant gas sales agreements.

### Receivable from crude oil sales to third parties

Receivables from crude oil sales represent a petroleum sold to third parties, for which no consideration was transferred to the Group as of 31 December 2021 and 2020.

## 13. Share capital, additional paid-in capital, other reserves and non-controlling interest

### Share capital and additional paid-in capital

As at 31 December 2021 and 31 December 2020 the Company had authorised, issued and fully paid 100 ordinary shares at par at US dollars 24,158 each. Each share entitles one vote to the shareholder. As at 31 December 2021 and 31 December 2020 additional paid-in capital amounted to US dollars 31,481.

### Other reserves

On 13 April 2015 the Company sold its 30% interest in its subsidiary – TANAP A.Ş. to BOTAS. In addition, on 16 April 2015 the Company sold 12% interest in its subsidiary – TANAP A.Ş. to BP Pipelines (TANAP) Limited (“BP”). The difference between the net book value of interest in net assets sold (US dollars 338,831) and the fair value of considerations received from BOTAS and BP was recognised as loss on sale of share in subsidiary in other reserves in the amount of US dollars 45,176.

On 9 February 2018 the Company sold to STEAS 7% interest in its subsidiary– TANAP A.Ş. The difference between the net book value of equity interest (US dollars 179,359) and the fair value of consideration received from STEAS was recognised as gain on sale of share in subsidiary in other reserves in the amount of US dollars 10,995.

In May 2019, the Group’s associate – TAP AG entered into hedge relations to hedge the risk arising from its loans and signed interest rate swap agreements. As the result of change in fair value of hedge instrument, TAP AG recognized other comprehensive income in the amount of US dollars 127,385 for the year ended 31 December 2021 (2020: loss in the amount of US dollars 91,905) and the Group’s share in this income amounted US dollars 25,477 (2020: loss in the amount of US dollars 18,381).

## 14. Borrowings and Government grant

As at 31 December 2021 and 2020 interest-bearing borrowings were comprised of the following:

Facility	31 December 2021	31 December 2020
Bonds	4,389,529	4,720,831
Loans from non-controlling shareholders	1,043,724	1,349,418
Loans from financial institutions	2,242,779	2,415,693
<b>Total borrowings</b>	<b>7,676,032</b>	<b>8,485,942</b>



*(Amounts presented are in thousands of US dollars, unless otherwise stated)***14. Borrowings and Government grant (continued)**

Original currency and maturities of the borrowings as at 31 December 2021 are presented below:

Facility	Original currency	Maturity date	31 December 2021	
			Non-current portion	Current portion
Bonds issued to SOFAZ	USD	May-November 2024	2,315,798	3,981
Eurobond 1	USD	March 2026	988,758	23,822
Eurobond 2	USD	March 2026	1,057,170	–
Loan from BOTAS	USD	December 2036	469,953	371,286
Loan from Commercial Banks guaranteed by BP International Limited	USD	March 2025	180,268	148,515
Loan from BP	USD	December 2036	6,754	–
Loan from STEAS	USD	December 2036	109,098	86,633
Loan from IBRD	USD	December 2046	382,660	16,000
Loan from AIIB	USD	December 2046	569,929	23,260
Loan from EBRD	USD	October 2035	423,314	33,000
Loan guaranteed by ADB	USD	December 2032	422,125	43,708
<b>Total borrowings</b>			<b>6,925,827</b>	<b>750,205</b>

Original currency and maturities of the borrowings as at 31 December 2020 are presented below:

Facility	Original currency	Maturity date	31 December 2020	
			Non-current portion	Current portion
Bonds issued to SOFAZ	USD	May-November 2024	2,231,740	412,475
Eurobond 1	USD	March 2026	988,758	22,765
Eurobond 2	USD	March 2026	1,065,094	–
Loan from BOTAS	USD	December 2036	811,622	274,348
Loan from Commercial Banks guaranteed by BP International Limited	USD	March 2025	317,968	109,739
Loan from BP	USD	December 2036	7,602	–
Loan from STEAS	USD	December 2036	191,830	64,015
Loan from IBRD	USD	December 2046	398,657	–
Loan from AIIB	USD	December 2046	592,836	–
Loan from EBRD	USD	October 2035	455,425	33,000
Loan guaranteed by ADB	USD	December 2032	464,360	43,708
<b>Total borrowings</b>			<b>7,525,892</b>	<b>960,050</b>

As at 31 December 2021, the Group's exposures to borrowings with variable interest rates linked to US dollar 1 month LIBOR and US dollar 6 months LIBOR are equal to US dollars 1,372,507 and US dollars 3,835,115, respectively (31 December 2020: US dollars 1,777,124 and US dollars 4,233,544, respectively).

