

**State Oil Company of
the Azerbaijan Republic**

**International Financial Reporting Standards
Consolidated financial statements**

31 December 2016

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Independent auditor's report

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Independent auditor's report

To the Management of the State Oil Company of the Azerbaijan Republic

Opinion

We have audited the accompanying consolidated financial statements of the State Oil Company of the Azerbaijan Republic and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects the consolidated financial position of the Group as at 31 December 2016 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Impairment of oil and gas assets

We considered this matter to be one of most significance in the audit due to significance of the balances of the Group's oil and gas assets, the high level of subjectivity in respect of assumptions underlying impairment analysis and significant judgements and estimates made by the management. The assessment of the asset carrying values is further complicated as external market evidence, such as market transactions, become less relevant in a period of significant changes in oil prices. In addition, a significant and rapid decrease in oil prices over the last few years has impacted the Group's operations and cash flows and triggers potential impairment.

We evaluated the change in risk profile of the group's assets and scrutinized impairment considerations. We involved our internal valuation experts and compared assumptions used in impairment testing such as expected market oil prices, reserves and resources volumes and discount rates with available external data. We also performed audit procedures on the mathematical integrity of impairment models and sensitivity analysis and procedures to ensure the completeness of the impairment charge as well as testing of write offs of unsuccessful exploration assets.

Details of key assumptions used by management and results of impairment tests are disclosed in Note 3 to the consolidated financial statements.

Estimation of oil and gas reserves

The estimate of oil and gas reserves has a significant impact on the impairment test and depreciation and decommissioning provisions. The Group involved internationally recognized independent reserves engineers to evaluate its oil and gas reserves as of 1 January 2017. As part of the audit procedures, we checked that assumptions used by the reserve engineers are in line with the Group's approved budget and historical data. We critically assessed the underlying assumptions and analyzed the reserves report and verified that the updated estimates of reserves and resources were appropriately included in the consideration of impairment, depreciation, depletion and amortization and decommissioning provisions. Further details on estimation of oil and gas reserves are disclosed in Note 3 to the consolidated financial statements.

Other information included in the Group's 2016 Annual Report

Other information consists of the information included in the Group's 2016 Annual Report other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Group's 2016 Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and the Management Board for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs 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.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

The Management Board is responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

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

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Management Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Management Board with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Management Board, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The partner in charge of the audit resulting in this independent auditor's report is Nargiz Karimova.

Ernst & Young Holdings (CIS) B.V.

Ernst & Young Holdings (CIS) B.V.
Branch in the Republic of Azerbaijan

30 June 2017

Azerbaijan, Baku, 153 Neftchilar avenue

Consolidated statement of financial position*(Amounts presented are in millions of Azerbaijani Manats)*

	Note	31 December 2016	31 December 2015
Assets			
Current assets			
Cash and cash equivalents	8	4,163	4,881
Restricted cash	9	121	203
Deposits	8	1,039	143
Available-for-sale investments	10	82	77
Trade and other receivables	11	8,618	6,146
Inventories	12	4,968	1,903
Other current financial assets	14	1,564	611
Total current assets		20,555	13,964
Non-current assets			
Property, plant and equipment	15	20,116	17,236
Goodwill	38	342	275
Intangible assets other than goodwill	16	689	716
Investments in joint ventures	17	4,555	3,171
Investments in associates	18	4,442	2,838
Deferred tax assets	33	841	712
Other non-current financial assets	14	578	502
Other non-current assets	13	889	540
Total non-current assets		32,452	25,990
Total assets		53,007	39,954
Equity			
Charter capital	27	1,802	1,617
Additional paid-in-capital	27	2,159	1,423
Retained earnings		6,265	6,191
Other capital reserves		(46)	(12)
Put option on company's shares	35	(1,305)	(1,305)
Gain on sale of subsidiary share	27	1,280	1,234
Cumulative translation differences		6,292	4,427
Equity attributable to equity holders of the Group		16,447	13,575
Non-controlling interests		1,257	1,073
Total equity		17,704	14,648

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statement of financial position*(Amounts presented are in millions of Azerbaijani Manats)*

	Note	31 December 2016	31 December 2015
Liabilities			
Current liabilities			
Trade and other payables	19	9,662	6,253
Short-term and current portion of long-term borrowings	20	6,717	3,085
Taxes payable	21	616	532
Other provisions for liabilities and charges	23	74	70
Deferred acquisition consideration payable	26	153	133
Deferred income	24	98	–
Other current liabilities	25	1,052	174
Total current liabilities		18,372	10,247
Non-current liabilities			
Long-term borrowings	20	8,210	7,826
Asset retirement obligations	22	968	748
Other provisions for liabilities and charges	23	149	142
Deferred income	24	74	79
Deferred tax liabilities	33	1,272	1,037
Advances received for the sale of shares	34	2,897	2,097
Put option liabilities	35	2,832	2,492
Other non-current liabilities	25	529	638
Total non-current liabilities		16,931	15,059
Total liabilities		35,303	25,306
Total liabilities and equity		53,007	39,954

Approved for issue and signed on behalf of the Group on 30 June 2017.



Mr. Rovnag Abdullayev
President

Mr. Suleyman Gasymov
Vice-President for Economic Affairs

Consolidated statement of profit or loss and other comprehensive income*(Amounts presented are in millions of Azerbaijani Manats)*

	Note	2016	2015
Revenue	28	51,905	33,103
Cost of sales	29	(47,387)	(29,849)
Gross profit		4,518	3,254
Distribution expenses	29	(814)	(653)
General and administrative expenses	29	(1,092)	(855)
Loss on disposal of property, plant and equipment and intangible assets		(34)	(19)
Social expenses		(148)	(143)
Exploration and evaluation expenses	29	(35)	(31)
Other operating expenses	29	(1,196)	(427)
Other operating income	30	697	161
Operating profit		1,896	1,287
Finance income	31	189	65
Finance costs	32	(841)	(476)
Foreign exchange gains and losses, net		(1,284)	(2,934)
Share of result of joint ventures	17	767	273
Share of result of associates	18	209	201
Profit/(loss) before income tax		936	(1,584)
Income tax expense	33	(586)	(201)
Profit/(loss) for the year		350	(1,785)
Other comprehensive income			
Other comprehensive income to be reclassified to profit or loss in subsequent periods – currency translation differences, net of tax		1,818	5,024
Other comprehensive (loss)/income not to be reclassified to profit or loss in subsequent periods – loss on cash flow hedge, net of tax		(34)	6
Other comprehensive income for the year, net of tax		1,784	5,030
Total comprehensive income for the year		2,134	3,245
Profit/(loss) is attributable to:			
Equity holders of the Group		147	(1,818)
Non-controlling interests		203	33
		350	(1,785)
Total comprehensive income attributable to:			
Equity holders of the Group		1,978	2,815
Non-controlling interests		156	430
		2,134	3,245

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity*(Amounts presented are in millions of Azerbaijani Manats)*

		Attributable to the equity holders of the parent							Non-controlling interests	Total equity		
Note	Charter capital	Additional paid-in capital	Put option on an entity's own shares	Gain on sale of subsidiary share	Other capital reserves	Retained earnings	Currency translation difference	Total				
Balance at 1 January 2015		1,496	963	(179)	122	(18)	8,348	(200)	10,532	525	11,057	
Profit/(loss) for the year		-	-	-	-	-	(1,818)	-	(1,818)	33	(1,785)	
Currency translation differences, net of tax		-	-	-	-	-	-	4,627	4,627	397	5,024	
Other comprehensive income		-	-	-	-	6	-	-	6	-	6	
Total comprehensive income for 2015		-	-	-	-	6	(1,818)	4,627	2,815	430	3,245	
Net gain on sale of subsidiary share		-	-	-	1,112	-	-	-	1,112	126	1,238	
Put option on company's shares		-	-	(1,126)	-	-	-	-	(1,126)	-	(1,126)	
Increase in charter capital		27	121	(121)	-	-	-	-	-	-	-	
Additional paid-in-capital		27	-	581	-	-	-	-	581	-	581	
Distribution to the Government		27	-	-	-	-	(339)	-	(339)	-	(339)	
Dividends declared by subsidiary			-	-	-	-	-	-	-	(8)	(8)	
Balance at 31 December 2015			1,617	1,423	(1,305)	1,234	(12)	6,191	4,427	13,575	1,073	14,648
Profit for the year			-	-	-	-	147	-	147	203	350	
Currency translation differences, net of tax			-	-	-	-	-	1,865	1,865	(47)	1,818	
Other comprehensive loss			-	-	-	(34)	-	-	(34)	-	(34)	
Total comprehensive income for 2016			-	-	-	-	(34)	147	1,865	1,978	156	2,134
Net gain on sale of subsidiary share		27	-	-	-	46	-	-	46	172	218	
Contribution in charter capital of subsidiaries by non-controlling shareholder			-	-	-	-	-	-	-	10	10	
Increase in charter capital		27	185	(185)	-	-	-	-	-	-	-	
Additional paid-in-capital		27	-	921	-	-	-	-	921	-	921	
Distribution to the Government		27	-	-	-	-	(73)	-	(73)	-	(73)	
Dividends declared by subsidiary			-	-	-	-	-	-	-	(154)	(154)	
Balance at 31 December 2016			1,802	2,159	(1,305)	1,280	(46)	6,265	6,292	16,447	1,257	17,704

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statement of cash flows*(Amounts presented are in millions of Azerbaijani Manats)*

	Note	2016	2015
Cash flows from operating activities			
Profit before income tax		936	(1,584)
<i>Adjustments for:</i>			
Depreciation of property, plant and equipment	29	1,014	1,049
Amortisation of intangible assets	16	40	30
Impairment of property, plant and equipment	15	322	254
Impairment of trade and other receivables and other financial assets	29	493	38
Change in provisions	29	71	58
Change in asset retirement obligations recognized in profit or loss		2	(10)
Loss on disposals of property, plant and equipment and intangible assets		34	19
Finance income	31	(189)	(65)
Finance costs	32	841	476
Foreign exchange rate differences		1,011	3,212
Share of result of associates and joint ventures	17, 18	(976)	(474)
Gain on release of borrowings	30	–	(22)
Other non-cash transactions		(122)	29
Operating cash flows before working capital changes		3,477	3,010
(Increase)/decrease in trade and other receivables		(2,329)	698
Increase in inventories		(2,628)	(3)
Increase in trade and other payables		2,863	232
(Decrease) in taxes payable		–	(15)
Change in other assets and liabilities		148	(341)
Utilization of provisions		(75)	(79)
Cash generated from operations		1,456	3,502
Income taxes paid		(472)	(196)
Interest paid		(743)	(387)
Net cash flows from operating activities		241	2,919
Cash flows from investing activities			
Acquisitions of subsidiary (net of cash acquired), additional share in joint operations, additional contribution in associates and joint ventures		(941)	(1,504)
Purchase of property, plant and equipment		(3,526)	(1,625)
Purchase of intangible assets	16	(22)	(22)
Placement of deposits		(892)	(72)
Interest received		195	65
Dividends received from associates and joint ventures		190	708
Proceeds from sale of property, plant and equipment		12	–
Prepayments for acquisition of subsidiary		–	(6)
Advances received for sale of interest		466	563
Loans issued to joint venture		(63)	–
Loans issued to third parties		(9)	–
Net cash flows used in investing activities		(4,590)	(1,893)
Cash flows from financing activities			
Proceeds from borrowings		6,751	3,481
Repayment of borrowings		(4,261)	(2,335)
Contribution in subsidiary by non-controlling shareholder		10	–
Proceeds from sale of non-controlling interests	27	218	1,439
Increase in charter capital and additional paid-in capital	27	921	581
Dividends paid to non-controlling interests		(154)	(8)
Distribution to the Government	27	(73)	(326)
Change in restricted cash related to borrowings		81	(24)
Net cash flows from financing activities		3,493	2,808
Net foreign exchange difference on cash and cash equivalents		138	(445)
Net (decrease)/increase in cash and cash equivalents		(718)	3,389
Cash and cash equivalents at the beginning of the year	8	4,881	1,492
Cash and cash equivalents at the end of the year	8	4,163	4,881

The accompanying notes are an integral part of these consolidated financial statements.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

1 The Group and its operations

The State Oil Company of the Azerbaijan Republic ("SOCAR") was established by the Presidential Decree on 13 September 1992 in accordance with Azerbaijani legislation and is domiciled in the Azerbaijan Republic. SOCAR is involved in upstream, midstream and downstream operations. SOCAR's main functions pertain to the extraction, refining, transportation of oil, gas and gas condensates, and sale of gas and oil and gas products. SOCAR is 100 per cent owned by the Government of the Azerbaijan Republic (the "Government").

SOCAR's registered address is 121 Heydar Aliyev avenue, AZ 1029 Baku, Azerbaijan Republic.

Information about subsidiaries

The consolidated financial statements of the Group include the following material subsidiaries:

Name	Principal activities	Country of incorporation	% equity interest	
			2016	2015
SOCAR Turkey Enerji A.Ş.	Refinery	Turkey	86.99%	86.99%
Azerbaijan (ACG) Ltd	Oil production	Cayman Islands	100%	100%
Azerbaijan (Shah Deniz) Ltd	Gas production	Cayman Islands	100%	100%
Caspian Drilling Company (CDC)	Drilling operations	Azerbaijan	92.44%	92.44%
SOCAR Energy Georgia LLC	Sales and Distribution	Georgia	51%	51%
SOCAR Overseas LLC	Sales and Distribution	UAE	100%	100%
SOCAR Trading Holding	Sales and Distribution	Malta	100%	100%
Azerbaijan (BTC) Ltd	Sales and Distribution	Cayman Islands	100%	100%
Cooperative Menkent U.A.	Sales and Distribution	Netherlands	100%	100%
SOCAR Energy Holdings AG	Sales and Distribution	Switzerland	100%	100%
SOCAR Energy Ukraine	Sales and Distribution	Ukraine	100%	100%
Azerbaijan (SCP) LTD	Sales and Distribution	Cayman Islands	100%	100%
SOCAR Petroleum CJSC	Sales and Distribution	Azerbaijan	100%	100%
Baku Shipyard Company	Construction	Azerbaijan	65%	65%
Socar Polymer LLC	Chemicals production	Azerbaijan	71%	71%
BOS Shelf LLC	Construction	Azerbaijan	90%	90%

2 Basis of preparation and significant accounting policies

Basis of preparation

These consolidated financial statements of SOCAR and its subsidiaries, associates and joint ventures (collectively referred to as "the Group") have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Group and its subsidiaries as at 31 December 2016.

Subsidiaries are all entities (including special-purpose entities) over which the Group has control. 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; and
- ▶ The ability to use its power over the investee to affect its returns.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Basis of consolidation (continued)

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.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary.

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated. Unrealized losses are also eliminated but considered an impairment indicator of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

Total comprehensive income within a subsidiary is attributed to the non-controlling interests even if that results in a deficit balance.

Business combinations

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, which is measured at acquisition date fair value, and the amount of any non-controlling interests in the acquiree. For each business combination, the acquirer measures the non-controlling interests in the acquiree at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses. When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is re-measured to fair value at the acquisition date through profit or loss.

Transactions with non-controlling interests

Changes in the Group's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions (i.e. transactions with owners in their capacity as owners). In such circumstances the carrying amounts of the controlling and non-controlling interests shall be adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in equity and attributed to the owners of the Group.

Business combinations with entities under common control

The Group applies acquisition method of accounting for business combinations with entities under the common control.

Investments in associates and joint ventures

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Investments in associates and joint ventures (continued)

A joint venture ("JV") is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The considerations made in determining significant influence or joint control is similar to those necessary to determine control over subsidiaries.

The Group's investments in its associate and joint venture are accounted for using the equity method. Under the equity method, the investment in an associate or a joint venture is initially recognized at cost. The carrying amount of the investment is adjusted to recognize changes in the Group's share of net assets of the associate or joint venture since the acquisition date. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The statement of profit or loss reflects the Group's share of the results of operations of the associate or joint venture. Any change in OCI of those investees is presented as part of the Group's OCI. Any gain or loss on sale of share that was recognized directly in the equity of the associate or joint venture is reflected as a gain or loss within the Group share of associate's or joint venture's profit or loss. Unrealised gains and losses resulting from transactions between the Group and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.

The aggregate of the Group's share of profit or loss of an associate and a joint venture is shown on the face of the statement of profit or loss outside operating profit and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate or joint venture.

The financial statements of the associate or joint venture are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognize an impairment loss on its investment in its associate or joint venture. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate or joint venture is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying value, and then recognizes the loss as 'Share of profit of an associate and a joint venture' in the statement of profit or loss.

Upon loss of significant influence over the associate or joint control over the joint venture, the Group measures and recognizes any retained investment at its fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognized in profit or loss.

Investments in Production Sharing Agreements ("PSAs")

Certain of the Group's upstream activities are governed by the PSAs. According to the terms of PSAs, the Group owns the portion of project's assets and liable for its portion of project's liabilities. At the same time the Group is entitled to its portion of expenses incurred and revenues earned by the whole project. Therefore, the Group accounts for its investment in PSA's by recognizing the portion of underlying assets, liabilities, expenses incurred and income earned by the projects using undivided interest method.

PSA is the method to execute exploitation of mineral resources by taking advantage of the expertise of a commercial oil and gas entity. The Government retains title to the mineral resources (whatever the quantity that is ultimately extracted) and often the legal title to all fixed assets constructed to exploit the resources. The Government takes a percentage share of the output which may be delivered in product or paid in cash under an agreed pricing formula. The contracting parties may only be entitled to recover specified costs plus an agreed profit margin. It may have the right to extract resources over a specified period of time. Operating company is a legal entity created by one or more contracting parties to operate PSA.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Investments in Production Sharing Agreements ("PSAs") (continued)

As a contracting party to various PSAs the Group evaluates and accounts for the PSAs in accordance with the substance of the arrangement. It records only its own share of oil and gas under a PSA as revenue. Neither revenue nor cost is recorded by the Group for the oil and gas extracted and sold on behalf of the Government. The Group acts as the Government's agent to extract, deliver or sell the oil and gas and remit the proceeds.

Costs that meet the recognition criteria as intangible or fixed assets in accordance with IAS 38 and IAS 16, respectively, are recognized where the entity is exposed to the majority of the economic risks and has access to the probable future economic benefits of the assets. Acquisition, development and exploration costs are accounted for in accordance with policies stated herein.

Assets subject to depreciation, depletion or amortization are expensed using the appropriate depletion or depreciation method stipulated by the present accounting policies over the shorter of the PSA validity period or the expected useful life of the related assets.

Foreign currency translation

All amounts in these consolidated statements are presented in millions of Azerbaijani Manats ("AZN"), unless otherwise stated.

The functional currencies of the Group's consolidated entities are the currencies of the primary economic environments in which the entities operate. The functional currency of SOCAR and its 23 business units and the Group's presentation currency is the national currency of the Azerbaijan Republic, AZN. However, US Dollar ("USD"), Swiss Franc ("CHF"), Georgian Lari ("GEL"), Ukrainian Hryvnia ("UAH"), Japanese Yen ("JPY") and Turkish Lira ("TRY") are considered the functional currency of the Group's certain subsidiaries, associates and joint ventures as majority of these investments' receivables, revenues, costs and debt liabilities are either priced, incurred, payable or otherwise measured in these currencies.

The transactions executed in foreign currencies are initially recorded in the functional currencies of respective Group entities by applying the appropriate rates of exchanges prevailing at the date of transaction.

Monetary assets and liabilities denominated in foreign currencies other than functional currency of respective Group entity are translated into the functional currency of that entity at the appropriate exchange rates prevailing at the reporting date.

Foreign exchange gains and losses resulting from the re-measurement into the functional currencies of respective Group's entities are recognized in profit or loss.

The results and financial position of the Group entities which functional currency differ from the presentation currency of the Group and not already measured in the Group's presentation currency (functional currency of none of these entities is a currency of a hyperinflationary economy) are translated into the presentation currency of the Group as follows:

- (i) assets and liabilities for each statement of financial position are translated at the closing rate at the date of that statement of financial position;
- (ii) income and expenses for each statement of profit or loss and other comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- (iii) all resulting exchange differences are recognized as a separate component of equity – currency translation difference.

At 31 December 2016 the principal rate of exchange used for translating foreign currency balances was USD 1 = AZN 1.7707, EUR 1 = AZN 1.8644, CHF 1 = AZN 1.7351, GEL 1 = AZN 0.6663, UAH 1 = AZN 0.0653, TRY 1 = AZN 0.5023, JPY 100 = AZN 1.5168 (2015: USD 1 = AZN 1.5594, EUR 1 = AZN 1.7046, CHF 1 = AZN 1.5709, GEL 1 = AZN 0.6511, UAH 1 = AZN 0.0655, TRY 1 = AZN 0.5358, JPY 100 = AZN 1.2946).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Financial instruments – key measurement terms

Depending on their classification financial instruments are carried at fair value, or amortized cost as described below.

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. The principal or the most advantageous market must be accessible to 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.

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 recognized in the financial statements at fair value 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.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes transaction costs. Measurement at cost is only applicable to investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost is the amount at which the financial instrument was recognized at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest rate method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related statement of financial position items.

