INDEPENDENT AUDITOR’S REPORT

On

ENERGY SECTOR PROGRAM – PHASE 1 PROJECT

Implemented by

MINISTRY OF ENERGY AND NATURAL RESOURCES
GENERAL DIRECTORATE FOR EU AFFAIRS AND FOREIGN RELATIONS

And

Financed Under
World Bank Grant Agreement numbered TF016532-TR

As of December 31, 2016 and For The Year Then Ended

Report Number
84/14 - 34/16

Prepared by:

Nuri ATEŞ
Senior Treasury Controller

Selçuk KIRBAŞ
Junior Treasury Controller

22 June 2017
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A. Project Summary

The Grant Agreement for the Energy Sector Program - Phase 1 Project with European Union Instrument for Pre-Accession Trust Fund Grant Number TF016532-TR was signed on 30/05/2014 by the World Bank acting as administrator of the aforementioned Trust Fund and Undersecretary of Ministry of Energy and Natural Resources representing the recipient of the grant, Republic of Turkey. The World Bank agreed to extend to the recipient, on the terms and conditions set forth or referred to in the Grant Agreement, a grant in an amount equal to EUR 10.625.000.

The objective of the Energy Sector Program - Phase 1 Project (Project) is enhancement of the Turkish Energy Sector in line with the EU energy priorities and strategies in energy efficiency, renewable energy and the natural gas market.

Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations, Department for EU Affairs and IFIs was appointed by the Grant Agreement as the project implementation unit to carry out the Project.

The project consists of the following parts;

- Part A: Ministry of Energy and Natural Resources
- Part B: Natural Gas Market Development
- Part C: Renewable Energy Development
- Part D: Energy Efficiency Promotion
- Part E: Visibility and Public Awareness

According to the provisions of the Grant Agreement, the procurements made for the Project are classified into a single category named "Consultants' Services Under the Project". According to the Section IV article B(2) of the Schedule 2 "Project Execution" part of the Grant Agreement, the closing date of the Project is March 31, 2017 originally. Out of the negotiations between the World Bank and the Ministry of Energy and Natural Resources, the closing date of the Project has been postponed to September 28, 2017.

The expenditure realized throughout the current audit period of 01.01.2016-31.12.2016 is EUR 2.747.701,84 resulting in the cumulative spending by the end of the audit period amount to EUR 3.476.701,84.

B. Objectives of Audit

The objectives of our audit are;

a) To give an opinion on whether the financial statements, prepared as of December 31, 2016 and for the period then ended, present fairly, in all material respects, the financial position of the project in accordance with the cash receipts and disbursements basis of accounting,
b) To determine, as of December 31, 2016, whether the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations has complied, in all material respects, with the rules and procedures of the Grant Agreement numbered TF016532-TR,

c) To examine whether adequate supporting documentation has been maintained to support claims to the World Bank for reimbursements of expenditures incurred with respect to SOEs and evaluate eligibility of these expenditures for financing under the Grant Agreement.

C. Scope of Audit

We have performed an audit of financial statements of Energy Sector Program - Phase 1 Project as of December 31, 2016 and for the period then ended in accordance with the cash receipts and disbursements basis of accounting. We have also performed a compliance audit on whether project activities are in line with the Grant Agreement.

Our audit was conducted in accordance with International Standards on Auditing published by International Federation of Accountants (IFAC) applicable to the audit of financial statements and compliance auditing.

There was no limitation in our scope for the Project's audit.

D. Audit Results

For the financial statements of project; our audit resulted with an unqualified opinion.

As of December 31, 2016, Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations has complied, in all material respects, with the rules and procedures of the Grant Agreement numbered TF016532-TR.

In addition, with respect to SOEs, adequate supporting documentation has been maintained to support claims to the World Bank for reimbursements of expenditures incurred; and which expenditures are eligible for financing under the Grant Agreement numbered TF016532-TR.

E. Management Recommendations

A management letter, dated June 22, 2017, to the attention of the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations was issued separately from this report. The objective of this Management Letter is to enable the auditors to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditors have identified during the audit and that, in the auditors' professional judgment, are of sufficient importance to merit their respective attentions. For this purpose, our recommendations are attached to the Letter.
INDEPENDENT AUDITOR’S REPORT &
FINANCIAL STATEMENTS OF THE PROJECT
INDEPENDENT AUDITOR'S REPORT

TO MINISTRY OF ENERGY AND NATURAL RESOURCES,
General Directorate for EU Affairs and Foreign Relations, ANKARA

Opinion

We have audited the Statement of Sources and Uses of Funds, Statement of Cumulative Investments, Statement of Requests for Reimbursement (SOE Statement) and Statement of Special Account of the Energy Sector Program - Phase 1 Project as of December 31, 2016, and for the period then ended, and a summary of significant accounting policies and other explanatory information. The financial statements have been prepared by Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations based on relevant provisions of the Grant Agreement Numbered TF016532-TR.