**Government grant**

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. 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 recognised US dollars 704,270 of difference between fair value and nominal amount of the bond as government grant in its consolidated statement of financial position.

During the year ended 31 December 2021 the Group recognized income from government grant in the amount of US dollars 21,847 which was recognized within other income (2020: US dollars 26,375).

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***14. Borrowings and Government grant (continued)****Changes in liabilities arising from financing activities**

	<b>1 January 2021</b>	<b>Cash flows</b>	<b>Non-cash flows</b>	<b>Finance cost</b>	<b>31 December 2021</b>
Non-current interest-bearing loans and borrowings	7,525,892	–	(974,742)	374,677	6,925,827
Non-current lease liabilities	24,404	–	(8,663)	1,445	17,186
Current lease liabilities	4,113	(7,181)	8,663	243	5,838
Current interest-bearing loans and borrowings	960,050	(1,195,636)	974,742	11,049	750,205
<b>Total liabilities from financing activities</b>	<b>8,514,459</b>	<b>(1,202,817)</b>	<b>–</b>	<b>387,414</b>	<b>7,699,056</b>
	<b>1 January 2020</b>	<b>Cash flows</b>	<b>Non-cash flows</b>	<b>Finance cost</b>	<b>31 December 2020</b>
Non-current interest-bearing loans and borrowings	8,268,105	98,388	(1,244,821)	404,220	7,525,892
Non-current lease liabilities	28,794	–	(6,177)	1,787	24,404
Current lease liabilities	5,507	(7,854)	6,177	283	4,113
Current interest-bearing loans and borrowings	192,507	(486,043)	1,244,821	8,765	960,050
<b>Total liabilities from financing activities</b>	<b>8,494,913</b>	<b>(395,509)</b>	<b>–</b>	<b>415,055</b>	<b>8,514,459</b>

**15. 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:

	<b>31 December 2021</b>	<b>31 December 2020</b>
<b>Opening carrying amount</b>	<b>183,052</b>	<b>157,704</b>
Additional liability during the year	7,700	10,752
Unwinding of present value discount	8,554	8,050
Effect of discount rate revision	152	6,546
<b>Closing carrying amount</b>	<b>199,458</b>	<b>183,052</b>

Under the provisions of the SD PSA, SCP and TANAP 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, SCP and TANAP.

The maximum amount of decommissioning fund cannot exceed 10% of the capital costs in accordance with the 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 the SD PSA was US dollars 231,317 as at 31 December 2021 (31 December 2020: US dollars 220,302). The Group used a 3% (31 December 2020: 2.9%) inflation rate in its estimate of the retirement obligation. The Group used a 4.08% (31 December 2020: 4.1%) rate that reflects current market assessments of the time value of money to discount expected decommissioning costs.

The Group's share of expected undiscounted cost to decommission the SCP pipeline facilities at 31 December 2021 was US dollars 36,566 (31 December 2020: US dollars 34,634). The Group used a 2.5% (31 December 2020: 2.5%) inflation rate in its estimate of the retirement obligation upon termination of HGA. The Group used a 8% (31 December 2020: 8%) rate that reflects current market assessments of the time value of money to discount expected decommissioning costs.

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

## 15. Decommissioning liabilities (continued)

The Group's share of expected undiscounted cost to decommission the TANAP pipeline facilities at 31 December 2021 was US dollars 219,421 (31 December 2020: US dollars 219,421). The Group used a 2.24% (31 December 2020: 1.5%) inflation rate in its estimate of the retirement obligation upon termination of HGA. The Group used a 6.7% (31 December 2020: 6%) pre-tax rate that reflects current market assessments of the time value of money to discount expected decommissioning costs.

## 16. Trade and other payables accrued liabilities

Trade and other payables and accrued liabilities mainly consist of payables related to SD Stage 2 development, operation of SCP expansion and TANAP Phase 0 and 1 as at 31 December 2021 and 31 December 2020.

## 17. Revenue

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

	<u>2021</u>	<u>2020</u>
Revenue from sale of gas	382,840	137,418
Revenue from sale of crude oil	135,093	55,659
Revenue from transportation of gas	1,245,159	668,474
<b>Total revenue</b>	<b><u>1,763,092</u></b>	<b><u>861,551</u></b>

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 four quarters of both years presented the profit oil and gas was shared at a ratio of 55% to 45% in favour of the Contractor Parties.

