JSC Liberty Bank and Subsidiaries

Consolidated financial statements

Year ended 31 December 2015
together with independent auditor's report

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Independent auditor's report

To the shareholders and Board of Directors of JSC Liberty Bank -

We have audited the accompanying consolidated financial statements of JSC Liberty Bank and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2015, and the consolidated statement of profit or loss, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the fairness of these consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing audit procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The audit procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the preparation and fair presentation of the consolidated 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 also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management of the audited entity, as well as evaluating the overall presentation of the consolidated financial statements.

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 consolidated financial statements present fairly, in all material respects, the financial position of the Group and its subsidiaries as at 31 December 2015, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

EY Georgia LLC

12 April 2016

Consolidated statement of financial position

As of 31 December 2015

(thousands of Georgian Lari)

	Notes	2015	2014
Assets			
Cash and cash equivalents	6	502,340	479,998
Amounts due from credit institutions	7	58,502	50,946
Loans to customers	8	641,116	692,110
Investment securities:	9		
- Loans and receivables		79,469	–
- Held to maturity		124,321	196,906
Property and equipment	10	128,617	118,797
Intangible assets	11	20,257	11,269
Prepayments	13	4,235	9,183
Other assets	13	14,889	19,148
Total assets		1,573,746	1,578,357
Liabilities			
Amounts due to credit institutions	14	118,915	6,037
Amounts due to customers	15	1,244,023	1,412,981
Current income tax liabilities		548	–
Deferred income tax liabilities	12	7,865	5,972
Other liabilities	13	13,199	12,864
Subordinated debt	16	58,346	15,846
Total liabilities		1,442,896	1,453,700
Equity	17		
Share capital		53,863	53,383
Additional paid-in capital		34,886	42,559
Treasury shares		(9,712)	–
Convertible preferred shares		6,139	6,139
Retained earnings		37,392	14,121
Other reserves		8,282	8,455
Total equity		130,850	124,657
Total liabilities and equity		1,573,746	1,578,357

Signed and authorised for release on behalf of the Management Board of the Bank:

Aleksi Khoroshvili — Chief Executive Officer

David Melikidze — Chief Financial Officer

12 April 2016

The accompanying notes on pages 6 to 56 are an integral part of these consolidated financial statements.

Consolidated statement of profit or loss

For the year ended 31 December 2015

(thousands of Georgian Lari)

	Notes	2015	2014
Interest income			
Loans to customers		229,009	203,419
Investment securities		17,147	12,743
Amounts due from credit institutions		4,991	2,853
		251,147	219,015
Interest expense			
Amounts due to customers		(110,280)	(111,537)
Amounts due to credit institutions		(337)	(237)
Subordinated debt		(5,780)	(274)
Other		–	(65)
		(116,397)	(112,113)
Net interest income		134,750	106,902
Loan impairment charge	8	(32,332)	(25,257)
Net interest income after loan impairment charge		102,418	81,645
Net fee and commission income	19	24,817	24,171
Net gains/(losses) from foreign currencies:			
- Dealing		21,479	6,931
- Translation differences		(15,626)	174
Other income	20	15,387	10,365
Non-interest income		46,057	41,641
Personnel expenses	21	(58,822)	(48,731)
General and administrative expenses	21	(34,381)	(28,877)
Depreciation and amortisation	10, 11	(16,555)	(15,145)
Other operating expenses		(3,774)	(4,860)
Other impairment and provisions reversal/(charge)	13	177	(3,190)
Non-interest expense		(113,355)	(100,803)
Profit before income tax expense		35,120	22,483
Income tax expense	12	(2,974)	(709)
Profit for the year		32,146	21,774
Earnings per share:	17		
- Basic and diluted earnings per share (in GEL full amount)		0.00576	0.00380

The accompanying notes on pages 6 to 56 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2015

(thousands of Georgian Lari)

	Notes	2015	2014
Profit for the year		32,146	21,774
Other comprehensive income			
Other comprehensive income not to be reclassified to profit or loss in subsequent periods:			
Revaluation of buildings	10	–	(13,380)
Income tax effect	12, 17	–	2,051
Net other comprehensive loss not to be reclassified to profit or loss in subsequent periods		–	(11,329)
Other comprehensive loss for the year, net of tax		–	(11,329)
Total comprehensive income for the year		32,146	10,445

The accompanying notes on pages 6 to 56 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2015

(thousands of Georgian Lari)

	Attributable to shareholders of the Bank						
	Share capital	*Additional paid-in capital*	*Treasury shares*	*Convertible preferred shares*	*Retained earnings / (accumulated losses)*	*Other reserves*	*Total*
31 December 2013	53,284	42,559	–	5,179	(7,196)	20,282	114,108
Total comprehensive income/(loss) for the year	–	–	–	–	21,774	(11,329)	10,445
Depreciation of revaluation reserve (Note 17)	–	–	–	–	423	(423)	–
Revaluation reserve of sold fixed assets (Note 17)	–	–	–	–	–	(75)	(75)
Dividends paid on the convertible preferred shares (Note 17)	–	–	–	–	(880)	–	(880)
Issue of share capital (Note 17)	99	–	–	–	–	–	99
Issue of the convertible preferred shares (Note 17)	–	–	–	960	–	–	960
31 December 2014	53,383	42,559	–	6,139	14,121	8,455	124,657
Total comprehensive income for the year	–	–	–	–	32,146	–	32,146
Depreciation of revaluation reserve (Note 17)	–	–	–	–	169	(169)	–
Revaluation reserve of sold fixed assets (Note 17)	–	–	–	–	–	(4)	(4)
Dividends paid on the ordinary shares (Note 17)	–	–	–	–	(8,000)	–	(8,000)
Dividends paid on the convertible preferred shares (Note 17)	–	–	–	–	(1,044)	–	(1,044)
Purchase of treasury shares (Note 17)	–	(7,673)	(9,712)	–	–	–	(17,385)
Issue of share capital (Note 17)	480	–	–	–	–	–	480
31 December 2015	53,863	34,886	(9,712)	6,139	37,392	8,282	130,850

The accompanying notes on pages 6 to 56 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2015

(thousands of Georgian Lari)

	Notes	2015	2014
Cash flows from operating activities			
Interest received		240,253	209,684
Interest paid		(108,305)	(105,664)
Fees and commissions received		30,215	28,154
Fees and commissions paid		(5,337)	(3,902)
Net realised gains from dealing in foreign currencies		21,639	6,713
Recoveries of assets previously written off	8, 13	733	564
Other income received		15,312	10,390
Personnel expenses paid		(56,888)	(47,481)
General, administrative and other operating expenses paid		(36,341)	(32,144)
Cash flows from operating activities before changes in operating assets and liabilities		101,281	66,314
Net (increase)/decrease in operating assets			
Amounts due from credit institutions		3,127	(10,093)
Loans to customers		32,465	(110,588)
Other assets		3,030	(3,154)
Net increase/(decrease) in operating liabilities			
Amounts due to credit institutions		112,107	3,560
Amounts due to customers		(250,539)	231,605
Other liabilities		(3,715)	(2,347)
Net cash flows (used in)/from operating activities before income tax		(2,244)	175,297
Income tax paid		–	–
Net cash (used in)/from operating activities		(2,244)	175,297
Cash flows from investing activities			
Proceeds from redemption of investments available for sale		166	42
Purchase of investment securities		(176,527)	(258,884)
Proceeds from redemption of investment securities		174,000	199,549
Purchase of intangibles, property and equipment		(31,195)	(22,054)
Proceeds from sale of property and equipment		128	187
Proceeds from sale of investment property		416	–
Proceeds from sale of repossessed property		217	–
Net cash used in investing activities		(32,795)	(81,160)
Cash flows from financing activities			
Proceeds from issue of share capital	17	480	99
Purchase of treasury shares	17	(17,385)	–
Sale of subordinated debt		34,481	15,534
Proceeds from issue of the convertible preferred shares		–	960
Dividends paid to shareholders of the ordinary shares	17	(8,000)	–
Dividends paid to shareholders of the convertible preferred shares	17	(1,044)	(880)
Net cash from financing activities		8,532	15,713
Effect of exchange rates changes on cash and cash equivalents		48,849	15,059
Net increase in cash and cash equivalents		22,342	124,909
Cash and cash equivalents, beginning	6	479,998	355,089
Cash and cash equivalents, ending	6	502,340	479,998

The accompanying notes on pages 6 to 56 are an integral part of these consolidated financial statements.

(thousands of Georgian Lari)

1. Principal activities

JSC Liberty Bank (the "Bank") is a joint stock company, formed in accordance with legislation of Georgia in 1993. The Bank operates under a general banking license No. 3500/10 issued by the National Bank of Georgia (the "NBG"), the central bank of Georgia, on 10 February 1993.

The Bank accepts deposits from the public and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its retail and corporate customers. Its main office is in Tbilisi, Georgia and it had as of 31 December 2015, 667 (31 December 2014: 629) branches, service centers, distribution outlets and mobile banking units operating in Georgia. The Bank's registered legal address is Liberty Tower, 74, I. Chavchavadze Avenue, 0162 Tbilisi, Georgia.

As of 31 December 2015 and 2014, the following shareholders owned more than 1% of the outstanding ordinary shares. Other shareholders owned less than 1% individually of the outstanding ordinary shares.

	2015		*2014*	
Shareholder	*Ownership interest, %*	*Voting rights, %*	*Ownership interest, %*	*Voting rights, %*
Liberty Holding Georgia LLC (former Liberty Capital LLC)	58.18%	70.65%	70.83%	70.83%
Liberty Bank (Treasury Shares)	17.65%	–	–	–
BNY Limited (Nominees)	10.20%	12.38%	12.14%	12.14%
Lado Gurgenidze	3.95%	4.80%	–	–
Stichting Liberty ESOP*	2.11%	2.56%	2.98%	2.98%
JSC Liberty Capital	–	–	7.12%	7.12%
Other shareholders (individually holding less than 1%)	7.91%	9.61%	6.93%	6.93%
Total	100.00%	100.00%	100.00%	100.00%

* *Ordinary shares sold on a deferred payment basis to Stichting Liberty ESOP as the trustee for the share based compensation programme (Note 17).*

The Bank is a publicly traded company and its ordinary shares are traded on the Georgian Stock Exchange. The free float amounted to 29.4% as of 31 December 2015 (31 December 2014: 22.1%).

The majority equity interest of the Group is ultimately beneficially owned and controlled by Mr. Denis Korotkov-Koganovich and Mr. Malik Ishmuratov.

As of 31 December 2015 and 2014, 3,201,321,628 ordinary shares held by Liberty Holdings Georgia LLC (58.18% of the 5,502,254,354 ordinary shares outstanding, inclusive of 971,234,382 treasury ordinary shares) were encumbered by the order of Tbilisi City Court in connection with civil litigation. For details please refer to Note 26.

The Bank is the parent company of the group (the "Group") which consists of the following entities consolidated in the financial statements:

		The Group ownership interest			
Name	*Country of incorporation*	*31 December 2015*	*31 December 2014*	*Date of incorporation*	*Activities*
Bus Stop LLC*	Georgia	100.00%	100.00%	27 August 2009	Outdoor advertising
LBF Luxembourg S.A.	Luxembourg	100.00%	–	20 July 2015	Financial intermediary services
JSC Smartex**	Georgia	21.47%	21.26%	5 January 2009	Courier services / Startup incubator and angel investor

* *Subsequent to the year end, as a non-core asset of the Group, constructions of Bus Stop LLC have been successfully disposed to the third party via tender offer announced by Tbilisi City Municipality (see Note: 26).*

** *21.47% is held by the Bank and 78.53% is beneficially held by Mr. Lado Gurgenidze. It is accounted for in the Group's financial statements under the equity method.*

(thousands of Georgian Lari)

2. Basis of preparation

General

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The Bank and its subsidiaries maintain their accounting records in accordance with IFRS.

The consolidated financial statements have been prepared under the historical cost convention except for derivative financial instruments, investment properties, buildings and available for sale securities as disclosed in the accounting policies below.

These consolidated financial statements are presented in thousands of Georgian Lari ("GEL"), except per share amounts and unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS which are effective for annual periods beginning on or after 1 January 2015:

Amendments to IAS 19 Defined Benefit Plans: Employee Contributions

IAS 19 requires an entity to consider contributions from employees or third parties when accounting for defined benefit plans. Where the contributions are linked to service, they should be attributed to periods of service as a negative benefit. These amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognise such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. This amendment is not relevant to the Group, since none of the entities within the Group has defined benefit plans with contributions from employees or third parties.

Annual improvements 2010-2012 cycle

These improvements are effective from 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 2 Share-based Payment

This improvement is applied prospectively and clarifies various issues relating to the definitions of performance and service conditions which are vesting conditions, including:

- a performance condition must contain a service condition;
- a performance target must be met while the counterparty is rendering service;
- a performance target may relate to the operations or activities of an entity, or to those of another entity in the same group;
- a performance condition may be a market or non-market condition;
- if the counterparty, regardless of the reason, ceases to provide service during the vesting period, the service condition is not satisfied.

These amendments do not impact the Group's accounting policies.

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies that all contingent consideration arrangements classified as liabilities (or assets) arising from a business combination should be subsequently measured at fair value through profit or loss whether or not they fall within the scope of IFRS 9 (or IAS 39, as applicable). This amendment does not impact the Group's accounting policy.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

IFRS 13 Short-term Receivables and Payables – amendments to IFRS 13

This amendment to IFRS 13 clarifies in the Basis for Conclusions that short-term receivables and payables with no stated interest rates can be measured at invoice amounts when the effect of discounting is immaterial. This is consistent with the Group's current accounting policy, and thus this amendment does not impact the Group's accounting policy.

IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets

The amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortisation is the difference between the gross and carrying amounts of the asset. The Group did not record any revaluation adjustments during the current period.

IAS 24 Related Party Disclosures

The amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services. This amendment is not relevant for the Group as it does not receive any management services from other entities.

