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TRANSPORT REFORM AND REHABILITATION CENTER

LOAN NO.8547-GE
(EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT PROJECT)

Special Purpose Project Financial Statements

For the Period from 10 February 2016 to 31 December 2016

TRANSPORT REFORM AND REHABILITATION CENTER
EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT
LOAN NO.8547-GE

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TRANSPORT REFORM AND REHABILITATION CENTER
EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT
LOAN NO.8547-GE

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS FOR THE PERIOD FROM 10 FEBRUARY 2016 TO 31 DECEMBER 2016

Management of the East-West Highway Corridor Improvement Project (the "Project") implemented by the Transport Reform and Rehabilitation Center ("TRRC") is responsible for the preparation of the special purpose project financial statements that present fairly the financial position of the Project as at 31 December 2016, and its sources and uses of funds and movement in designated account for the period from 10 February 2016 to 31 December 2016, in compliance with the Cash Basis International Public Sector Accounting Standard, *Financial Reporting under the Cash Basis of Accounting* ("IPSAS – Cash Basis"), and in conformity with the World Bank's Financial Management Sector Board's "Guidelines: Annual Financial Reporting and Auditing for World Bank Financed Activities" (the "World Bank Guidelines").

In preparing the special purpose project financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IPSAS – Cash Basis are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Project, financial position and its sources and uses of funds and movements in designated accounts;
- Making an assessment of the Projects ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Project;
- Maintaining adequate accounting records that are sufficient to show and explain the Project's transactions and disclose with reasonable accuracy at any time the financial position of the Project, and which enable them to ensure that the special purpose project financial statements of the Project comply with the Guidelines on Annual Financial Reporting and Auditing for World Bank – Financed Activities issued by the World Bank's Financial Management Sector Board;
- Maintaining statutory accounting records in compliance with Georgian legislation;
- Taking such steps that are reasonably available to them to safeguard the assets of the Project; and
- Preventing and detecting fraud and other irregularities.

The special purpose project financial statements for the period from 10 February 2016 to 31 December 2016 were authorized for issue on 29 June 2017 by the Management.

On behalf of Management:

Giorgi Tsagareli
Director

29 June 2017

Marina Majagaladze
Financial Manager

29 June 2017

KPMG Georgia LLC
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4, Besiki Street
0108 Tbilisi, Georgia
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Independent Auditors' Report on Special Purpose Project Financial Statements

To the management of Transport Reform and Rehabilitation Center

Opinion

We have audited these special purpose project financial statements of the East-West Highway Corridor Improvement Project (the "Project"), financed under the International Bank for Reconstruction and Development (the "IBRD"), Loan Agreement No. 8547-GE, dated 10 February 2016, implemented by the Transport Reform and Rehabilitation Center (the "Center"), which comprise the Statement of Balance Sheet as at 31 December 2016 and the Statements of Sources and Uses of Funds, Statement of Expenditures Withdrawal Schedule ("SOEs") and Special Account Statement for the period from 10 February 2016 to 31 December 2016, and notes, comprising a summary of significant accounting policies and other explanatory information. The special purpose project financial statements have been prepared by management in accordance with the International Public Sector Accounting Standard: Financial Reporting Under the Cash Basis of Accounting and in conformity with the World Bank's Financial Management Sector Board's "Guidelines: Annual Financial Reporting and Auditing for World Bank-Financed Activities" (the "World Bank Guidelines") as described in Note 2 to the special purpose project financial statements.

In our opinion, the accompanying special purpose project financial statements present fairly, in all material respects, the financial position of the Project as at 31 December 2016, and its sources and uses of funds for the for the period from 10 February 2016 to 31 December 2016 in accordance with the International Public Sector Accounting Standard: Financial Reporting Under the Cash Basis of Accounting and the World Bank Guidelines.

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 Auditors' Responsibilities for the Audit of the Special Purpose Project Financial Statements section of our report. We are independent of the Center in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Matter

Data included on pages 4 to 11 of the accompanying special purpose project financial statements that are marked as *"Unaudited"* have not been audited.

Emphasis of Matter - Basis of Accounting and Restriction on Use

We draw attention to Note 2 to the special purpose project financial statements, which describes the basis of accounting. The special purpose project financial statements are prepared to assist the Center to comply with the requirements of IBRD and for providing information to the Government of Georgia and IBRD to assist them in evaluating the Project implementation. As a result, the special purpose project financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

KPMG Georgia LLC, a company incorporated under the Laws of Georgia, a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

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

Management is responsible for the preparation and fair presentation of these special purpose project financial statements in accordance with the International Public Sector Accounting Standard: Financial Reporting Under the Cash Basis of Accounting and the World Bank Guidelines, for determining the acceptability of the basis of accounting and for such internal control as management determines is necessary to enable the preparation of special purpose project financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditors' Responsibilities for the Audit of the Special Purpose Project Financial Statements

Our objectives are to obtain reasonable assurance about whether the special purpose project financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' 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 special purpose 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 special purpose 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 Center'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 special purpose project financial statements, including the disclosures, and whether the special purpose project financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We 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.