In our opinion;

a) The accompanying Statement of Sources and Uses of Funds, Statement of Cumulative Investments, Statement of Requests for Reimbursement (SOE Statement) and Statement of Special Account present fairly, in all material respects, the financial position and accounting policies of the Energy Sector Program - Phase 1 Project as of December 31, 2016 and for the period then ended in accordance with the provisions of the Grant Agreement Numbered TF016532-TR.

b) Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations, as of December 31, 2016 has complied with, in all material respects, the requirements of the Grant Agreement Numbered TF016532-TR.

c) With respect to SOEs, adequate supporting documentation has been maintained to support claims to the World Bank for reimbursement of expenditures incurred, and these expenditures are eligible for financing under the Grant Agreement Numbered TF016532-TR.

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 Financial Statements" section of this report. We are independent of the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations within the meaning of ethical requirements and have fulfilled our other responsibilities under those ethical requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Basis of Accounting and Restriction on Distribution and Use

We draw attention to Note “2” to the financial statements, which describe the basis of accounting.
The financial statements are prepared to assist the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations to comply with the financial reporting provisions of the World Bank Grant Agreement Numbered TF016532-TR. As a result, the financial statements may not be suitable for another purpose. Our report is intended solely for the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations, Undersecretariat of Treasury, and World Bank, and should not be distributed or used by other parties.

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

Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations is responsible for the preparation and fair presentation of these financial statements in accordance with Grant Agreement Numbered TF016532-TR, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Those charged with governance are responsible for overseeing the Ministry of Energy and Natural Resources, General Directorate for EU Affairs and Foreign Relations’ financial reporting process.

Auditor’s Responsibilities for the Audit of the Financial Statements

The objectives of our audit are to obtain reasonable assurance about whether the 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 financial statements.

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

- Identify and assess the risks of material misstatement of the 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 entity’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 financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We are required to communicate with those charged with governance 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 are also required to provide those charged with governance 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, related safeguards.

Ahmet Umit SUCU
Acting Chairman of
Board of Treasury Controllers

Ali ÇALIŞKAN
(Audit Partner)
Vice-Chairman

Nuri ATEŞ
Senior Treasury Controller

Selçuk KIRBAŞ
Junior Treasury Controller

Date: June 22, 2017
Address: T.C. Başbakanlık Hazine Müsteşarlığı
Hazine Kontrolörleri Kurulu Başkanlığı
06510 Ankara/TURKEY
## I- SOURCE OF FUNDS

<table>
<thead>
<tr>
<th>Notes</th>
<th>Actual YTD</th>
<th>Actual Cumulative</th>
<th>Planned YTD</th>
<th>Planned Cumulative</th>
<th>Variance YTD</th>
<th>Variance Cumulative</th>
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<td>2- Special Account</td>
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<td>5,216,077,00</td>
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<td>0,00</td>
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<td>a- Advance</td>
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<td>3,216,077,00</td>
<td>3,216,077,00</td>
<td>3,216,077,00</td>
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<td>c- Summary Sheets</td>
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<td>TOTAL SOURCES</td>
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<td>5,216,077,00</td>
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## II- USES OF FUNDS

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<tr>
<th>Notes</th>
<th>YTD</th>
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<td>Section A-E: CS-01 Acquis Alignment &amp; Institutional Capacity of MENR Unbundling Support of BOTAŞ and Visibility &amp; Public Awareness</td>
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<td>1,410,884,64</td>
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<td>Section B: CS-03 Design and Implementation Plan for Gas Trading Platform</td>
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<td>Section D: CS-04 Energy Efficiency</td>
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<tr>
<td>NET USES OF FUNDS</td>
<td>2,747,701,84</td>
<td>3,476,701,84</td>
</tr>
</tbody>
</table>