Annual improvements 2011-2013 cycle

These improvements are effective from 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies for the scope exceptions within IFRS 3 that:

- joint arrangements, not just joint ventures, are outside the scope of IFRS 3;
- this scope exception applies only to the accounting in the financial statements of the joint arrangement itself.

The Group is not a joint arrangement, and thus this amendment is not relevant for the Group and its subsidiaries.

IFRS 13 Fair Value Measurement

The amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IFRS 9 (or IAS 39, as applicable). The Group does not apply the portfolio exception in IFRS 13.

IAS 40 Investment Property

The description of ancillary services in IAS 40 differentiates between investment property and owner-occupied property (i.e., property, plant and equipment). The amendment is applied prospectively and clarifies that IFRS 3, and not the description of ancillary services in IAS 40, is used to determine if the transaction is the purchase of an asset or business combination. This amendment does not impact the accounting policy of the Group.

Meaning of 'Effective IFRSs' – amendments to IFRS 1

The amendment clarifies in the Basis for Conclusions that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first IFRS financial statements. This amendment to IFRS 1 had no impact on the Group, since the Group is an existing IFRS preparer.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Basis of consolidation

Subsidiaries, which are those entities which are controlled by the Group, are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- exposure, or rights, to variable returns from its involvement with the investee;
- the ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- the contractual arrangement(s) with the other vote holders of the investee;
- rights arising from other contractual arrangements;
- the Group's voting rights and potential voting rights.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss.

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognised at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Group's share of net assets of the associate. The Group's share of its associates' profits or losses is recognised in profit or loss, and its share of movements in reserves is recognised in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless the Group is obliged to make further payments to, or on behalf of, the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Fair value measurement

The Group measures financial instruments, such as trading and available for sale securities, derivatives and non-financial assets such as investment properties, at fair value at each balance sheet date. Also, fair values of financial instruments measured at amortised cost are disclosed in Note 23.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- in the principal market for the asset or liability; or
- in the absence of a principal market, in the most advantageous market for the asset or liability.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Fair value measurement (continued)

The principal or the most advantageous market must be accessible by the Group. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

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

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 – quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 – valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- Level 3 – valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Financial assets

Initial recognition

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, or available for sale financial assets, as appropriate. The Group determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Date of recognition

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Held to maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held to maturity when the Group has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period are not included in this classification. Held to maturity investments are subsequently measured at amortised cost. Gains and losses are recognised in profit or loss when the investments are impaired, as well as through the amortisation process.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available for sale. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the NBG, excluding obligatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Amounts due from credit institutions

In the normal course of business, the Group maintains advances or deposits for various periods of time with other banks. Amounts due from credit institutions are initially recognised at fair value and are subsequently measured at amortised cost using the effective interest method. Amounts due from credit institutions are carried net of any allowance for impairment losses.

Derivative financial instruments

In the normal course of business, the Group enters into various derivative financial instruments including forwards and swaps in the foreign exchange and capital markets. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the consolidated statement of profit or loss as net gains/(losses) from trading securities or net gains/(losses) from foreign currencies dealing, depending on the nature of the instrument.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to credit institutions, amounts due to customers, debt securities issued and subordinated debt. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated statement of profit or loss when the borrowings are derecognised as well as through the amortisation process.

If the Group purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is recognised in the consolidated statement of profit or loss.

Leases

i. Operating – Group as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

ii. Operating – Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognised in profit or loss on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognised as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

Measurement of financial instruments at initial recognition

When financial instruments are recognised initially, they are measured at fair value, adjusted, in the case of instruments not at fair value through profit or loss, for directly attributable fees and costs.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price. If the Group determines that the fair value at initial recognition differs from the transaction price, then:

- if the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e., a Level 1 input) or based on a valuation technique that uses only data from observable markets, the Group recognises the difference between the fair value at initial recognition and the transaction price as a gain or loss;
- in all other cases, the initial measurement of the financial instrument is adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Group recognises that deferred difference as a gain or loss only when the inputs become observable, or when the instrument is derecognised.

3. Summary of accounting policies (continued)

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the consolidated statement of financial position.

Impairment of financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Amounts due from credit institutions and loans to customers

For amounts due from credit institutions and loans to customers carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the consolidated statement of profit or loss.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Group's internal product monitoring system that considers credit risk characteristics such as asset type, industry, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Held to maturity financial investments

For held to maturity investments the Group assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in profit or loss.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to the consolidated statement of profit or loss.

Available for sale financial investments

For available for sale financial investments, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available for sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in profit or loss – is reclassified from other comprehensive income to the consolidated statement of profit or loss. Impairment losses on equity investments are not reversed through the consolidated statement of profit or loss; increases in their fair value after impairment are recognised in other comprehensive income.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in the consolidated statement of profit or loss. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the consolidated statement of profit or loss.

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements, agreement of new loan conditions and improvement of collateral. Once the terms have been renegotiated, the loan is no longer considered past due.

The accounting treatment of such restructuring is conducted in 2 basic scenariosIf the loan restructuring is not caused by the financial difficulties of the borrower but the cash flows were renegotiated, the loan is not recognised as impaired. The new effective interest rate is determined based on the remaining cash flows under the loan agreement till maturity. If the new effective interest rate is below the market rate at the date of restructuring, the new carrying amount is calculated as the fair value of the loan after restructuring, being the present value of the future cash flows discounted using the market rate at the date of restructuring. In this case, the difference between the carrying amount before restructuring and the fair value of the loan after restructuring is recognised as a loss on loans restructuring:

- if the loan is impaired after restructuring, the Group uses the original effective interest rate in respect of new cash flows to estimate the recoverable amount of the loan. The difference between the recalculated present value of the new cash flows taking into account collateral and the carrying amount before restructuring is included in loan impairment charge for the period.

Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; and
- the Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, in "Other liabilities", being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of the expenditure that is required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the consolidated statement of profit or loss. The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.

Taxation

The current income tax expense is calculated in accordance with the regulations of Georgia. It represents the sum of the current and deferred tax expenses.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Taxation (continued)

Georgia also has various operating taxes, which are assessed on the Group's activities. These taxes are included as a component of other operating expenses.

Property and equipment

Property and equipment, except for buildings, is carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Following initial recognition at cost, buildings are carried at a revalued amount, which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuations are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Any revaluation surplus is credited to the revaluation reserve for property and equipment included in other comprehensive income, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss, in which case the increase is recognised in profit or loss. A revaluation deficit is recognised in profit or loss, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

An annual transfer from the revaluation reserve for property and equipment to retained earnings is made for the difference between depreciation based on the revalued carrying amount of the assets and depreciation based on the assets original cost. Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis at the following annual prescribed rates:

Land and buildings	2%-5%
Furniture and fixtures	10%-20%
Computer and office equipment	20%-25%
Motor vehicles	20%-25%
Leasehold improvements	10%-25%

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalisation.

Land is not amortised and carried at fair value. Leasehold improvements are amortised over the life of the related leased assets.

Assets under construction comprise costs directly related to construction of property and equipment including an appropriate allocation of directly attributable variable and fixed overheads that are incurred in construction. Depreciation of these assets, on the same basis as similar property assets, commences when the assets are put into operation.

Compensation from third parties for items of property and equipment that were impaired, lost or given up is included in other income when the compensation becomes receivable.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Investment properties

The Group holds certain properties as investments to earn rental income, generate capital appreciation or both and which are not used or held for the sale in the ordinary course of business. Investment properties are initially recognised at cost, including transaction costs, and subsequently remeasured at fair value reflecting market conditions at the end of the reporting period. Fair value of the Group's investment properties is determined on the base of various sources including reports of independent appraisers, who hold a recognised and relevant professional qualification and who have recent experience in valuation of property of similar location and category. Earned rental income is recorded in the profit or loss within income arising from non-banking activities. Gains and losses resulting from changes in the fair value of investment properties are recorded in consolidated statement of profit or loss and presented within other income or other operating expenses lines.

Intangible assets

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be finite. Intangible assets with finite lives are amortised over the useful economic lives of 5 to 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Retirement and other benefit obligations

The Group does not have any pension arrangements separate from the state pension system of Georgia. In addition, the Group has no post-retirement benefits.

Share capital

Share capital and additional paid in capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Treasury shares

Where the Bank purchases the Bank's shares, the consideration paid, including any attributable transaction costs, net of income taxes, is deducted from total equity as treasury shares until they are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received is included in equity. Treasury shares are stated at weighted average cost.

Dividends

Dividends are recognised as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the financial statements are authorised for issue.

Segment reporting

The Group's segment reporting is based on the following operating segments: Retail Banking, Corporate and SME (Small & Medium Size) Banking, Private Banking and Corporate Centre functions.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Contingencies

Contingent liabilities are not recognised in the consolidated statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

For all financial instruments measured at amortised cost and interest bearing securities classified as trading or available for sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Fee and commission income

The Group earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- *Fee income earned from services that are provided over a certain period of time*

  Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

- *Fee income from providing transaction services*

  Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Dividend income

Revenue is recognised when the Group's right to receive the payment is established.

Foreign currency translation

The consolidated financial statements are presented in Georgian Lari, which is the Bank's and subsidiaries' functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the consolidated statement of profit or loss as gains less losses from foreign currencies – translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Foreign currency translation (continued)

The exchange rates used by the Group in the preparation of the consolidated financial statements as of 31 December 2015 and 31 December 2014 are as follows:

	2015	*2014*
GEL / 1 US dollar	2.3949	1.8636
GEL / 1 Euro	2.6169	2.2656

Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets, but no impact on the classification and measurement of the Group's financial liabilities. The Group expects an impact on its equity due to adoption of IFRS 9 impairment requirements, but it will need to perform a more detailed analysis which considers all reasonable and supportable information, including forward-looking elements to determine the extent of the impact.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Revenue arising from lease contracts within the scope of IAS 17 *Leases*, insurance contracts within the scope of IFRS 4 *Insurance Contracts* and financial instruments and other contractual rights and obligations within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments*, if early adopted) is out of IFRS 15 scope and is dealt by respective standards.

Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue.

The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018 with early adoption permitted. The Group is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

IFRS 14 Regulatory Deferral Accounts

IFRS 14 is an optional standard that allows an entity, whose activities are subject to rate-regulation, to continue applying most of its existing accounting policies for regulatory deferral account balances upon its first-time adoption of IFRS. Entities that adopt IFRS 14 must present the regulatory deferral accounts as separate line items on the statement of financial position and present movements in these account balances as separate line items in the statement of profit or loss and other comprehensive income. The standard requires disclosures on the nature of, and risks associated with, the entity's rate-regulation and the effects of that rate-regulation on its financial statements. IFRS 14 is effective for annual periods beginning on or after 1 January 2016. Since the Group is an existing IFRS preparer, this standard would not apply.

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests

The amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business must apply the relevant IFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained. In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.

The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are prospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments will not have any impact to the Group.

Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation

The amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are effective prospectively for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments will not have any impact on the Group's consolidated financial statements given that the Group has not used a revenue-based method to depreciate its non-current assets.

Amendments to IAS 16 and IAS 41 Agriculture: Bearer Plants

The amendments change the accounting requirements for biological assets that meet the definition of bearer plants. Under the amendments, biological assets that meet the definition of bearer plants will no longer be within the scope of IAS 41. Instead, IAS 16 will apply. After initial recognition, bearer plants will be measured under IAS 16 at accumulated cost (before maturity) and using either the cost model or revaluation model (after maturity). The amendments also require that produce that grows on bearer plants will remain in the scope of IAS 41 measured at fair value less costs to sell. For government grants related to bearer plants, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* will apply. The amendments are retrospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments will not have any impact on the Group's consolidated financial statements as the Group does not have any bearer plants.

Amendments to IAS 27 Equity Method in Separate Financial Statements

The amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. Entities already applying IFRS and electing to change to the equity method in its separate financial statements will have to apply that change retrospectively. For first-time adopters of IFRS electing to use the equity method in its separate financial statements, they will be required to apply this method from the date of transition to IFRS. The amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments will not have any impact on the Group's consolidated financial statements.

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

The amendments address the acknowledged inconsistency between the requirements in IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is contributed to an associate or a joint venture. The amendments clarify that an investor recognises a full gain or loss on the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture. The amendments are applied prospectively to transactions occurring in annual periods beginning on or after 1 January 2016. Earlier application is permitted.

(thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Standards and interpretations issued but not yet effective (continued)

Amendments to IAS 1 Disclosure Initiative

The amendments to IAS 1 *Presentation of Financial Statements* clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- the materiality requirements in IAS 1;
- that specific line items in the statement(s) of profit or loss and OCI and the statement of financial position may be disaggregated;
- that entities have flexibility as to the order in which they present the notes to financial statements;
- that the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and OCI. These amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value. Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries. These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Annual improvements 2012-2014 cycle

These improvements are effective on or after 1 January 2016 and are not expected to have a material impact on the Group. They include:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations – changes in methods of disposal

Assets (or disposal groups) are generally disposed of either through sale or through distribution to owners. The amendment to IFRS 5 clarifies that changing from one of these disposal methods to the other should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. There is therefore no interruption of the application of the requirements in IFRS 5. The amendment also clarifies that changing the disposal method does not change the date of classification. The amendment must be applied prospectively to changes in methods of disposal that occur in annual periods beginning on or after 1 January 2016, with earlier application permitted.

IFRS 7 Financial Instruments: Disclosures – servicing contracts

IFRS 7 requires an entity to provide disclosures for any continuing involvement in a transferred asset that is derecognised in its entirety. The Board was asked whether servicing contracts constitute continuing involvement for the purposes of applying these disclosure requirements. The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and arrangement against the guidance for continuing involvement in paragraphs IFRS 7.B30 and IFRS 7.42C in order to assess whether the disclosures are required. The amendment must be applied for annual periods beginning on or after 1 January 2016, with earlier application permitted. The amendment is to be applied such that the assessment of which servicing contracts constitute continuing involvement will need to be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.

