Fintechaudit

Financial Statements and Independent Auditor's Report

“ARTSAKH HEK”

Open Joint Stock Company

December 31, 2012

Content

Members of the board

Spartak Tevosyan	Chairman Ministry of Finance and Economics of the Nagorno-Karabakh Republic
Emin Ohanjanyan	“ArmSwissbank” CJSC
Hayk Beglaryan	
Raffi Balyozian	
Arman Hakobyan	
Vahram Beglaryan	“ARTSAKH HEK”OJSC, General Director
Karen Arabyan	“ARTSAKH HEK”OJSC, Debuty General Director

Company’s management staff

Vahram Beglaryan	General Director
Karen Arabyan	Debuty General Director
Armen Gasparyan	Technical Director
Jan Hovhannisyan	Financial and Economy Director
Arayik Davtyan	Chief Accountant

List of board members and Company’s management staff is presented as of 31 December 2012.

«ՖԻՆՏԵԽ ԱՈՒԴԻՏ» ՓԲԸ

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Independent auditor's report

To the shareholders of "ARTSAKH HEK" Open Joint Stock Company

We have audited the accompanying financial statements of the"ARTSAKH HEK" Open Joint Stock Company (the "Company"), which comprise the statement of financial position as of December 31, 2012, and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Company as of December 31, 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

March 20, 2013

Anik Martirosyan

Director-Partner

Andreas Hovhannisyan

Auditor-Partner

Statement of financial position

In thousand AMD

	Ref.	As of December 31, 2012	As of December 31, 2011
Assets			
Non-current assets			
Property, plant and equipment	4	14,644,866	14,174,518
Intangible assets		-	200
Deferred tax assets	5	751	-
Prepayments	6	264,600	20,273
		14,910,217	14,194,991
Current assets			
Inventories	7	36,244	32,217
Trade and other receivables	8	1,028,698	1,107,668
Income tax prepayment		2,766	19,665
Borrowings provided		2,000	50,000
Cash and bank balances	9	79,834	40,682
		1,149,542	1,250,232
Total assets		16,059,759	15,445,223
Equity and payables			
Capital and reserves			
Share capital	10	10,650,000	10,650,000
Emission income	10	457,127	457,127
Capital reserve	10	123,220	106,292
Accumulated profit		385,517	581,880
		11,615,864	11,795,299
Non-current payables			
Loans and borrowings	11	2,941,774	1,921,556
		2,941,774	1,921,556
Current payables			
Loans and borrowings	11	1,461,978	1,702,200
Trade and other payables	12	40,143	26,168
		1,502,121	1,728,368
Total equity and payables		16,059,759	15,445,223

The financial statements were approved on March 20, 2013 by:

Vahram Beglaryan General Director	Arayik Davtyan Chief Accountant

The statement of financial position is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 30.

Statement of comprehensive income

In thousand AMD

	Ref.	Year ended December 31, 2012	Year ended December 31, 2011
Revenue	13	1,516,318	1,029,859
Cost of sales	14	(518,352)	(343,641)
Gross profit		997,966	686,218
Other income		1,852	8,425
Distribution and marketing expenses		(2,542)	(5,158)
Administrative expenses	15	(201,097)	(183,518)
Other expenses	16	(58,083)	(49,740)
Results from operating activities		738,096	456,227
Finance expenses	17	(246,745)	(4,775)
Other financial items	18	(111,156)	(194,691)
Profit before tax		380,195	256,761
Income tax expense	19	(27,130)	(24,265)
Profit for the year		353,065	232,496
Other comprehensive income		-	-
Total comprehensive income for the year		353,065	232,496
Profit per share	10	33 drams	29 drams

The statement of comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 30.

Statement of changes in equity

In thousand AMD

	Share capital	Emission income	Capital reserve	Accumulated profit	Total
As of January 1, 2011	7,362,074	158,748	43,645	1,148,239	8,712,706
Profit for the year	-	-	-	232,496	232,496
Total comprehensive income for the year	-	-	-	232,496	232,496
Issue of share capital	3,287,926	298,379	-	-	3,586,305
Transfer to reserves	-	-	62,647	(62,647)	-
Dividends	-	-	-	(736,208)	(736,208
As of December 31, 2011	10,650,000	457,127	106,292	581,880	11,795,299
Profit for the year	-	-	-	353,065	353,065
Total comprehensive income for the year	-	-	-	353,065	353,065
Transfer to reserves	-	-	16,928	(16,928)	-
Dividends				(532,500)	(532,500)
As of December 31, 2012	10,650,000	457,127	123,220	385,517	11,615,864

The statement of changes in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 30.