The effective interest rate method is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Financial instruments – key measurement terms (continued)

The effective interest rate discounts cash flows of variable interest instruments to the next interest re-pricing date except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

Financial assets

The Group classifies its financial assets in the following measurement categories: a) financial assets at fair value through profit or loss; b) loans and receivables; c) financial assets held-to-maturity and d) available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

The subsequent measurement of financial assets depends on their classification, as follows:

- (a) *Financial assets at fair value through profit or loss.* Financial assets at fair value through profit or loss are financial assets held for trading (a financial asset is classified in this category if acquired principally for the purpose of selling in the short term) and financial assets designated upon initial recognition as at fair value through profit or loss. Derivatives are classified as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.
- (b) *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 included in current assets, except for maturities greater than 12 months after the reporting date. These are classified as non-current assets. Loans and receivables are classified as trade and other receivables in the statement of financial position.
- (c) *Held-to-maturity financial assets.* This classification includes quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has both the intention and ability to hold to maturity. Management determines the classification of investment securities held-to-maturity at their initial recognition and reassesses the appropriateness of that classification at each reporting date.
- (d) *Available-for-sale financial assets.* Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the reporting date.

Regular purchases and sales of financial assets are recognized on the trade date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the statement of profit or loss and other comprehensive income. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables, investment securities held-to-maturity are carried at amortized cost using the effective interest rate method.

Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are presented in the statement of profit or loss and other comprehensive income within other gains/(losses) in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the statement of profit or loss and other comprehensive income as part of other income when the Group's right to receive payments is established.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale are analyzed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognized in profit or loss; translation differences on non-monetary securities are recognized in equity. Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognized in equity.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Financial assets (continued)

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the statement of profit or loss and other comprehensive income as gains and losses from investment securities. Interest on available-for-sale securities calculated using the effective interest rate method is recognized in the statement of profit or loss and other comprehensive income as part of other income. Dividends on available-for-sale equity instruments are recognized in the statement of profit or loss and other comprehensive income as part of other income when the Group's right to receive payments is established.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in other comprehensive income – is removed from equity and recognized in the statement of profit or loss. Impairment losses recognized in the statement of profit or loss and other comprehensive income on equity instruments are not reversed through the profit or loss.

Financial liabilities

The Group classifies its financial liabilities into the following measurement categories: (a) held for trading which also includes financial derivatives and (b) other financial liabilities. Liabilities held for trading are carried at fair value with changes in value recognized in the consolidated statement of profit or loss and other comprehensive income in the period in which they arise. Other financial liabilities are carried at amortised cost.

Derecognition of financial assets

The Group derecognizes financial assets when (i) the assets are redeemed or the rights to cash flows from the assets have otherwise expired or (ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Group has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Derecognition of financial liabilities

The Group derecognizes financial liability when the obligation under the liability is discharged, 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 the derecognition of the original liability and the recognition of a new liability, such that the difference in the respective carrying amounts, together with any costs or fees incurred is recognized in the statement of profit or loss.

Financial guarantee contracts

Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognized initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the reporting date and the amount recognized less cumulative amortisation.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Derivative financial instruments and hedge accounting

Oil and Gas derivative financial instruments, including paper and physical contracts, are initially measured at fair value through profit or loss as well as subsequent changes in fair value. Fair value is defined as the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial assets or financial liabilities at fair value through profit or loss includes financial assets or financial liabilities held for trading that do not meet the hedge accounting criteria as defined by IAS 39 *Financial Instruments: Recognition and Measurement* and derivatives (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument) within the scope of IAS 39.

Financial instruments are differentiated as quoted in an active market and when there is no active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. If no active market, fair value has to be established using valuation techniques, including:

- Recent transaction prices;
- The current fair value of similar instruments;
- Discounted cash flow analysis;
- Option pricing models (e.g. Black & Scholes model).

Current market conditions, credit and liquidity risk are also considered by the Group in the determination of fair value.

For the purpose of hedge accounting, hedges are classified as:

- Fair value hedges when hedging the exposure to changes of a recognized asset or liability or an unrecognized firm commitment.
- Cash flow hedges when hedging the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction or the foreign currency risk in an unrecognized firm commitment.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of changes in the hedging instrument's fair value in offsetting the exposure to changes in the hedged item's fair value. Such hedges are expected to be highly effective in achieving offsetting changes in fair value and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Fair value hedges

When hedges meet the strict criteria for hedge accounting and an unrecognized firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognized as an asset or liability with a corresponding gain or loss recognized in the income statement.

Cash flow hedges

The effective portion of the gain or loss on the hedging instrument is recognized in OCI in the cash flow hedge reserve, while any ineffective portion is recognized immediately in the statement of profit or loss as other operating expenses. Amounts recognized as OCI are transferred to profit or loss when the hedged transaction affects profit or loss, such as when the hedged financial income or financial expense is recognized or when the forecast sale or expense occurs.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Trade and other receivables

Trade and other receivables are carried at amortised cost using the effective interest rate method. The Group first assesses 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 risk 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, recognized are not included in a collective assessment of impairment.

A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of provision is recognized in profit or loss. The primary factors that the Group considers when determining whether a receivable is impaired is its overdue status and realisability or related collateral, if any.

The following other principal criteria are also used to determine whether there is an objective evidence that an impairment loss has occurred:

- ▶ the counterparty experiences a significant financial difficulty as evidenced by its financial information that the Group obtains;
- ▶ the counterparty considers bankruptcy or a financial reorganisation;
- ▶ there is an adverse change in the payment status of the counterparty as a result of changes in the national or local economic conditions that impact the counterparty;
- ▶ the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

Trade and other receivables are derecognized upon cash receipts from customers and borrowers or other similar settlements.

Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less.

Restricted cash

Restricted cash is presented separately from cash and cash equivalents. Restricted balances are excluded from cash and cash equivalents for the purposes of cash flow statement.

Trade payables

Trade payables are accrued when the counterparty performed its obligations under the contract. Trade payables are recognized initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

Borrowings

All borrowings are initially recognized at fair value of the proceeds received net of issue costs associated with the borrowing. Borrowings are carried at amortised cost using the effective interest rate method.

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Property, plant and equipment

The Group elected to measure property, plant and equipment at the date of transition to IFRS (1 January 2007) at their fair value and use that fair value as their deemed cost at that date. Fair value was determined by reference to market-based evidence and by using the depreciated replacement cost method. Subsequent to transition to IFRS, property, plant and equipment are stated at cost as described below, less accumulated depreciation and provision for impairment, where required.

The initial cost of an asset purchased after 1 January 2007 comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of decommissioning obligation, if any, and, for qualifying assets, borrowing costs. The assets held under finance lease are also included within property, plant and equipment. Non-recoverable value-added tax related with acquisition of property, plant and equipment is capitalized by the Group. Non-recoverable value-added tax related with operational activities is charged to profit or loss.

Exploration and evaluation costs

Property leasehold acquisition costs are capitalised until the determination of reserves is evaluated. If a commercial discovery has not been achieved, these costs are charged to expense. Capitalisation is made within property, plant and equipment or intangible assets according to the nature of the expenditure.

The Group accounts for exploration and evaluation activities, capitalizing exploration and evaluation costs until such time as the economic viability of producing the underlying resources is determined.

Exploration and evaluation costs related to resources determined to be not economically viable are expensed through operating expenses in the consolidated statement of profit or loss and other comprehensive income.

Development tangible and intangible assets

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of commercially proven development wells is capitalised within tangible and intangible assets according to nature. When development is completed on a specific field, it is transferred to production assets (oil and gas properties).

The present value of the estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, are recognized when the obligation is incurred and are included within the carrying value of property, plant and equipment, subject to depletion using unit-of-production method.

All minor repair and maintenance costs are expensed as incurred. Cost of replacing major parts or components of property, plant and equipment items are capitalized and the replaced part is retired.

At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's or cash generating unit's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss, if any, is recognized in the statement of profit or loss and other comprehensive income. An impairment loss recognized for an asset or cash generating unit in prior years is reversed if there are indicators that impairment loss may no longer exist or may have decreased.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. Gains and losses are recognized in profit or loss.

Depreciation

Property, plant and equipment related to oil and natural gas properties are depreciated using a unit-of-production method.

Depreciation of oil and gas assets is computed on a field-by-field basis over proved developed reserves or over total proved reserves, as appropriate. Shared oil and gas properties and equipment (e.g. internal delivery systems, processing units, etc.) are depleted over total proved reserves.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Depreciation (continued)

Land is not depreciated. Property, plant and equipment other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Assets under construction are not depreciated.

The estimated useful lives of the Group's property, plant and equipment (other than oil and gas properties) are as follows:

Buildings and constructions	12 to 40 years
Plant and machinery	3 to 50 years
Vessels	25 years

The expected useful lives of property, plant and equipment are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life unless scrap value is significant. The assets' residual values are reviewed, and adjusted if appropriate, at each reporting date.

Operating leases

Where the Group is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the lease term.

The lease term is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

When assets are leased out under an operating lease, the lease payments receivable are recognized as rental income on a straight-line basis over the lease term.

Goodwill

Goodwill is initially measured at cost being (the excess of the aggregate of the consideration transferred and the amount recognized for non-controlling interests) over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss. After initial recognition, goodwill is measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Intangible assets

Intangible assets are stated at cost, less accumulated amortization and accumulated impairment losses. Intangible assets include rights and computer software, patents, licences, customer relationships, trade name, water rights and development projects.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Intangible assets (continued)

The useful lives of intangible assets are assessed as either finite or indefinite. Intangible assets with finite lives are amortised on a straight-line basis over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognized in the statement of profit or loss and other comprehensive income in the expense category consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortised, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

(a) Rights and computer software

Software is carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method over the estimated useful lives of such assets. Land property rights consist of the rights over the dam, factory site, port site, site development, site and the water transmission line. Land property rights obtained at the acquisition of Petkim Petrokimya Holding A.Ş. ("Petkim") (Note 16) were initially recognized at their fair values in accordance with IFRS 3 as at 30 May 2008 and amortised over their remaining useful lives commencing from the date of acquisition, except for the water transmission line which is not amortised as it is deemed to have an indefinite useful life.

(b) Customer relationships

Customer relationships acquired as part of net assets of Petkim were initially recognized at their fair values in accordance with IFRS 3 as at 30 May 2008 and amortised over their remaining useful lives of 22 years commencing from the date of the acquisition (Note 16).

Customer relationships acquired as part of net assets of SOCAR Switzerland were initially recognized at their fair values in accordance with IFRS 3 as at 30 June 2012 and amortised over their remaining useful lives commencing from the date of acquisition. The estimated useful life of retail card end customers is 18 years, retail distribution network and fuel customers are 30 years.

(c) Petkim trade name

Petkim trade name acquired at the Petkim acquisition was initially recognized at its fair value in accordance with IFRS 3 as at 30 May 2008. Petkim trade name is not amortised as it is deemed to have an indefinite useful life (Note 16).

(d) Water rights

Water rights acquired with the Petkim acquisition were initially recognized at their fair value in accordance with IFRS 3 as at 30 May 2008 and amortised over their remaining useful lives of 47 years commencing from the date of the acquisition (Note 16).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Intangible assets (continued)

(e) Development projects

Development projects (design and testing of new or improved products) acquired with the Petkim acquisition were initially recognized at their fair value in accordance with IFRS 3 as of 30 May 2008 and amortised on a straight-line basis over their remaining useful lives of 5 years commencing from the date of the acquisition. Cost incurred on development projects (relating to the design and testing of new or improved products) are recognized as intangible assets when it is probable that the project will be operational considering its commercial and technological feasibility, and only if the cost can be measured reliably. Other expenditures on research and development activities are recognized as an expense in the period in which they incurred. When there is an impairment, the carrying values of the intangible assets are written down to their recoverable amounts. Intangible assets with indefinite useful lives are not amortized, however are tested for impairment annually.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

Corporate income taxes

Corporate income taxes have been provided for in the consolidated financial statements in accordance with the applicable legislation enacted or substantively enacted by the reporting date. The income tax charge comprises current tax and deferred tax and is recognized on the profit or loss unless it relates to transactions that are recognized, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

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

Deferred tax relating to items outside profit or loss is recognized either in OCI or directly in equity.

Deferred income taxes are provided in full on temporary differences arising on recognition and subsequent measurement of provision for asset retirement obligation and related adjustments to cost of property, plant and equipment.

Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is assigned by the weighted average method. Cost comprises direct purchase costs, cost of production, transportation and manufacturing expenses (based on normal operating capacity).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Government grants

Grants from the Government are recognized at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions. Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred income and are credited to profit or loss on a straight line basis over the expected lives of the related assets.

When the grant relates to an expense item, it is recognized as income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed.

Asset retirement obligations

Liabilities for asset retirement obligation costs are recognized when the Group has an obligation to dismantle and remove a facility or an item of plant and to restore the site on which it is located, and when a reasonable estimate of that liability can be made. Where an obligation exists for a new facility, such as oil and natural gas production or transportation facilities, this will be on construction or installation. An obligation for asset retirement may also crystallize during the period of operation of a facility through a change in legislation. The amount recognized is the present value of the estimated future expenditure determined in accordance with local conditions and requirements.

The cost of property, plant and equipment is also adjusted for amounts of estimated liabilities for asset retirement obligations.

Any change in the present value of the obligation resulting from changes in estimates of the amounts or timing of future expenditures is reflected as an adjustment to the provision and the corresponding capitalized costs within property, plant and equipment. Changes in estimates of the amounts or timing of future expenditures to dismantle and remove fully depreciated plant or facility is recognized in the statement of profit or loss and other comprehensive income. Changes in the present value of the obligation resulting from unwinding of the discount are recognized as finance costs in the statement of profit or loss and other comprehensive income.

Provisions for liabilities and charges

Provisions for liabilities and charges are liabilities of uncertain timing or amount. They are accrued when the Group has a present legal or constructive obligation as a result of past events, 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 the obligation can be made. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

Distribution to the Government

Distribution to the Government represent cash distributions or financing which the Group may be required to make to the state budget, various government agencies and projects administered by the Government based on the particular decisions of the Government.

Such distributions are recorded as a reduction of equity. Distributions in the form of transfers of non-monetary assets are recognized at the carrying value of transferred assets.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Contributions by the Government

Contributions by the Government are made in the form of cash contributions, transfer of other state-owned entities or transfer of all or part of the Government's share in other entities. Transfer of the state-owned entities to the Group is recognized as contribution through equity statement in the amount being the fair value of the transferred entity (in case of transfer by the Government of its share in other entities – the transferred share in the fair value of the respective entity).

Value-added tax

The tax authorities permit the settlement of sales and purchases value-added tax ("VAT") on a net basis.

VAT payable

VAT payable represents VAT related to sales that is payable to tax authorities upon recognition of sales to customers, net of VAT on purchases which have been settled at the reporting date. VAT related to sales which have not been settled at the reporting date (VAT deferral) is also included in VAT payable. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT where applicable. The related VAT deferred liability is maintained until the debtor is written off for tax purposes.

VAT recoverable

VAT recoverable relates to purchases which have not been settled at the reporting date. VAT recoverable is reclaimable against VAT on sales upon payment for the purchases.

In accordance with ACG and Shah Deniz PSA provisions, AzACG and AzSD are charged with zero per cent VAT effective in the Azerbaijan Republic for a contractor party under the respective PSAs according to a VAT certification issued by tax authorities and effective until 19 September 2019 and 3 June 2026, respectively.

Revenue recognition

Revenue comprises the fair value of consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of VAT, returns, discounts, and other sales-based taxes, if any, after eliminating sales within the Group.

Revenues from sales of crude oil are recognized at the point of transfer of risks and rewards of ownership of the crude oil, normally when the oil is loaded into the oil tanker or other transportation facilities. Revenues from sales of petroleum products are recognized at the point of transfer of risks and rewards of ownership of the petroleum products, normally when the products are shipped. Revenue from sales of natural gas are recorded on the basis of regular meter readings (monitored on a monthly basis) and estimates of customer usage from the last meter reading to the end of the reporting period. Natural gas prices and gas transportation tariffs to the final consumers in the Azerbaijan Republic are established by the Tariff Council of the Azerbaijan Republic.

Revenues from sales of other goods are recognized at the point of transfer of risks and rewards of ownership of the goods.

Sales of services are recognized in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Interest income is recognized on a time-proportion basis using the effective interest rate method.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Overlift/underlift of crude oil

Overlift or underlift of crude oil occurs when the volume of oil lifted by a partner in a joint operation differs from its participating interest in the production. Underlift is recognized as a sale of crude oil at the point of lifting by the underlifter to the overlifter. Overlift is recognized as a purchase of oil by the overlifter from the underlifter. The extent of underlift is reflected by the Group as an asset in the statement of financial position, and the extent of overlift is reflected as a liability. The initial measurement of the overlift liability or underlift asset is at the market price of crude oil at the date of lifting. Subsequent measurement of overlift/underlift liabilities and assets depends on the settlement terms of the related operating agreements.

If such terms allow for a cash settlement of the overlift/underlift balances between the parties, the balances are remeasured at fair value at reporting dates subsequent to initial recognition. The overlift/underlift balances that are settled through delivery of physical quantities of crude oil are measured at the lower of carrying amount and fair value at reporting dates subsequent to initial recognition.

Employee benefits

Wages, salaries, contributions to the Social Protection Fund of the Azerbaijan Republic, paid annual leave and sick leave, bonuses, and non-monetary benefits (e.g. health services and kindergarten services) are accrued in the year in which the associated services are rendered by the employees of the Group.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision maker. Segments whose revenue, result or assets are ten per cent or more of all the segments are reported separately.

Related parties

Related parties are defined in IAS 24 *Related Party Disclosures*.

Governmental economic and social policies affect the Group's financial position, results of operations and cash flows. The Government imposed an obligation on the Group to provide an uninterrupted supply of oil and gas to customers in the Azerbaijan Republic at government controlled prices. Transactions with the state include taxes which are detailed in Note 21.

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.

It is the nature of transactions with related parties that they cannot be presumed to be carried out on an arm's length basis.

Carried interest arrangements

A carried interest arrangement where the Group participate as carried party is an agreement under which the carrying party agrees to pay for a portion or all of the pre-production costs of the carried party on a project in which both parties own participating interest. If the project is unsuccessful then the carrying party will not be reimbursed for the costs that it has incurred on behalf of the carried party. If the project is successful then the carrying party will be reimbursed either in cash out of proceeds of the share of production attributable to the carried party, or by receiving a disproportionately high share of the production until the carried costs are fully recovered.

Depending on the terms of the carried interest agreements the Group recognizes them either as financing-type arrangement or purchase/sale-type arrangement.

The finance-type arrangements presume that carrying party provides funding to the carried party and receives a lender's return on the funds provided, while the right to additional production acts as a security that underpins the arrangement.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

2 Basis of preparation and significant accounting policies (continued)

Carried interest arrangements (continued)

In the purchase/sale-type arrangement, the carried party effectively sells an interest or a partial interest in a project to the carrying party. The carrying party will be required to fund the project in exchange for an increased share of any proceeds if the project succeeds, while the carried party retains a much reduced share of any proceeds. The Group does not have any purchase/sale-type arrangement recognized in these consolidated financial statements.

During exploration stage of projects when the outcome of projects and probability of the carrying party to recover costs incurred on behalf of the carried party are not certain the Group does not recognize any carry related transactions and balances in the consolidated financial statements.

Step-acquisition of subsidiary that is not a business

Step-acquisition of subsidiary which has been previously accounted as investment in associates is recognized in the amount being the carrying value under the equity method related to the original interest in associate plus cost of additional investments made by the Group in order to obtain control over associate ("deemed cost").

Upon obtaining of the control over associate it becomes subsidiary of the Group and the "deemed" cost is allocated to the individual identifiable assets and liabilities of the subsidiary as following:

- ▶ monetary assets and monetary liabilities are recognized at their fair value;
- ▶ the amount of "deemed" cost remained after deduction of the fair value of monetary assets and monetary liabilities is allocated to non-monetary assets and non-monetary liabilities on the basis of their fair value at the date of acquisition.

Non-current assets held for sale or for distribution to equity holders of the parent and discontinued operations

The Group classifies non-current assets and disposal groups as held for sale or for distribution to equity holders of the parent if their carrying amounts will be recovered principally through a sale or distribution rather than through continuing use. Such non-current assets and disposal groups classified as held for sale or as held for distribution are measured at their carrying amount.

The criteria for held for distribution classification is regarded as met only when the distribution is highly probable and the asset or disposal group is available for immediate distribution in its present condition. Actions required to complete the distribution should indicate that it is unlikely that significant changes to the distribution will be made or that the decision to distribution will be withdrawn. Management must be committed to the distribution expected within one year from the date of the classification. Similar considerations apply to assets or a disposal group held for sale.

Property, plant and equipment and intangible assets are not depreciated or amortised once classified as held for sale or as held for distribution. Assets and liabilities classified as held for sale or for distribution are presented separately as current items in the statement of financial position.

A disposal group qualifies as discontinued operation if it is:

- ▶ Represents a separate major line of business or geographical area of operations;
- ▶ Is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- ▶ Is a subsidiary acquired exclusively with a view to resale.

Discontinued operations are excluded from the results of continuing operations and are presented as a single amount as profit or loss after tax from discontinued operations in the statement of profit or loss. All notes to the consolidated financial statements include amounts for continuing operations.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

3 Critical accounting estimates and judgments

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates and judgments are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgments, apart from those involving estimations, in the process of applying the accounting policies. Judgments that have the most significant effect on the amounts recognized in these consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities at reporting date include:

Estimation of oil and gas reserves

Oil and gas reserves are key elements in the Group's investment decision-making process. They are also an important element of testing for impairment. Changes in proved oil and gas reserves, particularly proved developed reserves, will affect unit-of-production depreciation charges in the statement of profit or loss and other comprehensive income.