3. Summary of accounting policies (continued)

Standards and interpretations issued but not yet effective (continued)

IFRS 7 Financial Instruments: Disclosures – applicability of the offsetting disclosures to condensed interim financial statements

In December 2011, IFRS 7 was amended to add guidance on offsetting of financial assets and financial liabilities. In the effective date and transition for that amendment IFRS 7 states that "[A]n entity shall apply those amendments for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods. The interim disclosure standard, IAS 34, does not reflect this requirement, however, and it is not clear whether those disclosures are required in the condensed interim financial report.

The amendment removes the phrase 'and interim periods within those annual periods', clarifying that these IFRS 7 disclosures are not required in the condensed interim financial report. The amendment must be applied retrospectively for annual periods beginning on or after 1 January 2016, with earlier application permitted.

IAS 19 Employee Benefits – regional market issue regarding discount rate

The amendment to IAS 19 clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. The amendment must be applied for annual periods beginning on or after 1 January 2016, with earlier application permitted.

IAS 34 Interim Financial Reporting – disclosure of information 'elsewhere in the interim financial report'

The amendment states that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report (e.g., in the management commentary or risk report). The Board specified that the other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time. If users do not have access to the other information in this manner, then the interim financial report is incomplete. The amendment should be applied retrospectively for annual periods beginning on or after 1 January 2016, with earlier application permitted.

4. Significant accounting judgments and estimates

The preparation of the Group's consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the balance sheet date and the reported amount of income and expenses during the year ended. Management evaluates its estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The following estimates and judgments are considered important to the Group's financial condition.

Allowance for impairment of loans

The Group regularly reviews its loans to assess for impairment. The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans and receivables. The Group considers accounting estimates related to allowance for impairment of loans and receivables a key source of estimation uncertainty because (i) they are highly susceptible to change from period to period as the assumptions about future default rates and valuation of potential losses relating to impaired loans and receivables are based on recent performance experience, and (ii) any significant difference between the Group's estimated losses and actual losses would require the Group to record provisions which could have a material impact on its consolidated financial statements in future periods.

The Group uses management's judgment to estimate the amount of any impairment loss in cases where a borrower has financial difficulties and there are few available sources of historical data relating to similar borrowers. Similarly, the Group estimates changes in future cash flows based on past performance, past customer behavior and observable data indicating an adverse change in the payment status of borrowers in a group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans. The Group uses management's judgment to adjust observable data for a group of loans to reflect current circumstances not reflected in historical data.

(thousands of Georgian Lari)

4. Significant accounting judgments and estimates (continued)

Allowance for impairment of loans (continued)

The Group considers the fair value of collateral when estimating the amount of impairment loss for collateralised loans and receivables. Management monitors market value of collateral on a regular basis. Management uses its experienced judgment or independent opinion to adjust the fair value to reflect current circumstances. The amount and type of collateral required depends on the assessment of credit risk of the counterparty.

The allowances for impairment of financial assets in the consolidated financial statements have been determined on the basis of existing economic and political conditions. The Group is not in a position to predict what changes in conditions will take place in Georgia and what effect such changes might have on the adequacy of the allowances for impairment of financial assets in future periods.

Measurement of fair value of investment properties and buildings

Investment properties and buildings are stated at fair value. The fair value represents the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction at the date of valuation, in accordance with International Valuation Standards Committee standards.

Buildings of the Group are subject to revaluation on a regular basis. The date of latest revaluation was 31 December 2014. Refer to Note 10.

As of 31 December 2015, fair value of investment properties was determined by independent professionally qualified appraisers. Fair value was determined by applying income approach based on discounted cash flow method, supported by the terms of any existing lease and other contracts and, when available, by external evidence such as current market rents for similar properties in a comparable location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows. The estimates of future cash flows include projections of cash outflows for rent or purchase of the land.

The estimates described above are subject to change as new transaction data and market evidence become available.

Taxation

Tax legislation in Georgia is subject to varying interpretations, and changes can occur frequently. Management interpretation of such legislation and changes as applied to the transactions and activity of the Group may be challenged by the relevant authorities. As such, additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for six years including the year of review. Management believes that as of 31 December 2015 its interpretation of the relevant legislation is appropriate and that the Group's tax position will be sustained.

5. Segment information

For management purposes, the Group is organised into the following operating segments based on products and service:

Retail Banking	Principally handling individual customers' deposits, and providing consumer loans, overdrafts, credit card facilities, funds transfer payments and electronic banking services.
Corporate and SME Banking	Principally handling loans and other credit facilities and deposit and current accounts for corporate and institutional customers.
Private Banking	Principally providing private banking and wealth management services to high net worth individuals.
Corporate Centre	Principally providing treasury and back office services to all operating segments of the Bank.
Other	Segments not classified above, comprising non-banking operations.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance, as explained in the table below, is measured differently from profit or loss in the consolidated financial statements. Income taxes are managed on a group basis and are not allocated to operating segments.

(thousands of Georgian Lari)

5. Segment information (continued)

The Group operates in one geographical market – Georgia. Since the Group's assets are located in single geographical area, the Group's external income, total assets and capital expenditure are allocated to a single location.

2015	*Retail banking*	*Corporate & SME banking*	*Private banking*	*Corporate centre*	*Other*	*Adjustments and eliminations*	*Total*
Net interest income	107,550	12,429	2,269	12,491	1	10	134,750
Net fee and commission income	19,764	3,481	497	1,119	(44)	–	24,817
Net gains from foreign currencies	3,512	1,463	293	585	–	–	5,853
Other income	9,668	4,604	767	307	340	(299)	15,387
Total revenue	140,494	21,977	3,826	14,502	297	(289)	180,807
Loan impairment (charge)/reversal	(30,906)	(1,436)	10	–	–	–	(32,332)
Personnel expenses	(43,504)	(8,817)	(582)	(5,878)	(41)	–	(58,822)
Depreciation and amortisation	(11,331)	(2,461)	(164)	(2,463)	(136)	–	(16,555)
Other impairment and provisions reversal/(charge)	114	66	5	10	(18)	–	177
General and administrative and other operating expenses	(26,348)	(7,401)	(579)	(3,815)	(270)	258	(38,155)
Segment results	28,519	1,928	2,516	2,356	(168)	(31)	35,120
Income tax expense	–	–	–	–	–	–	(2,974)
Profit for the year	–	–	–	–	–	–	32,146
Segment assets	1,191,321	30,413	8,989	344,228	825	(2,030)	1,573,746
Segment liabilities	789,435	390,002	144,042	119,411	367	(361)	1,442,896
Other segment information							
Investments in associates	–	–	–	384	–	–	384
Share of loss of associates	–	–	–	(75)	–	–	(75)

2014	*Retail banking*	*Corporate & SME banking*	*Private banking*	*Corporate centre*	*Other*	*Adjustments and eliminations*	*Total*
Net interest income	82,421	11,685	1,713	11,074	1	8	106,902
Net fee and commission income	19,251	3,390	484	1,090	(44)	–	24,171
Net gains from foreign currencies	4,263	1,776	355	711	–	–	7,105
Other income	6,462	3,077	514	205	344	(237)	10,365
Total revenue	112,397	19,928	3,066	13,080	301	(229)	148,543
Loan impairment (charge)/reversal	(25,260)	(1,525)	26	–	–	1,502	(25,257)
Personnel expenses	(34,750)	(7,629)	(482)	(5,845)	(25)	–	(48,731)
Depreciation and amortisation	(10,358)	(2,250)	(150)	(2,251)	(136)	–	(15,145)
Other impairment and provisions charge	(991)	(571)	(40)	(86)	–	(1,502)	(3,190)
General and administrative and other operating expenses	(23,318)	(6,547)	(513)	(3,376)	(307)	324	(33,737)
Segment results	17,720	1,406	1,907	1,522	(167)	95	22,483
Income tax expense	–	–	–	–	–	–	(709)
Profit for the year	–	–	–	–	–	–	21,774
Segment assets	1,188,848	61,257	9,493	319,761	870	(1,872)	1,578,357
Segment liabilities	409,223	862,511	61,844	120,113	345	(336)	1,453,700
Other segment information							
Investments in associates	–	–	–	401	–	–	401
Share of income of associates	–	–	–	25	–	–	25

6. Cash and cash equivalents

Cash and cash equivalents comprise:

	2015	*2014*
Cash on hand	140,590	139,491
Current accounts with the NBG	333,098	126,535
Current accounts with other credit institutions	28,652	66,372
Time deposits with credit institutions up to 90 days	–	147,600
Cash and cash equivalents	502,340	479,998

As of 31 December 2015, GEL 13,299 (31 December 2014: GEL 55,866) was placed on current accounts with internationally recognised OECD banks that are the counterparties of the Group in performing international settlements. As of 31 December 2015, no short-term time and overnight deposits were placed with the NBG (31 December 2014: GEL 147,600).

7. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	2015	*2014*
Obligatory reserve with the NBG	53,894	44,608
Time deposits for more than 90 days	4,608	6,338
Amounts due from credit institutions	58,502	50,946

Credit institutions are required to maintain an interest-earning cash deposit (obligatory reserve) with the NBG, the amount of which depends on the level of funds attracted by the credit institution. The Group's ability to withdraw these deposits is restricted by the statutory legislature.

As of 31 December 2015, GEL 3,592 (31 December 2014: GEL 2,795) was placed on inter-bank deposits with internationally recognised OECD banks, that are the main counterparties of the Group in performing international settlements. The interest rate on such deposits ranges from 0.05%-0.1% per annum.

8. Loans to customers

Loans to customers comprise:

	2015	*2014*
Loans to retail clients with regular inflows	366,410	429,830
Consumer loans	156,957	134,430
Micro loans	94,638	81,084
Gold pawn loans	50,805	47,088
Residential mortgage loans	17,633	17,367
Corporate and SME loans	12,017	29,963
Gross loans to customers	698,460	739,762
Less – allowance for loan impairment	(57,344)	(47,652)
Loans to customers	641,116	692,110

Loans to retail clients with regular inflows are provided to individuals who have a stream of regular (typically monthly) inflows into their accounts at the Bank either in form of a salary, state pension or welfare payment.

8. Loans to customers (continued)

Allowance for impairment of loans to customers

A reconciliation of the allowance for impairment of loans to customers by class is as follows:

	Loans to retail clients with regular inflows	*Consumer loans*	*Micro loans*	*Gold pawn loans*	*Residential mortgage loans*	*Corporate & SME loans*	*Total*
At 1 January 2015	20,328	19,692	1,808	434	267	5,123	47,652
Charge for the year	11,590	14,112	2,007	3,032	155	1,436	32,332
Recoveries	447	184	17	–	–	26	674
Amounts written off	(12,391)	(6,271)	(284)	(2)	–	(4,366)	(23,314)
At 31 December 2015	19,974	27,717	3,548	3,464	422	2,219	57,344
Individual impairment	–	–	–	3,464	–	1,427	4,891
Collective impairment	19,974	27,717	3,548	–	422	792	52,453
	19,974	27,717	3,548	3,464	422	2,219	57,344
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	–	7,607	–	6,166	13,773

	Loans to retail clients with regular inflows	*Consumer loans*	*Micro loans*	*Gold pawn loans*	*Residential mortgage loans*	*Corporate & SME loans*	*Total*
At 1 January 2014	14,026	8,007	418	–	255	4,116	26,822
Charge for the year	9,383	12,143	1,615	434	155	1,527	25,257
Recoveries	373	140	10	–	–	31	554
Amounts written off	(3,454)	(598)	(235)	–	(143)	(551)	(4,981)
At 31 December 2014	20,328	19,692	1,808	434	267	5,123	47,652
Individual impairment	–	–	–	434	–	3,649	4,083
Collective impairment	20,328	19,692	1,808	–	267	1,474	43,569
	20,328	19,692	1,808	434	267	5,123	47,652
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	–	585	–	13,674	14,259

Individually impaired loans

Interest income accrued on loans, for which individual impairment allowances have been recognised as of 31 December 2015 comprised GEL 1,254 (2014: GEL 2,843). Related allowance charges were recognised both in 2015 and 2014 and are recorded in consolidated statement of profit or loss under net impairment charge on interest-bearing assets.

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:

- for lending to legal entities, mortgages over real estate properties, inventory and trade receivables;
- for retail lending, mortgages over residential properties and gold over gold pawns.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for loan impairment.

8. Loans to customers (continued)

Concentration of loans to customers

As of 31 December 2015, the concentration of loans granted by the Group to ten largest third party borrowers comprised GEL 8,508 accounting for 1.2% of the gross loan portfolio of the Group (2014: GEL 14,960 and 2.0%, respectively). An allowance of GEL 2,905 (2014: GEL 2,834) was established against these loans.

Loans have been extended to the following types of customers:

	2015	*2014*
Individuals	683,506	703,578
Private companies	14,954	36,184
Loans to customers, gross	698,460	739,762
Less – allowance for loan impairment	(57,344)	(47,652)
Loans to customers, net	641,116	692,110

Loans are made principally within Georgia in the following industry sectors:

	2015	*2014*
Individuals	683,506	703,578
Trade and service	10,996	23,883
Construction	392	2,248
Other	3,566	10,053
Loans to customers, gross	698,460	739,762
Less – allowance for loan impairment	(57,344)	(47,652)
Loans to customers, net	641,116	692,110

9. Investment securities

Loans and receivables comprise:

	2015	*2014*
Certificates of deposit of the NBG	50,946	–
Treasury bonds of the Ministry of Finance of Georgia	22,152	–
Treasury bills of the Ministry of Finance of Georgia	6,371	–
Loans and receivables	79,469	–

Due to the lack of an active market for securities during 2015 (based on NBG statistics), the Group qualified securities purchased in 2015 as loans and receivables at amortised cost with no impact on consolidated statement of profit or loss.