Statement of cash flows

In thousand drams	Year ended December 31, 2012	Year ended December 31, 2011
Cash flows from operating activities		
Profit for the year	353,065	232,496
Adjustments for:		
Depreciation	244,055	142,211
Loss on disposal of property and equipment	15,103	14,960
Income tax expense	27,130	24,265
Interest expense	255,227	4,775
Interest income	(8,482)	-
Foreign exchange loss	111,156	194,691
Operating profit before working capital changes	997,254	613,398
Change in inventories	(4,027)	(8,157)
Change in trade and other receivables	78,970	(515,624)
Change in trade and other payables	14,307	(167,884)
Cash used in operations	1,086,504	(78,267)
Interest paid	(236,541)	(4,775)
Income tax paid	(10,982)	(73,756)
Net cash from/(used in) operating activities	838,981	(156,798)
Cash flows from investing activities		
Acquisition of property, plant and equipment and intangible assets	(973,766)	(2,636,166)
Proceeds from disposal of property, plant and equipment	133	900
Provided borrowings, net	48,000	(50,000)
Interest income received	8,482	-
Net cash used in investing activities	(917,151)	(2,685,266)
Cash flows from financing activities		
Proceeds from issue of share capital	-	3,586,305
Net proceeds from/repayments of loans and borrowings	655,195	(512,079)
Dividends paid	(532,500)	(736,208)
Net cash from financing activities	122,695	2,338,018
Net increase/(decrease) in cash and cash equivalents	44,525	(504,046)
Foreign exchange effect on cash	(5,373)	(3,739)
Cash and cash equivalents at the beginning of the year	40,682	548,467
Cash and cash equivalents at the end of the year	79,834	40,682

Notes to the financial statements

1 Nature of operations and general information

“ARTSAKH HEK” Open Joint Stock Company (hereinafter: the Company) is established under the laws of the Republic of Nagorno-Karabagh on June 9, 2008. The Company is a legal successor of “ARTSAKH HEK” CJSC.

The major stockholder of the Company is the Republic of Nagorno-Karabagh: Government of the NKR, 47.9 percent as of reporting data.

The Company is mainly involved in production and sale of electricity. The electricity is produced by 5 power plants built in NKR with total power volume of 66.7 megawatts.

- Sarsang HPP,
- Trghi 1 HPP,
- Trghi 2 HPP,
- Mataghis 1 HPP,
- Mataghis 2 HPP:

Trghi 3 another HPP with power volume of 4.2 megawatts is under construction.

Whole produced electricity is realized to a Company which is sole Electricity transfer nets managing operating company in NKR.

The licenses for each operating HPP is provided for 15 years. The managment of the Company thinks that the licenses will prolonge without interaption.

The Company have licences production of electricity which is determined by Public Services Regulatory Commission of the Republic of Nagorno-Karabagh.

- “Sarsang” HPP’s license for production of electriciy is provided in 28.07.2008 for 15 years.

- “Trghi 1” HPP’s license for production of electriciy is provided in 11.06.2010 for 15 years.

- “Trghi 2” HPP’s license for production of electriciy is provided in 26.12.2011 for 15 years.

- “Mataghis 1” HPP’s and “Mataghis 2” HPP’s license for production of electriciy is provided in 17.07.2012 for 15 years, HPPs were put into operation from september 2012.

The legal address of the Company is 25a V. Sargsyan Street, Stepanakert, the Republic of Nagorno-Karabagh.

The annual average number of employees during 2012 was 167 employees (2011: 128 employees).

2 Basis of preparation

2.1 Statement of compliance

The financial statements have been prepared and presented in accordance with International Financial Reporting Standards (“IFRS”).

2.2 Basis of measurement

The financial statements have been prepared on the historical cost basis with the exception of certain financial instruments that have been presented at their fair value.

2.3 Functional and presentation currency

The national currency of the Republic of Nagorno-Karabagh is the Armenian dram (“dram”), which is the Company’s functional currency, since this currency best reflects the economic substance of the underlying events and transactions of the Company.

These financial statements are presented in Armenian drams, since management believes that this currency is more useful for the users of these financial statements. All financial information presented in Armenian drams has been rounded to the nearest thousand.

2.4 Use of estimates and judgment

The preparation of financial statements in conformity with IFRS requires management to make critical accounting estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Significant areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in the note 22 to the financial statements.

2.5 IFRS 9 Financial instruments

IFRS 9 was issued in November 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.

IFRS 9 will be adopted in January 1, 2015 for the annual period beginning January 1, 2015.

Management has not assessed yet the impact that this amendment is likely to have on the financial statements of the Company.