Set out below is the disaggregation of the Group's revenue from contracts with customers as of 31 December:

<u>31 December 2021</u>	<u>Oil and gas</u>	<u>Distribution</u>	<u>Total</u>
<b>Type of goods/service</b>			
Sale of natural gas	382,840	–	<b>382,840</b>
Sale of crude oil	135,093	–	<b>135,093</b>
Transportation revenue	–	1,245,159	<b>1,245,159</b>
<b>Total</b>	<b><u>517,933</u></b>	<b><u>1,245,159</u></b>	<b><u>1,763,092</u></b>
Azerbaijan	517,933	4,412	<b>522,345</b>
Georgia	–	2,173	<b>2,173</b>
Turkey	–	1,238,574	<b>1,238,574</b>
<b>Total</b>	<b><u>517,933</u></b>	<b><u>1,245,159</u></b>	<b><u>1,763,092</u></b>
Good transferred at a point in time	517,933	–	<b>517,933</b>
Services transferred over time	–	1,245,159	<b>1,245,159</b>
<b>Total</b>	<b><u>517,933</u></b>	<b><u>1,245,159</u></b>	<b><u>1,763,092</u></b>

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***17. Revenue (continued)**

<b>31 December 2020</b>	<b>Oil and gas</b>	<b>Distribution</b>	<b>Total</b>
<b>Type of goods/service</b>			
Sale of natural gas	137,418	–	<b>137,418</b>
Sale of crude oil	55,659	–	<b>55,659</b>
Transportation revenue	–	668,474	<b>668,474</b>
<b>Total</b>	<b>193,077</b>	<b>668,474</b>	<b>861,551</b>
Azerbaijan	193,077	4,883	<b>197,960</b>
Georgia	–	2,405	<b>2,405</b>
Turkey	–	661,186	<b>661,186</b>
<b>Total</b>	<b>193,077</b>	<b>668,474</b>	<b>861,551</b>
Good transferred at a point in time	193,077	–	<b>193,077</b>
Services transferred over time	–	668,474	<b>668,474</b>
<b>Total</b>	<b>193,077</b>	<b>668,474</b>	<b>861,551</b>

**18. Cost of sales**

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

	<b>Note</b>	<b>2021</b>	<b>2020</b>
Depreciation and depletion of oil and gas properties	6	313,012	285,072
Other costs	5	15,705	10,462
		<b>328,717</b>	<b>295,534</b>

**19. Interest income**

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

	<b>Note</b>	<b>2021</b>	<b>2020</b>
Accrued income on loan receivable from STEAS	9	22,020	23,677
Accrued income on loan receivable from BOTAS	9	10,397	11,240
Income on deposits	11	480	1,079
Other interest income		1,104	1,362
<b>Total interest income</b>		<b>34,001</b>	<b>37,358</b>

**20. Taxation**

The Group's income tax expenses consisted of the following for the year ended 31 December:

	<b>2021</b>	<b>2020</b>
Current income tax charge	9,612	5,139
Deferred tax charge	8,021	2,996
<b>Income tax expenses</b>	<b>17,633</b>	<b>8,135</b>

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

## 20. Taxation (continued)

Reconciliation between the expected and the actual tax charge is provided below:

	2021	2020
<b>Profit before tax</b>	<b>813,195</b>	<b>21,207</b>
<b>Theoretical tax charge at statutory rate of 20 per cent</b>	<b>162,639</b>	<b>4,241</b>
Effects of different tax rate for a subsidiary (27 per cent)	2,602	1,378
(Income)/loss which is tax exempt	(149,272)	182
Other	1,664	2,334
<b>Income tax expense reported in profit or loss</b>	<b>17,633</b>	<b>8,135</b>

The Group does not file a consolidated tax return. In the context of the Group's current structure, tax losses and current tax assets of different Group companies may not be offset against current tax liabilities and taxable profits of other Group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

In accordance with Azerbaijani tax legislation, tax losses arising at any period can be carried forward for five years. SGC CJSC has accumulated losses in the amount of US dollars 764,530 in 2021 statutory books (2020: US dollars 638,657) which are not expected to be fully utilised within five years. The Group did not recognise deferred tax assets on these losses.

The temporary differences associated with investments in the Group's subsidiaries for which a deferred tax liability has not been recognised as at 31 December 2021 aggregate to US dollars 673,915 (31 December 2020: US dollars 7,955). The Group expects that the undistributed profits of its subsidiaries will not be distributed in the foreseeable future.

