

# **Project Financial Statements and Independent Auditor's Report**

## **“High Voltage Electric Networks” CJSC**

Electricity Supply Reliability Project Loan number  
8055-AM

As of and for the year ended 31 December 2018



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# Independent auditor's report

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To the shareholder of "High Voltage Electric Networks" CJSC

## *Opinion*

We have audited the accompanying project financial statements of the Electricity Supply Reliability Project (the "Project" or the "ESRP"), financed by the International Bank for Reconstruction and Development (the "IBRD") Loan Agreement number 8055-AM, which comprise the statement of financial position as of 31 December 2018, the statement of the Project sources and uses of funds, the statement of uses of funds by Project activities, the designated account statement as of and for the year ended 31 December 2018 as well as the statement of expenditures ("SOE") submitted to the World Bank for the year ended 31 December 2018 in support of Loan Agreement number 8055-AM withdrawals, and notes to the project financial statements, including a summary of significant accounting policies.

In our opinion, the project financial statements give a true and fair view of the financial position of the Electricity Supply Reliability Project as of 31 December 2018, and of the funds received and expenses incurred for the year then ended, in accordance with the accounting policies described in the note 2 to the project financial statements, the International Bank for Reconstruction and Development guidelines, and the relevant points of the Loan Agreement number 8055-AM.

In addition, in our opinion, the SOEs submitted together with the internal controls and procedures involved in their preparation can be relied upon to support the applications for the Loan Agreement number 8055-AM withdrawals.

## *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 Project Financial Statements section of our report. We are independent of the "High Voltage Electric Networks" CJSC (the "Company") in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in the Republic of Armenia, and we have fulfilled our other ethical responsibilities in accordance with those ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## *Emphasis of Matters*

- We draw attention to note 2 to the project financial statements, which describes the basis of accounting. The project financial statements are prepared to assist the management of the "High Voltage Electric Networks" CJSC to meet the requirements of the financial reporting of the International Bank for Reconstruction and Development. As a result, the project financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.
- We draw attention to note 3 to the project financial statements which states that the closing date of the Project was defined as 31 December 2019. Our opinion is not modified in respect of this matter.

- We draw attention to note 9 to the project financial statements, which states that the Audit Chamber of the Republic of Armenia has revealed certain inconsistencies, as well as other facts in the framework of the Loan project implemented by the Company. Our opinion is not modified in respect of this matter.

### *Responsibilities of Management and Those Charged with Governance for the Project Financial Statements*

Management of "High Voltage Electric Networks" CJSC is responsible for the preparation and fair presentation of the project financial statements in accordance with the accounting policies described in the note 2 to the project financial statements, the International Bank for Reconstruction and Development guidelines, and the relevant points of the Loan Agreement number 8055-AM, and for such internal control as management determines is necessary to enable the preparation of project financial statements that are free from material misstatement, whether due to fraud or error.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

### *Auditor's Responsibilities for the Audit of the Project Financial Statements*

Our objectives are to obtain reasonable assurance about whether the project 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 project 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 project financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Evaluate the overall presentation, structure and content of the project financial statements, including the disclosures, and whether the project financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the management, 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.

28 June 2019

Gagik Gyulbudaghyan  
Managing Partner

Emil Vassilyan, FCCA  
Engagement Partner



# Statement of financial position

US dollars	Note	As of 31 December 2018	As of 31 December 2017
<i>Assets</i>			
Accumulated Project expenses		37,503,891	36,456,295
Advances	4	1,150,974	1,576,644
Bank balances		166,711	157,447
<b>Total assets</b>		<b>38,821,576</b>	<b>38,190,386</b>
<i>Funds and liabilities</i>			
<i>Funds</i>			
Accumulated Project financing		38,493,563	33,867,615
Exchange rate difference		(137,002)	(142,592)
		<b>38,356,561</b>	<b>33,725,023</b>
<i>Current liabilities</i>			
Accounts payable	5	465,015	4,465,363
		<b>465,015</b>	<b>4,465,363</b>
<b>Total funds and liabilities</b>		<b>38,821,576</b>	<b>38,190,386</b>

The project financial statements were approved on 28 June 2019 by:

<p>Hayk Harutyunyan General Director</p>  	<p>Gevorg Muradyan Chief Accountant</p> 
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This statement is to be read in conjunction with the notes to and forming part of the special purpose project financial statements set out on pages 10 to 14.