3 Significant accounting policies

3.1 Foreign currencies

Foreign currency transactions

In preparing the financial statements, transactions in currencies other than the functional currency are recorded at the rates of exchange defined by the Central Bank of Armenia prevailing on the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated at the rates defined by the Central Bank of Armenia prevailing on the reporting date, which is 403.58 drams for 1 US dollar as of December 31, 2012 (December 31, 2011: 385.77 drams for 1 US dollar) and 532.24 drams for 1 Euro as of December 31, 2012 (December 31, 2011: 498.72 drams for 1 Euro). Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historic cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement and retranslation of monetary items, are included in profit or loss for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period, except for differences arising on the translation of non-monetary items in respect of which gains and losses are recognized directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognized directly in equity.

3.2 Property and equipment

Property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. When an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Properties in the course of construction are carried at cost, less any recognized impairment loss. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

The gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the statement of comprehensive income.

Expenditure to replace a component of an item of property and equipment that is accounted for separately is capitalized with the carrying amount of the component being written off. Other subsequent expenditure is capitalized if future economic benefits will arise from the expenditure. All other expenditure, including repair and maintenance, is recognized in the statement of comprehensive income as incurred.

Depreciation is charged to the statement of comprehensive income on a straight line basis over the estimated useful lives of the individual assets. Depreciation commences when assets are available for use. The estimated useful lives are as follows:

Buildings and constructions	- 20-60 years
Conveyance schemes	- 20-60 years
Machinery and equipment	- 20-60 years
Transportation means	- 5 years
Computers and accessories	- 1 year
Other fixed assets	- 5 years.

3.3 Intangible assets

Intangible assets, which are acquired by the Company and which have finite useful lives, are stated at cost less accumulated amortization and impairment losses.

Amortization is charged to the statement of comprehensive income on a straight line basis over the estimated useful lives of the intangible assets, which is

Accounting software - 10 years

3.4 Leased assets

In accordance with IAS 17 *Leases*, the economic ownership of a leased asset is transferred to the lessee if the lessee bears substantially all the risks and rewards related to the ownership of the leased asset. The related asset is then recognized at the inception of the lease at the fair value of the leased asset or, if lower, the present value of the lease payments plus incidental payments, if any. A corresponding amount is recognized as an obligation under finance lease, irrespective of whether some of these lease payments are payable up-front at the date of inception of the lease.
All leases are treated as operating leases. Payments on operating lease agreements are recognized as an expense on a straight-line basis. Associated costs, such as maintenance and insurance, are expensed as incurred.

3.5 Inventories

Inventories are stated at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of inventories is based on the Average cost method and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition.

3.6 Financial instruments

Financial assets and financial liabilities are recognized when the Company becomes a part to the contractual provisions of the financial instrument.

Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred.

Financial liabilities are derecognized when they are extinguished, discharged, cancelled or expire.

Financial assets and financial liabilities are measured initially at fair value plus transaction costs, except for financial assets and financial liabilities carried at fair value through profit or loss, which are measured initially at fair value.

Financial assets and financial liabilities are measured subsequently as described below.

Financial assets

Financial assets other than hedging instruments are divided into the following categories:
- receivables
- financial assets at fair value through profit or loss
- available-for-sale financial assets.

Financial assets are assigned to the different categories on initial recognition, depending on the characteristics of the instrument and its purpose. A financial instrument's category is relevant for the way it is measured and whether any resulting income and expenses are recognized in profit or loss or directly in equity. See note 20.2 for a summary of the Company's financial assets by category.

Generally, the Company recognizes all financial assets using settlement date accounting. An assessment of whether a financial asset is impaired is made at least at each reporting date. All income and expense relating to financial assets are recognized in the statement of comprehensive income line item "finance costs" or "finance income", respectively.

I. Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Current accounts receivable are initially recognized at fair value. Subsequently they are measured at amortized cost less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor and default and delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset’s carrying amount and the present value of the estimated future cash flows, discounted at the original effective interest rate.

The balance of the allowance is adjusted by recording a charge or income to the statement of comprehensive income of the reporting period. Any amount written-off with respect to customer account balances is charged against the existing allowance for doubtful accounts. All accounts receivable for which collection is not considered probable are written-off.

II. Cash and bank balances

The Company’s cash and bank balances comprise cash in hand, bank accounts and cash in transit, which fall into “loans and receivables” category of financial instruments.

Financial liabilities

The Company's financial liabilities include borrowings, trade and other payables, which are measured at amortized cost using the effective interest rate method. A summary of the Company's financial liabilities by category is given in the note 20.2.

i Loans and borrowings

Loans and borrowings are recognized initially at fair value, net of issuance costs associated with the borrowing. Subsequent to initial recognition, loans and borrowings are stated at amortized cost with any difference between cost and redemption value recognized in the statement of comprehensive income over the period of the borrowings on an effective interest basis. Interest and other costs incurred in connection with borrowings are expensed as incurred as part of finance expenses, except for the borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, which are capitalized as part of that asset.

ii Trade and other payables

Trade and other payables are stated at fair value and subsequently stated at amortized cost.