Held to maturity securities comprise:

	2015	*2014*
Treasury bonds of the Ministry of Finance of Georgia	124,321	124,403
Treasury bills of the Ministry of Finance of Georgia	–	55,616
Certificates of deposit of the NBG	–	16,887
Held to maturity securities	124,321	196,906

As of 31 December 2015, the investment securities with book value of GEL 127,756 were pledged as a collateral for short-term loan received from NBG (as of 31 December 2014: nil). Please refer to Note 14.

10. Property and equipment

The movements in property and equipment were as follows:

	Land and buildings	*Furniture and fixtures*	*Computers and office equipment*	*Motor vehicles*	*Leasehold improve-ments*	*Total*
Cost or revalued amount						
31 December 2014	75,090	49,325	21,905	12,538	7,936	166,794
Additions	2,734	14,350	3,883	1,269	1,053	23,289
Disposals	(36)	–	–	(24)	(293)	(353)
31 December 2015	77,788	63,675	25,788	13,783	8,696	189,730
Accumulated depreciation and impairment						
31 December 2014	560	21,459	14,300	8,627	3,051	47,997
Depreciation charge	1,642	5,544	3,267	2,082	828	13,363
Disposals	(1)	–	–	(7)	(239)	(247)
31 December 2015	2,201	27,003	17,567	10,702	3,640	61,113
Net book value						
31 December 2014	74,530	27,866	7,605	3,911	4,885	118,797
31 December 2015	75,587	36,672	8,221	3,081	5,056	128,617

	Land and buildings	*Furniture and fixtures*	*Computers and office equipment*	*Motor vehicles*	*Leasehold improve-ments*	*Total*
Cost or revalued amount						
31 December 2013	90,839	40,959	17,519	12,138	6,175	167,630
Additions	3,058	8,366	4,386	526	1,584	17,920
Disposals	(162)	–	–	(126)	(14)	(302)
Revaluation	(18,454)	–	–	–	–	(18,454)
Reclassifications	(191)	–	–	–	191	–
31 December 2014	75,090	49,325	21,905	12,538	7,936	166,794
Accumulated depreciation and impairment						
31 December 2013	3,397	16,709	12,018	6,570	611	39,305
Depreciation charge	2,036	4,750	2,282	2,168	2370	13,606
Disposals	(7)	–	–	(111)	(14)	(132)
Revaluation	(4,782)	–	–	–	–	(4,782)
Reclassification	(84)	–	–	–	84	–
31 December 2014	560	21,459	14,300	8,627	3,051	47,997
Net book value						
31 December 2013	87,442	24,250	5,501	5,568	5,564	128,325
31 December 2014	74,530	27,866	7,605	3,911	4,885	118,797

Buildings and land of the Group are subject to revaluation on a regular basis. The date of the latest revaluation was 31 December 2014.

The gross carrying amount of fully depreciated property and equipment that is still in use is as follows:

	Furniture and fixtures	*Computers and office equipment*	*Motor vehicles*	*Total*
Cost or revalued amount				
31 December 2015	3,644	11,578	3,839	19,061
31 December 2014	1,882	9,438	2,780	14,100

(thousands of Georgian Lari)

10. Property and equipment (continued)

The Group's buildings are classified to Level 3 of the fair value hierarchy. There were no transfers among the levels of the fair value hierarchy in 2015.

If the land and buildings were measured using the cost model, the carrying amounts would be as follows:

	2015	*2014*
Cost	51,639	48,941
Accumulated depreciation and impairment	(7,355)	(6,322)
Net carrying amount	44,284	42,619

11. Intangible assets

The movements in intangible assets, which comprised computer software and licenses, were as follows:

	Computer software and licenses
Cost	
31 December 2014	17,655
Additions	12,180
31 December 2015	29,835
Accumulated amortisation	
31 December 2014	6,386
Amortisation charge	3,192
31 December 2015	9,578
Net book value	
31 December 2014	11,269
31 December 2015	20,257

	Computer software and licenses
Cost	
31 December 2013	14,507
Additions	3,148
31 December 2014	17,655
Accumulated amortisation	
31 December 2013	4,847
Amortisation charge	1,539
31 December 2014	6,386
Net book value	
31 December 2013	9,660
31 December 2014	11,269

(thousands of Georgian Lari)

12. Taxation

The corporate income tax expense comprised:

	2015	*2014*
Current year tax charge	1,081	–
Deferred tax charge – origination and reversal of temporary differences	1,893	709
Income tax expense	2,974	709

Georgian legal entities must file individual tax declarations. The tax rate for banks for profits other than on state securities was 15% for 2015 and 2014. The tax rate for interest income on state securities and the NBG deposits is 0%.

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2015	*2014*
Profit before income tax	35,120	22,483
Statutory tax rate	15%	15%
Theoretical income tax expense at the statutory rate	5,268	3,372
Change in unrecognised deferred tax asset	–	(770)
Tax effect from income from state securities and deposits placed with the NBG at 0%	(2,680)	(2,197)
Non-tax deductible expenses	386	304
Income tax expense	2,974	709

Deferred tax assets and liabilities as of 31 December and their movements for the respective years comprise:

		Origination and reversal of temporary differences			*Origination and reversal of temporary differences*	
	2013	*In the statement of profit or loss*	*Effect of change in statement of comprehensive income*	*2014*	*In the statement of profit or loss*	*2015*
Tax effect of deductible temporary differences						
Taxable loss carried forward	1,295	(770)	–	525	(525)	–
Loans to customers	4,649	(558)	–	4,091	(1,609)	2,482
Equity investments	1,073	(798)	–	275	–	275
Other assets	353	483	–	836	174	1,010
Other liabilities	475	149	–	624	148	772
Gross deferred tax assets	7,845	(1,494)	–	6,351	(1,812)	4,539
Unrecognised deferred tax asset	(1,295)	770	–	(525)	525	–
Deferred tax asset	6,550	(724)	–	5,826	(1,287)	4,539
Tax effect of taxable temporary differences						
Property and equipment and intangible assets	(13,864)	15	2,051	(11,798)	(606)	(12,404)
Deferred tax liabilities	(13,864)	15	2,051	(11,798)	(606)	(12,404)
Net deferred tax assets/(liabilities)	(7,314)	(709)	2,051	(5,972)	(1,893)	(7,865)

(thousands of Georgian Lari)

12. Taxation (continued)

During 2015 year, the Bank did not utilise a taxable loss carry forward of GEL 3,497 with the respective tax effect of the utilisation amounting to GEL 525. During 2014 year, the Bank utilised a taxable loss carry forward of GEL 5,133 with the respective tax effect of the utilisation amounting to GEL 770. The schedule of the available taxable loss carried forward with the respective expiration dates is presented below:

Year of expiration	*2015*	*2014*
2015	–	3,497
Taxable loss carried forward, gross	–	3,497
Unrecognised taxable loss carried forward	–	(3,497)
Taxable loss carried forward, net	–	–

13. Other assets, prepayments and other liabilities

Other assets comprise:

	2015	*2014*
Investment properties	4,665	5,017
Receivables from remittances systems operators	3,855	2,622
Guarantee deposits placed	2,119	1,647
Repossessed property	1,443	1,252
Receivable from guarantees paid	899	1,276
Prepaid taxes other than income tax	550	1,097
Investment in associate	342	401
Receivable from documentary operations	172	341
Derivative asset	58	4,033
Investments available for sale	42	–
Current income tax assets	–	533
Other	5,874	4,999
	20,019	23,218
Less – allowance for impairment of other assets	(5,130)	(4,070)
Other assets	14,889	19,148

Investment properties primarily comprise of class B office space located in downtown Zugdidi with total rental space of 1,848 square meters and a warehouse building located in an industrial area of Tbilisi with gross usable space of 8,706 square meters, as well as several other properties located outside of Tbilisi. The warehouse building was disposed to third party subsequent to the year end in February 2016 (refer to Note 26).

Investment properties are stated at fair value. The fair value represents the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. The date of latest revaluation was 31 December 2015. The valuation was performed by an accredited independent valuator with a recognised and relevant professional qualification and with recent experience in the locations and categories of the investment properties being valued. The valuation models in accordance with those recommended by the International Valuation Standards Committee have been applied and are consistent with the principles in IFRS 13. Refer to Note 23 for details.

During 2015, the Group disposed one of its investment properties to third party. The sale was accomplished at most recent fair value revaluation of the property of GEL 414. There were no other significant movements in investment properties except for fair value revaluation.

The Group's investment properties items are classified to Level 3 of the fair value hierarchy. There were no transfers among the levels of the fair value hierarchy in 2015.

Receivables from remittances in the amount of GEL 3,855 (2014: GEL 2,622) represent money transfers made in advance toward the retail clients at the period end that were subsequently settled by the systems operators within several days in accordance with respective service contracts.

Guarantee deposits placed as of 31 December 2015 primarily represent pledged funds at VISA Inc. and MasterCard Inc. in the amount of GEL 825 and GEL 1,274, respectively (31 December 2014: VISA Inc. for GEL 654, MasterCard Inc. for GEL 992).

13. Other assets, prepayments and other liabilities (continued)

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

	2015			*2014*		
	Notional	*Fair values*		*Notional*	*Fair value*	
	amount	*Asset*	*Liability*	*amount*	*Asset*	*Liability*
Foreign exchange contracts						
Forwards and swaps – domestic	1,800	58	–	56,076	4,033	–
Total derivative assets/liabilities	1,800	58	–	56,076	4,033	–

As of 31 December 2015, the Group has positions in the following types of derivatives:

Forwards

Forwards contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

The Group's forward is classified to Level 2 of the fair value hierarchy. There were no transfers among the levels of the fair value hierarchy in 2015.

Prepayments comprise:

	2015	*2014*
Prepayments for security services	963	2,145
Prepayments for fixed and intangible assets	654	5,446
Prepayments for professional services	511	211
Prepaid insurance	446	266
Other	1,661	1,115
Total prepayments	4,235	9,183

Advances for security service represent a prepayment made to Legal Entity of Public Law (LEPL) Security Police Department (SPD). On 30 May 2012, the Bank signed a five year service agreement with SPD for 63 months until 1 September 2017 in the amount of GEL 5 million. According to the agreement, SPD provides security services at the Bank's head office, branches and other distribution outlets, as well as for vehicles used for cash transportation. In connection with this agreement, the Bank has recognised an expense in the amount of GEL 1,182 for the year ended 31 December 2015 (2014: GEL 1,152).

Other liabilities comprise:

	2015	*2014*
Bonus accrual	6,261	4,319
Funds pending settlements	1,516	3,341
Sundry creditors	1,238	1,385
Provision for various contingencies including guarantees and commitments	482	1,661
Taxes payable other than income tax	346	233
Other	3,356	1,925
Other liabilities	13,199	12,864

(thousands of Georgian Lari)

13. Other assets, prepayments and other liabilities (continued)

Forwards (continued)

The movements in other impairment allowances and provisions were as follows:

	Other assets	*Provision for various contingencies including guarantees and commitments*	*Total*
31 December 2014	4,070	1,661	5,731
Charge/(reversal)	1,002	(1,179)	(177)
Write-offs	(1)	–	(1)
Recoveries	59	–	59
31 December 2015	5,130	482	5,612

	Other assets	*Provision for various contingencies including guarantees and commitments*	*Total*
31 December 2013	2,374	159	2,533
Charge/(reversal)	1,688	1,502	3,190
Write-offs	(2)	–	(2)
Recoveries	10	–	10
31 December 2014	4,070	1,661	5,731

Provisions for claims, guarantees and commitments are recorded in other liabilities.

14. Amounts due to credit institutions

Amounts due to credit institutions comprise:

	2015	*2014*
Current accounts	2,959	5,105
Time deposits and loans	115,956	932
Amounts due to credit institutions	118,915	6,037

As of 31 December 2015, time deposits and loans included GEL 115,000 of short-term loan received from the NBG (31 December 2014: nil). Certain securities with book value of GEL 127,756 were pledged as a collateral for this loan (Note 9).

15. Amounts due to customers

The amounts due to customers include the following:

	2015	*2014*
Current accounts	625,525	843,773
Time deposits (including certificates of deposits)	618,498	569,208
Amounts due to customers	1,244,023	1,412,981
Held as security against guarantees issued	1,258	2,713

At 31 December 2015, amounts due to customers of GEL 178,069 (14.3%) were due to the ten largest customers (31 December 2014: GEL 289,246 (20.5%)).

15. Amounts due to customers (continued)

Amounts due to customers include accounts with the following types of customers:

	2015	*2014*
Individuals	847,874	774,121
State and public sector	272,417	447,570
Private enterprises	123,732	191,290
Amounts due to customers	1,244,023	1,412,981

The amounts due to customers by economic sector are as follows:

	2015	*2014*
Individuals	847,874	774,121
State and public sector	272,417	447,570
Trade	26,859	26,369
Transport and communication	11,885	25,269
Energy	10,588	28,504
Real estate constructions	1,883	4,962
Agriculture	469	440
Mining	76	87
Other	71,972	105,659
Amounts due to customers	1,244,023	1,412,981

16. Subordinated debt

In November 2014, the Bank commenced the sale of unsecured Subordinated Loan Contracts (the "SLCs") to high net worth individuals and corporate clients. The primary reason for issuance of the SLCs was to attract Tier 2 qualified capital to support the Bank's capitalisation.

As of 31 December 2015, the Bank had GEL 58,346 (31 December 2014: GEL 15,846) of Subordinated Debt outstanding, of which GEL 44,198 (31 December 2014: GEL 6,485) qualified for the inclusion in the Tier 2 capital in accordance with the NBG rules.

17. Equity

Share capital

As of 31 December 2015, the authorised share capital of the Bank comprised 7,500,000,000 ordinary shares, of which 5,502,254,354 were issued, 5,386,315,867 ordinary shares were fully paid and 971,234,382 shares represent treasury shares (31 December 2014: 7,500,000,000 ordinary shares, of which 5,502,254,354 were issued and 5,338,298,249 were fully paid). Each share has nominal value of GEL 0.01. Out of total number of ordinary shares issued, 115,938,487 shares have been sold on a deferred payment basis to Stichting Liberty ESOP (2014: 163,956,105) and are attributable to the share based compensation programme.