Proved oil and gas reserves are the estimated quantities of crude oil and natural gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e. prices and costs as of the date the estimate is made. Proved developed reserves are reserves that can be expected to be recovered through existing wells with existing equipment and operating methods. Estimates of oil and gas reserves are inherently imprecise, require the application of judgment and are subject to future revision.

Accordingly, financial and accounting measures (such as depletion and amortization charges and provision for asset retirement obligations) that are based on proved developed or proved reserves are also subject to change. Proved reserves are estimated by reference to available reservoir and well information. All proved reserves estimates are subject to revision, either upward or downward, based on new information, such as from drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans. In general, changes in the technical maturity or hydrocarbon reserves resulting from new information becoming available from development plans. In general, changes in the technical maturity of hydrocarbon reserves resulting from new information becoming available from development and production activities have tended to be the most significant cause of annual revisions.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are developed and being depleted. As a field goes into production, the amount of proved reserves will be subject to future revision once additional information becomes available through, for example, the drilling of additional wells or the observation of long-term reservoir performance under producing conditions. As those fields are further developed, new information may lead to revisions.

Proved reserves of the SOCAR as of 1 January 2017 were based on reports prepared by independent reservoir engineers in accordance with Petroleum Resources Management System rules.

Asset retirement obligations

As further discussed in Note 22, management makes provision for the future costs of decommissioning oil and gas production and storage facilities, pipelines and related support equipment and site restoration based on the estimates of future cost and economic lives of those assets. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future. Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

3 Critical accounting estimates and judgments (continued)

Asset retirement obligations (continued)

The Group assesses its asset retirement obligation liabilities in accordance with the guidelines of International Financial Reporting Interpretations Committee ("IFRIC") 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the reporting date based on current applicable legislation and regulations, and is also subject to changes because of modifications, revisions and changes in laws and regulations and respective interpretations thereof. Governmental authorities are continually considering applicable regulations and their enforcement. Consequently, the Group's ultimate asset retirement liabilities may differ from the recorded amounts. As a result of the subjectivity of these provisions there is uncertainty regarding both the amount and estimated timing of incurring such costs. Estimated liability of dismantling oil and gas production and storage facilities, including abandonment and site restoration costs, amounted to AZN 968 at 31 December 2016 (2015: AZN 748). Changes in any of these conditions may result in adjustments to provisions recorded by the Group.

Management determines discount rates used for discounting abandonment and site restoration costs as a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. The discount rate used as at 31 December 2016 was in range of 5.59-8.24 per cent (2015: 5.95-8.28 per cent). Management believes that this discount rate appropriately reflects all risks and uncertainties pertaining to oil and gas exploration, evaluation, development and distribution in Azerbaijan as of the reporting date.

If the estimated discount rate used in the calculation had been 1 per cent higher/lower than management's estimate, the carrying amount of the provision would have been AZN 124 lower / AZN 185 higher, respectively.

Environmental obligations

As further discussed in Note 23, the Group records a provision in respect of estimated costs of remediation of the damage historically caused to the natural environment primarily in the Absheron area both by the activities of the Group and its legacy operations in periods preceding the formation of the Group.

The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the reporting date based on current applicable legislation and regulations, and is also subject to changes because of modifications, revisions and changes in laws and regulations and respective interpretations thereof. Governmental authorities are continually considering applicable regulations and their enforcement. Consequently, the Group's ultimate liability for environmental remediation may differ from the recorded amounts. As a result of the subjectivity of these provisions there is uncertainty regarding both the amount and estimated timing of incurring such costs. Estimated liability for environmental remediation as of 31 December 2016 amounted to AZN 76 (2015: AZN 88). Changes in any of these conditions may result in adjustments to provisions recorded by the Group.

Management determines discount rate used for discounting environmental remediation costs as pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability as of the reporting date. The discount rate used as at 31 December 2016 was 8.73 per cent (2015: 8.59 per cent). Management believes that this discount rate appropriately reflects all risks and uncertainties pertaining to oil and gas exploration, evaluation and development industry in Azerbaijan. Changes in any of these conditions may result in adjustments to provisions recorded by the Group. If the estimated discount rate used in the calculation had been 1 per cent higher/lower than management's estimate, the carrying amount of the provision would have been AZN 1 lower / AZN 1 higher, respectively.

Useful lives of property, plant and equipment and intangible assets

Management determines the estimated useful lives and related depreciation and amortisation charges for its property, plant and equipment and intangible assets. This estimate is based on projected period over which the Group expects to consume economic benefits from the asset. Management increases the depreciation charge where useful lives are less than previously estimated lives, or it write-offs or write-downs technically obsolete assets that have been abandoned or sold. The useful lives are reviewed at least at each financial year-end. Changes in any of the above conditions or estimates may result in adjustments to future depreciation rates.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

3 Critical accounting estimates and judgments (continued)

Deferred income tax assets recognition

The net deferred tax assets represent income taxes recoverable through future deductions from taxable profits and is recorded on the statement of financial position. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimation based on last three years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

Impairment of non-financial assets

Management assesses whether there are any indicators of possible impairment of all non-financial assets at each reporting date based on events or circumstances that indicate the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves. Goodwill and other indefinite life intangibles are tested for impairment annually and at other times when impairment indicators exist. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable.

When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows. In 2016, as the result of underperformance of some Cash Generating Units (CGUs) the Group carried out a review of the recoverable amounts of those CGUs resulting in impairment charge amounting to AZN 322 (2015: AZN 254). These assets are used in the Group's oil and gas, construction and refinery segments. In assessing whether impairment is required in the carrying value of a potentially impaired asset, its carrying value is compared with its recoverable amount.

The recoverable amount is the higher of the asset's fair value less costs to sell and value-in-use. Given the nature of the Group's activities, information on the fair value of an asset is usually difficult to obtain unless negotiations with potential purchasers are taking place.

Consequently, unless indicated otherwise, the recoverable amount used in assessing the impairment charges described below is value-in-use. The Group generally estimates value-in-use using a discounted cash flow model from financial budgets approved by management.

Key assumptions used in value-in-use calculations

The calculation of value-in-use for property, plant and equipment fields is most sensitive to the following assumptions:

Production volumes

Estimated production volumes of SOCAR operated fields are based on detailed data for the fields and take into account development plans for the fields agreed by management as part of the long-term planning process. It is estimated that, if all production were to be reduced by 10 per cent for the whole of the next 20 years, this would result in additional impairment charge of AZN 192.

Operating expenses

Operating expenses are based on previous year's actual figures. These are increased over the budget period for anticipated inflation rate.

Gross margins

Gross margins are based on previous year's actual figures. These are increased over the budget period for anticipated inflation rate.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

3 Critical accounting estimates and judgments (continued)

Impairment of non-financial assets (continued)

Capital expenditures

Capital expenditures necessary to maintain estimated production volumes are based on long-term development plans for particular oil field.

Crude oil price

Forecast commodity prices are publicly available.

Natural gas price

Natural gas prices are calculated based on the long-term sales contracts provisions and are either fixed or depend on crude oil prices and other inputs.

Discount rate

The pre-tax discount rate applied to the cash flow projections was in range of 13.01-19.29 per cent for different CGUs (2015: 13.70-16.49 per cent). The discount rate calculation is based on the specific circumstances of the Group and its operating segments and derived from its weighted average cost of capital (WACC). In calculating WACC the cost of equity was estimated using peer group data and the cost of debt is based on interest bearing borrowings, the Group is obliged to service. Specific risks are incorporated by applying individual beta factors, market risk and size of the Group. The beta factors are evaluated annually based on publicly available market data. If the estimated WACC used in the calculation had been 1 per cent higher management's estimate, no additional impairment loss would be recognized.

Inflation rate estimates

Rates used are Oxford Economics and Economic Intelligence Unit forecasts.

Excise taxes, road taxes and export duties

Excise taxes, road taxes and export duties on oil and gas and petroleum products are an important factor for oil and gas properties and equipment and are forecasted based on enacted tax and duty rates.

Impairment provision for trade receivables

The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will suffer bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, amount receivable is written off against associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

3 Critical accounting estimates and judgments (continued)

Disability provision

As further discussed in Note 23, the Group records a provision in accordance with Azerbaijan Labour Code and has an obligation to pay compensation for employees damaged at work. Estimated liability for disability remediation as of 31 December 2016 amounted to AZN 117 (2015: AZN 99).

Management determines discount rate used for discounting disability provision as pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability as of the reporting date. The discount rate used as at 31 December 2016 was 8.13 per cent (2015: 8.29 per cent). In addition, the Group estimated a life expectancy as 71 and 76 for men and women, respectively for the purpose of calculation of the lifetime payments to injured employees. Changes in any of these conditions may result in adjustments to provisions recorded by the Group.

If the estimated discount rate used in the calculation had been 1 per cent higher/lower than management's estimate, the carrying amount of the provision would have been AZN 7 lower / AZN 8 higher, respectively.

4 Adoption of new or revised standards and interpretations and new accounting pronouncements

The accounting policies adopted are consistent with those of the previous financial year, except for the following amendment to IFRS effective beginning on or after 1 January 2016:

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 OCI. The standard requires disclosure of the nature of, and risks associated with, the entity's rate-regulation and the effects of that rate-regulation on its financial statements. Since the Group is an existing IFRS preparer and is not involved in any rate-regulated activities, this standard does not apply.

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 *Business Combinations* principles for business combination accounting. The amendments also clarify that a previously held interest in a joint operation is not re-measured on the acquisition of an additional interest in the same joint operation if 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 applied prospectively. These amendments do not have any impact on the Group as there has been no interest acquired in a joint operation during the period.

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

The amendments clarify the principle in IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is a 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 applied prospectively and do not have any impact on the Group, given that it has not used a revenue-based method to depreciate its non-current assets. In addition, non-refundable purchase taxes amount should be capitalized as part of the cost of the asset.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

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 *Agriculture*. 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 applied retrospectively and do not have any impact on the Group as it does not have any bearer plants.

Amendments to IAS 27: Equity Method in Separate Financial Statements

The amendments 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 their separate financial statements have to apply that change retrospectively. These amendments do not have any impact on the Group's consolidated financial statements.

Annual improvements 2012-2014 cycle

These improvements include:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

Assets (or disposal groups) are generally disposed of either through sale or distribution to owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered 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. This amendment is applied prospectively.

IFRS 7 Financial Instruments: Disclosures

(i) Servicing contracts

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 the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be made retrospectively. However, the required disclosures need not to be provided for any period beginning before the annual period in which the entity first applies the amendments.

(ii) Applicability of the amendments to IFRS 7 to condensed interim financial statements

The amendment clarifies that the offsetting disclosure requirements do not apply to condensed interim financial statements, unless such disclosures provide a significant update to the information reported in the most recent annual report. This amendment is applied retrospectively.

IAS 19 Employee Benefits

The amendment 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. This amendment is applied prospectively.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Annual improvements 2012-2014 cycle (continued)

IAS 34 Interim Financial Reporting

The amendment clarifies 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 interim financial report (e.g., in the management commentary or risk report). 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. This amendment is applied retrospectively.

These amendments do not have any impact on the Group.

Amendments to IAS 1 Presentation of Financial Statements: Disclosure Initiative

The amendments to IAS 1 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 do not 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 *Consolidated Financial Statements*. 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 *Investments in Associates and Joint Ventures* 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 are applied retrospectively and do not have any impact on the Group as the Group does not apply the consolidation exception.

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* that replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for the financial instruments project: 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. Except for hedge accounting, retrospective application is required, but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Standards issued but not yet effective (continued)

(a) Classification and measurement

The Group does not expect a significant impact on its balance sheet or equity on applying the classification and measurement requirements of IFRS 9. It expects to continue measuring at fair value all financial assets currently held at fair value. Quoted equity shares currently held as available-for-sale with gains and losses recorded in OCI will be measured at fair value through profit or loss instead, which will increase volatility in recorded profit or loss. The AFS reserve currently presented as accumulated OCI will be reclassified to opening retained earnings. Debt securities are expected to be measured at fair value through OCI under IFRS 9 as the Group expects not only to hold the assets to collect contractual cash flows, but also to sell a significant amount on a relatively frequent basis. The equity shares in non-listed companies are intended to be held for the foreseeable future. The Group expects to apply the option to present fair value changes in OCI, and, therefore, believes the application of IFRS 9 would not have a significant impact.

If the Group were not to apply that option, the shares would be held at fair value through profit or loss, which would increase the volatility of loans as well as trade receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. Thus, the Group expects that these will continue to be measured at amortised cost under IFRS 9. However, the Group will analyse the contractual cash flow characteristics of those instruments in more detail before concluding whether all those instruments meet the criteria for amortised cost measurement under IFRS 9.

(b) Impairment

IFRS 9 requires the Group to record expected credit losses on all of its debt securities, loans and trade receivables, either on a 12-month or lifetime basis. The Group expects to apply the simplified approach and record lifetime expected losses on all trade receivables. The Group expects a significant impact on its equity due to the unsecured nature of its loans and receivables, 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.

(c) Hedge accounting

The Group believes that all existing hedge relationships that are currently designated in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of applying IFRS 9. The Group will assess possible changes related to the accounting for the time value of options, forward points or the currency basis spread in more detail in the future.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and establishes a five-step model to account for revenue arising from contracts with customers. 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 new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018. Early adoption is permitted. The Group plans to adopt the new standard on the required effective date using the full retrospective method. During 2016, the Group performed a preliminary assessment of IFRS 15, which is subject to changes arising from a more detailed ongoing analysis. Furthermore, the Group is considering the clarifications issued by the IASB in April 2016 and will monitor any further developments.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Standards issued but not yet effective (continued)

(a) Presentation and disclosure requirements

IFRS 15 provides presentation and disclosure requirements, which are more detailed than under current IFRS. The presentation requirements represent a significant change from current practice and significantly increases the volume of disclosures required in Group's consolidated financial statements. Many of the disclosure requirements in IFRS 15 are completely new. In 2016 the Group developed and started testing of appropriate systems, internal controls, policies and procedures necessary to collect and disclose the required information.

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 conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture, is recognised in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture. The IASB has deferred the effective date of these amendments indefinitely, but an entity that early adopts the amendments must apply them prospectively. The Group will apply these amendments when they become effective.

IAS 7 Disclosure Initiative – Amendments to IAS 7

The amendments to IAS 7 *Statement of Cash Flows* are part of the IASB's *Disclosure Initiative* and require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. These amendments are effective for annual periods beginning on or after 1 January 2017, with early application permitted. Application of the amendments will result in additional disclosures provided by the Group.

IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses – Amendments to IAS 12

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognised in the opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact. These amendments are effective for annual periods beginning on or after 1 January 2017 with early application permitted. If an entity applies the amendments for an earlier period, it must disclose that fact. These amendments are not expected to have any impact on the Group.

IFRS 2 Classification and Measurement of Share-based Payment Transactions – Amendments to IFRS 2

The IASB issued amendments to IFRS 2 *Share-based Payment* that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled. On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted. The Group is assessing the potential effect of the amendments on its consolidated financial statements.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Standards issued but not yet effective (continued)

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement Contains a Lease*, SIC-15 *Operating Leases-Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of ‘low-value’ assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to re-measure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the re-measurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under IFRS 16 is substantially unchanged from today’s accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases. IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17. IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard’s transition provisions permit certain reliefs. In 2017, the Group plans to assess the potential effect of IFRS 16 on its consolidated financial statements.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

The interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it), or on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognizes the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine a date of the transaction for each payment or receipt of advance consideration.

The amendments are effective from 1 January 2018 and may be applied on a fully retrospective basis; prospectively to all assets, expenses and income in its scope that are initially recognised on or after the beginning of the reporting period in which the entity first applies the interpretation; or, the beginning of a prior reporting period presented as comparative information in the financial statements of the reporting period in which the entity first applies the interpretation. The Group intends to adopt the amendments on the effective date, and does not expect the impact of adoption of the interpretation to be material.

IFRIC 23 Uncertainty over Income Tax Treatments

This Interpretation issued in June 2017 clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. In such a circumstance, an entity shall recognise and measure its current or deferred tax asset or liability applying the requirements in IAS 12 based on taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates determined applying this Interpretation. This interpretation is effective for annual reporting periods beginning on or after 1 January 2019.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

4 Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Standards issued but not yet effective (continued)

IAS 40 Transfers of Investment Property – Amendments to IAS 40

The amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use. A mere change in management's intentions for the use of a property does not provide evidence of a change in use. Entities should apply the amendments prospectively to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. An entity should reassess the classification of property held at that date and, if applicable, reclassify property to reflect the conditions that exist at that date. Retrospective application in accordance with IAS 8 is only permitted if that is possible without the use of hindsight. Early application of the amendments is permitted and must be disclosed. These amendments are effective for annual periods beginning on or after 1 January 2018.

5 Segment information

Operating segments are components that engage in business activities that may earn revenues or incur expenses, whose operating results are regularly reviewed by the management of the Group and for which discrete financial information is available.

The Group is organised into business units and subsidiaries based on their products and services and has four reportable segments as follows:

- ▶ Oil and gas – representing extraction of oil and gas products;
- ▶ Refining – representing refining of crude oil and gas condensate;
- ▶ Construction – representing construction of administrative premises and assets for extraction of oil and gas condensate;
- ▶ Sales and distribution – representing transportation and marketing of crude oil, natural gas, oil products and gas condensate.

No operating segments have been aggregated to form the above reportable operating segments.

The Group's segments are strategic business units and subsidiaries that focus on different customers. Management monitors the operating results of its business units and subsidiaries separately for the purpose of making decisions about resource allocation and performance assessment. Transfer prices between operating segments are either on an arm's length basis or non-arm's length basis.

Management evaluates performance of each segment based on profit after tax.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

5 Segment information (continued)

Information about reportable segment profit or loss, assets and liabilities

Segment information for the reportable segments for the year ended 31 December 2016 is set out below:

	Oil and gas	Refining	Construc- tion	Sales and distribu- tion	Unalloca- ted (*)	Elimina- tions (**)	Total
2016							
Revenues							
External customers	1,808	3,069	1,518	45,488	22	–	51,905
Inter-segment	1,896	286	416	16,867	428	(19,893)	–
Total revenue	3,704	3,355	1,934	62,355	450	(19,893)	51,905
Other operating income	(1)	30	401	192	139	(64)	697
Finance income	10	160	1	34	543	(559)	189
Foreign exchange gains/losses (net)	(12)	(106)	(69)	(107)	(689)	(301)	(1,284)
Raw materials and consumables used	(666)	(2,082)	(247)	(60,118)	(55)	18,903	(44,265)
Depreciation of property, plant and equipment	(507)	(147)	(119)	(203)	(78)	40	(1,014)
Wages, salaries and social security costs	(183)	(248)	(271)	(468)	(221)	94	(1,297)
Transportation and vehicle maintenance	(349)	(15)	(116)	(523)	(44)	333	(714)
Repairs and maintenance expenses	(151)	(6)	(121)	(44)	(5)	138	(189)
Impairment of property, plant and equipment	(144)	(37)	(138)	(3)	–	–	(322)
Mining tax	(103)	–	–	–	–	–	(103)
Utilities expense	(13)	(216)	(2)	(75)	(3)	2	(307)
Taxes other than on income	(73)	(10)	(3)	(26)	(66)	–	(178)
Amortization expense	–	(15)	–	(20)	(5)	–	(40)
Impairment of trade and other receivables and other financial assets	(4)	(75)	–	(407)	(7)	–	(493)
Change in other provisions for liabilities and charges	(16)	(11)	(17)	(12)	(15)	–	(71)
Other	(414)	(307)	(500)	(662)	(304)	656	(1,531)
Gains less losses on disposals of property, plant and equipment	47	(3)	(2)	(7)	(69)	–	(34)
Finance cost	(75)	(218)	(23)	(156)	(449)	80	(841)
Social expenses	(9)	(6)	(3)	(7)	(123)	–	(148)
Share of result of joint ventures	(55)	752	34	5	31	–	767
Share of result of associates	–	–	–	190	19	–	209
Income tax expense	(237)	(14)	(182)	(5)	(148)	–	(586)
Net profit/(loss) for the year	749	781	557	(67)	(1,099)	(571)	350

(*) These numbers include unallocated revenues and expenses related to research and development, IT, security and other functions that are not managed at the group level.

(**) Inter-segment revenues and expenses are eliminated on consolidation. Amounts shown as eliminations include intercompany transactions.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

5 Segment information (continued)

Information about reportable segment profit or loss, assets and liabilities (continued)

	Oil and gas	Refining	Construc- tion	Sales and distribu- tion	Unalloca- ted (*)	Elimina- tions (**)	Total
Investments in associates	–	–	–	4,410	32	–	4,442
Investments in joint ventures	333	3,900	218	54	50	–	4,555
Other reportable segment assets	15,930	8,157	2,765	20,730	14,181	(17,753)	44,010
Total reportable segment assets	16,263	12,057	2,983	25,194	14,263	(17,753)	53,007
Other reportable segment liabilities	(7,121)	(5,694)	(1,715)	(21,813)	(11,111)	12,151	(35,303)
Total reportable segment liabilities	(7,121)	(5,694)	(1,715)	(21,813)	(11,111)	12,151	(35,303)
Capital expenditure (***)							
Additions – business units, JV and associates	561	693	44	994	105	(20)	2,377
Additions – subsidiaries	904	974	372	247	10	–	2,507
Total capital expenditures	1,465	1,667	416	1,241	115	(20)	4,884

(*) These numbers include unallocated assets and liabilities related to research and development, IT, security and other functions that are not managed at the group level.