The Group's income tax payable as at 31 December 2021 was equal to US dollars 8,842 (31 December 2020: US dollars 6,878).

### Taxation under the SD Project

According to the provisions of the 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 the 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 2021 and 2020 the Group had no income taxes from the activities in the SD PSA as it declared losses in the tax books. There is no time limit on utilisation of accumulated losses.

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

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

## 20. Taxation (continued)

### Taxation under the SCP project (continued)

#### 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 2021 and 2020.

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). As at 31 December 2021, the Group's portion in the deferred tax liabilities of SCPC equalled to US dollars 20,033 (31 December 2020: US dollars 13,433).

#### Operating tax of TANAP A.Ş

As per the HGA between the Republic of Turkey and TANAP A.Ş., it was determined that the corporate income tax of TANAP A.Ş. will only be based on the amount of natural gas transmitted from the pipeline after the pipeline is put in use. According to tax ruling received on 7 April 2017 TANAP A.Ş. is not subject to corporate tax. TANAP A.Ş. is required to pay tax of US dollars 6.31 per thousand cubic metrics of gas measured at entry point (2020: US dollars 6.19 per thousand cubic metrics of gas).

## 21. Transactions with related parties

Transactions with related parties under the common control consisted of the following:

Related party	As at 31 December 2021					For the year ended 31 December 2021	
	Borrowings	Advance payments	Accounts receivable	Loan receivables	Revenue	Receipts from related parties	Payments to related parties
SOFAZ (Note 14)	2,319,779	–	–	–	–	–	441,437
AzSD (Note 7)	–	1,854,770	–	–	–	–	–
AzSCP (Note 7)	–	679,133	–	–	–	–	–
SOCAR MO	–	–	–	–	–	–	531
AGSC	–	–	149,532	–	1,114,398	1,019,570	–
BOTAS (Note 9, 14)	841,239	–	–	204,783	430,461	444,263	50,600
STEAS (Note 9, 14)	195,731	–	–	341,992	–	70,840	70,840
<b>Total for related parties</b>	<b>3,356,749</b>	<b>2,533,903</b>	<b>149,532</b>	<b>546,775</b>	<b>1,544,859</b>	<b>1,534,673</b>	<b>563,408</b>
<b>Total for related and unrelated parties</b>	<b>7,676,032</b>	<b>2,537,145</b>	<b>212,345</b>	<b>546,775</b>	<b>1,763,092</b>		

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***21. Transactions with related parties (continued)**

Related party	As at 31 December 2020					For the year ended 31 December 2020	
	Borrowings	Advance payments	Accounts receivable	Loan receivables	Revenue	Receipts from related parties	Payments to related parties
SOFAZ (Note 14)	2,644,215	–	–	–	–	–	–
AzSD (Note 7)	–	1,854,770	–	–	–	–	–
AzSCP (Note 7)	–	679,133	–	–	–	3,053	–
SOCAR MO	–	–	–	–	–	–	279
AGSC	–	–	54,704	–	296,861	377,454	–
BOTAS (Note 9, 14)	1,085,970	–	–	243,162	364,325	347,049	19,250
STEAS (Note 9, 14)	255,845	–	–	389,113	–	26,950	26,950
<b>Total for related parties</b>	<b>3,986,030</b>	<b>2,533,903</b>	<b>54,704</b>	<b>632,275</b>	<b>661,186</b>	<b>754,506</b>	<b>46,479</b>
<b>Total for related and unrelated parties</b>	<b>8,485,942</b>	<b>2,536,833</b>	<b>110,091</b>	<b>632,275</b>	<b>861,551</b>		

**SOCAR MO**

According to the crude oil sales agency agreement, the Group appointed SOCAR Marketing and Operations Department (“SOCAR MO”), a subsidiary of SOCAR, as its trading and marketing agent in respect of the SD 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.

**AGSC**

AGSC is a company established by the contractor parties of the SD PSA for marketing, accounting, billing, payment and reporting and other administrative activities related to the sales of SD gas. Receipts from AGSC represent cash received in the amount of US dollars 253,611 (2020: US dollars 112,147) from sale of gas to AGSC and transportation of natural gas by TANAP in the amount of US dollars 773,627 for the year ended 31 December 2021 (2020: 265,307).

Commitments to related parties under the common control are disclosed in Note 23.