Movements in the fully paid and repurchased ordinary and the convertible preferred shares are described below:

	Number of shares		*Nominal amount*		
	Convertible preferred	*Ordinary*	*Convertible preferred*	*Ordinary*	*Total*
31 December 2013	5,179,064	5,328,424,855	5,179	53,284	58,463
Increase in share capital	960,000	9,873,394	960	99	1,059
31 December 2014	6,139,064	5,338,298,249	6,139	53,383	59,522
Increase in share capital	–	48,017,618	–	480	480
Purchase of treasury shares	–	(971,234,382)	–	(9,712)	(9,712)
31 December 2015	6,139,064	4,415,081,485	6,139	44,151	50,290

17. Equity (continued)

Share capital (continued)

The share capital of the Bank was contributed by the shareholders in GEL and they are entitled to dividends and any capital distribution in GEL.

The increase of share capital represents the exercise of ESOP shares. No new ordinary shares have been issued or sold during 2015 and 2014.

As of 31 December 2015 and 2014, the book value per ordinary share comprised GEL 0.028 and GEL 0.022, respectively.

Treasury shares

On 12 November 2015, the Group commenced the buyback of ordinary shares (the "Buyback") at GEL 0.0179 per ordinary share, with the maximum number of 1,045,428,327 ordinary shares or 19.00% of the total number of issued and outstanding ordinary shares. The buyback was initiated considering the following conditions:

- As of 30 September 2015, the total capital adequacy ratio stood at 20.13%, the historical maximum achieved by the Group, which is far above the minimum threshold of 11.4% and is comfortably above the targeted 18% level.
- Given the contemporary macroeconomic conditions in Georgia, the Group faces muted growth prospects in 2016 which can be supported by internally generated additional capital, and, therefore had some excess regulatory capital.
- The common share price of the Bank on the Georgian Stock Exchange (the "GSE") had been at the low level not exceeding 0.5-0.6x trailing book value per ordinary share, with very low liquidity.

The Buyback period was set as 90 calendar days from announcement date, up until 10 February 2016; as of 31 December 2015 the Group bought back and fully settled 971,234,382 ordinary shares (17.65% of the total number of shares issued and outstanding). See Note 26 for subsequent Buyback completion results.

The consideration paid, including any attributable transaction costs is deducted from total equity as treasury shares until they are cancelled or reissued. Treasury shares are stated at weighted average cost.

Convertible preferred shares

In August 2012, the Bank issued and made available for sale to the general public in a public offer in Georgia 10,000,000 non-redeemable convertible preferred shares at the gross placement price of GEL 1 per convertible preferred share (with the permissible size of the public offer subsequently increased to 30,000,000 convertible preferred shares), of which 6,139,064 convertible preferred shares were outstanding and fully paid-up as of 31 December 2015 (2014: 6,139,064), The public offer period expired on 31 December 2015. The convertible preferred shares are perpetual and can be converted, at the holder's discretion, into ordinary shares of the Bank at the conversion price based on 1.05 times the IFRS audited ordinary equity book value of the Bank per ordinary share outstanding (net of any treasury shares) as of the end of the preceding calendar year.

The dividend rate on the convertible preferred shares is 17% per annum, payable annually, subject to the AGM approval in each given year. The dividends are non-cumulative. The conversion option was classified as equity component as of the initial recognition date.

The ability to pay dividends is subject to the Bank's financial condition and results of operations and compliance with the prudential capital adequacy requirements and may be restricted by, among other things, applicable laws and regulations, and by the NBG.

Basic/diluted earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period (net of any treasury shares). Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding of the effect of all dilutive potential ordinary shares (but ignoring any treasury shares), which comprise share options granted to employees and the convertible preferred shares.

In 2015, net income attributable to ordinary shareholders of the Bank comprised GEL 32,146 (2014: GEL 21,774) and the weighted average number of ordinary shares outstanding during the year was 5,400,007,513 (2014: 5,502,254,354), resulting in earnings per share of GEL 0.00576 for 2015 (2014: GEL 0.00380).

(thousands of Georgian Lari)

17. Equity (continued)

Basic/diluted earnings per share (continued)

At 31 December 2015, the convertible preferred shares did not have a dilutive effect as the conversion price of GEL 0.029 exceeded the quoted weighted average market price for the period of GEL 0.012. Thus, the potential dilution did not include the potential effect from the conversion of 6,139,064 convertible preferred shares into ordinary shares as of 31 December 2015 (at 31 December 2014, the convertible preferred shares did not have a dilutive effect as the conversion price of GEL 0.023 exceeded the quoted weighted average market price for the period of GEL 0.015).

Dividends

The Bank paid dividends on its ordinary shares in the amount of GEL 8,000 in 2015 (2014: GEL nil). The Bank paid dividends on the convertible preferred shares in the amount of GEL 1,044 in 2015 (2014: 880).

Other reserves

Movements in other reserves were as follows:

	Revaluation reserve for property and equipment	*Total*
At 31 December 2013	20,282	20,282
Revaluation of buildings	(13,380)	(13,380)
Tax effect of revaluation of buildings	2,051	2,051
Revaluation reserve of sold assets, net of tax	(75)	(75)
Depreciation of revaluation reserve, net of tax	(423)	(423)
At 31 December 2014	8,455	8,455
Revaluation reserve of sold assets, net of tax	(4)	(4)
Depreciation of revaluation reserve, net of tax	(169)	(169)
At 31 December 2015	8,282	8,282

Nature and purpose of other reserves

Revaluation reserve for property and equipment

The revaluation reserve for property and equipment is used to record increases in the fair value of the buildings and decreases to the extent that such decrease relates to an increase on the same asset previously recognised in equity.

18. Commitments and contingencies

Operating environment

In May and October 2015, the credit rating agencies reconfirmed their sovereign ratings of Georgia with stable outlook. In the recent years, Georgia implemented far-reaching structural reforms. In 2015 Country was No. 24 in the World Bank Ease of Doing Business global rankings and No. 22 in the Index of Economic Freedom. However, Georgia remains a small open economy, which is exposed to exogenous trends and pressures. The recession and/or slowdown in the economies of key regional trading partners (largely induced by the sharp falls in oil & gas and other commodity prices), resulted in a year-on-year decline in exports and remittance inflows in Georgia. The local currency depreciated by 28.5% against the US dollar, Real GDP growth amounted to 2.6% in 2015, as compared to 6.4%, 3.3% and 4.6% in 2012, 2013 and 2014, respectively.

Budget deficit in 2014 and 2015 amounted, on a preliminary basis, to 3.2% and 3.8% of GDP, respectively. Proper fiscal-monetary interaction and prudent banking sector supervision allowed to sustain positive development dynamics in the financial sector and credit risks, providing for flat (adjusted for exchange-rate effect) loan book growth while keeping the banking sector NPLs (defined as loans overdue by 90 days) at a relatively low level (below 5%). However, the banking sector remains relatively dollarised with 60% of sector loan portfolios denominated in the US dollars (the only exception of the Bank's loan book, 3%), that might create future moderate pressure on asset-quality, which is offset by strong Basel capital adequacy ratios of the banking sector.

(thousands of Georgian Lari)

18. Commitments and contingencies (continued)

Operating environment (continued)

The period average inflation rate changed from 3.1% as of 31 December 2014 to 4.0% as of 31 December 2015. Public debt as a share of GDP amounted to 39.4% and 33.2% as of 31 December 2015 and 31 December 2014, respectively. The government and the NBG sustain sufficient liquidity – in the form of the government cash deposit at the NBG and in the form of the NBG's international reserves (liquid assets/GDP equalled 2.4% and 3.6% as of 31 December 2015 and 31 December 2014, respectively). Regional growth appears to be improving in 2016, alongside the stabilisation and slight growth of the commodity prices.

The management believes that the Bank is well-equipped to withstand such pressures, due to the fact that 96% of gross loans and 71% of amounts due to customers are denominated in local currency, which is strengthened by well diversified retail loan book, low concentration in funding and fairly stable liquidity buffer. Despite the fall of the GEL against the US dollar, conversion of retail deposits and CDs into FX has been limited in 2015. Additionally, the Bank's refinancing risk is generally restricted due to significant reliance on retail fixed rate time deposits and CDs.

Legal

In the ordinary course of business, the Group is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Group.

The Group's commitments and contingencies comprised the following:

	2015	*2014*
Credit related commitments		
Guarantees	1,438	4,620
Undrawn loan commitments	29,094	39,033
	30,532	43,653
Operating lease commitments		
Not later than 1 year	7,079	4,701
Later than 1 year but not later than 5 years	20,360	12,907
Later than 5 years	9,940	6,309
	37,379	23,917
Capital expenditure commitments	213	645
Less – provisions	(22)	(1,661)
Commitments and contingencies (before deducting collateral)	68,102	66,554
Less – cash held as security against guarantees issued	(1,258)	(2,713)
Commitments and contingencies	66,844	63,841

As of 31 December 2015 and 31 December 2014, the Bank had Bankers Blanket Bond insurance, Directors and Officers liability insurance, and Property and Vehicle insurance coverage.

Litigation

In December 2008, then shareholders of the Bank – Irina Jincharadze, Elena Kovalenko, Giorgi Goguadze, Tamar Marshania, Gaioz Marshania, Ana Gerbyak (nee Agureeva) and Stark Road Resource Limited sold 1,403,223,900 ordinary shares of the Bank (then representing a 89.24% equity interest in the Bank) to Eurooil LLP under the share purchase agreement dated 29 December, 2008 (as amended on 29 December 2008) (hereinafter the "SPA"). The aggregate cash and non-cash consideration received by the selling shareholders equaled to GEL 36,478, amounting to 2.76 times the IFRS audited equity book value of the Bank as of 31 December, 2008. In September 2009, Eurooil LLP sold 1,434,047,026 ordinary shares of the Bank (then representing a 91.22% equity interest in the Bank) to Liberty Holding Georgia LLC.

(thousands of Georgian Lari)

18. Commitments and contingencies (continued)

Legal (continued)

On 31 October 2013, several of the former shareholders of the Bank – Irina Jincharadze, Elena Kovalenko and Tamar Marshania (hereinafter the "Original Claimants") – filed a claim at the Tbilisi City Court against the respondents Eurooil LLP, the Bank, Liberty Holding Georgia LLC, JSC Liberty Capital and Liberty Investments Holding BV (hereinafter the "Respondents"). In their claims the Original Claimants allege that they were coerced to sell their respective shares to Eurooil LLP and that EuroOil LLP and the Respondents had been related and/or acted in concert, and thus seek partial annulment of the SPA. The Original Claimants had sold 801,454,200 ordinary shares of the Bank for the aggregate consideration of GEL 23,782. In conjunction with the claim, the Original Claimants requested injunctive relief in the form of an encumbrance over 51% of the Bank's ordinary shares held by Liberty Holding Georgia LLC and nine units of real estate property owned by JSC Liberty Bank. On 1 November, 2013, the Tbilisi City Court partially satisfied the Original Claimants' application for an injunction and encumbered 50.97% of the ordinary shares of the Bank held by Liberty Holding Georgia LLC.

On 21 November 2013, one other former shareholder Ana Gerbyak (the Original Claimants and Ana Gerbyak hereafter jointly referred to as the "Former Shareholders") filed a claim at the Tbilisi City Court against the same Respondents requesting partial annulment and avoidance of the SPA pursuant to which she had sold 113,373,100 ordinary shares of the Bank (representing at that time a 7.21% equity interest in the Bank) to Eurooil LLP. As injunctive relief, Ana Gerbyak requested the encumbrance of 7.21% of the Bank's ordinary shares held by Liberty Holding Georgia LLC. On 25 November 2013 the Tbilisi City Court satisfied the injunction application of Ana Gerbyak and encumbered 7.21% of shares of the Bank held by Liberty Holding Georgia LLC. As a result, 3,201,321,628 ordinary shares of the Bank owned by Liberty Holding Georgia LLC, equivalent to the IFRS ordinary equity book value of GEL 68,956 as of 31 December 2014 (63,377 as of 31 December 2013) and currently representing a 58.18% ordinary equity interest in the Bank, were encumbered by the Tbilisi City Court pending the outcome of the litigation. In 2009-2014, the Bank's ordinary equity has increased by GEL 109,294, as a result of the cumulative net income of GEL 52,157 and the issuance of new ordinary shares, purchased by certain Respondents as well as minority investors for the aggregate consideration of GEL 69,974. Thus, management believes that the injunctive relief has been greatly inequitable; even though the sale of 914,827,300 ordinary shares, with the then book value of GEL 8,606 has been disputed, 3,201,321,628 ordinary shares with the book value of GEL 68,956 (as of 31 December 2014), have been encumbered.

The Tbilisi City Court subsequently joined the claims filed by the Original Claimants and Ana Gerbyak and the case in currently pending as one.

The Respondents successfully appealed the Tbilisi City Court's injunctive relief decisions on the cases initiated by the Former Shareholders and in March 2014 the Tbilisi City Court reversed its decisions encumbering the ordinary shares of the Bank. Following the counter appeal of the Former Shareholders, in July 2014 the Tbilisi Court of Appeals returned the case back to the Tbilisi City Court for further consideration retaining the encumbrance on the shares.

The Tbilisi City Court reconsidered the issue of the encumbrance and once again partially satisfied the claims by the Respondents and ruled on 28 November 2014 that the Former Shareholders shall provide an undertaking in the amount of US$ 1,983 in cash in the designated escrow account within seven calendar days from the date of the ruling. The Original Claimants failed to provide the requested cash undertaking and, on 12 December 2014, the Tbilisi City Court issued a ruling, ordering the removal of the encumbrance on the ordinary shares. On 19 December 2014, the Former Shareholders appealed this ruling and on 20 March 2015, Tbilisi Court of Appeal issued a resolution and returned the case back to the Tbilisi City Court for the reconsideration and determination of certain factual aspects on the case. 3,201,321,628 ordinary shares of the Bank continue to be encumbered.