(**) Inter-segment balances are eliminated on consolidation. Amounts shown as eliminations include intercompany balances.

(***) Capital expenditure represents additions to non-current assets other than financial instruments, deferred tax assets and post-employment benefit assets.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

5 Segment information (continued)**Information about reportable segment profit or loss, assets and liabilities (continued)**

Segment information for the reportable segments for the year ended 31 December 2015 is set out below:

	Oil and gas	Refining	Construc- tion	Sales and distribu- tion	Unalloca- ted (*)	Elimina- tions (**)	Total
2015							
Revenues							
External customers	1,616	2,272	1,153	28,004	58	–	33,103
Inter-segment	1,822	325	515	10,219	371	(13,252)	–
Total revenue	3,438	2,597	1,668	38,223	429	(13,252)	33,103
Other operating income	8	44	38	45	65	(39)	161
Finance income	9	34	–	31	1,235	(1,244)	65
Foreign exchange gains/losses (net)	(116)	(222)	(287)	(95)	(2,111)	(103)	(2,934)
Raw materials and consumables used	(607)	(1,650)	(367)	(36,838)	(54)	12,380	(27,136)
Depreciation of property, plant and equipment	(670)	(108)	(74)	(156)	(78)	37	(1,049)
Wages, salaries and social security costs	(168)	(178)	(228)	(333)	(202)	93	(1,016)
Transportation and vehicle maintenance	(323)	(16)	(147)	(66)	(39)	339	(252)
Repairs and maintenance expenses	(167)	(18)	(118)	(59)	(14)	156	(220)
Impairment of property, plant and equipment	(252)	–	–	(2)	–	–	(254)
Mining tax	(110)	–	–	–	–	–	(110)
Utilities expense	(12)	(195)	(2)	(33)	(2)	2	(242)
Taxes other than on income	(54)	(6)	(5)	(21)	(30)	1	(115)
Amortization expense	(1)	(10)	–	(14)	(6)	1	(30)
Impairment of trade and other receivables and other financial assets	–	(3)	–	(37)	2	–	(38)
Change in other provisions for liabilities and charges	(20)	(9)	(7)	(8)	(14)	–	(58)
Other	(328)	(178)	(642)	(263)	(118)	234	(1,295)
Gains less losses on disposals of property, plant and equipment	(6)	(15)	(1)	6	(3)	–	(19)
Finance cost	(64)	(93)	(15)	(85)	(251)	32	(476)
Social expenses	(9)	(7)	(5)	(7)	(115)	–	(143)
Share of result of joint ventures	4	234	21	4	10	–	273
Share of result of associates	–	–	–	197	4	–	201
Income tax expense	(116)	8	(65)	(88)	43	17	(201)
Net profit/(loss) for the year	436	209	(236)	401	(1,249)	(1,346)	(1,785)

(*) These numbers include unallocated revenues and expenses related to research and development, IT, security and other functions that are not managed at the group level.

(**) Inter-segment revenues and expenses are eliminated on consolidation. Amounts shown as eliminations include intercompany transactions.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

5 Segment information (continued)

Information about reportable segment profit or loss, assets and liabilities (continued)

	Oil and gas	Refining	Construc- tion	Sales and distribu- tion	Unalloca- ted (*)	Elimina- tions (**)	Total
Investments in associates	–	–	–	2,818	20	–	2,838
Investments in joint ventures	388	2,472	227	44	40	–	3,171
Other reportable segment assets	13,550	6,849	2,593	13,019	12,826	(14,892)	33,945
Total reportable segment assets	13,938	9,321	2,820	15,881	12,886	(14,892)	39,954
Other reportable segment liabilities	(5,892)	(4,403)	(1,815)	(13,215)	(9,563)	9,582	(25,306)
Total reportable segment liabilities	(5,892)	(4,403)	(1,815)	(13,215)	(9,563)	9,582	(25,306)
Capital expenditure (***)							
Additions – business units, JV and associates	512	681	60	395	1,543	(3)	3,188
Additions – subsidiaries	752	407	114	112	223	–	1,608
Total capital expenditures	1,264	1,088	174	507	1,766	(3)	4,796

(*) These numbers include unallocated revenues and expenses related to research and development, IT, security and other functions that are not managed at the group level.

(**) Inter-segment revenues and expenses are eliminated on consolidation. Amounts shown as eliminations include intercompany transactions.

(***) Capital expenditure represents additions to non-current assets other than financial instruments, deferred tax assets and post-employment benefit assets.

Geographical information

Revenues for each individual country for which the revenues are material are reported separately as follows:

	2016	2015
Switzerland	40,438	23,847
Azerbaijan	5,171	4,629
Turkey	3,479	2,571
UAE	1,156	948
Georgia	1,046	748
Other	615	360
Total consolidated revenues	51,905	33,103

The analysis is based on the country of incorporation of the selling entity.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

5 Segment information (continued)

Geographical information (continued)

Non-current assets other than financial instruments, deferred tax assets, post-employment benefit assets and rights arising under insurance contracts for each individual country for which it is material is reported separately as follows:

	2016	2015
Azerbaijan	20,632	16,806
Turkey	6,949	5,284
UAE	1,803	1,361
Switzerland	856	584
Georgia	526	483
Other	267	258
Total	31,033	24,776

The analysis is based on location of assets.

6 Financial risk management

Financial risk factors

In the ordinary course of business, the Group is exposed to credit, liquidity and market risks. Market risk arises from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial position. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position. Although there are no structured formal management procedures, management of the Group identifies and evaluates financial risks with reference to the current market position.

(i) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to USD. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

The majority of the Group's borrowings and sales as well as receivables from foreign customers are denominated in USD.

The following table demonstrates the sensitivity to a reasonably possible change in the USD, JPY, EUR, TRY, GEL, CHF exchange rates, with all other variables held constant, of the Group's post-tax profit:

2016	Change in rates (+/-)	Effect on post-tax profit
USD/AZN	20.00%/-20.00%	(438)/438
JPY/AZN	2.60%/-2.60%	(4)/4
EUR/AZN	20.00%/-20.00%	(117)/117
TRY/AZN	13.00%/-29.00%	(11)/24
GEL/AZN	2.80%/-1.40%	(1)/1
USD/TRY	10.00%/-10.00%	(182)/182
EUR/TRY	10.00%/-10.00%	(8)/8
USD/GEL	14.00%/-7.00%	(42)/21
EUR/USD	10.00%/-10.00%	4/(4)
USD/CHF	8.00%/-8.00%	(27)/27

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Financial risk factors (continued)

2015	Change in rates (+/-)	Effect on post-tax profit
USD/AZN	60.00%/-15.00%	(2,300)/575
JPY/AZN	47.75%/-7.75%	(61)/10
EUR/AZN	60.00%/-15.00%	12/(3)
TRY/AZN	50.00%/-33.50%	(28)/19
GEL/AZN	45.00%/-4.00%	(75)/7
USD/TRY	10.00%/-10.00%	(142)/142
EUR/TRY	10.00%/-10.00%	2/(2)
USD/GEL	15.00%/-11.00%	(23)/17
EUR/USD	12.50%/-12.50%	3/(3)
USD/CHF	20.00%/-22.00%	(4)/5

Group's exposure to foreign currency changes for all other currencies is not material.

(ii) Commodity price risk

The Group is exposed to certain price risk due to volatility of oil market prices. Due to the risk the Group's management has developed and enacted a risk management strategy regarding oil price risk and its mitigation.

Based on forecasts about oil purchases and sales, the Group hedges the price using futures and sales contracts, options and contracts for difference.

The following sensitivity analysis is based upon derivative price exposures that existed at 31 December 2016, whereby if oil future prices had moved, as illustrated in the table below, with all other variables held constant, post-tax profit after the impact of hedge accounting and equity would have been as follows:

	Change in year-end price	Effect on profit before tax	Effect on equity
2016	5%/(5%)	(106)/106	(106)/106
2015	5%/(5%)	(67)/67	(67)/67

(iii) Interest rate risk

The Group is subject to interest rate risk on financial liabilities and assets with variable interest rates. To mitigate this risk, the Group's management performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In case where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favourable interest rate terms.

Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new debts management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable over the expected period until maturity.

The floating rate for majority of interest bearing liabilities and assets exposes the Group to fluctuation in interest payments and receipts mainly due to changes in LIBOR.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Financial risk factors (continued)

The following table demonstrates the sensitivity to a reasonably possible change in interest rates on loans and borrowings payable and receivable.

Loans and borrowings, net of loans receivable	Increase/ decrease in basis points	Effect on post-tax profit
2016	+60/-8	0.9/0.2
2015	+50/-12	(12.6)/2.8

Credit risk and concentration of credit risk

Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if counterparty defaults on its contractual obligations.

The Group's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, including restricted cash, trade receivables and loans receivable.

The Group's maximum exposure to credit risk is represented by carrying amounts of financial assets and is presented by class of assets as shown in the table below:

	2016	2015
Cash and cash equivalents excluding cash on hand (Note 8)	4,148	4,872
Restricted cash (Note 9)	121	203
Deposits (Note 8)	1,039	143
Trade and other receivables	7,398	4,622
Available-for-sale investments (Note 10)	82	77
Other current financial assets (Note 14)	1,564	611
Other non-current financial assets (Note 14)	578	502
Financial guarantees given (Note 37)	604	354
Total maximum exposure to credit risk	15,534	11,384
Financial guarantees – amounts of guarantees of indebtedness of others (Note 37)	(580)	(628)
Total exposure to credit risk net of guarantees received	14,954	10,756

The Group places its cash with reputable financial institutions in the Azerbaijan Republic. The Group's cash is mainly placed with the International Bank of Azerbaijan ("IBA") which is controlled by the Azerbaijani Government. The balance of cash and cash equivalents and deposit held with the IBA at 31 December 2016 was AZN 1,154 (2015: AZN 2,529). The Group continually monitors the status of the banks where its accounts are maintained.

Trade receivables consist primarily of balances with local and foreign customers, including related parties, for crude oil, oil products and natural gas sold. SOCAR has an obligation to secure uninterrupted supply of crude oil, oil products and natural gas to certain customers under control of the Azerbaijani Government, including such companies as Azerenergy OJSC, Azal CJSC and Azerbaijan State Caspian Shipping Company which operate important public infrastructure facilities in the Azerbaijan Republic. Actual settlement terms applicable to the Group's relationships with these customers are affected to a large extent by the social and economic policies of the Government of the Azerbaijan Republic. The Group's credit risk arising from its trade balance with private sector and other third-party unrelated customers is mitigated by continuous monitoring of their creditworthiness. Management of the Group believes that the Group is not exposed to high credit risk as the impairment provision has already been accrued in the accompanying consolidated financial statements for all debtors which are not expected to be recovered in a future.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Credit risk and concentration of credit risk (continued)

As at 31 December 2016, letters of guarantee and bank guarantees in total amount of AZN 485 (TRY 965 million) (2015: AZN 538 (TRY 1,004 million)) were received from certain domestics and foreign customers of SOCAR Turkey Energy A.S ("STEAS").

The Group categorized its financial assets as follows:

31 December 2016	Standard	Sub-standard	Past due but not impaired	Individually impaired
Cash and cash equivalents excluding cash on hand	2,994	1,154	–	–
Restricted cash (Note 9)	121	–	–	–
Deposits	1,039	–	–	–
Trade and other receivables	5,571	195	1,632	588
Available-for-sale investments (Note 10)	–	82	–	–
Other current financial assets (Note 14)	–	1,564	–	–
Other non-current financial assets (Note 14)	–	578	–	–
Total	9,725	3,573	1,632	588

31 December 2015	Standard	Sub-standard	Past due but not impaired	Individually impaired
Cash and cash equivalents excluding cash on hand	4,872	–	–	–
Restricted cash (Note 9)	203	–	–	–
Deposits	143	–	–	–
Trade and other receivables	3,359	75	1,187	294
Available-for-sale investments (Note 10)	–	77	–	–
Other current financial assets (Note 14)	–	611	–	–
Other non-current financial assets (Note 14)	–	502	–	–
Total	8,577	1,265	1,187	294

Standard grade represents receivables from borrowers having a minimal level of credit risk, normally with a credit rating on or close to sovereign level or very well collateralized. Sub-standard grade represented by receivables from other borrowers with good financial position and good debt service which are neither past due nor impaired.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure 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. In managing liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows.

Prudent liquidity risk management includes maintaining sufficient working capital and the ability to close out market positions. Management monitors rolling forecasts of the Group's liquidity reserve on the basis of expected cash flows.

All of the Group's financial liabilities represent non-derivative financial instruments. The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period from the reporting date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Liquidity risk (continued)

The maturity analysis of financial liabilities as of 31 December 2016 and 2015 is as follows:

At 31 December 2016	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Trade and other financial payables	9,286	–	–	–	9,286
Deferred acquisition consideration payable	–	153	–	–	153
Other current financial liabilities	–	1,052	–	–	1,052
Interest bearing borrowings	5,351	1,566	4,330	5,671	16,918
Other non-current liabilities	–	–	397	–	397
Put option liabilities	–	–	3,469	–	3,469
Financial guarantees given	–	–	604	–	604
Total undiscounted financial liabilities	14,637	2,771	8,800	5,671	31,879

At 31 December 2015	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Trade and other financial payables	5,851	–	–	–	5,851
Deferred acquisition consideration payable	–	133	–	–	133
Other current financial liabilities	–	174	–	–	174
Interest bearing borrowings	2,119	1,187	4,919	4,908	13,133
Other non-current liabilities	–	–	505	16	521
Put option liabilities	–	–	3,240	–	3,240
Financial guarantees given	–	–	354	–	354
Total undiscounted financial liabilities	7,970	1,494	9,018	4,924	23,406

Capital management

The primary objective of the Group's capital management policy is to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain government, investor and creditor confidence to support its business activities.

The Group considers total capital under management to be as follows:

	2016	2015
Total borrowings (Note 20)	14,927	10,911
Total equity attributable to the Group's equity holders	16,447	13,575
Less: cash and cash equivalents (Note 8)	(4,163)	(4,881)
Total capital under management	27,211	19,605

The Group is periodically mandated to contribute to the state budget and finance various projects undertaken by the Government of the Azerbaijan Republic. There were no changes to the Group's approach to capital management during the year.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Fair value of financial instruments

The fair value of the financial assets and liabilities is included at the amount 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 estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. Management has used all available market information in estimating the fair value of financial instruments.

Set out below is a comparison by class of the carrying amounts and fair value of the Group's financial instruments that are carried in the consolidated financial statements.

31 December 2016		
	Carrying amounts	Fair values
Cash and cash equivalents (Note 8)	4,163	4,163
Deposits (Note 8)	1,039	1,039
Restricted cash (Note 9)	121	121
Trade receivables and other receivables	7,398	7,398
Available-for-sale investments (Note 10)	82	82
Other current financial assets (Note 14)	1,564	1,564
Other non-current financial assets (Note 14)	578	553
Total financial assets	14,945	14,920
Trade and other payables (Note 19)	(9,286)	(9,286)
Other current financial liabilities	(1,052)	(1,052)
Short-term borrowings and current portion of long-term borrowings (Note 20)	(6,717)	(6,717)
Long-term borrowings (Note 20)	(8,210)	(8,371)
Deferred acquisition consideration payable	(153)	(153)
Other non-current liabilities	(368)	(336)
Put option liabilities	(2,832)	(2,832)
Total financial liabilities	(28,618)	(28,747)

31 December 2015		
	Carrying amounts	Fair values
Cash and cash equivalents (Note 8)	4,881	4,881
Deposits (Note 8)	143	143
Restricted cash (Note 9)	203	203
Trade receivables and other receivables	4,622	4,622
Available-for-sale investments (Note 10)	77	77
Other current financial assets (Note 14)	611	611
Other non-current financial assets (Note 14)	502	494
Total financial assets	11,039	11,031
Trade and other payables (Note 19)	(5,792)	(5,792)
Other current financial liabilities	(174)	(174)
Short-term borrowings and current portion of long-term borrowings (Note 20)	(3,085)	(3,085)
Long-term borrowings (Note 20)	(7,826)	(7,494)
Deferred acquisition consideration payable	(133)	(133)
Other non-current liabilities	(498)	(498)
Put option liabilities	(2,492)	(2,492)
Total financial liabilities	(20,000)	(19,668)

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Fair value of financial instruments (continued)

The following methods and assumptions were used to estimate the fair values:

- (i) Current financial assets and liabilities approximate their carrying amounts largely due to the current maturities of these instruments;
- (ii) Long-term fixed-rate and variable-rate receivables/borrowings are evaluated by the Group using Level 3 inputs based on parameters such as interest rates, specific country risk factors, individual creditworthiness of customers and the risk characteristics of the financed project.

Fair value hierarchy

The following table provides the fair value measurement hierarchy of the Group's assets and liabilities:

At 31 December 2016, the Group held the following classes of financial instruments measured at fair value:

	Total	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets measured at fair value				
Other current financial assets	445	18	427	–
Investment available for sale	82	82	–	–
Liabilities measured at fair value				
Other current financial liabilities	(1,017)	(539)	(478)	–
Assets for which fair value are disclosed				
Cash and cash equivalents	4,163	4,163	–	–
Restricted cash	121	121	–	–
Deposits	1,039	–	–	1,039
Trade and other receivables	7,398	–	–	7,398
Other current financial assets	1,119	–	–	1,119
Other non-current financial assets	553	–	–	553
Liabilities for which fair values are disclosed				
Trade and other payables	(9,286)	–	–	(9,286)
Other current financial liabilities	(35)	–	–	(35)
Short-term borrowings and current portion of long-term borrowings	(6,717)	–	–	(6,717)
Long-term borrowings	(8,371)	–	–	(8,371)
Deferred acquisition consideration payable	(153)	–	–	(153)
Other non-current liabilities	(336)	–	–	(336)
Put option liabilities	(2,832)	–	–	(2,832)

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

6 Financial risk management (continued)

Fair value hierarchy (continued)

At 31 December 2015, the Group held the following classes of financial instruments measured at fair value:

	Total	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets measured at fair value				
Other current financial assets	280	229	51	–
Investments available for sale	77	77	–	–
Liabilities measured at fair value				
Other current financial liabilities	(161)	–	(161)	–
Assets for which fair value are disclosed				
Cash and cash equivalents	4,881	4,881	–	–
Restricted cash	203	203	–	–
Deposits	143	–	–	143
Trade and other receivables	4,622	–	–	4,622
Other current financial assets	331	–	–	331
Other non-current financial assets	494	–	–	494
Liabilities for which fair values are disclosed				
Trade and other payables	(5,792)	–	–	(5,792)
Other current financial liabilities	(13)	–	–	(13)
Short-term borrowings and current portion of long-term borrowings	(3,085)	–	–	(3,085)
Long-term borrowings	(7,494)	–	–	(7,494)
Deferred acquisition consideration payable	(133)	–	–	(133)
Other non-current liabilities	(480)	–	–	(480)
Put option liabilities	(2,492)	–	–	(2,492)

There were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into or out of Level 3 fair value measurements during 2016 and 2015.

7 Balances and transactions with related parties

Key management compensation

Key management of the Group includes the President of SOCAR and its twelve Vice-Presidents. All of the Group's key management are appointed by the President of the Azerbaijan Republic. Key management individuals are entitled to salaries and benefits of SOCAR in accordance with the approved payroll matrix as well as to compensation for serving as members of the Boards of directors for certain Group companies. During 2016 compensation of key management personnel totalled to AZN 0.717 (2015: AZN 0.535).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

7 Balances and transactions with related parties (continued)

Key management compensation (continued)

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions or had significant balances outstanding are detailed below.