3.7 Impairment

Impairment of property, plant and equipment, intangible assets

Assets with the indefinite period of useful life do not amortized and should be tested for impairment each year. In general fixed assets need be reviewed for impairment only if there is some indication that impairment has occurred. Impairment is measured by comparing the carrying value of the fixed asset with its recoverable amount.

Recoverable amount is the higher of net selling price and value in use. If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. Impairment losses are recognized as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss recognized for the asset or cash-generating unit in prior years. A reversal of an impairment loss is recognized as income immediately, unless the relevant asset is carried at a revalued amount, in which case any reversal of impairment loss is treated as a revaluation increase.

Impairment of financial assets

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at each reporting date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset’s carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account.

With the exception of available-for-sale equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

3.8 Employee benefits

Short-term employee benefits include wages, salaries, short-term compensated absences (such as paid annual live and paid sick leave), and bonuses.

When an employee has rendered service to the Company during an accounting period, the Company recognizes the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

a) As a liability after deucting the amount already paid. If the amount already paid exceeds the undiscounted amount of benefits, the Company recognizes this difference as an asset to the extent this prepayment will lead e. g. To a decrease in future payments, or recovery of financial resources, and

b) As an expense, unless it is included in the carrying amount of another asset.

3.9 Equity

Equity instruments issued by the Company are recorded at the nominal value. Difference between the proceeds from the share issue and nominal value is presented as share premium.
Imcremental costs directly attributable to issue of ordinary shares are recognized as a deduction from equity.

Dividends are recognized as a liability in the period in which they are declared.

The Company creats capital reserve for covering the Company's losses as well as for redemption of Company's debt and shares when the Company's profit and other assets are not enough to cover those.

Basic earnings per share is calculated by dividing profit by weighted average number of orninary shares outstanding during the period.

The weighted average number of ordinary shares outstanding during the period is the number of ordinary shares outstanding at the beginning of the period, adjusted by the number of ordinary shares bought back or issued during the period multiplied by a time-weighting factor. The time-weighting factor is the number of days that the share are outstanding as a proportion of the total number of days in the period; a reasonable approximation of the weighted average is adequate in many circumstances.

3.10 Provisions

A provision is recognized in the statement of financial position when the Company has a legal or constructive obligation as a result of past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows 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.

3.11 Income tax

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

3.12 Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable taking into account the amount of any trade discounts and rebates allowed by the Company.

The Company's revenue is mainly derived from sale of electricity and power recovery.

The Company recognizes revenue when the services are provided to buyer and when it is possible to measure reliably the amount of revenue and it is probable that the economic benefits associated with the transaction will flow to the Company.

4 Property, plant and equipment

	Buildings, constructions	Conveyance schemes, structures	Machinery and equipment, transportation means,	Office equipment and tools	Out-off use	Construction in rocess	Other	Total
Cost								
As of January 1, 2011	3,807,896	224,100	4,453,447	15,451	15,210	5,592,566	4,525	14,113,195
Addition	611	6,190	189,667	6,097	49,355	2,444,344	1,986	2,698,250
Disposals	-	-	(1,598)	(67)	(15,210)	-	-	(16,875)
Reclassification	518,771	399,291	1,453,113	5,122	(856)	(2,375,037)	(404)	-
As of December 31, 2011	4,327,278	629,581	6,094,629	26,603	48,499	5,661,873	6,107	16,794,570
Addition	292	202,199	155,704	2,557	2,165	365,561	961	729,439
Disposals	-	-	(16,053)	(992)	-	-	(381)	(17,426)
Reclassification	1,847,923	2,812,001	1,407,411	-	(50,664)	(6,016,671)	-	-
As of December 31, 2012	6,175,493	3,643,781	7,641,691	28,168	-	10,763	6,687	17,506,583
Accumulated depreciation								
As of January 1, 2011	1,113,208	5,338	1,354,252	5,289	-	-	1,588	2,479,675
Charge for the year	76,342	48,767	14,004	-	-	-	2,279	141,392
Eliminated on disposal	-	-	(1,015)	-	-	-	-	(1,015)
Reclassification	(28,225)	(984)	29,249	(40)	-	-	-	-
As of December 31, 2011	1,161,325	53,121	1,396,490	5,249	-	-	3,867	2,620,052
Charge for the year	77,430	34,026	125,590	4,304			2,505	243,855
Eliminated on disposal			(1,039)	(829)			(322)	(2,190)
As of December 31, 2012	1,238,755	87,147	1,521,041	8,724			6,050	2,861,717
Carrying amount								
As of December 31, 2011	3,165,953	576,460	4,698,139	21,354	48,499	5,661,873	2,240	14,174,518
As of December 31, 2012	4,936,738	3,556,634	6,120,650	19,444	-	10,763	637	14,644,866

The Company did not have any pledged property, plant and equipment as of December 31, 2012 and December 31, 2011.