**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 2021 and 2020. 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 is shown below:

	2021	2020
Aggregate remuneration	244	230
Number of persons	5	5

The Company 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 1,667 during the year ended 31 December 2021 (2020: US dollars 1,162) under the Operator Services Agreement signed in December 2014.

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

## 22. 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 program focuses on the unpredictability of financial markets and seeks to minimise 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) Interest rate risk

The Group is subject to interest rate risk on financial liabilities and assets with variable interest rates. To mitigate this risk, the Group's management performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis.

The floating rate for majority of interest-bearing liabilities and assets exposes the Group to fluctuation in interest payments and receipts mainly due to changes in LIBOR.

2021	Change in floating variable		Effect on profit before tax	
	Increase	Decrease	After increase	After decrease
LIBOR	+1.25	-0.25	(25,826)	4,838

  

2020	Change in floating variable		Effect on profit before tax	
	Increase	Decrease	After increase	After decrease
LIBOR	+1.00	-0.25	(33,219)	7,836

#### (ii) 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, accounts receivable and other current and non-current assets 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 1,317,616 and US dollars 1,082,232 as at 31 December 2021 and 31 December 2020, respectively.

The Group places its cash with high credit quality financial institutions, primarily with those rated A1 by credit rating agencies. The Group generally trades with recognised and reputable third parties. It is the Group's policy that all customers who wish to trade for condensate are required to procure the issuance of letters of credit. Gas sales are made through AGSC to state-owned entities or entities with strong financial position.

#### (iii) 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)***22. Financial risk management objectives and policies (continued)****Financial risk factors (continued)**

The tables below summarise the maturity profile of the Group's financial liabilities at 31 December 2021 and 2020 based on contractual undiscounted payments:

<b>2021</b>	<b>On demand</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>&gt;5 years</b>	<b>Total</b>
Trade and other payables	–	54,155	–	–	<b>54,155</b>
Accrued liabilities	–	39,675	–	–	<b>39,675</b>
Lease liabilities	1,769	5,396	18,681	–	<b>25,846</b>
Interest-bearing borrowings	–	936,393	6,573,990	1,598,761	<b>9,109,144</b>
<b>Total</b>	<b>1,769</b>	<b>1,035,619</b>	<b>6,592,671</b>	<b>1,598,761</b>	<b>9,228,820</b>

  

<b>2020</b>	<b>On demand</b>	<b>3 to 12 months</b>	<b>1 to 5 years</b>	<b>&gt;5 years</b>	<b>Total</b>
Trade and other payables	–	46,967	–	–	<b>46,967</b>
Accrued liabilities	–	47,923	–	–	<b>47,923</b>
Lease liabilities	1,890	5,625	25,846	–	<b>33,361</b>
Interest-bearing borrowings	–	1,139,588	5,350,118	3,809,504	<b>10,299,210</b>
<b>Total</b>	<b>1,890</b>	<b>1,240,103</b>	<b>5,375,964</b>	<b>3,809,504</b>	<b>10,427,461</b>

**(iv) Foreign exchange risk**

The Company's functional currency is USD, and financial assets/liabilities are primarily denominated in USD. The Company is exposed to foreign currency risk arising through the impact of the rate changes on the translation to foreign currency denominated assets and liabilities. Foreign exchange risk arises due to future transactions and recorded assets and liabilities. These risks are balanced with monitoring and analysing of foreign currency position.

**(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:

	<b>31 December 2021</b>	<b>31 December 2020</b>
Long-term borrowings (Note 14)	6,925,827	7,525,892
Short-term and current portion of long-term borrowings (Note 14)	750,205	960,050
Less: cash and cash equivalents (Note 11)	(235,481)	(57,955)
<b>Net debt</b>	<b>7,440,551</b>	<b>8,427,987</b>
Equity attributable to the Parent's equity holders	2,236,604	1,778,372
<b>Capital</b>	<b>9,677,155</b>	<b>10,206,359</b>
<b>Gearing ratio</b>	<b>77%</b>	<b>83%</b>

The current target of the Group's capital management is to maintain the debt-to-equity ratio within 75-85%: 25-15%.

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***22. Financial risk management objectives and policies (continued)****Financial risk factors (continued)****(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, judgement 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.