All of the above procedural steps concerned interim relief on the encumbrance of the ordinary shares. Consideration on the merits took place in summer and fall 2015, however, on 1 December 2015, the judge presiding over the case was promoted to the Tbilisi Court of Appeals. The pending shareholder dispute was then was assigned to a different judge in the Tbilisi City Court and the date of the next hearing is yet to be announced.

Management of the Bank strongly believes that the aforementioned lawsuit is frivolous and opportunistic in nature and wholly without merit and anticipates that, provided the court deliberations are objective, the litigation will end in favour of the Respondents.

(thousands of Georgian Lari)

19. Net fee and commission income

Net fee and commission income comprised:

	2015	*2014*
Plastic card operations	8,296	7,502
Settlements operations	6,055	6,174
Remittances	5,440	6,113
Cash operations	3,444	2,928
Fee income received from bill payments	1,801	1,237
Guarantees and letters of credit	64	393
Other	5,165	3,794
Fee and commission income	30,265	28,141
Plastic card operations	(4,537)	(3,163)
Settlements operations	(884)	(781)
Cash operations	(15)	(13)
Guarantees and letters of credit	(12)	(13)
Fee and commission expense	(5,448)	(3,970)
Net fee and commission income	24,817	24,171

20. Other income

Other income comprised:

	2015	*2014*
Income from penalty on late payments on customer loans and advances	13,331	7,807
Income from rent	777	762
Gain from sale of assets	363	68
Income from advertising	62	107
Gain from revaluation of investment properties	62	–
Other	792	1,621
Total other income	15,387	10,365

21. Personnel and general and administrative expenses

Personnel and general and administrative expenses comprise:

	2015	*2014*
Salaries	45,264	40,195
Variable monthly bonuses	5,778	3,397
Performance based discretionary bonus pool	6,062	3,939
Employee retention of the convertible preferred shares	1,718	1,200
Personnel expenses	58,822	48,731

21. Personnel and general and administrative expenses (continued)

	2015	*2014*
Occupancy and rent	7,592	5,854
Legal and other professional services	5,252	2,703
Communications	3,751	3,116
Office supplies	3,375	3,295
Marketing and advertising	2,912	3,159
Utility expense	1,987	1,928
Operating taxes	1,339	1,299
Security	1,187	1,158
Repair and maintenance	1,148	839
Travel expenses	1,116	661
Insurance	926	474
Corporate hospitality and entertainment	676	555
Other	3,120	3,836
General and administrative expenses	34,381	28,877

22. Risk management

Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk, market risk, operational risk and other non-financial risks. The risk management framework adopted by the Group sets the boundaries of risk bearing capacity for each risk and business line and ensures its compliance.

The responsibility of the individuals responsible for risk management is to ensure the compliance of the Group to the Risk Appetite Statement ("RAS") set by the Supervisory Board of the Bank. The compliance is ensured by continuous monitoring of the RAS parameters and proposing any changes to these parameters when circumstances change. RAS establishes escalation routes for trigger events and limits breaches in order to timely and effectively initiate and implement pre-defined mitigation actions. For the purposes of effective inclusion into daily activities of the Group, RAS parameters are detailed into more granular business unit and transactional levels. With the active involvement of Management Board risk management functions ensure proper communication and clarity at all levels regarding risk objectives, constant monitoring of risk profile against risk appetite, timely escalation of risk-related alerts and design of mitigating actions.

Risk management framework and structure

The Supervisory Board of the Bank has overall responsibility for the establishment and oversight of the Group's risk management framework. The Supervisory Board has established committees, which are responsible for developing and monitoring Group risk management policies in relevant specified areas.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Group, through its management standards, procedures and trainings aims, has a disciplined and constructive control environment, in which all employees understand their roles and obligations.

Audit Committee

The Audit Committee is responsible for monitoring compliance with the Group's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. The Audit Committee has the overall responsibility for monitoring of the RAS set by the Supervisory Board. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions. The Audit Committee is assisted in these functions by Internal Audit.

22. Risk management (continued)

Risk management framework and structure (continued)

Internal Audit

Risk management processes throughout the Group are audited by the internal audit function, which examines, by undertaking regular and ad-hoc reviews, both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with the Management Board, and reports its findings and recommendations to the Audit Committee.

Other structural units

The Supervisory Board is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks. Risk Appetite metrics are set by the Supervisory Board and monitored by the following committees and units with the active involvement of Management Board:

- Credit risk is managed by the Credit Risk Committees;
- Liquidity risk is managed by Asset-Liability Committee (ALCO);
- Market risk is managed by ALCO;
- Operational risk is managed by the Operational Risk Management Department;
- Information security and technology risks are managed by Information Security Committee.

All committees have representatives of all relevant business units and report regularly to the Management Board.

Business lines represent the primary owners of risks affecting daily activities and operations within the Group. Business processes incorporate controlling activities performed by the relevant risk unit representatives. Units with risk management functions represent the second line of defense. The following departments are responsible for day-to-management of credit, liquidity, market, operational and other financial risks:

- Credit Underwriting;
- Credit Administration;
- Credit Controlling;
- Collections;
- Operational Risk Management;
- Information Security;
- Enterprise Risk Management.

AML and Compliance Risks are managed by Operational Risk Department. Collections function is divided into two broad sub-functions, each responsible for leading and monitoring collection process per types of outstanding receivables.

Business lines represent the primary owners of risks affecting daily activities and operations within the Group. Business processes incorporate day-to-day involvement of risk management representatives, with focus on risk identification, analysis, evaluation and treatment.

Risk measurement and reporting systems

The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience.

Monitoring and controlling risks is primarily performed based on limits established by the RAS. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Management Board, and the head of each business division. The report includes aggregate credit exposure, hold limit exceptions, liquidity ratios and risk profile changes. Senior management assesses the appropriateness of the allowance for credit losses on a monthly basis.

(thousands of Georgian Lari)

22. Risk management (continued)

Risk measurement and reporting systems (continued)

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

The Group uses collateral and diversification to mitigate its credit risks.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographical location. The Group risk management functions ensure that potential negative impact from concentration is identified in a timely manner, respective risks properly measured and evaluated, and, ultimately, responsive actions planned and realised.

Credit risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Group manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Group has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. The credit quality review process allows the Group to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Actual exposure per borrower against limits is monitored on loans granted. The Credit Committee may initiate a change in the limits.

Where appropriate, the Bank obtains collateral and corporate guarantees. The credit risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

Credit-related commitments risks

The Group makes available to its customers guarantees which may require that the Group make payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

(thousands of Georgian Lari)

22. Risk management (continued)

Credit risk (continued)

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Group's internal credit policies. The table below shows the credit quality by class of asset for loan-related lines in the statement of financial position, based on the categories specified in the tables.

As of 31 December 2015	*Notes*	*Neither past due nor impaired*	*Past due but not fully impaired*	*Past due and fully impaired*	*Individually impaired*	*Total*
Cash and cash equivalents, except for cash on hand	6	361,750	–	–	–	361,750
Amounts due from credit institutions	7	58,502	–	–	–	58,502
Loans to customers	8					
Loans to retail clients with regular inflows		340,960	7,941	17,509	–	366,410
Consumer loans		124,218	9,663	23,076	–	156,957
Micro loans		89,996	1,620	3,022	–	94,638
Gold pawn loans		41,087	2,111	–	7,607	50,805
Residential mortgage loans		16,956	299	378	–	17,633
Corporate & SME loans		5,058	90	703	6,166	12,017
		618,275	21,724	44,688	13,773	698,460
Investment securities	9					
- Loans and receivables		79,469	–	–	–	79,469
- Held to maturity		124,321	–	–	–	124,321
		203,790	–	–	–	203,790
Total		1,242,317	21,724	44,688	13,773	1,322,502

As of 31 December 2014	*Notes*	*Neither past due nor impaired*	*Past due but not fully impaired*	*Past due and fully impaired*	*Individually impaired*	*Total*
Cash and cash equivalents, except for cash on hand	6	340,507	–	–	–	340,507
Amounts due from credit institutions	7	50,946	–	–	–	50,946
Loans to customers*	8					
Loans to retail clients with regular inflows		402,461	10,176	17,193	–	429,830
Consumer loans		109,801	8,637	15,992	–	134,430
Micro loans		78,646	977	1,461	–	81,084
Gold pawn loans		44,324	2,179	–	585	47,088
Residential mortgage loans		16,819	342	206	–	17,367
Corporate & SME loans		14,491	481	1,317	13,674	29,963
		666,542	22,792	36,169	14,259	739,762
Investment securities	9					
- Loans and receivables		–	–	–	–	–
- Held to maturity		196,906	–	–	–	196,906
		196,906	–	–	–	196,906
Total		1,254,901	22,792	36,169	14,259	1,328,121

* Classification of loans to customers in comparative information was changed to be in consistence with current year presentation. Loans to customers in amount to GEL 36,169 classified under individually impaired caption as of 31 December 2014 were reclassified to past due and fully impaired caption.

(thousands of Georgian Lari)

22. Risk management (continued)

Credit risk (continued)

An analysis of past due but not fully impaired loans, by age, is provided below. The majority of the past due loans are not considered to be impaired.

It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories. The attributable risk ratings are assessed and updated regularly.

Aging analysis of past due but not fully impaired loans per class of financial assets

As of 31 December 2015	*Notes*	*Less than 30 days*	*31 to 60 days*	*61 to 90 days*	*More than 90 days*	*Total*
Loans to customers	8					
Loans to retail clients with regular inflows		4,701	2,050	1,190	–	7,941
Consumer loans		5,059	2,604	2,000	–	9,663
Micro loans		1,004	341	275	–	1,620
Gold pawn loans		773	407	306	625	2,111
Residential mortgage loans		263	26	10	–	299
Corporate & SME loans		6	–	84	–	90
Total		11,806	5,428	3,865	625	21,724

As of 31 December 2014	*Notes*	*Less than 30 days*	*31 to 60 days*	*61 to 90 days*	*More than 90 days*	*Total*
Loans to customers	8					
Loans to retail clients with regular inflows		5,978	2,328	1,870	–	10,176
Consumer loans		5,200	1,860	1,577	–	8,637
Micro loans		562	222	193	–	977
Gold pawn loans		808	424	361	586	2,179
Residential mortgage loans		332	10	–	–	342
Corporate & SME loans		481	–	–	–	481
Total		13,361	4,844	4,001	586	22,792

See Note 8 for more detailed information with respect to the allowance for impairment of loans to customers.

Carrying amount per class of financial assets whose terms have been renegotiated

The table below shows the carrying amount for renegotiated financial assets, by class.

	2015	*2014*
Loans to customers		
Loans to retail clients with regular inflows	7,356	3,247
Consumer loans	8,475	12,027
Micro loans	755	745
Corporate & SME loans	134	3,362
Total	16,720	19,381

(thousands of Georgian Lari)

22. Risk management (continued)

Credit risk (continued)

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue or there are any known difficulties in the cash flows of counterparties or infringement of the original terms of the contract. The Group addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Group determines the allowances appropriate for each individually significant loan on an individual basis. The main consideration for the individual assessment include whether any payment of principal or interest are overdue by more than 90 days for all loans. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of other financial support and the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans to customers, both, significant as well as non-significant, where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date for each portfolio based on overdue day's buckets.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration historical losses on the portfolio and the appropriate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance. The impairment allowance is then reviewed by the management to ensure alignment with the Group's overall policy.

The geographical concentration of the Group's assets and liabilities is set out below:

	2015				*2014*			
	Georgia	*OECD*	*CIS and other foreign countries*	*Total*	*Georgia*	*OECD*	*CIS and other foreign countries*	*Total*
Assets								
Cash and cash equivalents	486,284	13,299	2,757	502,340	422,811	55,866	1,321	479,998
Amounts due from credit institutions	54,910	3,592	–	58,502	48,151	2,795	–	50,946
Loans to customers	641,116	–	–	641,116	692,110	–	–	692,110
Investment securities:								
- Loans and receivables	79,469	–	–	79,469	–	–	–	–
- Held to maturity	124,321	–	–	124,321	196,906	–	–	196,906
All other assets	165,145	1,421	1,432	167,998	152,335	5,533	529	158,397
	1,551,245	18,312	4,189	1,573,746	1,512,313	64,194	1,850	1,578,357
Liabilities								
Amounts due to credit institutions	118,759	–	156	118,915	6,037	–	–	6,037
Amounts due to customers	1,169,292	30,307	44,424	1,244,023	1,348,983	23,091	40,907	1,412,981
All other liabilities	21,612	–	–	21,612	18,836	–	–	18,836
Subordinated debt	38,303	17,561	2,482	58,346	12,028	3,761	57	15,846
	1,347,966	47,868	47,062	1,442,896	1,385,884	26,852	40,964	1,453,700
Net assets/(liabilities)	203,279	(29,556)	(42,873)	130,850	126,429	37,342	(39,114)	124,657

(thousands of Georgian Lari)

22. Risk management (continued)

Liquidity risk and funding management

Liquidity risk management and supervision

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The primary objective of the liquidity risk management is to ensure with a high degree of confidence that the Group is in a position to both address its daily liquidity obligations and withstand a period of liquidity stress, the source of which could be either Group-specific or market-wide. Other objectives include securing a balanced financing mix for the Group's activities, compliance with standards set by the NBG, managing crisis situations and controlling the cost of funding.

The main liquidity risk mitigation techniques are building liquidity reserves, diversifying funding sources and extending financing maturities. However, significant liquidity in excess of statutory requirements due to unexpected net cash inflows should be avoided and the Management Board should examine options to reduce liquidity to an appropriate level.

The Treasury Department is responsible for the management of the liquidity and funding risk within targets, boundaries and limits being set out in the RAS. The Treasury Department manages the liquidity risk on a centralised level and reports to the Management Board at least weekly. Key decisions on liquidity risk management and monitoring are taken by the ALCO.