As of December 31, 2012 assets with an initial price of 48,533 thousand drams (as of December 31, 2011: 19,885 thousand drams) were accounted with the carrying amount of nil.

2012 and 2011 depreciation expense has been allocated as follows:

In thousand drams

	Year ended December 31, 2012	Year ended December 31, 2011
Cost of sales	226,763	119,184
Administrative expenses	17,092	22,208
	243,855	141,392

During 2012, the increases of PPE consist:

Addition nature	Amount In thousand drams
1. Construction and installation works for Mataghis 1 and Mataghis 2 SHPPs	353,665
2. Acquisition of equipments and other PPEs	102,726
3. Capitalized borrowing costs	273,048
	729,439

During 2011, the increases of PPE consist:

Addition nature	Amount In thousand drams
1. Construction of Trghi 2 SHPP	458,023
2. Construction of Mataghis 1 SHPP	370,219
3. Construction of Mataghis 2 SHPP	393,431
4. Construction of Mataghis dam	3,013
5. Water intake fencing works of Mataghis 1SHPP	5,165
6.Renovation of Mataghis 1 and Mataghis 2 SHPPs administrative buildings	79,461
7. Acquisition of equipments and other PPEs	377,436
8. Capitalized borrowing costs	625,629
9. Other capitalizations and acquisitions	385,873
	2,698,250

5 Deferred income taxes

The movement of deferred income taxes is disclosed below:

In thousand drams	2012	2011
Balance at beginning of year	-	-
Charged to statement of comprehensive income	751	-
Balance at end of year	751	-

Deferred income taxes for the year ended December 31, 2012 can be summarized as follows:

In thousand drams	January 1, 2012	Recognized in statement of comprehensive income	December 31, 2012
Deferred income tax assets			
Trade receivables			
Provision on unused holidays	-	751	751
	-	751	751
Deferred income tax liabilities			
	-	-	-
Net position – deferred income tax assets	-	751	751

Analyzed as:	2012	2011
To be recovered/redeemed after more than 12 months	751	-
To be recovered/redeemed within 12 months	-	-

6 Prepayments

The Company made prepayments for acquisition of PPEs, from which at the amount of drams 258,600 thousand was paid to “Hydro Energy Italy” CJSC for purchase of equipments for Trghi 3 HPP.

7 Inventories

In thousand drams	As of December 31, 2012	As of December 31, 2011
Materials	13,574	14,181
Fuel	15,694	14,898
Other materials	6,976	3,138
	36,244	32,217

8 Trade and other receivables

In thousand drams

	As of December 31, 2012	As of December 31, 2011
Trade receivables	588,601	483,542
Advances and prepayments	35,522	14,001
Receivables from the State budget	402,754	609,805
Other receivables	1,821	320
	1,028,698	1,107,668

The average credit period on sales of services is 142 days (2011: 171 days). No interest is charged on the trade receivables.

Receivables from the State budget includes deferred VAT subject to set-off - 402,286 thousand drams (2011: 609,216 thousand drams), which will set-off with VAT of revenue, when the Company pays appropriate invoices.

Management believes that the receivables from the State budget are fully recoverable.

Refer to note 21.1 for the currencies in which the trade and other receivables are denominated.

9 Cash and bank balances

In thousand drams

	As of December 31, 2012	As of December 31, 2011
Cash in hand	1,509	565
Bank accounts (AMD)	7,669	40,050
Bank accounts (foreign currency)	70,656	67
	79,834	40,682

10 Equity

10.1 Share capital

	Ordinary shares 2012	Ordinary shares 2011
Number of ordinary shares (unit)	10,650,000	10,650,000
Nominal value of ordinary shares	1,000	1,000
	10,650,000	10,650,000

The Company has one class of ordinary shares, which carry no right to fixed income.

As of December 31, 2012 number of issued ordinary shares are 10,650,000 and the number of declared (but not issued) ordinary shares are 4,450,000.

As of December 31, 2012 the number of shareholders is.

	31.12.2012		31.12.2011	
	unit	%	unit	%
The Government of NKR	5,100,000	47.9	5,100,000	47.9
Josef Ughurlian (USA, New York)	1,262,901	11.9	1,262,901	11.9
“Multicontinental distribution” LLC (Great Britain, Isle of Main IM 2AP)	1,193,692	11.2	1,193,692	11.2
“AEG” LLC (NKR, Stepanakert)	616,000	5.8	640,000	6.0
“V.P.B.P” ՓԲԸ (NKR, Stepanakert)	630,270	5.9	630,270	5.9
Other (Less 5%)	1,847,137	17.3	1,823,137	17.1
	10,650,000	100	10,650,000	100.0

Share premium represents difference between the proceeds from and nominal value of share issues.