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:

	<b>31 December 2021</b>	
	<b>Carrying amounts</b>	<b>Fair values</b>
Cash and cash equivalents (Note 11)	235,481	235,481
Deposits (Note 11)	320,278	320,278
Accounts receivable (Note 12)	212,345	212,345
Other current assets	2,078	2,078
Other non-current assets	659	659
Loan receivables (Note 9)	546,775	557,917
<b>Total financial assets</b>	<b>1,317,616</b>	<b>1,328,758</b>
Trade and other payables	(54,155)	(54,155)
Accrued liabilities (Note 16)	(39,675)	(39,675)
Short-term and current portion of long-term borrowings (Note 14)	(750,205)	(750,205)
Eurobonds (Note 14)	(2,045,928)	(2,304,080)
Long-term borrowings (fixed rate), excluding Eurobonds (Note 14)	(382,660)	(375,684)
Long-term borrowings (floating rate) (Note 14)	(4,497,239)	(4,498,193)
<b>Total financial liabilities</b>	<b>(7,769,862)</b>	<b>(8,021,992)</b>
	<b>31 December 2020</b>	
	<b>Carrying amounts</b>	<b>Fair values</b>
Cash and cash equivalents (Note 11)	57,955	57,955
Deposits (Note 11)	278,927	278,927
Accounts receivable (Note 12)	110,091	110,091
Other current assets	2,359	2,359
Other non-current assets	625	625
Loan receivables (Note 9)	632,275	636,019
<b>Total financial assets</b>	<b>1,082,232</b>	<b>1,085,976</b>
Trade and other payables	(46,967)	(46,967)
Accrued liabilities (Note 16)	(47,923)	(47,923)
Short-term and current portion of long-term borrowings (Note 14)	(960,050)	(960,050)
Eurobonds (Note 14)	(2,053,852)	(2,051,100)
Long-term borrowings (fixed rate), excluding Eurobonds (Note 14)	(398,657)	(393,730)
Long-term borrowings (floating rate) (Note 14)	(5,073,383)	(5,057,776)
<b>Total financial liabilities</b>	<b>(8,580,832)</b>	<b>(8,557,546)</b>

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

## 22. Financial risk management objectives and policies (continued)

### Financial risk factors (continued)

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, and individual creditworthiness of customers and the risk characteristics of the financed project.
- (iii) Eurobonds are evaluated using Level 1 inputs based on quoted market prices.

The fair values of the Group's interest-bearing borrowings and loans receivable are determined by using the discounted cash flow ("DCF") method using discount rate that reflects the market borrowing rate as at the end of the reporting period.

## 23. Commitments and contingencies

### Commitments related to participating interest in the SD PSA

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

As of 31 December 2021, the SD PSA operator has entered or is expected to enter into a number of capital commitments. The Group estimated its 6.67% share of these capital commitments in the amount of US dollars 102,097 (31 December 2020: US dollars 109,405).

### Commitment related to TAP

In late 2018 TAP AG reached financial close under the project financing in the total amount of EUR 3,962,700 (three billion nine hundred and sixty-two million seven hundred thousand) which is equivalent to US dollars 4,490,532 at the reporting date, provided by a large group of financial institutions. The Group acted as one of the guarantors of the loan facilities for the 20% shares that it holds in TAP AG. Financial Completion under the project financing was reached on 31 March 2021 and some of the guarantees of the guarantors, including that of the Group, were released on the same date. The Group, as well as the other guarantors, continues to cover potential non-payments of TAP AG post Financial Completion period arising solely due to very limited events of default.

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

#### *BOTAS Rollover GSA*

On September 30, 2021, AGSC and BOTAS executed a new gas sale and purchase agreement with respect to the sale by AGSC to BOTAS at Georgia-Turkey border of certain volumes of Gas (0.64 BCcm first partial delivery year, 2.55 BCcm second delivery year and 3.7 BCcm plateau period).

#### *Stage 2 SPA*

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 SD Stage 2 Gas (2 BCcm first delivery year, 4 BCcm second delivery year, 6 BCcm plateau period). In December 2012, SOCAR transferred and assigned the rights and obligations under Stage 2 SPA to AGSC. The commencement date under Stage 2 SPA was June 30, 2018.

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

### **23. Commitments and contingencies (continued)**

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

##### *BOTAS contract for BTC fuel gas*

AGSC is obliged under the agreement with BOTAS to make available 0.15 BCcm of gas annually until the expiry of the contract at a price, which is calculated based on the formula established in the contract.

##### *Azeri SPA*

AGSC is obliged under the agreement signed with SOCAR to make available a minimum of approximately 1.5 bcm of gas annually in 2022 and onwards at a price calculated based on the formula established in the agreement. SOCAR novated all of its rights and obligations under the Azeri SPA to "Azerkontrakt" Open Joint-Stock Company ("Azerkontrakt") with effect from June 11, 2021.