The Group maintains a Contingency Funding Plan which details how liquidity stress events of varying severity would be managed. Since the precise nature of any stress event cannot be known in advance, the plans are designed to be flexible to the nature and severity of the stress event and provide a menu of options that could be used as appropriate at the time. The Contingency Funding Plan also contains Recovery Plan which considers actions to generate additional liquidity in order to facilitate recovery in a severe stress.

The Group uses stress testing and scenario analysis to evaluate the impact of a sudden and severe stress events on its liquidity position. The scenarios cover the Group-specific and market related risk events.

Statutory requirement

The NBG requires all banks in Georgia to maintain liquid assets of no less than 30.0% of its liabilities on daily basis. The Bank's average liquidity ratio was 59.9% for 31 December 2015 (31 December 2014: 53.1%).

From September 2014 the NBG introduced the minimum liquidity coverage ratio (LCR). The NBG requires all banks to maintain the LCR of 100.0% in GEL, foreign currency and total on a daily basis. As of 31 December 2015, the Bank's total LCR stood at 232.6% and the LCR in GEL was 141.3% (2014: total LCR stood at 183.2% and the LCR in GEL was 153.6%).

Analysis by remaining contractual maturities

The tables below summarise the maturity profile of the Group's financial liabilities as of 31 December 2015 and as of 31 December 2014 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

As of 31 December 2015	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
Financial liabilities					
Amounts due to credit institutions	118,662	486	–	–	119,148
Amounts due to customers	775,349	393,645	129,772	2,354	1,301,120
Subordinated debt	2,008	6,025	81,431	5,672	95,136
Total undiscounted financial liabilities	896,019	400,156	211,203	8,026	1,515,404

(thousands of Georgian Lari)

22. Risk management (continued)

Liquidity risk and funding management (continued)

As of 31 December 2014	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
Financial liabilities					
Amounts due to credit institutions	5,850	187	–	–	6,037
Amounts due to customers	1,001,947	358,058	103,949	2,075	1,466,029
Subordinated debt	558	1,673	23,751	1,340	27,322
Total undiscounted financial liabilities	1,008,355	359,918	127,700	3,415	1,499,388

The table below shows the contractual expiry by maturity of the Group's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

	Less than 3 months	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
2015	31,863	5,719	20,552	9,990	68,124
2014	44,429	3,916	13,511	6,359	68,215

The Group expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables above. These balances are included in amounts due in less than three months in the tables above.

Maturity analysis of assets and liabilities

Treasury Department manages the maturity analysis of assets and liabilities. Modeling of assets and liabilities is necessary where contractual maturity does not adequately reflect the liquidity risk position. The most significant example in this context for the Group would be current and savings accounts from retail, corporate and municipal and other state entities. Although, contractually, current accounts are repayable on demand and savings accounts at short notice, the Bank's broad base of customers – numerically and by depositor type – helps protect against unexpected fluctuations in balances. Such accounts form a stable funding base for the Group's operations and liquidity needs. Table below shows the maturity analysis of the Group's monetary assets and liabilities according to when they are expected to be recovered or settled.

	2015			*2014*		
	Within one year	*More than one year*	*Total*	*Within one year*	*More than one year*	*Total*
Cash and cash equivalents	502,340	–	502,340	479,998	–	479,998
Amounts due from credit institutions	58,502	–	58,502	50,946	–	50,946
Loans to customers	442,408	198,708	641,116	455,467	236,643	692,110
Investment securities:						
- Loans and receivables	72,677	6,792	79,469	–	–	–
- Held to maturity	44,831	79,490	124,321	76,550	120,356	196,906
Total	1,120,758	284,990	1,405,748	1,062,961	356,999	1,419,960
Amounts due to credit institutions	118,915	–	118,915	6,037	–	6,037
Amounts due to customers, of which:	540,701	703,322	1,244,023	893,272	519,709	1,412,981
- Current accounts	25,015	600,510	625,525	402,537	441,236	843,773
- Time deposits (including certificates of deposit)	515,686	102,812	618,498	490,735	78,473	569,208
Other liabilities	–	–	–	2	–	2
Subordinated debt	–	58,346	58,346	–	15,846	15,846
Total	659,616	761,668	1,421,284	899,311	535,555	1,434,866
Net	461,142	(476,678)	(15,536)	163,650	(178,556)	(14,906)

(thousands of Georgian Lari)

22. Risk management (continued)

Liquidity risk and funding management (continued)

The maturity of the assets is based on their carrying value and upon earliest legally exercisable maturity as of 31 December of the year concerned. The maturity of liabilities is based on the earliest contractual maturity or first call. The portion of current and savings accounts is presented in more than one year maturity range due to their stability. Customer deposits diversification by number and type of depositors and the past experience of the Group indicate that such accounts and deposits provide a long term and stable source of funding, and as a result they are allocated per expected time of the funds outflow in the gap analysis table on the basis of the statistical data accumulated by the Group during the previous periods and assumptions made regarding the "permanent" part of current account balances.

As of 31 December 2015, total Amounts due to customers amounted to GEL 1,244,023 (As of 31 December 2014: GEL 1,412,981), of which current accounts comprised GEL 625,525 (as of 31 December 2014: GEL 843,773). The Bank conducts the analysis of the stability of the current account balances for the period of the preceding two years on a daily basis. These balances have not fallen below GEL 600,510 (2014: GEL 441,236) for the respective periods of the preceding 24 months. As such, it is reasonable to present these funds in Amounts due to customers in more than one year maturity range in the above schedule. If the contractual maturities of Amounts due to customers were considered, the cumulative liquidity gap within one year as of 31 December 2015 would have been negative GEL 139,368 (31 December 2014: negative GEL 277,586).

As of 31 December 2015, the Bank had sufficient liquid collateral to additionally draw down GEL 67,845 (2014: GEL 187,061) from the NBG at immediate notice.

On 21 April 2015, Fitch Ratings affirmed the Bank's Long-Term Foreign Currency Issuer Default Rating (IDR) of 'B', Short-term IDR of 'B', Individual Rating of 'D/E', Support Rating of '4' and Support Rating Floor of 'B'. The Outlook for the Long-term IDR is Stable (In 2010 Fitch Ratings assigned the Bank a Long-Term Foreign Currency Issuer Default Rating (IDR) of 'B', Short-term IDR of 'B', Individual Rating of 'D/E', Support Rating of '4' and Support Rating Floor of 'B'. The Outlook for the Long-term IDR is Stable).

On 8 August 2015, Standard & Poor's assigned the Bank long-term counterparty credit rating of 'B' and short-term counterparty credit rating of 'B'. The outlook is Stable.

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. The Bank's strategy is not to be involved in trading book activity or investments in commodities. Accordingly, the Bank`s exposure to market risk is limited to interest rate risk and currency risk.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments.

The sensitivity of the statement of profit or loss is the effect of the assumed changes in interest rates on the net interest income for one year, due to re-pricing or maturity period characteristics of financial instruments. The Bank is exposed to interest rate risk in case of material drop in interest rates from competitors on loan products or rise in the cost of funds due to macro and Bank specific events.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The NBG requires the Bank to monitor both balance-sheet and total aggregate (including off-balance sheet) open currency positions and to maintain the later one within 20.0% of the Bank's total regulatory capital. As at 31 December 2015, the Bank maintained an aggregate open currency position of 2.4% of regulatory capital (31 December 2014: 1.5%).

The Bank has approved Foreign Currency Risk Management Policy, which is intended to establish parameters for the Bank for the management of foreign currency exposures.

22. Risk management (continued)

Market risk (continued)

The process of foreign currency risk management includes, but is not limited to:

- selection of adequate methodology for foreign currency risk identification and quantitative measurement;
- daily monitoring of the open foreign currency position;
- minimising currency risk through compliance with established limits;
- revealing existing and anticipated negative tendencies of increased currency risk followed by the analysis of its causes and implications;
- making recommendations on the currency risk management strategy;
- determining the types and limits on instruments used in the foreign currency risk operations.

ALCO sets limits on the level of exposure by currency as well as on aggregate exposure positions which are more conservative than those set by the NBG. The Bank's compliance with such limits is monitored daily by Treasury and Enterprise Risk Management Departments.

The tables below indicate the currencies to which the Group had significant exposure at 31 December on its non-trading monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the GEL, with all other variables held constant on the statement of profit or loss (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the statement of profit or loss. A negative amount in the table reflects a potential net reduction in statement of profit or loss or equity, while a positive amount reflects a net potential increase.

Currency	*Appreciation/ (depreciation) of the exchange rate of GEL against the respective currency in % 2015*	*Effect on profit before tax 2015*	*Appreciation/ (depreciation) of the exchange rate of GEL against the respective currency in % 2014*	*Effect on profit before tax 2014*
USD	-28.51%	974	-7.33%	112
EUR	-15.51%	(27)	5.17%	(10)

Operational risk

Operational risk is defined as the risk of a financial loss resulting from the inadequacy or failure of internal processes, systems or people, or from external events, whether deliberate, accidental or natural occurrences. External events include, but are not limited to fraud, floods, fire, earthquakes and terrorist or hacker attacks. Credit or market events such as default or fluctuations in value do not fall in the scope of operational risk. Compliance risk is included under operational risk. Compliance risk is the potential that the Bank may incur regulatory sanctions, financial loss and/or reputational damage arising from its failure to comply with applicable laws, rules and regulations. The operational risk does not cover the reputational risk.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Group standards for the management of operational risk in the following areas:

- requirements for the reconciliation and monitoring of transactions;
- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial actions;
- development of contingency plans;
- risk mitigation, including insurance.

(thousands of Georgian Lari)

22. Risk management (continued)

Operational risk (continued)

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of respective business lines, with summaries submitted to the Audit Committee and Supervisory Board.

23. Fair value disclosures

Fair value measurement procedures

External Valuators are involved for valuation of significant assets, such as properties. Involvement of external Valuators is decided upon annually by the management after discussion with and approval by the Bank's audit committee. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained. Valuators are normally rotated every three years. The management decides, after discussions with the Group's external Valuators, which valuation techniques and inputs to use for each case.

At each reporting date, the management analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Group's accounting policies. For this analysis, the management verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents. The management, in conjunction with the Group's external Valuators, also compares each the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable. On an interim basis, the management and the Group's external Valuators present the valuation results to the audit committee and the Group's independent auditors. This includes a discussion of the major assumptions used in the valuations.

Fair value hierarchy

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy.

		Fair value measurement using			
At 31 December 2015	*Date of valuation*	*(Level 1)*	*(Level 2)*	*(Level 3)*	*Total*
Assets measured at fair value					
Foreign exchange forwards and swaps	31 December 2015	–	58	–	58
Investment properties	31 December 2015	–	–	4,665	4,665
Property and equipment – land and buildings	31 December 2014	–	–	75,587	75,587
		–	58	80,252	80,310
Assets for which fair values are disclosed					
Investment securities:	31 December 2015				
- Loans and receivables		–	78,227	–	78,227
- Held to maturity		–	113,141	–	113,141
		–	191,368	–	191,368

		Fair value measurement using			
At 31 December 2014	*Date of valuation*	*(Level 1)*	*(Level 2)*	*(Level 3)*	*Total*
Assets measured at fair value					
Foreign exchange forwards and swaps	31 December 2014	–	4,033	–	4,033
Investment properties	31 December 2014	–	–	5,017	5,017
Property and equipment – land and buildings	31 December 2014	–	–	74,530	74,530
		–	4,033	79,547	83,580
Assets for which fair values are disclosed					
Investment securities:	31 December 2014				
- Loans and receivables		–	–	–	–
- Held to maturity		–	200,552	–	200,552
		–	200,552	–	200,552

There were no transfers among the levels of the fair value hierarchy in 2015 and 2014.

(thousands of Georgian Lari)

23. Fair value disclosures (continued)

Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison by class of the carrying amounts and fair values of the Group's financial instruments that are carried in the consolidated statement of financial position. The table does not include the fair values of non-financial assets and non-financial liabilities.

	Carrying value 2015	*Fair value 2015*	*Unrecognised gain/ (loss) 2015*	*Carrying value 2014*	*Fair value 2014*	*Unrecognised gain/ (loss) 2014*
Financial assets						
Investment securities:						
- Loans and receivables	79,469	78,227	(1,242)	–	–	–
- Held to maturity	124,321	113,141	(11,180)	196,906	200,552	3,646
Total unrecognised change in unrealised fair value			(12,422)			3,646

Valuation techniques and assumptions

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits and savings accounts without a specific maturity.

Derivatives

Derivatives valued using a valuation technique with market observable inputs are mainly interest rate swaps, currency swaps and forward foreign exchange contracts. The most frequently applied valuation techniques include forward pricing and swap models, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates and interest rate curves.

Financial assets and financial liabilities carried at amortised cost

Fair value of the quoted notes and bonds is based on price quotations at the reporting date, as such they fall under level 2 fair value hierarchy. The fair value of unquoted instruments, loans to customers, customer deposits, amounts due from credit institutions and amounts due to the NBG and credit institutions and other financial assets and liabilities, is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

Investment properties and buildings

There are three main approaches to valuation of real property:

Market approach

Establishes limits on the market value for the real estate by examining the prices commonly paid for properties that compete with the subject property for buyers. Sales are investigated to ensure that the parties to the transaction were adequately motivated. Sale prices reflecting motivation other than that of a typical market participant, i.e. transactions of special purchasers who are willing to pay a premium for a particular property, should be eliminated. The method involves analysing units of comparison such as a price per square metre of gross building area. Adjustments are made to the sales/listing for differences in location, size, age and condition, financing and various other factors which may have any influence on the value.

In the analysis of the market value of appraised properties by the sales comparison (market data) approach, it is utilised the sales/listing measured to the best available, most recent and overall similar sales/listing available as of the report date.

(thousands of Georgian Lari)

23. Fair value disclosures (continued)

Valuation techniques and assumptions (continued)

Information on the comparable sales and listing is obtained from brokerage companies, agents and brokers, as well as public information, including commercial broker listings on websites and published data. Then such information is further confirmed with owners and/or principles or brokers involved in the listed transactions.