In thousand drams

	2012	2011
Opening balance	457,127	158,748
Share issue		
Proceeds from share issue	-	3,649,598
Share capital	-	(3,287,926)
	-	361,672
Underwriting direct expenses	-	(63,293)
Closing balance	457,127	457,127

Issue proceeds for 2011 share issue was 1,110 AMD per share.

10.2 Capital reserve

In thousand drams

	2012	2011
Opening balance	106,292	43,645
Transfer to reserves	16,928	62,647
Closing balance	123,220	106,292

Based on the resolution of the Company’s Shareholders General Meeting 2012, transfer to capital reserve equal to the amount of 5% 16,928 thousand was made from net profit of the year 2011 (5.7% 16,647 thousand drams of net profit of the year 2010).

10.3 Dividends

Based on the resolution of the Company’s Shareholders General Meeting 2012, based on financial results of 2011 dividends was payed to Company’s sharholders at the amout of drams 532,500 thousand, 50 dram per share (in 2011, based on financial results of 2010 dividends was payed to Company’s sharholders at the amout of drams 736,207 thousand, 100 dram per share).

10.4 Basic earnings per share

	2012	2011
Net profit for the year (in thousand drams)	353,065	232,496
Weighted average number of shares (units)	10,650,000	7,910,062
Basic earnings per share (drams)	33	29

11 Loans and borrowings

In thousand drams

	Current		Non-current	
	2012	2011	2012	2011
Loans	1,242,706	1,083,950	1,412,285	1,799,222
Borrowings	219,272	618,250	112,923	122,334
Bonds	-	-	1,416,566	-
	1,461,978	1,702,200	2,941,774	1,921,556

Loans and borrowings are secured by State guaranties issued by the Government of the NKR, it means that the Company does not have any pledged assets.

Interest expenses equals to drams 521,357 thousand, from which 273,048 thousand drams were capitalized and 248,309 thousand drams were classified as current expenses.

Annual interest rates of loans and borrowings for the reporting period by currencies are presented as:

Average rate	US dollar	13%
	Euro	13%
	AMD	15%
		14%

Bonds

On 5 December 2012, the Company issued 600 (six hundred) units of ordinary nominal non-documentary bonds, with a nominal value of US dollars 10,000, total amount eqauls to US dollars 6,000,000. In 2012 the amount of placed bonds was 3,510,000 US dollars, and the rest was placed in January 2013.

Bonds rendement is 10% per annum, which will be payed in semi-annual periods. The type of the placement is non-guaranteed.

Refer to note 21.1 for more information about the Company’s exposure to interest rate and foreign currency risks.

12 Trade and other payables

In thousand drams

	As of December 31, 2012	As of December 31, 2011
Trade payables	2,999	3,635
Advances	300	-
Taxes and duties payable	9,845	8,740
Provision on unused holidays	15,017	11,000
Payables to the participants	11,533	2,309
Other payables	449	484
	40,143	26,168

No interest is charged on the trade payables. The Company has financial risk management policies to ensure that all payables are paid within the credit timeframe.

13 Revenue

In thousand drams

	Year ended December 31, 2012	Year ended December 31, 2011
From realization of produced electricity		
Sarsang HPP	881,226	845,917
Trghi -1 HPP	203,493	156,797
Trghi -2 HPP	328,958	27,145
Mataghis -2 HPP	102,641	-
	1,516,318	1,029,859

The price on services rendered by the Company is determined by Public Services Regulatory Commission of the NKR.

Price per 1 KWtH for transferred electricity built on natural water flow equals to (without VAT):

- from big hydro power plants (Sarsang)- 9 AMD,
- from small hydro power plants (Trghi -1) -19.171 AMD,
- from small hydro power plants (Trghi -2) -19.171 AMD,
- from small hydro power plants (Mataghis-2) -19.171 AMD:

According to the electricity purchase agreement signed between the Company and the buyer dated on 15 June, 2010, the rate per 1 kWtH transferred electricity equals to

- Sarsang HPP- 9 AMD,
- from small hydro power plants (Trghi -1) -18 AMD,
- from small hydro power plants (Trghi -2) -18 AMD,
- from small hydro power plants (Mataghis-2) -18 AMD:

14 Cost of sales

In thousand drams	Year ended December 31, 2012	Year ended December 31, 2011
Employee benefits and social sec. payments	194,814	142,666
Depreciation	226,963	119,511
Maintenance of plants	33,400	36,128
Material expenses	29,815	23,672
Repair expenses	13,415	3,851
Other exoenses	19,945	17,813
	518,352	343,641