## III. Cash at the beginning of the period
1,271,000,00

## IV. Cash at the end of the period
1,739,375,16

Ali Muralı BECERİKLİ
Head Of Department
### MINISTRY OF ENERGY AND NATURAL RESOURCES
### GENERAL DIRECTORATE OF FOREIGN RELATIONS AND EU
### ENERGY SECTOR PROGRAMME PHASE-I PROJECT
(EU/IPA GRANT NUMBER: TR016532-TR)
### STATEMENT OF CUMULATIVE INVESTMENTS
As of December 31, 2016 and For The Year Then Ended (In EURO)

#### 1- INVESTMENTS

<table>
<thead>
<tr>
<th>Component Name</th>
<th>Actual YTD</th>
<th>Actual Cumulative</th>
<th>Planned YTD</th>
<th>Planned Cumulative</th>
<th>Variance YTD</th>
<th>Variance Cumulative</th>
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<tbody>
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<td>1- INVESTMENT COSTS</td>
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<tr>
<td>Section A-E: CS-01 Acquis Alignment &amp; Institutional Capacity of MENR Unbundling Support of BOTAS and Visibility &amp; Public Awareness</td>
<td>906.884,64</td>
<td>1.410.884,64</td>
<td>906.884,64</td>
<td>1.410.884,64</td>
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<td>0,00</td>
</tr>
<tr>
<td>Section B: CS-03 Design and Implementation Plan for Gas Trading Platform</td>
<td>675.000,00</td>
<td>900.000,00</td>
<td>675.000,00</td>
<td>900.000,00</td>
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<td>0,00</td>
</tr>
<tr>
<td>Section D: CS-04 Energy Efficiency</td>
<td>1.056.077,00</td>
<td>1.056.077,00</td>
<td>1.056.077,00</td>
<td>1.056.077,00</td>
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<td>0,00</td>
</tr>
<tr>
<td>TOTAL INVESTMENT COSTS</td>
<td>2.747.701,84</td>
<td>3.476.701,84</td>
<td>2.747.701,84</td>
<td>3.476.701,84</td>
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<td>PROJECT INVESTMENTS</td>
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#### 2- INVESTMENTS BY THE CATEGORIES

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<th>Category Name</th>
<th>Actual YTD</th>
<th>Actual Cumulative</th>
<th>Planned YTD</th>
<th>Planned Cumulative</th>
<th>Variance YTD</th>
<th>Variance Cumulative</th>
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<tbody>
<tr>
<td>2- Consultancy services within the project</td>
<td>2.747.701,84</td>
<td>3.476.701,84</td>
<td>2.747.701,84</td>
<td>3.476.701,84</td>
<td>0,00</td>
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</tbody>
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Ali Murat BEGERIKLI
Head of Department
MINISTRY OF ENERGY AND NATURAL RESOURCES
GENERAL DIRECTORATE OF FOREIGN RELATIONS AND EU
ENERGY SECTOR PROGRAMME PHASE-I PROJECT
(EU/PA GRANT NUMBER: TR016532-TR)
STATEMENT OF REQUESTS FOR DISBURSEMENT (SOE STATEMENT)
As of December 31, 2016 and For The Year Then Ended (In EURO)

<table>
<thead>
<tr>
<th>I- REQUEST REIMBURSED</th>
<th>Disbursement Categories</th>
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<tr>
<td>Application Date</td>
<td>Application Nr</td>
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<td>22.1.2016</td>
<td>MENR-2</td>
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<tr>
<td>28.6.2016</td>
<td>MENR-3</td>
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<td>Total</td>
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<table>
<thead>
<tr>
<th>II- PENDING REIMBURSEMENT</th>
<th>Disbursement Categories</th>
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</thead>
<tbody>
<tr>
<td>Application Date</td>
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<td></td>
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<tr>
<td>Total</td>
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<p>| III- TOTAL AMOUNT OF WITHDRAWAL APPLICATIONS |</p>
<table>
<thead>
<tr>
<th>Consultancy Services</th>
<th>Total</th>
<th>Paid Amount</th>
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<tbody>
<tr>
<td>3.216.077,00</td>
<td>3.216.077,00</td>
<td>3.216.077,00</td>
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</tbody>
</table>

Ali Murat BECERİKLİ
Head of Department
MINISTRY OF ENERGY AND NATURAL RESOURCES
GENERAL DIRECTORATE OF FOREIGN RELATIONS AND EU
ENERGY SECTOR PROGRAMME PHASE-I PROJECT
(EU/IPA GRANT NUMBER: TR016532-TR)
SPECIAL ACCOUNT STATEMENT
As of December 31, 2016 and For The Year Then Ended (In EURO)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
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<tbody>
<tr>
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<tr>
<td>Reimbursements to SA</td>
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<tr>
<td>a) Advance</td>
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</tr>
<tr>
<td>b) SOE</td>
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<tr>
<td>c) Summary Sheet</td>
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<td>Ozel Hesaba Yapilan ladeler</td>
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<td>Available Funds</td>
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<td>Payment Made for Expenditures</td>
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<td>Service charges for the Account</td>
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<tr>
<td>Total Uses of Funds from SA</td>
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</tr>
<tr>
<td>Closing Balance</td>
<td>1,739,375.16</td>
</tr>
</tbody>
</table>