# Statement of the Project sources and uses of fund

As of and for the year ended 31 December 2018  
In US dollars

	Actual		Planned		Variance		Life of Project
	For the year	As of 31 December 2018	For the year	As of 31 December 2018	For the year	As of 31 December 2018	
<i>Sources of funds</i>							
IBRD Loan Number 8055-AM (note 6)	4,419,492	31,070,336					
Government co-financing	193,499	7,072,095					
“High Voltage Electric Networks” CJSC financing	12,957	350,774					
Other	-	358					
<b>Total</b>	<b>4,625,948</b>	<b>38,493,563</b>					
Exchange rate difference	5,590	(137,002)					
<i>Less: Uses of funds</i>							
Goods, works, non-consulting services, consultants' services, including training and audit, and operating costs for Project*	962,248	35,017,451	8,271,427	42,326,630	(7,309,179)	(7,309,179)	48,759,310
Land acquisition/grievance mechanisms under the Project	85,348	1,670,487	338,209	1,923,348	(252,861)	(252,861)	2,000,000
Refund of the preparation advance	-	718,453	-	718,453	-	-	1,143,190
Front-end Fee	-	97,500	-	97,500	-	-	97,500
<b>Total</b>	<b>1,047,596</b>	<b>37,503,891</b>	<b>8,609,636</b>	<b>45,065,931</b>	<b>(7,562,040)</b>	<b>(7,562,040)</b>	<b>52,000,000</b>
Net increase in working capital (note 7)	3,583,942	852,670					

\*In the framework of the contract signed between “High Voltage Electric Networks” CJSC (“HVEN”) and “Kalpataru Power Transmission Limited” (the “Contractor”), HVEN and the Contractor signed Agreement number 1 (dated 26 December 2018). In this Agreement, the contract amount has been changed. In addition, according to the same Agreement, the Contractor, as per preliminary estimate, waives USD 1,146,232 (debt forgiveness/cancelation) from the remainder of the debt. In order to determine the final amount of the debt waived/forgiven by the Contractor towards the HVEN, the Parties are obliged, after the Agreement comes into force, to do comparison of the accounting balances and prepare a document with the final balance of the recorded amount forgiven.

During the reporting period works have been accepted, price regulations have been done, etc, for which the debts have been forgiven. The amount for these services has not been included in the project financial statements.

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# Statement of uses of funds by Project activities

As of and for the year ended 31 December 2018  
In US dollars

	Actual		Planned		Variance		Life of Project
	For the year	As of 31 December 2018	For the year	As of 31 December 2018	For the year	As of 31 December 2018	
A Strengthening of the power transmission network	958,372	32,492,155	8,066,382	39,600,165	(7,108,010)	(7,108,010)	45,300,000
B Technical assistance	89,224	4,914,236	543,254	5,368,266	(454,030)	(454,030)	4,700,000
Physical contingencies	-	-	-	-	-	-	1,400,000
Price contingencies	-	-	-	-	-	-	500,000
Front-end fee	-	97,500	-	97,500	-	-	100,000
<b>Total</b>	<b>1,047,596</b>	<b>37,503,891</b>	<b>8,609,636</b>	<b>45,065,931</b>	<b>(7,562,040)</b>	<b>(7,562,040)</b>	<b>52,000,000</b>

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# SOE withdrawal schedule

For the year ended 31 December 2018  
In US dollars

Application No.	Goods, works, non-consulting services, consultants' services, including Training and audit, and Operating Costs for Project	Land acquisition/grievance mechanisms under the Project	Total
DA-112	1,064,877	933,291	1,998,168
DA-114	165,654	-	165,654
DA-116	2,380	-	2,380
Total	1,232,911	933,291	2,166,202

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14



# Designated account statement

Loan number 8055-AM  
As of and for the year ended 31 December 2018  
In US dollars

Opening balance as of 1 January 2018		157,447
Add:		
Cumulative unexplained discrepancy	-	
Loan replenishment during the year	<u>4,419,492</u>	<u>4,419,492</u>
	<u>4,419,492</u>	<u>4,419,492</u>
<i>Less: Refund to the International Bank for Reconstruction and Development from the designated account during the year</i>		-
Present outstanding amount advanced to the designated account (1)		<u>4,576,939</u>
Closing balance as of 31 December 2018		166,711
Add:		
Amount of eligible expenditures paid during the year	4,410,228	
Service charges (if applicable)	-	
	<u>4,410,228</u>	<u>4,410,228</u>
<i>Less: Interest earned (if credited into the designated account)</i>		-
Total advance accounted for (2)		<u>4,576,939</u>
Discrepancy (1) – (2) to be explained		-

This statement is to be read in conjunction with the notes to and forming part of the project financial statements set out on pages 10 to 14.