15 Administrative expenses

In thousand drams	Year ended December 31, 2012	Year ended December 31, 2011
Employee benefits and social sec. payments	111,569	90,461
Depreciation and amortisation	17,093	22,087
Traveling and representative expenses	6,463	4,702
Lease expenses	14,880	14,880
Telecommunication expenses	5,218	5,312
Utility and office expenses	13,235	20,898
Non recoverable expenses	18,247	14,485
Audit and consulting expenses	7,111	5,500
Other expenses	7,281	5,193
	201,097	183,518

16 Other expenses

In thousand drams	Year ended December 31, 2012	Year ended December 31, 2011
Charges related to shares	6,184	6,627
Currency exchange transaction charges	5,856	12,054
Cost of sold inventory	-	110
Research and development expenses	292	2,923
Fines and penalties	3,542	7,699
Donations	23,337	18,252
Cost of sold PPE	15,102	-
Other expenses	3,770	2,075
	58,083	49,740

17 Finance costs, net

In thousand drams	Year ended December 31, 2012	Year ended December 31, 2011
Interest expenses on loans and borrowings	(248,309)	-
Interest expenses on bank transactions	(6,918)	(4,775)
Interest income on bank transactions	8,482	-
Finance costs, net	(246,745)	(4,775)

18 Other financial items

In thousand drams

	Year ended December 31, 2012	Year ended December 31, 2011
Foreign exchange effect on:		
Cash and cash equivalents	(5,373)	(3,739)
Trade payables	332	(824)
Loans and borrowings	(106,115)	(190,128)
	(111,156)	(194,691)

19 Income tax recovery

In thousand drams

	Year ended December 31, 2012	Year ended December 31, 2011
Current tax	27,881	24,265
Deferred tax (refer to note 5)	(751)	-
	27,130	24,265

Reconciliation of effective tax rate is as follows:

In thousand drams	Year ended December 31, 2012	Effective tax rate (%)	Year ended December 31, 2011	Effective tax rate (%)
Profit/loss before taxation (under IFRS)	380,195		256,761	
Tax calculated at a tax rate of 5% (2011: 5%)	19,010	5.00	12,838	5.00
Effect of expenses that are not taxable	8,120	2.14	11,427	4.45
Income tax recovery	27,130	7.14	24,265	9.45

20 Financial instruments

20.1 Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition and the basis on which income and expenses are recognized, in respect of each class of financial asset, financial liability and equity instrument are disclosed in the note 3.6.

20.2 Categories of financial instruments

The carrying amounts presented in the statement of financial position relate to the following categories of assets and liabilities:

Financial assets

In thousand drams

	As of December 31, 2012	As of December 31, 2011
Receivables:		
Trade receivables	590,422	483,862
Borrowings provided	2,000	50,000
Cash and bank balances	79,834	40,682
	672,256	574,544

Financial liabilities

In thousand drams	As of December 31, 2012	As of December 31, 2011
Financial liabilities measured at amortized costs:		
Loans and borrowings	4,403,752	3,623,756
Trade and other payables	29,998	17,428
	4,433,750	3,641,184

See note 3.6 for a description of the accounting policies for each category of financial instruments. The fair values are presented in the related notes.

21 Financial risk management

Exposure to market risk (including currency risk, interest rate risk and price risk), credit risk and liquidity risk arises in the normal course of the Company's business.

21.1 Financial risk factors

a) Market risk

The Company's activities expose it primarily to the financial risks of changes in foreign currency exchange rates, interest rates and equity price (see b, below).

b) Foreign currency risk

The Company undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise.

The exposure of the Company's financial assets and financial liabilities to the foreign currency risk is as follows:

Item

As of December 31, 2012	Armenian drams	USD	EUR
Financial assets			
Trade receivables	590,422	-	-
Borrowings provided	2,000	-	-
Cash and bank balances	9,178	70,632	24
	601,600	70,632	24
Financial liabilities			
Loans and borrowings	1,170,590	2,709,401	523,761
Trade and other payables	29,998	-	-
	1,200,580	2,709,401	523,761
Net position	(598,980)	(2,638,769)	(523,737)

Item

As of December 31, 2011	Armenian drams	USD	EUR
Financial assets			
Trade receivables	483,862	-	-
Borrowings provided	50,000	-	-
Cash and bank balances	40,614	58	10
	574,476	58	10
Financial liabilities			
Loans and borrowings	1,221,488	2,277,786	124,482
Trade and other payables	17,428	-	-
	1,238,916	2,277,786	124,482
Net position	(664,440)	(2,277,728)	(124,473)

The Company is mainly exposed to US dollar and Euro. The following table details the Company’s sensitivity to a 10% (2011: 10%) increase and decrease in dram against US dollar and Euro. 10% (2011: 10%) represents management’s assessment of the possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 10% (2011: 10%) change in foreign currency rates. The sensitivity analysis includes related party and non-related party loans. A negative number indicates an increase in profit or loss and other equity where dram lessen against the relevant currency.