The engagement partner on the audit resulting in this independent auditors' report is:

Karen Safaryan

KPMG Georgia LLC
Tbilisi, Georgia
29 June 2017

TRANSPORT REFORM AND REHABILITATION CENTER
EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT
LOAN NO. 8547-GE

STATEMENT OF SOURCES AND USES OF FUNDS
FOR THE PERIOD FROM 10 FEBRUARY 2016 TO 31 DECEMBER 2016
(in US Dollars)

	Actual as at 31 December 2016		Planned as at 31 December 2016		Variance	
	Period to date	Cumulative to date	Period to date	Cumulative to date	Period to date	Cumulative to date
			Unaudited	*Unaudited*	*Unaudited*	*Unaudited*
FUNDS RECEIVED BY SOURCES						
International Bank for Reconstruction and Development ("IBRD") Funds	1,150,000	1,150,000				
Government of Georgia ("GoG") co-financing	994,153	994,153				
TOTAL FUNDS RECEIVED	**2,144,153**	**2,144,153**				
LESS: EXPENDITURES						
Component 1 – Improvement and Asset Management of the E-60 Highway (IBRD - 85%)	-	-	-	-	-	-
Component 2 - Technical assistance to MoESD (IBRD - 85%)	35,295	35,295	35,295	35,295	-	-
IBRD TOTAL	**35,295**	**35,295**	**35,295**	**35,295**	**-**	**-**
Component 1 – Improvement and Asset Management of the E-60 Highway (GoG -15%)	994,153	994,153	994,153	994,153	-	-
Component 2 – Technical assistance to MoESD (GoG - 15%)	-	-	-	-	-	-
GoG TOTAL	**994,153**	**994,153**	**994,153**	**994,153**	**-**	**-**
TOTAL EXPENDITURES BY COMPONENTS	**1,029,448**	**1,029,448**	**1,029,448**	**1,029,448**	**-**	**-**
UNALLOCATED						
Front end fees	350,000	350,000	350,000	350,000	-	-
TOTAL UNALLOCATED EXPENDITURES	**350,000**	**350,000**	**350,000**	**350,000**	**-**	**-**
TOTAL PROJECT EXPENDITURES	**1,379,448**	**1,379,448**	**1,379,448**	**1,379,448**	**-**	**-**
NET FLOWS OF FUNDS	**764,705**	**764,705**				

The special purpose project financial statements were approved by the management of Transport Reform and Rehabilitation Center on 29 June 2017 and were signed on its behalf by:

Giorgi Tsagareli
Director

Marina Majagaladze
Financial Manager

29 June 2017

29 June 2017

The notes on pages 7 to 11 form an integral part of these special purpose project financial statements.

TRANSPORT REFORM AND REHABILITATION CENTER
EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT
LOAN NO. 8547-GE

BALANCE SHEET STATEMENT
AS OF 31 DECEMBER 2016
(in US Dollars)

	31 December 2016
ASSETS	
IBRD Designated Account	764,705
TOTAL ASSETS	**764,705**
Funds received:	
Funds received from IBRD for the period from 10 February 2016 to 31 December 2016	1,150,000
Funds received from GoG for the period from 10 February 2016 to 31 December 2016	994,153
Total funds received	**2,144,153**
Project expenditures:	
Financed by IBRD for the period from 10 February 2016 to 31 December 2016	35,295
Financed by GoG for the period from 10 February 2016 to 31 December 2016	994,153
Unallocated	350,000
Total project expenditures for the period from 10 February 2016 to 31 December 2016	**1,379,448**
TOTAL PROJECT EXPENDITURES AND OTHER FUNDS FOR THE PERIOD	**764,705**

The special purpose project financial statements were approved by the management of Transport Reform and Rehabilitation Center on 29 June 2017 and were signed on its behalf by:

Giorgi Tsagareli
Director

29 June 2017

Marina Majagaladze
Financial Manager

29 June 2017

The notes on pages 7 to 11 form an integral part of these special purpose project financial statements

TRANSPORT REFORM AND REHABILITATION CENTER
EAST-WEST HIGHWAY CORRIDOR IMPROVEMENT
LOAN NO. 8547-GE

DESIGNATED ACCOUNT STATEMENT
FOR THE PERIOD FROM 10 FEBRUARY 2016 TO 31 DECEMBER 2015
(in US Dollars)