# Notes to the Project financial statements

## 1 Nature of operations and general information

“High Voltage Electric Networks” CJSC (the “Company”) has been established based on the resolution of the Government of the Republic of Armenia N450 dated 20 July 1998 on restructuring “High Voltage Electric Networks” subsidiary to a Closed Joint Stock Company and on the resolution of the Government of the Republic of Armenia N709 dated 23 November 1999 on reorganizing “Specialized Security on Energetic Objects” SCJSC through joining it to “High Voltage Electric Networks” SCJSC. The Company is the successor of “High Voltage Electric Networks” subsidiary, “High Voltage Electric Networks” CJSC and “Specialized Security on Energetic Objects” SCJSC.

The Company implements the Electricity Supply Reliability Project (the “Project”) financed in accordance with the Loan Agreement number 8055-AM dated 1 June 2011 signed between the International Bank for Reconstruction and Development (the “IBRD”) and the Republic of Armenia. In accordance with the sub-loan agreement dated 18 November 2011 signed between the Ministry of Finance of the Republic of Armenia and the Company, the Ministry of Finance transferred to the Company the IBRD loan amount of 39,000,000 US dollars, which should be used only for the Project implementation.

The objective of the Project is to increase the reliability and capacity of the power transmission network.

The Project consists of the following parts:

Part A: Strengthening of the power transmission network

Provision of works, goods, and technical assistance for the replacement of an existing power transmission line from the Hrazdan Thermal Power Plant to Shinuhayr substation and existing Lalvar and Noyemberyan power transmission lines, including compensation and grievance mechanisms for land acquisition and resettlement.

Part B: Technical assistance

Provision of goods, technical assistance, including Training and Operating Costs, to the HVENC to strengthen its staff capacity in technical supervision, planning, procurement, financial management and Project management and supervision of field works.

The financing of the Project consists of the following parts:

Category	Amount of Loan allocated (in US dollars)	Percentage of expenses to be financed (excluding taxes)
Goods, works, non-consulting services, consultants’ services including training and audit, and operating costs for the Project	35,902,500	100%
Land acquisition/ grievance mechanisms under the Project	2,000,000	100%
Refund of the preparation advance	1,000,000	Amount to be reimbursed as per point 2.07(a) of the general provision
Front-end fee	97,500	Amount to be paid as per point 2.03 of the loan agreement and point 2.07(b) of the general provision
Total	<u>39,000,000</u>	

The legal address of the Company is Z. Andranik 1, Yerevan, Armenia.

## 2 Significant accounting policies

### 2.1 Basis of preparation

The project financial statements were prepared in accordance with the accrual basis of accounting as well as the International Bank for Reconstruction and Development guidelines and the relevant points of the requirements of the Loan Agreement number 8055-AM. Significant accounting policies are disclosed below.

### 2.2 Functional and presentation currency

The national currency of the Republic of Armenia is Armenian dram. These project financial statements are presented in US dollars (presentation currency).

In preparing the project financial statements, transactions in currencies other than US dollar are recorded at the rates of exchange defined by the Central Bank of Armenia prevailing on the dates of the transactions. For direct payments denominated in currencies other than the presentation currency to the contractor/consultant from the International Bank for Reconstruction and Development share, the exchange rate set out for the presentation of the operation in the system client connection (<https://clientconnection.worldbank.org>) is used. At each reporting date bank balances, advances and payables denominated in foreign currencies are retranslated at the rate defined by the Central Bank of Armenia prevailing on that date, which is 483.75 Armenian drams for 1 US dollar as of 31 December 2018 (as of 31 December 2017: 484.10 Armenian drams for 1 US dollar). Any exchange rate differences are recognized in the statement of the Project sources and uses of funds and the accumulated figure of exchange rate difference is disclosed in the Statement of financial position under "Funds".

### 2.3 Project financing

The financing received in the framework of the Loan Agreement number 8055-AM is recorded in the statement of financial position as "Accumulated Project financing" and is recognized at each replenishment. In addition, the current year funds received are disclosed in the statement of Project sources and uses of funds, showing the sources of funds.

### 2.4 Project expenses

The Project expenses are recognized on the accrual basis of accounting. The accumulated Project expenses are disclosed in the statement of financial position under assets. In addition, current year expenses are disclosed in the statement of Project sources and uses of funds and statement of uses of funds by Project activities.