	US dollar impact		EUR impact	
	2012	2011	2012	2011
Statement of comprehensive income	(263,877)	(227,773)	(52,374)	(12,447)

c) Credit risk

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the Company.

At the reporting date there was no significant concentration of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the statement of financial position.

d) Liquidity risk

The Company’s policy is to run a prudent liquidity management policy by means of holding sufficient cash and bank balances, as well as highly liquid assets for making all operational and debt service related payments when those become due.

21.2 Capital risk management

The Company manages its capital to ensure that it will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance.

The capital structure of the Company consists of equity comprising issued capital and accumulated profits and debt, which includes borrowings disclosed in the note 11.

The Company management reviews the capital structure on a regular basis to maintain the most optimal debt to equity balance, which is analyzed by calculating gearing ratio (net debt divided by total capital), as follows:

In thousand drams	As of December 31, 2012	As of December 31, 2011
Total borrowings	4,403,752	3,623,756
Less: cash and bank balances	(79,834)	(40,682)
Net debt	4,323,918	3,583,074
Total equity	11,615,864	11,795,299
Total capital	15,939,782	15,378,373
Gearing ratio	27%	23%

21.3 Fair values

Management believes that the carrying amount of financial assets and financial liabilities recorded at amortized cost in the financial statements approximates their fair values.

22 Critical accounting estimates and judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

22.1 Critical accounting estimates

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions 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.

Useful life of property and equipment

Company management has reviewed useful lives of fixed assets: 20 years for conveyance schemes, 5 years for machinery and equipments and 1 year for computer appliances. The management believes that estimated useful lives reflect the expected economic life of these assets. If this estimates change, the Company's financial statements would significantly differ.

Deferred tax valuation

As described in the note 5 deferred tax assets at the amount of 751 thousand drams have been recognized. Deferred income tax assets arise from allowances for employee benefits. The management believes that the Company would have taxable income in future to utilize the income tax assets based on the nature of Company's operations. If the Company would not have taxable income in future, than deferred tax assets would not be recovered.

23 Commitments

23.1 Operating lease commitments

The Company as lessee

Operating lease relates to the 2nd, 3nd floors and veranda of a building with a total area of 342.67 Sq.m (located at 25a V. Sargsyan street, Stepanakert), the leasing period is 1 year and is leased from individual. The monthly lease payment is determined at drams 1,160 thousand in accordance with the contract signed on 01.01.2012.

On January 2013 the lease agreement was prolonged to 1 year.

24 Contingencies

24.1 Business environment

Armenia and the Republic of Nagorno Kharabakh continues to undergo political and economic changes. As an emerging market, Armenia and the Republic of Nagorno Kharabakh do not possess a developed business and regulatory infrastructure that generally exists in a more mature free market economy. In addition, economic conditions continue to limit the volume of activity in the financial markets, which may not be reflective of the values for financial instruments. The main obstacle to further economic development is a low level of economic and institutional development, along with a centralized economic base, regional instability and international economic crises.

The possible effects of these factors on the Company may include the inability to pay creditors when they become due, impaired reputation, difficulties in selling the services, difficulties in obtaining funds, etc. All these problems may lead to the lessened liquidity of the Company and, accordingly, to going concern problems. However, as the number of variables and assumptions involved in these uncertainties is big, management cannot make a reliable estimate of the amounts by which the carrying amounts of assets and liabilities of the Company may be affected.

The financial statements of the Company do not include the effects of adjustments, if any, which might have been considered necessary, had the effects of the current global crisis become observable and reliably measurable in Armenia.

24.2 Insurance

The Armenian and the Republic of Nagorno Kharabakh insurance industry is in its development stage and many forms of insurance protection common in other parts of the world are not yet generally available in Armenia and the Republic of Nagorno Kharabakh. The Company does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on the Company property or relating to the Company operations. Until the Company obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets or environmental damage could have a materially adverse affect on the Company’s operations and financial position.

24.3 Taxes

The taxation system in Armenia and the Republic of Nagorno Kharabakh is relatively new and is characterized by frequently changing legislation, which is often subject to interpretation. Often differing interpretations exist among various taxation authorities and jurisdictions. Taxes are subject to review and investigations by tax authorities, which are enabled by law to impose severe fines and penalties.

These facts may create tax risks in Armenia and the Republic of Nagorno Kharabakh substantially more than in other developed countries. Management believes that it has adequately provided for tax liabilities based on its interpretation of tax legislation. However, the relevant authorities may have differing interpretations.

25 Related party transactions

25.1 Transactions with management and close family members

Key management received the following remuneration during the year, which is included in employee benefits.

In thousand drams	Year ended December 31, 2010	Year ended December 31, 2009
Salaries and bonuses, including contributions to Social State fund	25,925	23,920
	25,925	23,920