Account No.	202250201
Depository Bank	State Treasury
Address	16 V. Gorgasali street Tbilisi, 0114 Georgia

Balance as at 1 January 2016	-
ADD	
Funds received from IBRD in 2016	800,000
DEDUCT	
Funds used for the Project expenditures in 2016	(35,295)
Balance as at 31 December 2016	**764,705**

The special purpose project financial statements were approved by the management of Transport Reform and Rehabilitation Center on 29 June 2017 and were signed on its behalf by:

Giorgi Tsagareli
Director

29 June 2017

Marina Majagaladze
Financial Manager

29 June 2017

The notes on pages 7 to 11 form an integral part of these special purpose project financial statements.

1. BACKGROUND

The Investment Center for Euro-Asian Transport Corridor was established in 1995 as a non-entrepreneurial and non-profit legal entity under the laws of Georgia in accordance with the Georgian Presidential Decree. The founder of the Investment Center for Euro-Asian Transport Corridor is the Georgian Government. N119 dated 16 April 1995. The founder of the investment center for Euro-Asian Transport Corridor is the Georgian Government.

A project unit named "Transport Reform and Rehabilitation Center" (the "Center") was formed within the Investment Center for Euro-Asian Transport Corridor. The Center's principal activity is to manage allocated credits/loans received from the International Development Association ("IDA"), the International Bank for Reconstruction and Development ("IBRD"), the Asian Development Bank (ADB) and the European Investment Bank (EIB) and monitor the implementation of transport sector projects.

The Center implements the East-West Highway Corridor Improvement Project (the "Project"), financed under the International Bank for Reconstruction and Development (the "IBRD"). Loan Agreement No.8547-GE (the "Agreement") in the amount of US Dollars ("USD") 140 million was signed between the Government of Georgia ("GoG") and IBRD on 10 February 2016 ("inception"). The main objectives of the loan are: upgrading of existing 2-lane East-West Highway from Zemo Osiauri-Km 5.8 to Chumateleti (8.0 km) to a 2-lane dual carriageway road, including 7 bridges and 3 tunnels. Build on the on-going institutional strengthening activities financed under the on-going highway project. Also provide support to strengthen Roads Department's (RD) Intelligent Transport System (ITS) Unit and complement the road safety activities by providing real time information to improve mobility and traffic safety along the corridor. The project will also provide technical support to Ministry of Economy and Sustainable Development (MESD) to develop and implement a logistics strategy.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance – These special purpose project financial statements have been prepared in accordance with the Cash Basis International Public Sector Accounting Standard, *Financial Reporting under a Cash Basis of Accounting* and in conformity with the World Bank's Financial Management Sector Board's "Guidelines: Annual Financial Reporting and Auditing for World Bank-Financed Activities" (the "World Bank Guidelines").

The purpose of these special purpose project financial statements is to provide information to the Government of Georgia and International Bank for Reconstruction and Development (IBRD) to assist them in evaluating the Project implementation.

Cash basis of accounting - Project financing is recognized as a source of project funds when the cash is received. Project expenditures are recognized as a use of project funds when the payments are made.

Presentation currency – The national currency of Georgia is the Georgian Lari ("GEL"). These special purpose project financial statements are presented in United States Dollars ("US Dollar" or "USD"), since management believes that this currency is more meaningful for the users of the special purpose project financial statements. All financial information presented in USD has been rounded to the nearest USD unless otherwise stated.

Transactions in other currencies – Transactions in currencies other than reporting currencies are converted to US Dollars at the exchange rate prevailing at the date of the transaction.

Cash – Cash represents balances with State Treasury.

3. DESIGNATED ACCOUNT

Designated account is a designated disbursement account of the Project that will be maintained in US Dollars at the State Treasury to ensure the payment of eligible expenditures, within defined limits, which do not require individual authorization from IBRD in accordance with the Agreement.

4. BASIS OF FUNDING

The total cost of the Project is estimated at USD 164 million. The expenditures of all works, goods and consultant service contracts, including all applicable taxes amounted to USD 140 million, which is 85% of total Project cost, is co-financed by proceeds received from IBRD. The balance of USD 24 million, which is 15% of total Project cost is co-financed by proceeds received from the GoG.

The land acquisition and associated resettlement costs are funded entirely by the GoG.

5. METHODS OF WITHDRAWAL

The methods of withdrawal used from the inception of the loan to 31 December 2016 were as follows:

(a) Designated Account

The Center withdraws the eligible amounts from the designated account and prepares and sends replenishment requests to the World Bank with authorized signatures. The replenishment requests and respective documentation are reviewed by the World Bank and an approved amount is transferred to the designated account.