At 31 December 2016, the outstanding balances with related parties were as follows:

	Note	Government and entities under government control	Associates, joint ventures
Gross amount of trade receivables		399	68
Impairment provisions for trade and other receivables		(83)	–
Other receivables		–	86
Other non-current financial assets		–	10
Cash and cash equivalents		1,151	–
Restricted cash		27	–
Deposit		3	–
VAT and other taxes receivable		696	–
Advances received		(164)	–
Advances received for the sale of shares	34	–	(2,897)
Borrowings from IBA (at fixed rates varying from 3 to 4 per cent)		(1,303)	–
Borrowings from the Ministry of Finance of Azerbaijan Republic		(177)	–
Bond payable to Azerbaijan Investment Company ("AIC")		(158)	–
Trade and other payables		(125)	(940)
Taxes payable to State Oil Fund of Azerbaijan Republic ("SOFAZ")	21	(266)	–
Bond payable to SOFAZ		(889)	–
Other payables to SOFAZ		(1,083)	–
Taxes payable		(74)	–

The transactions with related parties for the year ended 31 December 2016 were as follows:

	Note	Government and entities under government control	Associates and joint ventures
Sales of natural gas		338	150
Sales of oil products		347	22
Sales of crude oil		–	4
Service rendered		21	324
Interest income on deposits		1	–
Interest on loans due to related parties		(51)	–
Corporate income tax		(166)	–
Excise tax	28	(423)	–
Price margin tax		(175)	–
Mining tax	29	(103)	–
Other taxes		(337)	–
Utilities costs		(51)	(5)
Other operating expenses		(42)	(12)
Social security deductions		(126)	–
Social expenses		(50)	–
Transportation expenses		(85)	(66)
Ecology service and environmental security		–	(2)
Security expenses		(10)	–
Purchases of PPE and inventory		(7,187)	(744)
Dividends received from joint ventures		–	102
Dividends received from associates		–	88

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

7 Balances and transactions with related parties (continued)

Key management compensation (continued)

At 31 December 2015, the outstanding balances with related parties were as follows:

	Note	Government and entities under government control	Associates, joint ventures
Gross amount of trade receivables		559	52
Impairment provisions for trade and other receivables		(72)	–
Other receivables		–	67
Cash and cash equivalents		2,525	–
Restricted cash		6	–
Deposit		4	–
VAT and other taxes receivable		606	–
Prepayment for corporate income tax		4	–
Advances received		(72)	–
Advances received for the sale of shares	34	–	(2,097)
Borrowings from IBA (at fixed rates varying from 3 to 4 per cent)		(1,095)	–
Bond payable to AIC		(135)	–
Trade and other payables		(104)	(684)
Other non-current liabilities		–	(70)
Taxes payable to SOFAZ	21	(234)	–
Bond payable to SOFAZ		(847)	–
Other payables to SOFAZ		(820)	–
Taxes payable		(118)	–

The transactions with related parties for the year ended 31 December 2015 were as follows:

	Note	Government and entities under government control	Associates and joint ventures
Sales of natural gas		364	148
Sales of oil products		393	58
Service rendered		11	381
Interest on loans due to related parties		(35)	–
Corporate income tax		(214)	–
Excise tax	28	(429)	–
Price margin tax		(130)	–
Mining tax	29	(110)	–
Other taxes		(317)	–
Utilities costs		(49)	(5)
Other operating expenses		(24)	(13)
Social security deductions		(121)	–
Social expenses		(50)	–
Transportation expenses		(78)	(62)
Ecology service and environmental security		–	(1)
Security expenses		(10)	–
Purchases of PPE and inventory		(7,022)	(491)
Dividends received from joint ventures		–	59
Dividends received from associates		–	649

Terms and conditions of transactions with related parties

The sales to and purchases from the Government and entities under government control are made at prices regulated by the Azerbaijani Government. Outstanding balances at the year-end are unsecured and settlement occurs in cash. There have been no guarantees provided for any related party receivables or payables.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

8 Cash and cash equivalents and deposits

	2016	2015
USD denominated bank balances	2,594	3,505
AZN denominated bank balances	718	917
EUR denominated bank balances	378	165
TRY denominated bank balances	249	126
CHF denominated bank balances	137	103
Other denominated bank balances	72	56
Cash on hand	15	9
Total cash and cash equivalents	4,163	4,881

Included in AZN denominated bank balances as at 31 December 2016 is a call deposit of AZN 21. Interest rate on this deposit for the year ended 31 December 2016 equalled 3 per cent.

At 31 December 2015 three call deposits in total amount of AZN 543 placed with local banks. These deposits bear annual interest rates within the range of 70 per cent of USD LIBOR overnight rate published by Reuters - 6 per cent. Call deposits have original maturity of less than three months.

Deposits

At 31 December 2016 term deposits included placements in the total amount of AZN 1,039 with maturity ranging from three months to one year, under fixed contractual interest rates ranging from 2.5 per cent to 6 per cent per annum.

At 31 December 2015 term deposits mainly included placements in the amount of AZN 139 with maturity ranging from three to six months, under fixed contractual interest rates ranging from 1.72 per cent to 2.85 per cent per annum.

All the bank balances and deposits in the amount of AZN 1,039 (31 December 2015: AZN 143) are neither past due nor impaired.

9 Restricted cash

At 31 December 2016 restricted cash was mainly represented by two cash collateral accounts. The Group has restricted cash account in the amount of AZN 66 (USD 37 million) in Deutsche Bank (2015: AZN 58) as a guarantee of minimum return payments payable to GSI according to the Put Option Agreement in relation to 13 percent shares of STEAS. In addition, the Group has account in the amount of AZN 19 (2015: nil) which held as collateral for the letter of credit.

At 31 December 2015 the Group had restricted cash account in Natixis in the amount of AZN 70 (EUR 40 million), which was opened as on-demand performance guarantee for the benefit of Hellenic Republic Assets Development Fund S.A. in accordance with the terms of agreement on acquisition of gas distribution company Desfa and restricted cash in the amount of AZN 40 (USD 26 million) pledged in favour of GSI in accordance with sales-purchase agreement regarding sale of 30 per cent of capital of Petlim Limancılık Ticaret A.Ş., a subsidiary of the Group.

10 Available-for-sale investments

At 31 December 2016 available-for-sale investments were represented by quoted equity instruments in the amount of AZN 82 (2015: AZN 77).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

11 Trade and other receivables

	2016	2015
Trade receivables	7,773	4,727
Less impairment loss provision	(570)	(291)
Total trade receivables	7,203	4,436
VAT recoverable	647	633
Other taxes receivable	81	80
Prepayments	380	553
Receivable for underlift of oil	109	48
Other receivables	216	399
Less impairment loss provision (other receivables)	(18)	(3)
Total trade and other receivables	8,618	6,146

Trade receivables are mainly represented by receivables for crude oil, oil products and natural gas sold to customers of the Group. The Group does not hold any collateral as security, except as described further in this note. At 31 December 2016 trade receivables of AZN 6,806 (2015: AZN 3,611) were denominated in foreign currencies, mainly in USD.

VAT recoverable relates to purchases which have not been settled at the reporting date. VAT recoverable is reclaimable against VAT on sales upon payment for the purchases.

Movements of the provision for impairment of trade and other receivables are as follows:

	2016	2015
At 1 January	294	233
Net change in provision charged to profit and loss	293	33
Translation to presentation currency	1	28
At 31 December	588	294

The impaired receivables mainly relate to overdue debts (in excess of 360 days) for oil, natural gas and oil products supplied to state-owned entities.

An analysis of the age of financial assets that are past due, but not impaired:

	2016	2015
1-30 days overdue	950	473
1-3 months overdue	192	153
Over 3 months overdue	490	560
Total overdue receivables	1,632	1,186

At 31 December 2016 trade receivables of AZN 1,632 (2015: AZN 1,186) were past due. The Group had overdue receivable from Azerenergy OJSC in amount of AZN 254 (2015: AZN 312). The Group is engaged in sales of natural gas and fuel oil to Azerenergy OJSC. Azerenergy OJSC is the biggest power producer and 100 per cent owned by the Government of the Azerbaijan Republic. Management believes that the receivable amount is not impaired and will be recovered in due course. The Group holds guarantee letters and letters of credits in total amount of AZN 3 (2015: AZN 5).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

12 Inventories

	2016	2015
Crude oil	2,134	654
Goods in transit	1,459	447
Finished goods	883	358
Raw materials and spare parts	374	357
Work in progress	97	66
Other	21	21
Total inventories	4,968	1,903

13 Other non-current assets

At 31 December 2016 other non-current assets were mainly represented by long-term prepayments for purchase of property, plant and equipment in the amount of AZN 733 (2015: AZN 318), for vessel hire in the amount of AZN 35 (2015: AZN 85), long-term prepaid expenses in the amount of AZN 28 (2015: AZN 39), long-term VAT receivable in the amount of AZN 62 (2015: AZN 53), long-term receivables for sold oil in the amount of AZN 9 (2015: AZN 14) and other non-current assets.

14 Other financial assets

Current

At 31 December 2016 other current financial assets were mainly represented by short-term loans receivable from third parties in the amount of AZN 16 (2015: AZN 89) and balances relating to margin deposits and financial derivatives in the amount of AZN 1,528 (2015: AZN 507).

Non-current

At 31 December 2016 and 2015 other non-current financial assets mainly comprised of loan receivables from third parties and related parties, long-term deposit and derivative instruments.

At 31 December 2016 carrying value of loan receivables from third parties equalled to AZN 186 (2015: AZN 122), bearing annual interest rate within the range of LIBOR plus 4.5 per cent – 6.75 per cent and payable on a quarterly basis. These loans are maturing during 2016-2021.

At 31 December 2016 the loan with the carrying value of AZN 157 (2015: AZN 122) is secured by certain assets pledged by the borrower. During subsequent period, the Group and the borrower are negotiating the terms for restructuring of this loan.

During 2016, the Group provided loan to its joint venture in the amount of AZN 63 with the interest rate of 4 per cent per annum. The Group has recognized loan receivable at its fair value on the date of acquisition of the receivable. At 31 December 2016 carrying value of this receivable equalled to AZN 63. In addition, the Group had loan receivable from its associate which does not bear interest and at initial recognition fair value of loan receivable was calculated as the present value using the market borrowing rate for similar financial instruments 4.785 per cent per annum. At 31 December 2016 this loan receivable equalled to AZN 42 (2015: AZN 35).

At 31 December 2016 the Group also had long-term deposit contracts with two banks in the total amount of AZN 53 (2015: AZN 31).

The Group has entered into a series of commodity swaps, commodity futures and foreign exchange futures to hedge risks. At 31 December 2016 the Group recognized unrealised fair value gains on physical positions in the amount of AZN 203 (2015: AZN 287), which is result of the asset on fair value hedge accounting for the one of the Group's gas supply contract. The fair value was determined based on the difference between the market value and contracted fixed value of buy and sell contracts.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

15 Property, plant and equipment

Movements in the carrying amount of property, plant and equipment ("PPE") were as follows:

	Buildings and constructions	Oil & gas properties and equipment	Plant and machinery	Vessels and port facilities	Other	Development costs	Construction in progress	Total
Cost								
At 1 January 2015	1,800	10,531	2,736	69	1,302	572	1,830	18,840
Additions	66	653	142	5	31	468	995	2,360
Disposals	(5)	(22)	(18)	(3)	(28)	–	(50)	(126)
Transfers	26	580	14	1	(132)	–	(489)	–
Translation to presentation currency	528	3,329	585	3	460	797	310	6,012
At 31 December 2015	2,415	15,071	3,459	75	1,633	1,837	2,596	27,086
Additions	589	672	111	137	80	551	1,283	3,423
Disposals	(17)	(35)	(36)	–	(11)	–	(16)	(115)
Transfers	32	626	134	258	26	–	(1,076)	–
Translation to presentation currency	144	936	(78)	3	(13)	307	45	1,344
At 31 December 2016	3,163	17,270	3,590	473	1,715	2,695	2,832	31,738
Depreciation and impairment								
At 1 January 2015	(496)	(4,390)	(1,112)	(6)	(439)	–	(263)	(6,706)
Depreciation charge for the year	(85)	(691)	(231)	(2)	(81)	–	–	(1,090)
Disposal	2	28	13	1	11	–	7	62
Impairment	(2)	(218)	–	–	–	–	(34)	(254)
Transfers	–	(1)	(1)	–	2	–	–	–
Translation to presentation currency	(198)	(1,334)	(204)	–	(126)	–	–	(1,862)
At 31 December 2015	(779)	(6,606)	(1,535)	(7)	(633)	–	(290)	(9,850)
Depreciation charge for the year	(126)	(555)	(277)	(2)	(93)	–	–	(1,053)
Disposal	4	26	28	–	6	–	2	66
Impairment	(141)	(74)	–	–	–	–	(107)	(322)
Transfers	1	(3)	1	–	1	–	–	–
Translation to presentation currency	(57)	(405)	24	–	(25)	–	–	(463)
At 31 December 2016	(1,098)	(7,617)	(1,759)	(9)	(744)	–	(395)	(11,622)
Net book value								
At 1 January 2015	1,304	6,141	1,624	63	863	572	1,567	12,134
At 31 December 2015	1,636	8,465	1,924	68	1,000	1,837	2,306	17,236
At 31 December 2016	2,065	9,653	1,831	464	971	2,695	2,437	20,116

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

15 Property, plant and equipment (continued)

During 2016, the Group capitalized finance costs in the amount of AZN 36 which was directly attributable to the construction and production of assets (2015: nil).

At 31 December 2016, impairment in the amount of AZN 149 (2015: AZN 254), AZN 137 (2015: nil) and AZN 36 (2015: nil) are resulted from oil and gas, construction and refinery activities, respectively.

As a result of letter of intention signed by the Group and Azerbaijan International Operating Company on 23 December 2016 in respect of Azeri-Chirag-Gunashli (ACG) PSA period extension, total available reserves related to ACG field increased which resulted in decrease of depreciation charge. During 2016, the Group recognized depreciation charge in the amount of AZN 194 (2015: AZN 367) in respect of its participating interest in ACG PSA.

16 Intangible assets other than goodwill

Movement of intangible assets other than goodwill and related accumulated amortization was as follows:

	Land and property rights	Water rights	Trade name	Customer relationship	Other intangible assets	Total
Cost						
At 1 January 2015	120	129	25	174	134	582
Additions	5	–	–	3	14	22
Disposal	(1)	–	–	–	(15)	(16)
Translation to presentation currency	67	75	14	147	25	328
At 31 December 2015	191	204	39	324	158	916
Additions	2	–	–	–	20	22
Disposal	–	–	–	–	(5)	(5)
Translation to presentation currency	(10)	(13)	(2)	17	4	(4)
At 31 December 2016	183	191	37	341	177	929
Amortization and impairment						
At 1 January 2015	(20)	(19)	–	(31)	(44)	(114)
Amortization charge for the year	(3)	(3)	–	(10)	(14)	(30)
Disposals amortization	–	–	–	–	8	8
Translation to presentation currency	(12)	(12)	–	(28)	(12)	(64)
At 31 December 2015	(35)	(34)	–	(69)	(62)	(200)
Amortization charge for the year	(5)	(4)	–	(16)	(15)	(40)
Disposals amortization	–	–	–	–	2	2
Translation to presentation currency	2	2	–	(2)	(1)	1
Impairment	(2)	–	–	–	(1)	(3)
At 31 December 2016	(40)	(36)	–	(87)	(77)	(240)
Net book value						
At 1 January 2015	100	110	25	143	90	468
At 31 December 2015	156	170	39	255	96	716
At 31 December 2016	143	155	37	254	100	689

At 31 December 2016 included carrying value of intangible assets was AZN 37 (2015: AZN 39) trade name of Petkim acquired through business combination in May 2008.

The carrying value of Petkim trade name at 31 December 2016 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined based on the relief from royalty approach. In applying this methodology, the Group estimated the value of the trade name by capitalising the royalties saved due to Petkim owning the trade name. The valuation exercises are highly sensitive to the change in royalty rate and change in WACC, which were taken into account by the Group as 0.2 per cent and 9.1 per cent throughout the projection period, respectively. As a result of the test performed, no impairment on the Petkim trade name was identified.

During 2016, total amortization expense amounting to AZN 40 (2015: AZN 30) have been allocated to general administrative and research and development expenses by AZN 20 (2015: AZN 16), cost of sales by AZN 14 (2015: AZN 10), and to marketing, selling and distribution expenses by AZN 6 (2015: AZN 4).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

17 Investments in joint ventures

The table below summarizes movements in the carrying amount of the Group's investment in joint ventures:

	Note	2016	2015
Carrying amount at 1 January		3,171	1,127
Additions to investments in joint ventures		260	713
Share of after tax results of joint ventures		767	273
Dividends received from joint ventures		(102)	(13)
Other		14	(10)
Exchange differences		445	1,081
Carrying amount at 31 December		4,555	3,171

At 31 December 2016 the summarized financial information of the Group's principal joint ventures, based on their IFRS financial statements, and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below:

	Azgerneft LLC	AZFEN	Azeri M-I Drilling Fluids	SOCAR Umid	SOCAR AQS	Azerbaijan Rigs	SOCAR Aurora Terminal	STYAS
Country of incorporation	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Panama	Turkey
Current assets	46	327	83	211	268	118	12	261
<i>including cash and cash equivalents</i>	2	52	3	8	–	15	11	77
Non-current assets	59	41	7	269	12	757	174	9,505
Current liabilities	(33)	(205)	(47)	(107)	(228)	–	(21)	(195)
<i>including current financial liabilities (except trade and other payables and provisions)</i>	–	–	–	–	(14)	–	(15)	(47)
Non-current liabilities	–	–	–	(3)	–	–	(47)	(3,054)
<i>including non-current financial liabilities (except trade and other payables and provisions)</i>	–	–	–	–	–	–	(47)	(3,027)
Net assets	72	163	43	370	52	875	118	6,517
Proportion of the Group's ownership	40%	60%	51%	80%	51%	10%	50%	60%
Interest in the net assets	29	98	22	296	27	88	59	3,910
Adjustments	–	–	–	8	(1)	(1)	(9)	(10)
Carrying value	29	98	22	304	26	87	50	3,900

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

17 Investments in joint ventures (continued)

	Azgerneft LLC	AZFEN	Azeri MI Drilling Fluids	SOCAR Umid	SOCAR AQS	Azerbaijan Rigs	SOCAR Aurora Terminal	STYAS
Revenue	39	1,019	203	–	150	–	30	–
Cost of sales	(22)	(819)	(156)	–	(244)	–	(13)	–
including depreciation	–	(14)	(1)	–	–	–	–	–
General and administrative expenses	–	(5)	(4)	(2)	(8)	–	(2)	(31)
Other income	–	–	–	1	–	–	2	10
Other expense	–	(1)	–	(73)	(6)	–	–	–
Forex gain/(loss)	–	29	(1)	–	–	4	–	–
Finance income	–	–	–	–	37	–	–	8
Finance costs	–	–	–	(1)	(55)	–	(4)	(67)
Profit/(loss) before tax	17	223	42	(75)	(126)	4	13	(80)
Income tax (expense)/ benefit	(4)	(48)	(9)	–	5	(1)	–	1,333
Profit/(loss) for the year	13	175	33	(75)	(121)	3	13	1,253
Group's share of profit/(loss) for the year	5	105	17	(60)	(62)	–	7	752
Adjustment	–	–	(1)	–	–	–	(2)	–
Group's share of profit/(loss) for the year	5	105	16	(60)	(62)	–	5	752

At 31 December 2016, the Group's interests in other joint ventures that are not significant both individually and in aggregate and their summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Current assets	Non- current assets	Current liabilities	Non- current liabilities	Revenue	Profit/ (loss)	Interest held	Country of incorporation
Oil and Gas Proserve	17	–	(5)	(2)	2	(1)	30%	Azerbaijan
Caspian Shipyard Company	77	14	(43)	–	215	24	20%	Azerbaijan
SOCAR KPS	29	1	(31)	–	1	(1)	50%	Azerbaijan
SOCAR-Construction	4	8	(1)	–	1	–	97%	Azerbaijan
SOCAR Baglan LLC	1	14	(13)	(6)	–	–	51%	Azerbaijan
SOCAR CAPE	48	34	(44)	(17)	156	27	51%	Azerbaijan
SOCAR Foster Wheeler Engineering	4	–	(3)	–	7	–	65%	Azerbaijan
SOCAR CNG	1	10	(26)	–	2	(4)	51%	Azerbaijan
SOCAR KBR	11	–	(11)	–	13	–	51%	Azerbaijan
AAS – Ekol	4	1	(1)	–	10	3	50%	Azerbaijan
SOCAR Fugro	9	2	(8)	–	16	1	51%	Azerbaijan
Total	205	84	(186)	(25)	423	49		

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

17 Investments in joint ventures (continued)

At 31 December 2015, the summarized financial information of the Group's principal joint ventures, based on their IFRS financial statements, and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below:

	Azgerneft LLC	AZFEN	Azeri M-I Drilling Fluids	SOCAR Umid	SOCAR AQS	Azerbaijan Rigs	SOCAR Aurora Terminal	STYAS
Country of incorporation	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Azerbaijan	Panama	Turkey
Current assets <i>including cash and cash equivalents</i>	40	258	69	175	335	170	15	173
Non-current assets	6	24	5	7	5	94	14	18
Current liabilities <i>including current financial liabilities (except trade and other payables and provisions)</i>	58	43	6	314	24	536	158	4,629
Non-current liabilities <i>including non-current financial liabilities (except trade and other payables and provisions)</i>	(39)	(196)	(32)	(40)	(153)	(4)	(28)	(426)
	-	-	-	-	-	-	(13)	(10)
	-	-	-	(3)	(33)	-	(54)	(371)
	-	-	-	-	-	-	(54)	(364)
Net assets	59	105	43	446	173	702	91	4,005
Proportion of the Group's ownership	40%	60%	51%	80%	51%	10%	50%	60%
Interest in the net assets	24	63	22	357	88	70	46	2,403
Adjustments	-	-	-	8	-	(1)	(7)	69*
Carrying value	24	63	22	365	88	69	39	2,472

* At 31 December 2015 the adjustment includes the amount of AZN 31 temporarily unpaid by the other shareholders of SOCAR TURKEY YATIRIM A.Ş. ("STYAS"). In addition, the Group recognized charges in total amount of AZN 38 under letter of credit agreements as additional investment in STYAS.