Ali Murat BEGERIKLI
Head of Department
I. OBJECTIVES AND STRUCTURE OF THE PROJECT/GRANT

The objective of the Project is the enhancement of the Turkish energy sector in line with the EU Energy priorities and strategies in energy efficiency, renewable energy, and the natural gas market.

The Project consists of the following parts:

Part A. Ministry of Energy and Natural Resources

Carry out the following in relationship to the Ministry of Energy and Natural Resources (“MENR”):

(a) Institutional review and capacity building of MENR, including preparation of a report on identification of the existing methodologies used for energy forecasting and planning and a plan for MENR to establish a technical and administrative structure for the management of energy information system.

(b) Review of the alignment of Turkey’s legal and institutional framework for electricity, natural gas, energy efficiency and renewable energy with the EU’s energy acquis, including identification of the main differences (gaps) between Turkey’s legislation and its implementation and the EU acquis (including EU’s third package of energy reforms) and carrying out gap analyses and regulatory impact assessments and cost/benefit analyses for each of the four regulatory areas to provide a basis for effective alignment.

Part B. Natural Gas Market Development

Carry out the following with respect to the development of the natural gas sector:

(a) Provision of support for the unbundling of the national gas supply and transmission company BOTAS, including preparation of a study of main obstacles and bottlenecks for further liberalisation of the market, preparation of a study on ways and methods of establishing a transparent and non-discriminatory framework, formulation of measures to promote the market, and introduction of measures to protect customers.

(b) Provision of support for the design of, and regulations for, a gas trading platform and a plan for effective gas market opening, including review of wholesale market opening and gas trading arrangements and volumes, and market participants’ interest and capacity to operate on a gas trading platform, preparation of a detailed survey and a report of best practices, and preparation of a further need assessment report and technical and functional design of a gas trading platform software.
Part C. Renewable Energy Development

Carry out the following with respect to the development of the renewable energy sector:

(a) Review of current situation and barriers, including preparation of a study of main obstacles and bottlenecks in the renewable energy sector, provision of support for the establishment of a monitoring and control mechanism for solar power plants, and review of issues and options in financing and support mechanisms for the promotion and implementation of small-scale renewable energy projects.

(b) Integration of the renewable energy grid to distribution and transmission systems, including preparation of a report for the identification of technical and administrative obstacles preventing the integration of small scale generation of electricity from renewable sources and a study covering a needs assessment and feasibility of the steps to be taken to improve the grid connection of renewable electricity generation facilities to the electricity grid.

(c) Provision of business development services to small and medium-sized industries (that is, an enterprise that has less than 40,000,000 Turkish Lira in sales and employs fewer than 250 employees), including preparation of feasibility studies and business plans.

Part D. Energy Efficiency Promotion

Carry out the following with respect to the promotion of energy efficiency (“EE”):

(a) Market development in the industrial and building sectors, including preparation of an action plan under Turkey’s 2012 Energy Efficiency Strategy, preparation of a study on the current situation of the EE market with respect to the EU acquis, provision of program management, policy and market support for energy service company (“ESCO”) development and financing mechanisms and provision of business development services (including preparation of feasibility studies and business plans) to small and medium-sized enterprises (that is, an enterprise that has less than 40,000,000 Turkish Lira in sales and employs fewer than 250 employees).

(b) Building capacity in the commercial energy efficiency lending market, including preparation of guidelines for ESCOs and individual firms regarding lending mechanisms and procedures and defining and assessing the feasibility of new banking products and financing modalities.

Part E. Visibility and Public Awareness

Establishment of a website to showcase Project activities, enhancement of MENR’s website and organization of conferences, workshops, and public awareness campaigns related to the above described Project activities.

II. DURATION OF THE GRANT

Closing date of the Project is September 28, 2017.