(b) Direct Payment

Available amounts are drawn from time to time within limits determined under the loan agreement for direct payments of eligible expenditures for sub-projects. Direct payments are made by the World Bank directly to third parties. The Center forms withdrawal applications for request of direct payments and sends it to the World Bank, for settlement.

(c) GoG Current Account

The Project maintains a separate account where funds from the GOG are accumulated. The funds are further disbursed to sub-contractors based on the share of expenditures to be incurred. The project has common GEL account and special organization code for their funds in Treasury.

6. STATEMENT OF EXPENDITURES (SOE)

Withdrawals are to be made on the basis of SOEs for expenses on contracts within the following contractual limits:

(i) All expenditures for works valued at less than USD 10,000,000;
(ii) Goods and non-consulting services valued at less than USD 300,000;
(iii) Consultant services contracts (firms) valued at less than USD 200,000;
(iv) Consultant services contracts (individuals) valued at less than USD 50,000.

7. RECONCILIATION OF AMOUNTS SHOWN AS RECEIVED FROM THE IBRD TO ACTUAL EXPENDITURES OF THE PROJECT

	31 December 2016
Application of Withdrawals Schedule	
Expenses incurred in 2016 as per the Applications of Withdrawals Schedule	35,295
Expenses incurred in 2016 without Applications of Withdrawals Schedule	-
	35,295
IBRD funds received in 2016	1,150,000
Front and Fees	(350,000)
Add:	
Opening Balance	
Designated Account	-
	-
Less:	
Closing Balance	
Designated Account	764,705
	764,705
TOTAL EXPENDITURES INCURRED IN 2016	**35,295**

8. PROJECT EXPENDITURES BY COMPONENTS

Project activities	Actual as at 31 December 2016		Planned as at 31 December 2016		Variance	
	Period to date	Cumulative to date	Period to date	Cumulative to date	Period to date	Cumulative to date
			Unaudited	*Unaudited*	*Unaudited*	*Unaudited*
Component 1 – Improvement and Asset Management						
Land Acquisition	811,912	811,912	811,912	811,912	-	-
Compensation for land	182,241	182,241	182,241	182,241	-	-
TOTAL COMPONENT 1	**994,153**	**994,153**	**994,153**	**994,153**	**-**	**-**
Component 2 – Institutional Strengthening and Technical Assistance						
Feasibility Study	35,295	35,295	35,295	35,295	-	-
TOTAL COMPONENT 2	**35,295**	**35,295**	**35,295**	**35,295**	**-**	**-**
TOTAL EXPENDITURES BY COMPONENTS	**1,029,448**	**1,029,448**	**1,029,448**	**1,029,448**	**-**	**-**
UNALLOCATED						
Front end fees	350,000	350,000	350,000	350,000	-	-
TOTAL UNALLOCATED EXPENDITURE	**350,000**	**350,000**	**350,000**	**350,000**	**-**	**-**
TOTAL PROJECT EXPENDITURES	**1,379,448**	**1,379,448**	**1,379,448**	**1,379,448**	**-**	**-**

The Project consists of the following main components:

- Upgrading of existing 2-lane East-West Highway from Zemo Osiauri-Km 5.8 to Chumateleti to a 2-lane dual carriageway road. The section to be upgraded is approximately 8.0 km long and runs through hilly and mountainous terrain, thus requiring many structural works including 3 tunnels and 7 bridges. The upgrading of the road requires traffic capacity expansion, a dual carriageway including man-made structures in difficult topographic and geological conditions.
- Strengthening Roads Department's Intelligent Transport System Unit complement the road safety activities by providing real time information to improve mobility and traffic safety along the corridor. Also technical assistance to Ministry of Economy and Sustainable Development (MESD) to develop and implement a logistic strategy.

The categories of expenditures incurred are presented in line with the categories specified in the Agreement.

Each component of the Project are further divided into four types of expenses for the SOE purposes: civil works, goods, consultants' services and operating costs.

9. COMMITMENTS AND CONTINGENCIES

Management is not aware of any commitments and contingencies which would have a material impact on this special purpose project financial statements as at 31 December 2016 for the period then ended.

10. GEORGIAN OPERATING ENVIRONMENT

The Center's operations are located in Georgia. Consequently, the Center is exposed to the economic and financial markets of Georgia, which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The special purpose project financial statements reflect management's assessment of the impact of the Georgian operating environment on the operations of the Center. The future operating environment may differ from management's assessment.

11. EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

There were no significant events subsequent to the balance sheet date.

12. APPROVAL OF FINANCIAL STATEMENTS

These special purpose project financial statements were authorized for issue by the management of the Center on 29 June 2017.