	Azgerneft LLC	AZFEN	Azeri MI Drilling Fluids	SOCAR Umid	SOCAR AQS	Azerbaijan Rigs	SOCAR Aurora Terminal	STYAS
Revenue	32	565	155	-	76	-	19	-
Cost of sales <i>including depreciation</i>	(27)	(498)	(122)	-	(102)	-	(13)	-
General and administrative expenses	-	(10)	(1)	-	(1)	-	-	-
Other income	-	(3)	(2)	(2)	(5)	-	-	(18)
Other expense	-	-	-	-	-	-	-	9
Forex gain (loss)	-	-	-	-	(7)	-	-	-
Finance income	-	-	(3)	-	(24)	16	-	-
Finance costs	-	-	-	-	-	-	-	3
	-	-	-	-	-	-	-	(16)
Profit/(loss) before tax	5	64	28	(2)	(62)	16	6	(22)
Income tax (expense)/ benefit	-	(15)	(6)	-	13	(3)	-	412
Profit/(loss) for the year	5	49	22	(2)	(49)	13	6	390
Group's share of profit/(loss) for the year	2	29	11	(2)	(25)	1	3	234
Adjustments	-	-	(5)	4	11*	-	1	-
Group's share of profit/(loss) for the year	2	29	6	2	(14)	1	4	234

* The amount represents elimination of unrealised profit from sales to AzNeft.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

17 Investments in joint ventures (continued)

At 31 December 2015, the Group's interests in other joint ventures that are not significant both individually and in aggregate and their summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Current assets	Non-current assets	Current liabilities	Non-current liabilities	Revenue	Profit/(loss)	Interest held	Country of incorporation
Oil and Gas Proserve Caspian Shipyard Company	19	–	(7)	(2)	3	1	30%	Azerbaijan
SOCAR KPS	89	8	(56)	–	142	24	20%	Azerbaijan
SOCAR-Construction	28	1	(29)	–	3	–	50%	Azerbaijan
Sarmatia	4	8	(1)	–	–	(1)	97%	Azerbaijan
SOCAR Baglan LLC	2	–	(1)	–	–	–	27%	Poland
SOCAR CAPE	1	14	(13)	(6)	–	–	51%	Azerbaijan
SOCAR Foster Wheeler Engineering	14	16	(16)	(11)	97	11	51%	Azerbaijan
Socar CNG	3	–	(2)	–	6	1	65%	Azerbaijan
SOCAR KBR	1	10	(22)	–	–	(10)	51%	Azerbaijan
AAS – Ekol	1	–	(1)	–	–	(1)	51%	Azerbaijan
Socar Fugro	3	1	(1)	–	9	3	50%	Azerbaijan
	13	3	(14)	–	14	1	51%	Azerbaijan
Total	178	61	(163)	(19)	274	29		

Investments which are jointly controlled by the Group and other ventures are recognized as investments in joint ventures.

During 2016, the Group has made additional contributions in share capital of its joint ventures Azerbaijan Rigs LLC in the amount AZN 17 (2015: AZN 36), STYAS in the amount of AZN 198 (2015: AZN 607), and AZN 1 to other joint ventures (2015: AZN 2), respectively.

In 2015, the Group signed letters of credit agreements in relation to the construction of Star Refinery complex (subsidiary of STYAS). Commission and interest expenses paid by the Group in total amount of AZN 44 (2015: AZN 38) were recognized as additional investment in STYAS.

18 Investments in associates

The table below summarises the movements in the carrying amount of the Group's investment in associates.

	Note	2016	2015
Carrying amount at 1 January		2,838	1,280
Additions to investments in associates		797	775
Share of after tax results of associates		209	201
Dividends received from associates		(88)	(649)
Other		(4)	(1)
Exchange differences		690	1,232
Carrying amount at 31 December		4,442	2,838

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

18 Investments in associates (continued)

At 31 December 2016 the summarized financial information of the Group's principal associates, based on their IFRS financial statements, and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below.

2016	South Caucasus Pipeline Company	BTC Co	Southern Gas Corridor
Country of incorporation	Cayman Islands	Cayman Islands	Azerbaijan
Current assets	243	204	799
Non-current assets	7,536	9,772	13,769
Current liabilities	(477)	(1,093)	(1,305)
Non-current liabilities	(367)	(1,879)	(8,048)
Net assets attributable to the Group	6,935	7,004	4,004
Net assets attributable to the NCI			1,211
Proportion of the Group's ownership	10%	25%	49%
Interest in the net assets	694	1,751	1,962
Adjustments	(2)	–	(21)*
Carrying value	692	1,751	1,941

* At 31 December 2016 the adjustment includes the amount of AZN 37 which represents over financing to SGC by the government and the rest of the amount represents the Group's share in loss on sale of its additional interests in Shah Deniz PSA to SGC in 2015.

2016	South Caucasus Pipeline Company	BTC Co	Southern Gas Corridor
Revenue	565	1,575	178
Cost of sales	(153)	(691)	(112)
General and administrative expenses	–	–	(12)
Distribution expenses	–	–	(5)
Other income	–	–	28
Finance income	–	–	12
Finance costs	(1)	(69)	(138)
Forex loss	–	–	(43)
Share of results of associates	–	–	(6)
Profit before tax	411	815	(98)
Income tax expense	(87)	–	(3)
Profit for the year	324	815	(101)
Group's share of profit for the year	32	204	(49)
Adjustments	–	2	–
Total	32	206	(49)

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

18 Investments in associates (continued)

At 31 December 2016, the Group's interests in other associates that are not significant both individually and in aggregate and their summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Total assets	Total liabilities	Revenue	Profit/(loss)	Interest held	Country of incorporation
Ateshgah Insurance Company	42	(27)	40	–	10%	Azerbaijan
Azerbaijan Gas Supply Company	550	(551)	2,304	–	28%	Cayman Islands
AzLab	5	(4)	2	–	50%	Azerbaijan
Caspian Geophysical	40	(2)	67	34	45%	Azerbaijan
Caspian Pipe Coatings LLC	33	(13)	34	9	50%	Azerbaijan
Cross Caspian Oil and Gas Logistics	3	(2)	8	–	34%	Azerbaijan
South Caucasus Pipeline Company Hold Co ("SCPC Hold Co.")	121	(1)	–	–	10%	Cayman Islands
Tankanlagen Mellingen AG (TAMAG)	13	(3)	–	–	33%	Switzerland
Tanklager Taegerschen AG (TLT)	2	–	–	–	21%	Switzerland
SOGEF AG	6	(5)	–	–	34%	Switzerland
UBAG AG	38	(32)	–	–	24%	Switzerland
SAPPRO SA	7	(5)	–	–	13%	Switzerland
SARACO SA	20	(20)	–	–	20%	Switzerland
Electrogas Malta	778	(781)	1	(2)	33%	Switzerland
Total	1,658	(1,446)	2,456	41		

During 2016, the Group has made additional contributions in share capital of its associates, SCPC and SGC in the amount of AZN 104 (2015: AZN 107) and AZN 693 (2015: AZN 665), respectively.

At 31 December 2015, the summarized financial information of the Group's principal associates, based on their IFRS financial statements, and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below.

2015	South Caucasus Pipeline Company	BTC Co	Southern Gas Corridor
Country of incorporation	Cayman Islands	Cayman Islands	Azerbaijan
Current assets	334	240	505
Non-current assets	5,191	7,972	7,628
Current liabilities	(475)	(1,087)	(806)
Non-current liabilities	(277)	(2,206)	(4,601)
Net assets attributable to the Group	4,773	4,919	2,195
Net assets attributable to the NCI			531
Proportion of the Group's ownership	10%	25%	49%
Interest in the net assets	477	1,230	1,076
Adjustments	–	(4)	16*
Carrying value	477	1,226	1,092

* The amount represents the Group's share in loss on sale of its additional interests in Shah Deniz PSA to SGC.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

18 Investments in associates (continued)

2015	South Caucasus Pipeline Company	BTC Co	Southern Gas Corridor
Revenue	330	1,286	156
Cost of sales	(114)	(487)	(72)
General and administrative expenses	(1)	–	(13)
Distribution expenses	–	–	(5)
Other expenses	–	–	–
Other income	–	–	17
Finance income	–	–	5
Finance costs	–	(15)	(58)
Share of results of associates	–	–	(6)
Profit before tax	215	784	24
Income tax expense	(63)	–	(4)
Profit for the year	152	784	20
Group's share of profit for the year	15	196	10
Adjustments	–	(5)	(18)*
Total	15	191	(8)

* The adjustment represents the recognition of Group's share in loss on sale of 42 per cent shares of TANAP that was recognized within equity of SGC.

At 31 December 2015, the Group's interests in other associates that are not significant both individually and in aggregate and their summarised aggregate financial information, including total assets, liabilities, revenues and profit or loss, were as follows:

Name	Total assets	Total liabilities	Revenue	Profit/ (loss)	Interest held	Country of incorporation
Ateshgah Insurance Company	33	(26)	44	–	10%	Azerbaijan
Azerbaijan Gas Supply Company	578	(578)	2,154	–	28%	Cayman Islands
AzLab	5	(4)	2	–	50%	Azerbaijan
Caspian Geophysical	49	(40)	26	6	45%	Azerbaijan
Caspian Pipe Coatings LLC	23	(8)	65	8	50%	Azerbaijan
Cross Caspian Oil and Gas Logistics	3	(3)	33	–	34%	Azerbaijan
SCPC Hold Co	87	(1)	–	–	10%	Cayman Islands
Interfax Azerbaijan	4	–	–	–	49%	Azerbaijan
TAMAG	12	(3)	3	–	33%	Switzerland
TLT	2	–	1	–	21%	Switzerland
SOGEF AG	2	(2)	4	–	34%	Switzerland
UBAG AG	32	(28)	15	1	24%	Switzerland
SAPPRO SA	5	(2)	11	–	13%	Switzerland
SARACO SA	17	(15)	14	1	20%	Switzerland
Electrogas Malta	293	(293)	–	–	33%	Switzerland
Total	1,145	(1,003)	2,372	16		

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

19 Trade and other payables

	2016	2015
Trade payables	5,772	4,322
Accrued liabilities	3,025	983
Other payables	489	487
Total financial payables	9,286	5,792
Liabilities for overlift of oil	52	22
Advances from customers	194	317
Payable to employees	130	122
Total trade and other payables	9,662	6,253

Financial payables in the amount of AZN 7,207 (2015: AZN 5,051) are denominated in foreign currencies, mainly in USD. Trade payables mainly represent payables for crude oil, oil products, gas, construction, drilling, transportation and utilities provided by vendors of the Group.

Accrued liabilities of the Group represent obligations occurred for purchase of crude oil and oil products, for which invoices have not yet been received.

Liabilities for overlift relate to the oil lifted by the Group in excess of its participating interest in ACG PSA and Shah Deniz PSA and thus, represent the Group's obligation to deliver physical quantities of oil out of its share of future production.

20 Borrowings

At 31 December 2016 short-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate	Maturity date	Total borrowed in original currency	Balance as at 31 December 2016
Short-term facilities in USD	0.25%-14%	January 2017 – December 2017	2,700	4,776
Short-term facilities in TRY	12.75%-14.7%	January 2017 – September 2017	292	148
Short-term facilities in GEL	11%-14.8%	January 2017 – December 2017	111	55
Short-term facilities in other currencies	3%-12%	January 2017 – November 2017	299	547
Current portion of long-term borrowings				1,191
Total short-term borrowings and current portion of long-term borrowings				6,717

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

20 Borrowings (continued)

At 31 December 2016 long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate*	Maturity date	Balance as at 31 December 2016	
			Non-current portion	Current portion
USD 1,000 million	4.75%	March 2023	1,757	25
USD 750 million	6.95%	March 2030	1,318	27
USD 489 million	LIBOR + 6.95%	July 2025	468	–
USD 485 million	LIBOR + 1%	December 2024	429	134
AZN 600 million	4%	July 2022	362	44
AZN 472 million	3.65%	October 2024	330	47
USD 200 million	LIBOR + 1.335%	December 2027	312	14
AZN 750 million	3.15%	July 2023	300	50
USD 106 million	LIBOR + 4.675%	March 2028	188	–
USD 100 million	LIBOR + 2.33%	June 2020	177	–
JPY 15,398 million	1.5%	April 2039	169	8
USD 90 million	5%	March 2028	160	–
USD 78 million	4%	December 2027	158	–
USD 150 million	LIBOR + 1.8%	December 2019	152	76
USD 150 million	LIBOR + 1.8%	November 2019	152	77
USD 100 million	5%	October 2021	147	2
USD 100 million	LIBOR + 2.4%	May 2020	126	51
USD 150 million	LIBOR + 2.5%	March 2019	115	78
USD 150 million	LIBOR + 2.2%	May 2019	114	77
USD 65 million	6.25%	December 2024	96	19
USD 52 million	6%	January 2020	92	–
USD 50 million	4.44%	December 2018	89	–
USD 55 million	5.58%	September 2024	84	14
AZN 198 million	3.5%	June 2026	80	20
USD 150 million	LIBOR + 2.5%	November 2018	77	77
USD 50 million	LIBOR + 2.2%	July 2020	75	14
EUR 40 million	EURIBOR + 2.25%	December 2020	74	–
AZN 1,292 million	4%	August 2027	70	1
EUR 35 million	LIBOR + 0.731%	November 2025	65	–
USD 50 million	LIBOR + 1.8%	November 2019	59	30
USD 29 million	4%	December 2027	59	–
USD 50 million	LIBOR + 1.8%	December 2019	51	25
USD 24 million	4.26%	December 2022	42	1
EUR 20 million	LIBOR + 0.872%	September 2023	34	3
EUR 20 million	1.64%	October 2023	34	3
USD 18 million	LIBOR + 2.8%	April 2022	31	2
USD 20 million	LIBOR + 2%	April 2023	31	7
USD 17 million	LIBOR + 2.8%	March 2022	28	2
USD 35 million	LIBOR + 2.35%	April 2020	22	9
EUR 12 million	LIBOR + 3%	March 2022	13	3
USD 6 million	4.26%	December 2022	10	–
USD 5 million	4.26%	December 2022	9	–
EUR 7 million	LIBOR + 3%	March 2022	8	2
USD 4 million	4.26%	December 2022	7	–
USD 4 million	4.26%	December 2022	7	–
EUR 5 million	LIBOR + 3%	March 2022	6	1
USD 6 million	LIBOR + 8.5%	October 2018	5	5
USD 6 million	LIBOR + 8.5%	February 2019	3	9
USD 500 million	5.45%	February 2017	–	175
CHF 22 million	LIBOR + 0.0714% or 0%	January 2017	–	38
USD 16 million	LIBOR + 1.70%	June 2017	–	7
Other long-term borrowings			15	14
Total long-term borrowings			8,210	1,191

(*) LIBOR and EURIBOR vary from 3 to 12 months.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

20 Borrowings (continued)

At 31 December 2015 short-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate	Maturity date	Total borrowed in original currency	Balance as at 31 December 2015
Short-term facilities in USD	0.84%-12%	January 2016 – October 2016	1,357	2,106
Short-term facilities in TRY	10.9%-14.25%	January 2016 – September 2016	298	160
Short-term facilities in GEL	11%-16%	January 2016 – December 2016	91	55
Short-term facilities in other currencies	3%-12%	February 2016 – May 2016	13	15
Current portion of long-term borrowings				749
Total short-term borrowings and current portion of long-term borrowings				3,085

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

20 Borrowings (continued)

At 31 December 2015 long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate*	Maturity date	Balance as at 31 December 2015	
			Non-current portion	Current portion
USD 1,000 million	4.75%	March 2023	1,559	22
USD 750 million	6.95%	March 2030	1,170	25
USD 500 million	5.45%	February 2017	780	17
USD 485 million	LIBOR + 1%	December 2024	432	115
AZN 472 million	3.65%	October 2024	377	47
AZN 750 million	3.15%	July 2023	350	50
USD 197 million	LIBOR + 4.675%	March 2028	306	–
USD 200 million	LIBOR + 1.335%	December 2027	287	25
AZN 200 million	4%	August 2018	200	–
USD 150 million	LIBOR + 1.8%	November 2019	199	34
USD 150 million	LIBOR + 1.8%	December 2019	199	34
USD 150 million	LIBOR + 2.5%	March 2019	166	69
USD 150 million	LIBOR + 2.2%	May 2019	166	68
USD 100 million	LIBOR + 2.4%	May 2020	154	1
USD 100 million	LIBOR + 2.33%	June 2020	154	–
JPY 15,398 million	1.5%	April 2039	151	7
USD 78 million	4%	December 2027	134	–
USD 150 million	LIBOR + 2.5%	November 2018	133	68
USD 59 million	LIBOR + 6.95%	July 2018	92	–
USD 52 million	6%	January 2020	81	–
USD 50 million	LIBOR + 1.8%	November 2019	77	–
USD 50 million	LIBOR + 2.2%	July 2020	77	1
AZN 70 million	4%	August 2027	70	1
EUR 40 million	EURIBOR + 2.25%	December 2020	67	–
USD 50 million	LIBOR + 1.8%	December 2019	66	11
USD 29 million	4%	December 2027	50	–
USD 24 million	4.26%	December 2022	38	–
CHF 22 million	LIBOR + 0.0714% or 0%	January 2017	35	–
EUR 20 million	LIBOR + 0.872%	September 2023	34	–
EUR 20 million	1.64%	October 2023	34	–
USD 20 million	LIBOR + 2%	April 2023	31	1
USD 35 million	LIBOR + 2.35%	April 2020	27	8
EUR 12 million	LIBOR + 3%	March 2022	15	3
GEL 22 million	14.75%	March 2017	14	–
USD 6 million	LIBOR + 8.5%	October 2018	10	4
USD 6 million	8.5%	February 2019	10	3
EUR 7 million	LIBOR + 3%	March 2022	9	2
USD 6 million	4.26%	December 2022	9	–
GEL 13 million	11%	June 2018	9	11
USD 5 million	4.26%	December 2022	8	–
USD 4 million	4.26%	December 2022	6	–
EUR 5 million	LIBOR + 3%	March 2022	6	1
USD 4 million	4.26%	December 2022	6	–
USD 16 million	LIBOR + 1.7%	June 2017	6	7
USD 50 million	LIBOR + 2.4%	December 2016	–	39
USD 100 million	LIBOR + 2.2%	October 2016	–	63
Other long-term borrowings			22	12
Total long-term borrowings			7,826	749

(*) LIBOR and EURIBOR vary from 3 to 12 months.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

21 Taxes payable

	Note	2016	2015
Payable to SOFAZ	7	266	234
Social security contributions		2	1
Other taxes payable		348	297
Total taxes payable		616	532

In 2008 apart from regular export tax the Group was liable to transfer a certain share of proceeds from sales of crude oil priced at the level exceeding the price determined by the government (USD 50 per barrel for 2009) to SOFAZ. No such taxes were imposed on the Group in 2009-2016.

Taxpayers operating under the Azerbaijani tax legislation are eligible for offsetting their taxes payable with taxes receivable and tax prepayments. Other taxes payable balance consists of corporate income tax, VAT, property, excise tax, personal income tax, price margin tax liabilities offset with tax receivables and prepayments.

22 Asset retirement obligations

The Group has a legal and constructive obligation with respect to decommissioning of oil and gas production and storage facilities and environmental clean-up. Movements in provisions for the related asset retirement obligations are as follows:

	Note	2016	2015
Carrying amount at 1 January		748	440
Additions/(disposals)		83	(7)
Unwinding of the present value discount	32	48	35
Effect of change in estimates		2	3
Exchange differences		87	277
Carrying amount at 31 December		968	748

The Group makes provision for the future cost of oil and natural gas production facilities retirement and related pipelines on a discounted basis on the installation of those facilities. The provision has been estimated using existing technology, at current prices and discounted using pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability as of the reporting date. These costs are expected to be incurred over the useful life of the fields and properties ranging between 10 and 66 years from the reporting date.

Asset retirement obligations related to the PSAs are determined with reference to capital costs incurred by contractor parties and they are limited to the maturities of respective PSAs.

Governmental authorities are continually reviewing regulations and their enforcement. Consequently, the Group's ultimate liabilities may differ from the recorded amounts.

Estimated costs of dismantling oil and gas production facilities, pipelines and related processing and storage facilities, including abandonment and site restoration costs amounting to AZN 392 at 31 December 2016 (2015: AZN 316) are included in the cost of oil and gas properties and equipment.

The maximum estimated cost to Azneft PU to abandon the production facilities employed was AZN 1,933 as at 31 December 2016 (2015: AZN 1,372). The Company used 8.24 per cent rate to discount this obligation (2015: 8.28 per cent).

The maximum estimated cost to Azerbaijan Shah Deniz Limited ("AzSD") to abandon the production facilities employed in Shah Deniz project was AZN 422 as at 31 December 2016 (2015: AZN 310). The Company used 5.59 per cent rate to discount this obligation (2015: 5.95 per cent).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

22 Asset retirement obligations (continued)

The maximum estimated cost to AzACG to abandon the production facilities employed in ACG project was AZN 743 at 31 December 2016 (2015: AZN 628). The Company used 6.34 per cent rate to discount this obligation (2015: 5.95 per cent).

The following inflation rates were applied in calculation of discounted cash flows:

Year	2017	2018	2019	2020	2021	2022 and later
Inflation rate	8.05%	6.55%	5.50%	5.05%	4.20%	4.00%

While the provision is based on the best estimate of future costs and the economic lives of the facilities and pipelines, there is uncertainty regarding both the amount and timing of incurring these costs.