III. FINANCING OF THE GRANT

Total amount of the € 10,625,000 (ten million and six hundred and twenty-five thousand Euro) all of which is funded by the World Bank.
IV. THE ACCOUNTING PRINCIPLES AND POLICIES WITH CHART OF ACCOUNTS AND FISCAL TABLES

1. Accounting Standard Applied

The Chart of Accounts of the Project has been prepared on an “Accrual Basis” in accordance with the International Accounting Standards. However, the accounting procedures function on a “cash basis” in order to avoid exchange differences in investment expenditures and costs.

2. Accounting Basis

The entire fiscal tables are prepared in accordance with the cash basis. In line with this basis, after the financial transactions and economic events took place, they are taken into accounting records when the cash or quasi cash assets have been collected or paid and are reflected to fiscal tables of the related period.

3. Currency

Our accounting records are kept by applying real time exchange for both currencies, Turkish Lira and Euro which is the financial currency of the loan agreement signed between the World Bank and the Turkish Government.

4. Fixed Assets

The fixed assets which have been purchased by the project resources are recorded in line with the costs on the procurement date, the project components and the expenditure categories. The amortization records related with the project assets are not carried out.

5. Exchange Transactions

Euro and TL records of the utilization of the resources and funds, and the investment expenditures, the daily current exchange buying rate on the collection and payment date published by the TC Ziraat Bank, is taken into account.

6. Receivables

The receivables are specified by net asset basis. Since the accounting system functions on a cash basis, the “receivables” are formulated by advance payments to the components and staff responsible. Advance payments in the period of arrangement of standard periodical reports by the World Bank are added to the related investment accounts.

7. Continuity

The Project shall execute the activities by September 28, 2017 or another date which shall be negotiated between the World Bank and the Republic of Turkey.
8. Severance Pay

In accordance with the Turkish Law the severance pay is paid in case of retirement or dismissal. The staff of the Projects Implementation Unit is the staff of MENR General Directorate of Foreign Relations and EU. The contracted consultants work under working contracts. Due to this fact, the severance pay is not under discussion and not made any provision.

9. The Capitalization of the Financial Expenditures

Neither commission fee nor charge has been paid to The Central Bank of Republic of Turkey.

10. Refunds to the special account

No amount has been refunded paid to the Republic of Turkey Ziraat Bank where Project Special Account exists.

V. THE LIMITED UTILIZATION OF THE FUND AND OTHER ASSETS

In accordance with the grant agreement signed between the Republic of Turkey and the World Bank, the funds under the Special Account are restricted to be utilized only in line with the project/Grant objectives. Fixed assets procured with the project funds of MENR, are restricted only to be used in line with the project objectives by the closing date of the Project/Grant. MENR, in order to control such assets, during the project and sub-project implementations, has kept each record relevant to this issue.

VI. THE GRANT OF INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (IBRD)

The amount of withdrawal from the grant for amount of € 10.625.000 to the account in the TC Ziraat Bank is € 5.216.077 as of December 31, 2016.

VII. THE ACTUAL CASH AMOUNT OF DECEMBER 31, 2016

The actual cash amount as of December 31, 2016 is as indicated in the chart below. The currency is stated in Euro.

<table>
<thead>
<tr>
<th></th>
<th>Loan Funds</th>
<th>Mutual Funds</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Special Account</td>
<td>1.739.375,16</td>
<td>0.00</td>
<td>1.739.375,16</td>
</tr>
<tr>
<td>Fixed Funds</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Checking Account</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Total</td>
<td>1.739.375,16</td>
<td>0.00</td>
<td>1.739.375,16</td>
</tr>
</tbody>
</table>
VIII. THE PLANNED EXPENDITURES FOR THE CURRENT YEAR

The expenditure planning for the year 2017 by grant activities are as follows: 5,000,000 € Euro for consultancy services. This total amount shall be received from the grant.

IX. DIFFERENCES BETWEEN THE REQUESTED AND PAID AMOUNTS UNDER THE SOE PROCEDURE

No withdrawal application has been made in the review period.

X. CORRECTION OF THE PREVIOUS YEAR'S FINANCIAL STATEMENTS

The Statement of Sources and Uses of Funds presented as of December 31, 2015 and for the period then ended erroneously included EUR 1,271,000 as advance and EUR 729,000 as SOE in terms of the sources of the funds. The sole source of the total funds as of the year 2015 amounting to EUR 2,000,000 is the advance payment disbursed by the World Bank into the special account. The Statement of Sources and Uses of Funds presented as of December 31, 2016 and for the period then ended (cumulative column) has been prepared in line with this correction pertaining to the previous year.

Ali Murat BECERİKLİ
Head of Department