##### *Azerbaijan Rollover GSA*

On April 16, 2021, AGSC and SOCAR entered into a new gas sale and purchase agreement concerning the sales by AGSC and purchase by SOCAR of certain volumes of Shah Deniz Gas at a price calculated based on the formula established in the agreement (3.0 bcm in all delivery years, except 3.8 bcm in 2022). SOCAR novated all of its rights and obligations under the Azeri Rollover GSA to "Azerkontrakt" Open Joint-Stock Company ("Azerkontrakt") with effect from June 11, 2021.

##### *Georgian gas obligation SPA*

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 annually from 2022 to the end of 2026, at a price which is calculated based on the formula established in the contract.

##### *Sale and purchase agreement with South Caucasus Pipeline Option Gas Company Limited ("OptionCo", a wholly owned subsidiary of SCPC)*

AGSC is obliged under the agreement signed with OptionCo to make available during each contract year a maximum of five percent of the volumes transported in the previous calendar year by AGSC via SCP through territory of Georgia, at a price, which is calculated based on a formula established in the contract.

##### *SD Stage 2 EU Long term Gas Sales Agreements ("GSAs")*

In September 2013, several EU GSAs were signed by SOCAR with EU Buyers (currently: DEPA, Bulgargaz Shell, Uniper, Axpo, ENGIE, Edison, Enel, Hera) and in December 2013 the GSAs were assigned to AGSC until the SD PSA expiry with re-assignment to SOCAR as SD Production declines. The commencement date for DEPA, Uniper, Shell (1<sup>st</sup> contract), Axpo (two contracts) and Bulgargaz GSAs was 31 December 2020. The commencement date for Hera and Enel was 1 April 2021 and for Edison – 30 June 2021. The first gas date for Shell (2<sup>nd</sup> contract) and Engie was 1 June 2022.

##### *Trans Anatolian Pipeline Gas Transportation Agreement ("TANAP GTA")*

AGSC is a party to TANAP GTA with annual reserved capacity as defined in the contract. The commencement date under the GTA was 1 July 2020. Physical commercial deliveries of natural gas started on 31 December 2020.

##### *Trans Adriatic Pipeline GTAs (TAP GTAs)*

AGSC is a party to TAP GTAs with annual capacities as defined in the contracts. The commencement dates under the GTAs were 15 November 2020. Physical commercial deliveries of natural gas started on 31 December 2020.

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

## **23. Commitments and contingencies (continued)**

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

#### *SNAM GTA*

AGSC is a party to SNAM GTA with annual reserved capacity as defined in the contract. The start date (as well as physical commercial deliveries of natural gas) was 31 December 2020.

#### *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 in 2022 and 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.

#### *Tap Operational Gas Sales Agreement*

In accordance with the TAP Operational Gas Sales Agreement ("TAP OGSA"), the Company is obliged to deliver up to circa 0.17 bcm of gas per annum necessary for operations of the TAP transportation system. The contract is due to expire on 1 October 2022.

#### *BOTAS Gas Transportation Agreement ("BOTAS GTA")*

TANAP is a party to BOTAS GTA 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 was 30 June 2018.

#### *Framework agreement*

A fully-termed Framework Agreement related to the novation of long-term GSAs and transfer of GTA capacity from AGSC to SOCAR after 2036 was executed on 19 October 2015 and further amended and restated on 28 September 2018.

## **24. Current business environment**

### **Azerbaijan economy**

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.

Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of the Azerbaijan economy is largely dependent upon these reforms and the effectiveness of economic, financial and monetary measures undertaken by the government as well as crude oil prices and stability of Azerbaijani manat.

During 2021, the government continued tight monetary policy as well as allocated foreign currency resources which stabilized Azerbaijani manat. This policy is expected to continue in 2022 with the aim of maintaining macroeconomic stability.

Management believes that this event does not adversely affect the Group's results and financial position as its functional currency is US dollar and the majority of its transactions, revenues, costs, property and equipment purchases, receivables and liabilities are either priced, incurred, payable or otherwise measured primarily in US dollars and management is taking all necessary measures to support the sustainability and development of the Group's business in the foreseeable future.

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

## 24. Current business environment (continued)

### Turkey economy

Turkish economy experienced a period of instability during 2021. Such instability was followed by significant inflation and devaluation of local currency against major foreign currencies such as USD and EUR by 80% (2020: 25%) and 65% (2020: 37%), respectively.