23 Other provisions for liabilities and charges

Movements in other provisions for liabilities and charges are as follows:

	Note	Environmen- tal obligations	Disability payments	Unused vacation	Total
Carrying amount at 1 January 2015		99	98	24	221
Additions		9	23	43	75
Utilisation		(23)	(13)	(43)	(79)
Unwinding of the present value discount	32	6	6	–	12
Effect of change in estimates		(3)	(14)	–	(17)
Carrying amount at 31 December 2015		88	100	24	212
of which:					
Current		31	15	24	70
Non-current		57	85	–	142
Carrying amount at 1 January 2016		88	100	24	212
(Disposals)/additions		(5)	21	53	69
Utilisation		(15)	(13)	(47)	(75)
Unwinding of the present value discount	32	7	8	–	15
Effect of change in estimates		1	1	–	2
Carrying amount at 31 December 2016		76	117	30	223
of which:					
Current		29	16	29	74
Non-current		47	101	1	149

Under the Presidential Decree number 1697 dated 28 September 2006 the Group prepared and approved Action Plan for Environmental Restoration with respect to the damage caused to the environment as a result of the Group's activities within Absheron area. In 2014 the Group amended the Action Plan in accordance with the Presidential Decree dated 27 February 2014, extending period to be covered up to 2018 and including other additional regions of Azerbaijan to be restored, as well as Absheron area. Corresponding provision is recognized at the present value of future costs to be incurred for the environmental remediation, discounted at the rate of 8.73 per cent (2015: 8.59 per cent).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

23 Other provisions for liabilities and charges (continued)

The Group has an obligation to compensate its employees for the damage caused to their health at workplace up to January 2012 (payments to employees injured after January 2012 are made by insurance company, based on insurance contract), as well as to compensate dependants of died employees. The compensations provided are linked to the salaries paid to the affected employees. The Group calculated the present value of the disability payments to employees using a discount rate of 8.13 per cent (2015: 8.29 per cent). For the purpose of calculation of the lifetime payments to injured employees, the Group estimated a life expectancy as 71 and 76 for men and women, respectively.

The inflation rates in Note 22 were applied to reflect the escalation in average salaries.

24 Deferred income

	2016	2015
Carrying amount at 1 January	79	77
Received during the year	203	7
Released to the statement of profit or loss	(110)	(5)
Carrying amount at 31 December	172	79
of which:		
Current	98	–
Non-current	74	79

Current

At 31 December 2016 current portion of deferred income comprised of government grants as a compensation of losses incurred from sale of natural gas and heating oil for the purpose of meeting local demand in the country. During 2016, the Group received government grants in the amount of AZN 203 (2015: nil) for compensation of losses.

Non-current

At 31 December 2016 and 2015 non-current portion of deferred income mainly comprised of government grants obtained for the purpose of gasification of Baku sub-urban area and regions of the Azerbaijan Republic in 2006.

25 Other current and non-current liabilities

Other liabilities comprise the following:

	2016	2015
Derivative liabilities	1,245	474
Liabilities under carried interest arrangement	172	125
Provision for employment termination benefits	76	83
Payables for drilling services received	–	70
Advances received from related parties	70	36
Other liabilities	18	24
Total other liabilities	1,581	812
Less other current liabilities	(1,052)	(174)
Total other non-current liabilities	529	638

The Group has financial liabilities related to margin calls and funds held on trading in the amount of AZN 83 (2015: AZN 69), unrealized losses on paper positions in the amount of AZN 913 (2015: AZN 344) and unrealized losses on physical positions in the amount of AZN 249 (2015: AZN 44). These liabilities were included in other current and non-current liabilities in the amounts of AZN 1,052 (2015: AZN 160) and AZN 193 (2015: AZN 297) financial liabilities.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

25 Other current and non-current liabilities (continued)

Under *Turkish Labor Law*, the Group is required to pay termination benefits to each employee who has completed one year of service and whose employment is terminated without due cause, is called up for military service, dies or who retires after completing 25 years of service (20 years for women) and achieves the retirement age (58 for women and 60 for men).

The liability is not funded, as there is no funding requirement. The provision is calculated by estimating the present value of the future probable obligation of the Group arising from the retirement of the employees. IAS 19 requires actuarial valuation methods to be developed to estimate the enterprises' obligation under defined benefit plans. Accordingly, the following actuarial assumptions were used in the calculation of the total liability:

	2016	2015
Discount rate (per cent)	3.61	4.39
Probability of retirement (per cent)	100	95

The principal assumption is that the maximum liability for each year of service will increase in line with inflation. Thus the discount rate applied represents the expected real rate after adjusting for the anticipated effects of future inflation.

Movement of the provision for employment termination benefits were as follows:

	2016	2015
Carrying amount at 1 January	83	38
Actuarial loss and service cost	4	5
Payments during the year	(8)	(4)
Defined (obligation)/benefit pension plan	(10)	13
Other	5	1
Translation to presentation currency	2	30
Carrying amount at 31 December	76	83

26 Deferred acquisition consideration payable

The Group has deferred cash consideration payable in the amount of AZN 67 (2015: AZN 59) for the purchase of remaining 49 per cent shares of SOCAR Petroleum CJSC from other shareholder.

In addition to this the Group has deferred cash consideration payable in the amount of AZN 86 (2015: AZN 74) for acquisition of SOCAR Trading and other entities.

27 Charter capital, additional paid-in-capital, retained earnings and gain on sale of subsidiary share

Charter capital

SOCAR as a holding company of the Group has a legal status of a state enterprise. Increase in the amount of AZN 185 in charter capital was registered during 2016 and accordingly the amount was reclassified from additional paid in capital to charter capital (2015: AZN 121).

Additional paid-in capital ("APIC")

During 2016 Government contributed to the charter capital of the Group in the amount of AZN 921 (2015: AZN 581). The increase in charter capital was not registered as of 31 December 2016 and recognized as APIC.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

27 Charter capital, additional paid-in-capital, retained earnings and gain on sale of subsidiary share (continued)

Distribution to the Government

Based on decisions of the Government, the Group is periodically mandated to make direct cash contributions or finance construction and repair works for the Government (including transfer of assets), various government agencies and projects administered by the Government. During the year 2016, such direct cash transfers to the Government and financing (made in the form of payments to sub-contractors of governmental entities) amounted to AZN 56 and AZN 17, respectively (2015: AZN 140 and AZN 186, respectively), mainly for repair and reconstruction of existing, as well as construction of new recreational, transport, educational and medical infrastructure of the Azerbaijan Republic. As at 31 December 2016 there was no financing in the form of transfer of assets constructed by the Group (2015: AZN 13).

Gain on sale of subsidiary share

During 2016, the Group sold its 6.75 per cent shares of Petkim Petrokimya Holding A.Ş with the carrying amount in the amount of AZN 172 (TRY 326 million) and recognized gain in the amount of AZN 46 (TRY 87 million) within the equity. Gain on sale of shares in subsidiaries during 2015 is disclosed in Note 35.

28 Analysis of revenue by categories

	2016	2015
Crude oil, net	29,613	14,453
Oil products, net	11,759	11,391
Petrochemicals	2,643	1,835
Natural gas	1,952	1,683
Other revenue	5,938	3,741
Total revenue	51,905	33,103

Revenue from crude oil sales is stated net of price margin tax which is levied in the Azerbaijan Republic on the margins between the international market price and internal state-regulated price on crude oil. The difference between the market price and the internal state-regulated price is taxed at the rate of 30 per cent and the amount of tax is transferred to the State Budget.

Revenue from oil product sales is stated net of excise tax of AZN 423 (2015: AZN 429).

Revenue from sales of crude oil produced under ACG PSA and condensate produced under Shah Deniz PSA is not subject to excise and price margin taxes mentioned above.

29 Analysis of expenses by nature

	Note	2016	2015
Raw materials and consumables used		44,265	27,136
Depreciation of property, plant and equipment		1,014	1,049
Wages, salaries and social security costs		1,297	1,016
Transportation and vehicle maintenance		714	252
Repairs and maintenance expenses		189	220
Impairment of property, plant and equipment	15	322	254
Mining tax	7	103	110
Utilities expense		307	242
Taxes other than on income		178	115
Amortization expense	16	40	30
Impairment of trade and other receivables and other financial assets		493	38
Change in other provisions for liabilities and charges	23	71	58
Other		1,531	1,295
Total cost of sales, exploration and evaluation, distribution, general and administrative and other operating expenses		50,524	31,815

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

30 Other operating income

	2016	2015
Government grant (Note 24)	110	5
Rig upgrade reimbursed by third party	387	–
Sales of other goods and services rendered	18	15
Gain on release of borrowings	–	22
Other	182	119
Total other operating income	697	161

31 Finance income

	2016	2015
Interest income on deposits and bank accounts	170	38
Other	19	27
Total finance income	189	65

32 Finance costs

	Note	2016	2015
Interest expense		778	429
Provisions for asset retirement obligations: unwinding of the present value discount	22	48	35
Environmental provision: unwinding of the present value discount	23	7	6
Provision for disability payments: unwinding of the present value discount	23	8	6
Total finance costs		841	476

33 Income taxes

Income tax expense comprises the following:

	2016	2015
Current tax expense	537	394
Deferred tax charge/(benefit)	49	(193)
Income tax expense reported in the statement of profit or loss	586	201

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

33 Income taxes (continued)

Reconciliation between the expected and the actual taxation charge is provided below:

	2016	2015
Profit/(loss) before tax	936	(1,584)
Theoretical tax charge/(benefit) at statutory rate of 20 per cent	187	(317)
Effects of different tax rates for certain subsidiaries (25 and 27 per cent)	22	5
Tax effect of items which are not deductible or assessable for taxation purposes:		
- Income which is exempt from taxation	(236)	(40)
- Non-deductible expenses	176	58
Allowance for deferred tax assets	294	535
Current income tax on non-resident dividends	38	14
Recognition of previously unrecognized deferred tax asset	(48)	-
Income not recognized in IFRS	15	31
Unused investment incentives on which deferred income tax assets recognized	(48)	(70)
Potential income tax on retained profit/(loss) of subsidiaries, associates and joint ventures	137	(12)
Other	49	(3)
Income tax expense reported in the statement of profit or loss	586	201

Non-deductible expenses are mainly comprised of the social and employee-related expenses, as well as the provision for impaired receivables which are not expected to be deductible from taxable income in future. Allowance for deferred tax assets mainly relates to the accumulated tax losses of the Group's subsidiaries which are not expected to utilize these losses.

At 31 December 2016 cumulative balance of unrecognized deferred tax assets is AZN 1,206 (2015: AZN 960).

At 31 December 2016 the Group recognized deferred income tax asset on the portion of unused investment incentive for which the realization of the related tax benefit through the future taxable profit has deemed probable with respect to its projections.

At 31 December 2016, benefits arising from previously unrecognized deferred tax assets were used during the year to reduce deferred tax and current tax expenses by the amount of AZN 39 and AZN 9 (2015: nil), respectively.

At 31 December 2016 and 2015 the Group recognized deferred income tax benefit and charge in the amount of AZN 19 and AZN 124, respectively, on the exchange differences arising on translation of the financial statements of foreign operations and charged to OCI.

As at 31 December 2016 the Group has not recognised deferred tax liability in the amount of AZN 148 (31 December 2015: AZN 65) in respect of taxable temporary differences associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and it is not expected to reverse them in the foreseeable future.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

33 Income taxes (continued)

Differences between IFRS and applicable domestic tax regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below:

	1 January 2016	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	Translation difference	31 December 2016
Tax effect of deductible/ (taxable) temporary differences					
Carry forward tax losses	42	40	–	(2)	80
Investments in associates and joint ventures	8	(7)	–	–	1
Trade and other payables	12	(15)	–	(2)	(5)
Impairment provision for receivables	4	(4)	–	–	–
Trade and other receivables	39	18	–	3	60
Inventory	13	3	–	–	16
Property, plant and equipment	412	26	–	5	443
Provisions for liabilities and charges	68	5	–	–	73
Unused Investment incentives	89	48	–	(8)	129
Employment termination benefits and seniority incentive bonus provision	9	–	–	(1)	8
Other	16	21	(1)	–	36
Deferred tax assets	712	135	(1)	(5)	841

	1 January 2016	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	Translation difference	31 December 2016
Tax effect of deductible/ (taxable) temporary differences					
Accruals	22	(27)	3	–	(2)
Investments in associates and joint ventures	(97)	6	–	(10)	(101)
Intangible assets	(43)	4	–	(4)	(43)
Trade and other payables	7	(1)	–	–	6
Trade and other receivables	(25)	(10)	–	(3)	(38)
Inventory	(22)	–	–	(3)	(25)
Property, plant and equipment	(796)	(35)	–	(64)	(895)
Provisions for liabilities and charges	114	5	2	16	137
Other	(197)	(126)	15	(3)	(311)
Deferred tax liabilities	(1,037)	(184)	20	(71)	(1,272)

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

33 Income taxes (continued)

	1 January 2015	Credited/ (charged) to profit or loss	Translation difference	31 December 2015
Tax effect of deductible/(taxable) temporary differences				
Carry forward tax losses	32	9	1	42
Investments in associates and joint ventures	7	1	–	8
Trade and other payables	7	4	1	12
Impairment provision for receivables	3	1	–	4
Trade and other receivables	(9)	49	(1)	39
Inventory	9	3	1	13
Property, plant and equipment	362	42	8	412
Provisions for liabilities and charges	82	(14)	–	68
Unused Investment incentives	9	52	28	89
Employment termination benefits and seniority incentive bonus provision	–	6	3	9
Other	12	4	–	16
Deferred tax assets	514	157	41	712

	1 January 2015	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	Translation difference	31 December 2015
Tax effect of deductible/ (taxable) temporary differences					
Accruals	8	9	–	5	22
Investments in associates and joint ventures	(68)	8	–	(37)	(97)
Intangible assets	(24)	1	–	(20)	(43)
Trade and other payables	(7)	14	–	–	7
Impairment provision for receivables	(7)	9	–	(2)	–
Trade and other receivables	(24)	15	–	(16)	(25)
Inventory	(9)	(2)	–	(11)	(22)
Property, plant and equipment	(452)	–	–	(344)	(796)
Provisions for liabilities and charges	51	8	–	55	114
Other	(48)	(26)	(124)	1	(197)
Deferred tax liabilities	(580)	36	(124)	(369)	(1,037)

The Group does not file a consolidated tax return. In the context of the Group's current structure, tax losses and current tax assets of different Group companies may not be offset against current tax liabilities and taxable profits of other Group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

In accordance with Azerbaijani tax legislation, tax losses arising in one period can be carried forward for five years.

The Group is a participant to ACG PSA through its subsidiary AzACG. However, AzACG is not explicitly defined as a contractor party in the ACG PSA. As a result, its tax-payer status is not clearly determinable. Based on current understanding from communication with relevant tax authorities, management believes that the status of the contractor party will be granted retrospectively and therefore AzACG has already assumed a tax-payer status. At the moment AzACG accrues and pays its income tax at the rate of 25 per cent in accordance with ACG PSA provisions.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

33 Income taxes (continued)

The governments of the Azerbaijan Republic, Turkey and Georgia together with the Group's subsidiary AzBTC and other BTC Project participants entered into Host Government Agreements ("HGAs"). The HGAs set out the legal and fiscal regime for the BTC Project and the mutual rights and obligations of the parties, including grants of rights and guarantees from the respective Countries to the investors in respect of matters necessary to ensure the success of the BTC Project. In accordance with the provisions of the HGAs, the BTC Project participants are individually liable for income taxes in Georgia and the Azerbaijan Republic and are responsible for filing returns for each taxable period. Accordingly, the Company is liable for Azerbaijani income taxes arising from participation in the BTC Project. In accordance with the provisions of the HGA, Azerbaijani income tax rate is twenty-seven per cent (27 per cent) which was effective at 31 December 2016 and 2015.

In addition, the Group is a participant to Shah Deniz PSA through its subsidiary AzSD. According to the provisions of Shah Deniz PSA, AzSD is liable for corporate income tax payments. However, in accordance with PSA, the Government makes profit tax payments on behalf of contractor parties from the proceeds from sales of profit petroleum attributable to the Government. AzSD was in loss position in 2016 and 2015, therefore, no corporate income tax related to Shah Deniz project was recognized for 2016 and 2015. At 31 December 2016 and 2015 deferred tax balance of AzSD was nil. AzSD is also exempt from certain ordinary operational taxes in the Azerbaijan Republic.

The Group operates in the tax environment of Turkey through its subsidiary, STEAS. Income tax rate in Turkey is 20 per cent. In accordance with the tax legislation of Turkey dividends paid to non-resident corporations, which have a place of business in Turkey are not subject to withholding tax that is 15 per cent. Corporate income taxes are payable quarterly. Besides that there are many exemptions in Corporate Tax Law of Turkey regarding corporations including deduction of investment incentives from fiscal gains during determination of tax base up to 25 per cent.

The Group's subsidiaries – SOCAR Overseas LLC, Azerbaijan (SCP) LTD, SOCAR Polymer LLC, Baku Shipyard LLC and Sermaye Investment Limited are exempt from taxation.

34 Advances received for sale of interest

In July 2014, the Group signed a Deferred Sales Purchase Agreement ("DSPA") to sell its 10 per cent interest in Shah Deniz PSA and 10 per cent interest in SCPC (together referred as "Interest") to SGC. According to the terms of this agreement SGC shall pay advance for these acquisitions to SOCAR, while control will pass to SGC in 2023 upon meeting of conditions preceding sale. As of 31 December 2016, total consideration, received for the interest in Shah Deniz PSA and SCPC amounted to AZN 2,897 (USD 1,636 million) (2015: AZN 2,097 (USD 1,346 million)). In addition, DSPA specifies certain progress payments related to acquisition consideration payable annually till the end of 2020.

35 Put option liabilities

On 12 August 2015, 891 million newly issued shares, representing 13 per cent of capital of STEAS, a subsidiary of the Group, were purchased by Goldman Sachs International ("GSI") in exchange for AZN 1,364 (USD 1,300 million).

At the same time, the Group entered into a put option agreement with GSI, whereby the Group has committed to purchase back the shares held by GSI, at a specified price, in case if the planned initial public offering of STEAS does not occur, or to settle the put option in case if certain conditions provided by the put option agreement are not met. Put option provided by the Group to GSI will be valid for 6 years following the signing of the put option agreement and represents non-current financial liability. At 31 December 2016 the fair value of the put option liability amounted to AZN 2,300 (USD 1,300 million).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

35 Put option liabilities (continued)

Analysis of the put option liability and gain on sale of subsidiary shares is as follows:

Sale amount of STEAS 13 per cent shares	1,364
The net book value of the shares sold	(238)
Gain on sale of STEAS 13 per cent shares	1,126
 Sale amount of shares of other subsidiaries	 75
The net book value of shares of other subsidiaries sold	(89)
Net gain on sales of subsidiary shares	1,112

The Group also has put option liability in the amount of AZN 443 (USD 250 million) (2015: AZN 390 (USD 250 million)) related to the put option agreement signed between STEAS and GSI in 2014 regarding 30 per cent shares of Petlim Limancılık Ticaret A.S. and additional liability in the amount of AZN 89 (USD 50 million) (2015: AZN 75 (USD 50 million)) derived from payment received from GSI in 2014 and repayable by STEAS according to the mentioned put option agreement.

36 Significant non-cash investing and financing activities

Investing and financing transactions that do not require the use of cash and cash equivalents and were excluded from the cash flow statement are as follows:

	2016	2015
Non-cash investing and financing activities		
Financing of Carbamid Plant construction through factoring arrangement	197	–
Transfer of account receivables to charter capital of joint venture	114	–
Capitalized decommissioning costs	83	6
Capital expenditures under carried interest arrangement	57	141
Transfer of property, plant and equipment to the Government (Note 27)	–	(13)
Non-cash investing and financing activities	451	134

37 Contingences, commitments and operating risks

Operating environment

The Group's operations are mainly conducted in the Azerbaijan Republic. As an emerging market, at the present time the Azerbaijan Republic is developing business and regulatory infrastructure that would generally exist in a more mature market economy.

Considering significant drop in crude oil prices beginning from the second half of 2014 and thereafter, there continues to be uncertainty regarding economic growth, access to capital and cost of capital, which could negatively affect the Group's future financial position, results of operations and business prospects. Moreover, Azerbaijani Manat has been devalued against major currencies by approximately 34 and further 48 per cent on 21 February 2015 and 21 December 2015, respectively. During 2016, Azerbaijani Manat fluctuated between AZN 1.4900 and AZN 1.7707 for 1 USD.

The future economic direction of the Azerbaijan Republic is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments. International credit rating agencies regularly evaluate credit rating of the Azerbaijan Republic and the Group. Subsequently Fitch and S&P have evaluated rating of the Group and rating of the Azerbaijan Republic as "BB+". Moody's Investors Service has kept the previous "Ba1" rating. Management is unable to predict all developments in the economic environment which would have an impact on the Group's operations and consequently what effect, if any, they could have on the financial position of the Group.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Operating environment (continued)

The Azerbaijani economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. While the Azerbaijan Government has introduced a range of stabilization measures and as management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

The Group's activities in Ukraine are exposed to, amongst others, low levels of liquidity in the capital markets and the existence of currency controls which cause the national currency to be illiquid outside of Ukraine. The stability of the Ukrainian economy will be significantly impacted by the Government's policies and actions with regard to administrative, fiscal, legal, and economic reforms. As a result, operations in Ukraine involve risks that are not typical for developed markets. The Ukrainian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world.