Cost approach

Establishes the value of the real estate by estimating the cost of acquiring the land and building a new property or renovating an old property for equivalent utilisation purposes with no undue cost due to delay. An estimate of entrepreneurial incentive or developer's profit/loss is commonly added to the land and construction costs. For mature properties, the cost approach is used to estimate the depreciation cost, including items of physical deterioration and functional obsolescence.

The main approach of the cost replacement method reflects the idea that one will not pay for the given property more than he/she would pay for the construction of that property.

The cost approach involves the following steps:

- estimate land value;
- estimate reproduction or replacement cost of the improvements;
- estimate accrued depreciation from all sources (physical deterioration, functional obsolescence, external and economic obsolescence);
- deduct accrued depreciation from the reproduction or replacement cost to arrive at the depreciated improvement cost;
- estimate equipment cost and deduct depreciation;
- add the depreciated improvement cost to depreciated equipment cost and to the land value to arrive at a total property value indication.

Income capitalisation approach

The income generation methodology is based on the hypothetical incomes generated through the use of the property being valued. The estimation of the real estate market value is based on the capitalisation coefficient which is calculated based on the long-term rate of the alternative investment methodology.

Discount cash flow (DCF)

The fair value of completed investment properties is determined using a discounted cash flow (DCF). Based on the actual and projected market demand, types of goods/ services to be produced/provided, pricing policy and expected competitive environment in the market, the strategic financial projections for the business is developed. Using DCF method, a property's fair value is estimated using explicit assumptions regarding the benefits and liabilities of ownership over the asset's life including an exit or terminal value. As an accepted method within the income approach to valuation, the DCF method involves the projection of a series of cash flows on a real property interest. To this projected cash flow series, an appropriate, market-derived discount rate is applied to establish the present value of the cash inflows associated with the real property. The duration of the cash flow and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related lease up periods, re-letting, redevelopment, or refurbishment. The appropriate duration is typically driven by market behaviour that is a characteristic of the class of real property.

In the case of investment properties, periodic cash flow is typically estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance cost, agent and commission costs and other operating and management expenses. The series of periodic net cash inflows, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

(thousands of Georgian Lari)

23. Fair value disclosures (continued)

Valuation techniques and assumptions (continued)

Movements in level 3 assets and liabilities at fair value

The following tables show a reconciliation of the opening and closing amount of investment properties in Level 3 assets and liabilities which are recorded at fair value. For the reconciliation of property and equipment – buildings refer to Note 10:

	At 1 January 2015	*Total gain/(loss) recorded in profit or loss*	*Purchases*	*Sales*	*At 31 December 2015*
Assets					
Investment properties	5,017	62	–	(414)	4,665
	5,017	62	–	(414)	4,665

	At 1 January 2014	*Total gain/(loss) recorded in profit or loss*	*Purchases*	*Sales*	*At 31 December 2014*
Assets					
Investment properties	4,986	(25)	56	–	5,017
	4,986	(25)	56	–	5,017

The following table shows the quantitative information about significant unobservable inputs used in the fair value measurement categorised within Level 3 of the fair value hierarchy:

As of 31 December 2015	*Carrying amount*	*Valuation techniques*	*Unobservable input*	*Range (weighted average)*
Land and buildings – head office	43,623	- Income Capitalisation Approach (DCF)	- 10% increase/decrease of rent price - 10% increase/decrease of Occupancy rate	(9.98%) up to 9.36%
Land and buildings	11,244	- Income Capitalisation Approach (DCF)	- 10% increase/decrease of rent price - 10% increase/decrease of Occupancy rate	(12.46%) up to 11.21%
Land and buildings	9,472	- Cost approach	- 10% increase/decrease of land price - 10% increase/decrease of Replacement cost	(8.37%) up to 8.71%
Land and buildings	11,248	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(8.59%) up to 9.87%
Investment properties – commercial building	2,038	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(10.0%) up to 10.0%
Investment properties – commercial building	790	- Cost approach	- 10% increase/decrease of land price - 10% increase/decrease of Replacement cost	(4,85%) up to 5.15%
Investment properties – commercial building	1,772	- Market approach	- Price volatility/adjustment: 10% increase/decrease of market prices	(10.0%) up to 10.0%
Investment properties – commercial building	65	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(11.1%) up to 7.4 %

As of 31 December 2014	*Carrying amount*	*Valuation techniques*	*Unobservable input*	*Range (weighted average)*
Land and buildings – head office	43,460	- Income Capitalisation Approach (DCF)	- 10% increase/decrease of rent price - 10% increase/decrease of Occupancy rate	(9.98%) up to 9.36%
Land and buildings	11,137	- Income Capitalisation Approach (DCF)	- 10% increase/decrease of rent price - 10% increase/decrease of Occupancy rate	(12.46%) up to 11.21%
Land and buildings	8,954	- Cost approach	- 10% increase/decrease of land price - 10% increase/decrease of Replacement cost	(8.37%) up to 8.71%
Land and buildings	10,979	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(8.59%) up to 9.87%
Investment properties – commercial building	1,954	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(11.21%) up to 9.07%

(thousands of Georgian Lari)

23. Fair value disclosures (continued)

Valuation techniques and assumptions (continued)

As of 31 December 2014	*Carrying amount*	*Valuation techniques*	*Unobservable input*	*Range (weighted average)*
Investment properties – commercial building	413	- Cost approach	- 10% increase/decrease of land price - 10% increase/decrease of Replacement cost	(7.88%) up to 6.81%
Investment properties – commercial building	824	- Cost approach	- 10% increase/decrease of land price - 10% increase/decrease of Replacement cost	(9.87%) up to 8.05%
Investment properties – commercial building	1,746	- Market approach	- Price volatility/adjustment: 10% increase/decrease of market prices	(13.86%) up to 10.94%
Investment properties – commercial building	80	- Market approach	- Price volatility adjustment: 10% increase/decrease of market prices	(10.53%) up to 8.70%

24. Related party disclosures

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The outstanding balances at the period end of and related income and expense arising from related party transactions are as follows:

	2015				*2014*			
	Parent	*Entities with significant influence over the Group*	*Entities under common control*	*Key manage-ment personnel*	*Parent*	*Entities with significant influence over the Group*	*Entities under common control*	*Key manage-ment personnel*
Loans outstanding at 1 January, gross	–	–	–	321	–	–	–	147
Loans issued during the year	–	–	393	4	–	–	279	289
Loan repayments during the year	–	–	(393)	(98)	–	–	(279)	(115)
Loans outstanding at 31 December, gross	–	–	–	227	–	–	–	321
Less: allowance for impairment at 31 December	–	–	–	(5)	–	–	–	(6)
Loans outstanding at 31 December, net	–	–	–	222	–	–	–	315
Interest income on loans	–	–	3	41	–	–	3	40
Impairment charge for loans	–	–	–	(1)	–	–	–	3

24. Related party disclosures (continued)

	2015				2014			
	Parent	*Entities with significant influence over the Group*	*Entities under common control*	*Key management personnel*	*Parent*	*Entities with significant influence over the Group*	*Entities under common control*	*Key management personnel*
Deposits at 1 January	–	–	827	1,934	620	–	587	360
Deposits received during the year	–	–	–	–	545	–	240	1,876
Deposits repaid during the year	–	–	(827)	(1,833)	(1,165)	–	–	(302)
Deposits at 31 December	–	–	–	101	–	–	827	1,934
Subordinated debt at 1 January	–	–	–	–	–	–	–	–
Subordinated debt received during the year	–	–	996	798	–	–	–	–
Subordinated debt at 31 December	–	–	996	798	–	–	–	–
Current accounts at 31 December	75	–	3,557	1,813	117	9	1,506	1,631
Interest expense on deposits and current accounts	6	–	121	230	126	–	224	213
Interest expense on subordinated debt	–	–	59	2	–	–	–	–
Commitments and guarantees issued	–	–	830	–	–	–	830	–
Fee and commission income	–	–	271	14	–	–	338	5
Other operating expenses	–	–	582	21	–	–	825	178

Entities under common control comprises of organisations in which shareholders of the Group exercise control which represent related parties to the Group.

The number of key personnel at 31 December 2015 was 8 (2014: 11) and their compensation comprised the following:

	2015	*2014*
Salaries, bonuses and other short term benefits	6,992	5,219
Retention bonus paid in cash for purchase of the subordinated debt contracts	1,718	–
Retention bonus paid in cash for purchase of the convertible preferred shares	–	1,164
Total key personnel compensation	8,710	6,383

25. Capital adequacy

The Bank is regulated by the NBG. As such, the Bank submits to the NBG monthly reports of its financial position and operation (the "Monthly Supervision Report"), which, *inter alia*, contains the Bank's capital adequacy ratios, calculated in accordance with the methodology required by the NBG.

The Bank maintains an actively managed capital base to cover risks inherent in the business and aims at further enhancing its capital base. The adequacy of the Group's capital is monitored using, among other measures, the ratios established by the NBG and the ratios established by the Basel Capital Accord 1988 in supervising the Group.

(thousands of Georgian Lari)

25. Capital adequacy (continued)

NBG Capital adequacy ratio

Under the current capital requirements, the NBG requires the banks to maintain throughout 2015 the minimum capital adequacy ratio of 11.4% (95.0% of 12.0%) of the risk-weighted exposures (RWE), as well as the minimum Tier 1 Capital adequacy ratio of 7.6% (95.0% of 8.0%) of the RWE, computed based on the Bank's stand-alone financial statements, prepared in accordance with the NBG requirements. The capital adequacy calculation methodology adopted by the NBG differs in certain material respects from the BIS (Basel I) framework, but has historically been more stringent, due, inter alia, to the higher market-risk weighting of the exposures.

As of 31 December 2015 and 31 December 2014, the Bank's Capital adequacy ratios were as follows:

	2015	*2014*
Core capital	90,597	106,958
Supplementary capital	76,947	37,157
Less: deductions from capital	(1,560)	(1,458)
Total capital	165,984	142,657
Risk-weighted assets	849,311	942,867
Tier 1 capital adequacy ratio	10.67%	11.34%
Capital adequacy ratio	19.54%	15.13%

NBG Basel II/III Capital adequacy ratio

After adoption of NBG Basel II/III requirements effective 30 June 2014, the banks are required to maintain a minimum Total Capital adequacy ratio of 10.5% of the RWE, minimum Tier 1 Capital adequacy ratio of 8.5% of the RWE and Common Equity Tier 1 Capital adequacy ratio of 7.0% of the RWE computed based on the Bank's stand-alone financial statements prepared in accordance with NBG requirements. The Bank's capital adequacy ratios calculated in accordance with NBG Basel II requirement were as follows:

	2015	*2014*
Common Equity Tier 1 capital	102,374	115,784
Additional Tier 1 capital	6,139	6,139
Tier 1 capital	108,513	121,923
Tier 2 capital	56,495	17,155
Total regulatory capital	165,008	139,078
Total risk weighted exposures	1,189,508	1,024,043
Common Equity Tier 1 capital ratio	8.61%	11.31%
Tier 1 capital ratio	9.12%	11.91%
Total regulatory capital ratio	13.87%	13.58%

(thousands of Georgian Lari)

25. Capital adequacy (continued)

Capital adequacy ratio under Basel Capital Accord 1988

The Group's capital adequacy ratios, computed in accordance with the Basel Capital Accord 1988, with subsequent amendments including the amendment to incorporate market risk, as of 31 December 2015 and 31 December 2014, were as follows:

	2015	*2014*
Tier 1 Capital	122,568	116,202
Tier 2 Capital	62,689	32,059
Total capital	185,257	148,261
Risk-weighted exposures	818,124	870,978
Tier 1 Capital adequacy ratio	14.98%	13.34%
Total Capital adequacy ratio	22.64%	17.02%

26. Events after the reporting period

Ordinary share buyback

On 12 November 2015, the Group commenced the Buyback of 1,045,428,327 or 19.00% of the total number of ordinary shares issued and outstanding. The Buyback period was set as 90 calendar days from announcement date and completed on 10 February 2016. As of the report issue date, the Buyback has been completed, with GEL 18,713 paid out to the participating ordinary shareholders. The Bank repurchased 1,045,428,327 ordinary shares or 19.00% of total number of ordinary shares issued and outstanding at weighed average price of GEL 0.0179 per ordinary share.

Disposal of investment property

In furtherance of the Group's efforts to dispose of its non-core assets, in February 2016, the Group disposed through a directly negotiated sale to third parties the immovable property located at 13 Cairo Street, Tbilisi, Georgia, a warehouse building sited in an industrial area of Tbilisi with the usable space of approximately 8,706 square meters and land area of approximately 13,890 square meters; The sale was accomplished at most recent fair value revaluation of the property of GEL 2,038.

Disposal of Bus Stop Constructions (property of 100% subsidiary Bus Stop LLC)

In June 2006, the Real Estate Development LLC (the "RED"), at that time 100% subsidiary of the Bank, signed a lease agreement (the "Lease Agreement") with Tbilisi City Municipality (the "Tbilisi City Municipality") to lease the plots of land within administrative territory of Tbilisi to further construct public bus stops (the "Bus Stop Constructions") as per the terms as announced by the Tbilisi City Municipality. In December 2009, the Bus Stop LLC (the "Bus Stop"), 100% subsidiary of the Bank, substituted the RED in the Lease Agreement with the Tbilisi City Municipality.

On 30 March 2016, Tbilisi City Municipality announced a new 5-day tender (ending on 4 April 2016) for the leased property under the conditions that the Lease Agreement is to be terminated by mutual agreement between the Bus Stop and the Tbilisi City Municipality and the winner of the tender to purchase the Bus Stop Constructions from the Bus Stop for no less than GEL 350 (excluding the VAT).

On 8 April 2016, in the best corporate interests of the Group to dispose of its legacy non-core assets, the Bus Stop Constructions were sold to third party, not affiliated with the Group and/or the management of the Group, with the aggregate sale price of GEL 350.