Management believes that events described above do not adversely affect the Group's results and financial position as its functional currency is US dollar and the majority of its transactions, revenues, costs, property and equipment purchases, receivables and liabilities are either priced, incurred, payable or otherwise measured primarily in US dollars and management is taking all necessary measures to support the sustainability and development of the Group's business in the foreseeable future.

### Effect of Covid-19 pandemic

Following the rapid spread of Covid-19 pandemic in 2020, which continued in 2021, many governments introduced various measures to combat the outbreak, including travel restrictions, quarantines, closure of business and other venues and lockdown of certain areas. These measures have affected the global supply chain, demand for goods and services, as well as scale of business activity. In response to these challenges, countries where the Group operates, introduced large economic and fiscal programs, including, but not limited to, subsidized lending to affected industries, payments to unemployed individuals, tax deferrals and easing of certain regulatory restrictions to support the financial sector. With the start of vaccination in 2021 the countries gradually started to eliminate quarantine regime measures, travel restrictions, closure of business and other venues.

## 25. Material partly-owned subsidiary

As at 31 December 2021 and 2020 49% of equity interest of TANAP A.Ş. was held by non-controlling shareholders. As at 31 December 2021 accumulated balance of NCIs amounted to US dollars 1,788,614 (31 December 2020: US dollars 1,449,223).

The summarised financial information of TANAP A.Ş. is provided below. This information is based on amounts before inter-company eliminations.

### Summarised statement of comprehensive income for the year ended 31 December

	2021	2020
Revenue	1,291,677	682,239
Cost of sales	(164,169)	(133,783)
<b>Gross profit</b>	<b>1,127,508</b>	<b>548,456</b>
General and administrative expenses	(247,715)	(192,777)
Other income	3,376	1,463
Interest income	540	353
Finance costs	(191,080)	(197,549)
Foreign exchange gain/ (loss), net	6	(550)
<b>Profit before income tax</b>	<b>692,635</b>	<b>159,396</b>
Income tax expense	–	–
<b>Profit for the year</b>	<b>692,635</b>	<b>159,396</b>
Other comprehensive income	–	–
<b>Total comprehensive income</b>	<b>692,635</b>	<b>159,396</b>
<b>Total comprehensive income attributable to NCIs</b>	<b>339,391</b>	<b>78,104</b>

*(Amounts presented are in thousands of US dollars, unless otherwise stated)***25. Material partly-owned subsidiary (continued)****Summarised statement of financial position as at 31 December**

	<b>2021</b>	<b>2020</b>
<b>Current assets</b>	<b>175,903</b>	<b>141,516</b>
including:		
Cash and cash equivalents	11,287	14,101
Trade and other receivables	124,414	89,182
Inventories	32,562	29,466
Other current assets	7,640	8,767
<b>Non-current assets</b>	<b>6,394,355</b>	<b>6,562,397</b>
including:		
Pipeline cost	6,373,703	6,392,636
Construction in progress	–	142,759
Right-of-use asset	20,180	26,399
Other non-current assets	472	603
<b>Current liabilities</b>	<b>1,294,918</b>	<b>968,870</b>
including:		
Trade and other payables and accrued liabilities	51,459	50,263
Current portion of the long-term borrowing	1,237,621	914,494
Current portion of lease liability	5,838	4,113
<b>Non-current liabilities</b>	<b>1,625,108</b>	<b>2,777,445</b>
including:		
Long-term borrowings	1,558,536	2,706,825
Decommissioning liabilities	39,385	36,722
Lease liability	17,186	24,404
Other non-current liabilities	10,001	9,494
<b>Total equity</b>	<b>3,650,232</b>	<b>2,957,598</b>
<b>Equity attributable to NCIs</b>	<b>1,788,614</b>	<b>1,449,223</b>

**Summarised cash flow information**

	<b>2021</b>	<b>2020</b>
Operating	1,018,628	429,975
Investing	(2,261)	(51,009)
Financing	(1,019,181)	(392,853)
<b>Net decrease in cash and cash equivalents</b>	<b>(2,814)</b>	<b>(13,887)</b>

**26. Events after the reporting date**

On 18 February 2022 the Group signed the Deferred Sale and Purchase Agreement (“New DSPA”) for the acquisition of additional 4.35% participating interest in the SD project and additional 3.48% shares in AGSC from AzSD and additional 4.35% shares in the SCP project from AzSCP. The control over the shares and participating interests is expected to pass to the Group on 31 March 2023, provided that certain conditions precedent are satisfied.