### 2.5 The IBRD financing

To finance eligible expenditures for the Loan Agreement number 8055-AM, the International Bank for Reconstruction and Development disburses proceeds from the Project account using one or more of the disbursement methods, which are stated below:

a. Reimbursement

The Bank may reimburse the borrower to finance eligible expenditures that the borrower has prefunded from its own resources.

b. Advance

The Bank may advance loan proceeds into a designated account of the borrower to finance eligible expenditures as they are incurred and for which supporting documents will be provided at a later date.

c. Direct payments

The Bank may make payments, at the borrower's request, directly to a third party for eligible expenditures.

d. Special commitment

The Bank may pay amounts to a third party for eligible expenditures under special commitments entered into, in writing, at the borrower's request and on terms and conditions agreed between the Bank and the borrower.

### 3. Closing date of the Project

According to the Loan Agreement, the Project closing date was defined as 31 December 2019.

### 4. Advances

In US dollars	As of 31 December 2018	As of 31 December 2017
Tractebel Engineering S.A	66,072	69,178
Kalpataru Power Transmission LTD	-	168,918
Gam Arak Industrial Co.	741,852	834,565
State Budget of the Republic of Armenia	340,845	500,683
Other	2,205	3,300
	<u>1,150,974</u>	<u>1,576,644</u>

The balances of advance to State Budget are disclosed below:

In US dollars	As of 31 December 2018	As of 31 December 2017
Gam Arak Industrial Co.	107,177	107,099
Tractebel Engineering S.A	14,911	14,901
Hifab Oy	-	27,397
Value Added Tax and custom duties	175,140	309,972
Other	43,617	41,314
	<u>340,845</u>	<u>500,683</u>

### 5. Accounts payable

In US dollars	As of 31 December 2018	As of 31 December 2017
Hifab Oy	-	32,092
Kalpataru Power Transmission LTD	-	4,240,741
Gam Arak Industrial Co.	220,935	-
Geo Capital LLC	-	2,186
"High Voltage Electric Networks" CJSC	244,080	182,128
State Budget of the Republic of Armenia	-	193
Other	-	8,023
	<u>465,015</u>	<u>4,465,363</u>

## 6. Loan 8055-AM

In US dollars

	For the year ended 31 December 2018	As of 31 December 2018
Special commitment	-	10,171,467
SOE and other procedures	4,852,218	5,565,881
Direct payments	-	11,058,195
Designated account advance	4,419,492	9,132,592
Redemption of the Designated account advance	(4,852,218)	(5,565,881)
Refunds		(11,603)
Front end fee	-	97,500
PPF and service fee		622,185
	<u>4,419,492</u>	<u>31,070,336</u>

## 7. Net increase in working capital

In US dollars

	For the year ended 31 December 2018	As of 31 December 2018
Increase in bank balances	9,264	166,711
Increase/(decrease) in advances	(425,670)	1,150,974
(Increase)/decrease in payables	4,000,348	(465,015)
	<u>3,583,942</u>	<u>852,670</u>

## 8. Reconciliation between the amounts received by the “High Voltage Electric Networks” CJSC and disbursed by the World Bank

Loan number 8055-AM  
For the year ended 31 December 2018  
In US dollars

Category	Appl.	Company	The World Bank	Difference
Goods, works, non-consulting services, consultants' services, including training and audit, and operating costs for Project	DA-112	2,908,699	2,908,699	-
	DA-114	165,654	165,654	-
	DA-116	33,990	33,990	-
	DA-119	810,584	810,584	-
		<u>3,918,927</u>	<u>3,918,927</u>	<u>-</u>
Land acquisition/grievance mechanisms under the Project	DA-121	933,291	933,291	-
		<u>933,291</u>	<u>933,291</u>	<u>-</u>
Advance to/(redemption from) designated account	DA-112	(3,841,990)	(3,841,990)	-
	DA-113	11,000	11,000	-
	DA-114	(165,654)	(165,654)	-
	DA-115	32,000	32,000	-
	DA-116	(33,990)	(33,990)	-
	DA-117	745,000	745,000	-
	DA-118	65,000	65,000	-
	DA-119	(810,584)	(810,584)	-
	DA-120	166,492	166,492	-
	DA-121	3,400,000	3,400,000	-
		<u>(432,726)</u>	<u>(432,726)</u>	<u>-</u>
Total		<u>4,419,492</u>	<u>4,419,492</u>	<u>-</u>

## 9. Legal issues

The Audit Chamber of the Republic of Armenia has revealed certain inconsistencies, as well as other facts in the framework of the loan project implemented by the Company. As of the reporting date the management of the Company cannot assess the effect of these investigations on the effectiveness of the Project.