Significant changes occurred in operating environment and political situation in Ukraine at the end of 2013 – beginning of 2014, which resulted in political and economic instability and continued to deteriorate significantly further. From 1 January 2016 to 31 December 2016, the Ukrainian Hryvnia (the "UAH") depreciated against major foreign currencies by approximately 12 and 8 per cent calculated based on the National Bank of Ukraine's ("NBU") exchange rates of UAH to US Dollar and Euro, respectively (from 1 January 2015 to 31 December 2015: 52 and 36 per cent respectively) and NBU continues to extend previously imposed restrictions on purchase of foreign currencies at the inter-bank market, cross border settlements (including payment of dividends) and also mandated obligatory conversion of foreign currency proceeds into UAH. The international rating agencies have downgraded sovereign debt ratings for Ukraine. The combination of the above events has resulted in a deterioration of liquidity and much tighter credit conditions where credit is available. Management is monitoring these developments in the current environment and taking actions where appropriate. Further negative developments, including the political unrest, could adversely affect the Group's subsidiary, SOCAR Energy Ukraine's results and financial position in a manner not currently determinable. These consolidated financial statements do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the period when they become known and estimable.

Legal proceedings

From time to time and in the normal course of business, claims against the Group are received. On the basis of its own estimates and both internal and external professional advice management is of the opinion that no material losses will be incurred in respect of claims in excess of provisions that have been made in these consolidated financial statements.

Tax legislation

Azerbaijan tax, currency and customs legislation is subject to varying interpretations, and changes, which may occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant authorities.

Fiscal periods remain open to review by the tax authorities in respect of taxes for three calendar years preceding the year of tax audit. Under certain circumstances such reviews may cover longer periods.

The Group's management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency legislation and customs positions will be sustained and potential tax liabilities of the Group will not exceed the amounts recorded in these consolidated financial statements. Accordingly, at 31 December 2016 and 2015 no provision for potential tax liabilities had been recorded.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Environmental matters

The enforcement of environmental regulation in the Azerbaijan Republic is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognized immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage above environmental obligation provision currently made by the Group. See Note 23.

The Group is subject to numerous national and local environmental laws and regulations concerning its products, operations and other activities. These laws and regulations may require the Group to take future action to remediate the effects on the environment of prior disposal or release of chemicals or petroleum substances by the Group or other parties. Such contingencies may exist for various sites including refineries, chemical plants, oil fields, service stations, terminals and waste disposal sites. In addition, the Group may have obligations relating to prior asset sales or closed facilities. The ultimate requirement for remediation and its cost are inherently difficult to estimate. However, the estimated cost of known environmental obligations has been provided in the consolidated financial statements in accordance with the Group's accounting policies. While the amounts of future costs could be significant and could be material to the Group's results of operations in the period in which they are recognized, it is not practical to estimate the amounts involved. The Group does not expect these costs to have a material effect on the Group's financial position or liquidity.

The Group also has obligations to decommission oil and natural gas production facilities and related pipelines. Provision is made for the estimated costs of these activities, however there is uncertainty regarding both the amount and timing of these costs, given the long-term nature of these obligations.

The Group believes that the impact of any reasonably foreseeable changes to these provisions on the Group's results of operations, financial position or liquidity will not be material.

Compliance with financial covenants

At 31 December 2016 the Group had loans payable in total amount of AZN 14,927 (2015: AZN 10,911) which were received for financing its investing and operating activity. The Group is subject to certain financial covenants related to these borrowings. Non-compliance with such covenants may result in negative consequences for the Group including growth in the cost of borrowings and declaration of default. Management believes that, as of 31 December 2016 and 2015 the Group was in compliance with all applicable financial covenants.

Commitments of Petkim

During 2015 Petlim Limancılık Ticaret A.Ş., where Group subsidiary Petkim owns 70 per cent shares, has signed a project finance credit agreement with AKBANK T.A.Ş. in the amount of USD 212 million (AZN 375) which has 13 years of maturity with no repayment during first 3 years period, for the external funding of the container port project. Petkim has pledged its shares in Petlim amounting to TRY 105 million (AZN 53) as a guarantee for the loan repayment. The project has financial ration liabilities that are valid during the operating period. Additionally, a mortgage amounting to USD 350 million (AZN 620) million was established by Petkim on Petlim's land sold.

At 31 December 2016 STEAS has a commitment to purchase 943,746,586 cubic meters of natural gas from BOTAS Petroleum Pipeline Corporation ("BOTAS") in 2017.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Guarantee received and given by Petkim

The following table demonstrates guarantees received and given by the Group at 31 December:

	2016	2015
Guarantees received		
Bank guarantees within the context of direct order collection system (DOCS)	247	321
Letters of guarantee received from customers	145	174
Letters of guarantee received from suppliers	96	90
Receivable Insurance	42	41
Letters of credit received	48	–
Other	2	2
Total guarantees received	580	628
Guarantees given		
Letters of guarantee given	604	354
Total guarantees given	604	354

Commitment of Azerigas PU

Based on Presidential Decree number 118 dated 27 February 2014, directed to social-economic development of Baku area and regions of the Republic of Azerbaijan, Azerigas PU has certain commitments with respect to improvement of gasification options in mentioned areas for years 2014-2018. According to this decree, Azerigas PU would be engaged in restoration of old local gas pipelines, continue gasification of new residential communities/regions/far locations, and renewal of old industrial and personal meters for physical customers.

Management believes that these expenditures will continue to be financed by the Government through contributions into capital.

Gas purchase commitment

Based on the Gas Sales and Purchase Agreement signed on 27 February 2003 between Azerbaijan Gas Supply Company ("AGSC") and the Ministry of Fuel and Energy of the Azerbaijan Republic (currently purchase rights under this agreement are executed by the Group), the Group has obligation to purchase seller's minimum annual quantity as indicated in the agreement for the period beginning from signing of the contract up to the termination date of Shah Deniz PSA. As at 31 December 2016 monetary amount of commitment to purchase seller's minimum annual quantity is USD 87 million (AZN 154) (2015: USD 87 million (AZN 136)).

Shah Deniz Debottlenecking agreement was signed between AGSC and SOCAR on 17 December 2013. Based on agreement the Group agreed to buy additional volume of (Low Pressure) Gas from Shah Deniz field. The Annual contractual volume of gas in the first delivery year (for year 2014) was defined as 0.65 bcm. The annual contractual volume for each delivery year, other than the first and the last delivery years is defined as 1.3 bcm (being 0.75 bcm in Turkey and 0.55 bcm in Azerbaijan). The contractual volume of gas to be made available in the last delivery year (1 January 2018 – 30 June 2018) is 0.64 bcm (being 0.37 bcm in Turkey and 0.27 bcm in Azerbaijan).

Participating interest in ACG PSA

Azerbaijan International Operating Company, the Operator of the ACG PSA has entered into a number of capital commitments and operating leases as at 31 December 2016. The Group estimated its 11.65 per cent (2015: 11.65 per cent) share of these commitments and operating leases to be USD 238 million (AZN 421) (2015: USD 462 million (AZN 720)) and USD 22 million (AZN 39) (2015: USD 17 million (AZN 26)), respectively.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Commitments related to participating interest in Shah Deniz

On 17 December 2013, Shah Deniz consortium announced the final investment decision for Stage 2 development of Shah Deniz gas field in the Azerbaijan Sector of the Caspian Sea and signed certain Addendums to Shah Deniz Exploration and Development and Production Sharing Agreement ("SD EDPSA"). According to the Eighth Addendum to SD EDPSA the parties agreed to extend the development and production period to 46 years ending on 6 March 2047. This extension is conditional upon execution of the additional work program where Contractor parties shall spend no less than USD 25 million (AZN 20) by 31 December 2018.

BP Exploration Shah Deniz Limited, the Operator of the Shah Deniz PSA has entered into a number of capital commitments and operating leases as at 31 December 2016. The Group estimated its 13.27 per cent share of these capital commitments and operating leases through its subsidiary and associate to be USD 1,372 million (AZN 2,430) (2015: USD 1,922 million (AZN 2,997)) and USD 66 million (AZN 117) (2015: USD 43 million (AZN 67)), respectively.

Commitments related to participating interest in AGSC

The Group holds 28 per cent direct interest in AGSC and indirect 2.62 per cent through its associate. In accordance with the agreements of AGSC the Group has the following commitments relating to AGSC's activity:

Stage 2 Gas Contract

On 25 October 2011 the Group and BOTAS executed a gas Sale and Purchase Agreement ("Stage 2 SPA") with respect to the sale by the Group to BOTAS of certain volumes of Shah Deniz Stage 2 Gas (2 bcm first delivery year, 4 bcm second delivery year, 6 bcm plateau period). In December 2012, the Group transferred and assigned the rights and obligations under the Stage 2 SPA to AGSC. The anticipated commencement of the first gas delivery under Stage 2 BOTAS SPA will be between 1 January and July 2018.

AGSC sales to BOTAS through BTC Co.

AGSC is obliged under the agreement with BOTAS to make available 0.16 bcm of gas annually from 2016 till 2019 at a price which is calculated based on a formula established in the contract.

Georgian gas obligation

AGSC is obliged under the agreement signed with Georgian Oil and Gas Corporation ("GOGC") and the government of Georgia to make available 0.5 bcm of gas in 2016 and onwards, at a price which is calculated based on a formula established in the contract.

Sale and purchase agreement with OptionCo.

AGSC is obliged under the agreement signed with OptionCo to make available 0.29 bcm of gas during the contract year started on 1 October 2015 and ending 1 September 2016. Thereafter, AGSC is obliged to deliver during the next contract year, which starts on 1 October 2016 and ends 30 September 2017, 0.3 bcm (a maximum of five percent of the volumes transported by AGSC through Georgia via the SCP in the previous contract year), at a price which is calculated based on a formula established in the contract.

BOTAS SPA

AGSC is obliged under the Gas contract signed with BOTAS to make available a maximum of approximately 6.6 bcm of gas annually from 2017 till 2021 at a price calculated based on a formula established by the Gas contract.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Commitments related to participating interest in AGSC (continued)

Shah Deniz Stage 2 EU Long term Gas Sales Agreements ("GSA")

In September 2013, ten EU GSA were signed by the Group with nine EU Buyers and in December 2013 the GSA were assigned to AGSC until Shah Deniz PSA expiry with re-assignment to the Group as Shah Deniz Production declines. The commencement date will be firmed up through funnelling mechanism within a 1-year window between 1 January 2020 and 1 January 2021 for DEPA, Shell, Axpo (PSV) and E.On; 1 July 2020 and 1 July 2021 for Axpo (WTB), GDF Suez, Gas Natural Fenosa, Enel, Hera and Bulgargaz. The GSA assume 2-3 years build up period, as defined in the contract, and with the following peak annual delivery obligations: AXPO (PSV) 0.48 bcm, GDF Suez 2.64 bcm, Gas Natural Fenosa 0.99 bcm, E.On 1.45 bcm, Shell 0.95 bcm, Hera 0.3 bcm, Enel 0.48 bcm, AXPO (WTB) 0.96 bcm, Bulgargaz 0.94 bcm, DEPA 1 bcm.

Transportation agreement with SCPC

AGSC is party to SCPC Gas Transportation Agreement ("GTA"), dated 27 February 2003 which was subsequently amended and re-stated ("SCP GTA") with effect from 17 December 2013 in order to provide additional transportation services in respect of Shah Deniz Stage 2 volumes. AGSC is obliged to pay certain tariffs, as calculated in accordance with the agreement, to SCPC starting from the commencement date, which is 1 October 2006. The SCP GTA provides for Minimum Monthly Payments ("MMP"), as calculated in accordance with the subject agreement, payable by AGSC to SCPC, regardless of whether natural gas is shipped or not, in respect of each contract year until the termination or expiry of the GTA. MMPs are funded by BP Exploration (Shah Deniz) Limited ("BPX SD") as operator for and on behalf of the SD JOA Parties under the amended Annual Reserved Capacity Deed ("ARC Deed"). Annual Minimum Payment ("AMP") due in 2017 is USD 310 million (AZN 549), as calculated and presented to AGSC by SCPC in January 2016. In addition to AMP amount, AGSC shall pay to SCPC Incremental Monthly Charges calculated in accordance with the GTA. Further, AGSC is obliged to provide SCPC, free of charge, the natural gas necessary to fill and pressurize the pipeline to its designed operating pressure and used as fuel gas.

Framework agreement

On 17 December 2013, AGSC executed a Term Sheet for GSA Novation and Capacity Transfer Framework Agreement with SOCAR ("Term Sheet"). A fully-termed Framework Agreement was negotiated with SOCAR to give effect to the Term Sheet. Framework Agreement relates to novation of long-term GSAs and transfer of GTA capacity between SOCAR and AGSC after 2036. The Framework Agreement was executed on 19 October 2015.

Trans Anatolian Pipeline Gas Transportation Agreement (TANAP GTA)

AGSC is a party to TANAP GTA with annual reserved capacity during the build-up period, as defined in the contract, of 6.1 bcm, 6.2 bcm, 7.2 bcm and plateau of 10.5 bcm after 18 months with 100 per cent ship or pay on the capacity reservation. The start date will be set through a funnelling mechanism inside the first window period between 1 July 2019 – 1 July 2021.

Trans Adriatic Pipeline Gas Transportation Agreement (TAP GTA)

AGSC is a party to TAP GTA with annual capacity of 9.08 bcm and additional annual regulated capacity of 0.46 bcm booked under TAP First Booking Phase ("FBP"). The planned commencement date is inside the second window period between 1 January 2020 – 31 December 2020.

Sale and purchase agreement with Baku-Tbilisi-Ceyhan Pipeline Company ("BTC Co")

AGSC is obliged under the Fuel Gas Sales and Purchase Agreement between AGSC and BTC Co, dated 30 November 2007 ("BTC SPA") to make 0.16 bcm during the following years until the termination of the contract subject to the right of BTC to reduce annual off-take, at a price which is calculated based on a formula established in the contract.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Oil shipment commitment

On 1 August 2002 the Group and other participants under the ACG PSA (the "Shipper Group") have entered into the ACG Field Production Transportation Agreement ("ACG TA") with the BTC Co which was amended on 3 February 2004. Under this Agreement, the Shipper Group have committed to ship through the BTC Pipeline all of their crude oil entitlement from the ACG field, other than any production which each participant may ship through the Western Export Route. The Group has agreed to transport its crude oil by rail unless BTC Co is operating at its full capacity. In accordance with ACG TA the Group has agreed not to use other transportation options if capacity of the BTC Co is sufficient. The BTC Pipeline was put into operation in May 2006.

The BTC Pipeline, with a throughput capacity of more than 1,200,000 barrels per day, is used as the Shipper Group's main export route. In accordance with the Transportation Agreement, the Shipper Group, the Group Representative, the lenders and security trustee to BTC Co, and the lenders and security trustee to certain participants of the ACG Shipper Group have agreed that payment of BTC Co tariff has a first priority claim on oil sale proceeds.

Commitments of SOCAR Switzerland

The Group has entered into a number of operating leases for the next years. The Group estimated its operating leases to be CHF 102 million (AZN 177).

Commitments of SOCAR Overseas

The Group has entered into number of Letter of Credit agreements during November and December 2016 with different banks (CA Indosuez, ING, Natixis, Societe Generale and etc.) against various shipments. As at 31 December 2016 the Group has outstanding amount in the amount of USD 250 million (AZN 458).

Commitment of SOCAR Energy Georgia

For the purposes of supplying natural gas in regions of Georgia and raising funds for investing in respective sphere, based on agreement formed with the Ministry of Economy of Georgia in 2008, the Group had to invest USD 40 million (AZN 31) and provide natural gas to additional 150,000 subscribers. However, on 19 December 2013 the terms of this commitment were amended and a new decree # 1988 of the government of Georgia was approved. According to this decree the commitment of investing in gas network increased to USD 250 million (AZN 443) and the number of new gas subscribers increased to 250,000. According to decree the maturity of commitment was defined to be 3 year beginning from conducting amendment agreement which is signed on 8 December 2014 by both parties.

As of 31 December 2016 SOCAR Energy Georgia had guarantees to banks in the total amount of AZN 16 in favour of third parties that engaged in the gasification process.

Commitments of Baku Shipyard LLC

At 31 December 2016, the Group had capital commitments to third parties in the amount of AZN 46 (2015: AZN 66) in respect of construction contracts.

Commitments of SOCAR Head Office

According to Equity Subscription Support and Retention Agreement ("ESSRA") which had been signed as a part of STAR Project Finance deal, the Group concluded letter of credit ("LC") facility agreements in the total amount of USD 1,429 million (AZN 2,228) with certain banks (The Lenders).

The LCs are intended to provide security to the Lenders for the unpaid portion and to serve as the credit support of the Project in case there would be cost overruns exceeding the contingency amount designated in the Project budget. The outstanding amount of LCs as of 31 December 2016 was USD 514 million (AZN 910) (2015: USD 1,269 million (AZN 1,979)).

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

Commitment related to SCP Expansion

Shah Deniz PSA Contractor Parties made the final investment decision on SCP Expansion project on 17 December 2013. SCP Expansion project objective is to expand the existing SCP pipeline system capacity. Due to SCP expansion additional facilities will be constructed in Georgia for the purposes of interconnection with TANAP. The Group has the commitment to fund the SCP Expansion project throughout the construction and initial operational phase.

The SCP Expansion remaining construction budget is estimated in the amount of USD 1,607 million (AZN 2,846) (the Group's 13.27 per cent share through its subsidiary and associate: USD 213 million (AZN 378)).

Construction of TANAP

At the financial statement date, the Group has capital commitment to fund construction of TANAP pipeline system. Remaining budget for construction of TANAP system is estimated in the amount of USD 5,028 million (AZN 8,903) (2015: USD 8,112 million (AZN 12,649)) and the Group's share through its associate at the financial statement date was USD 2,464 million (AZN 4,363) (2015: USD 3,975 million (AZN 6,198)).

Construction of TAP

The Group has the commitment to fund construction of TAP pipeline system. The remaining budget for construction of the TAP system is estimated in the amount of USD 3,121 million (AZN 5,527) (2015: USD 4,338 million (AZN 6,764)). The Group's share of commitment through its associate at the financial statement date was USD 306 million (AZN 542) (2015: USD 425 million (AZN 663)).

Commitments of SOCAR Trading S.A ("SOCAR Trading")

The Group has entered into a number of operating leases for the next years. The Group estimated its operating leases to be USD 62 million (AZN 110).

Deferred Sale and Purchase Agreement with SGC

According to Deferred Sale and Purchase Agreement ("DSPA") signed with SGC Upstream LLC and SGC Midstream LLC the Group agrees to sell its whole interest in Shah Deniz PSA, AGSC and SCPC in March 2023 upon meeting of the following conditions preceding sale:

- The full and unconditional repayment of the notes and fulfilment of other obligations under the Eurobonds agreements by SOCAR; and
- Confirmation of the payment of full consideration amount in accordance with agreement terms.

Commitment under the funding agreement with BOTAS (the "Funding Agreement")

On 26 May 2014 SOCAR and BOTAS signed Funding Agreement for financing BOTAS's 5 per cent shares in TANAP A.Ş., upon acquisition of shares in TANAP A.Ş. by BOTAS. Following the sale of Tanap to SGC, on 13 March 2015, the Group signed novation agreement with SGC and BOTAS, where all rights and obligations under the Funding Agreement were transferred from SOCAR to the SGC. According to agreement with BOTAS, the SGC has commitment for providing interest free loan to BOTAS for financing its 5 per cent share in TANAP A.Ş.'s future cash call requirements till TANAP becomes operational. The Group commitment in this financing equals to its share in SGC.

BOTAS Gas Transportation Agreement (BOTAS GTA)

TANAP is a party to BOTAS GTA and with annual reserved capacity during the build-up period, as defined in the contract, of 1.9 bcm (12 month period commencing on start date), 3.8 bcm (next 12 month period) and plateau of 5.7 bcm 24 months after the start date. The start date will be within the period from and including 1 May 2018 to and including 30 June 2018.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

37 Contingences, commitments and operating risks (continued)

SOCAR Gas Transportation Agreement (SOCAR GTA)

Based on this GTA, from and including the start date (6 March 2036) SOCAR shall pay to TAP AG the amount of actual monthly charge in relation of each booking of reserved capacity at each entry point and exit point at a price which is calculated based on the formula established in the contract.

TAP Deferral Gas Sales Agreement

The Group is obliged under the agreement signed with AGSC to Purchase minimum annual quantity of gas as indicated in the agreement during the period 1 May 2019 – 31 December 2020 (or until an earlier termination of the agreement in accordance with provisions of the agreement) at a price which is stipulated in the contract.

Feedstock supply agreement

On 20 June 2014 the Group and SOCAR Polymer signed a feedstock supply agreement according to which the Group bears obligation to supply ethylene and propylene at 44 per cent and 40 per cent discount of market price, respectively. SOCAR Polymer expects to start its production process in 2017.

Commitments of SOCAR Polymer

During 2015, SOCAR Polymer LLC signed agreements for provision of design, engineering, procurement, all onshore work and offshore assistance required for commissioning and testing for the polypropylene plant, high density polyethylene plant and utilities and off-sites. Total contract price of agreements is USD 503 million (AZN 891). During 2016, the SOCAR Polymer LLC incurred cost of USD 212 million (AZN 375) on the mentioned services.

38 Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business and goodwill

Goodwill

Movement in the carrying amount of goodwill was as follows:

	2016	2015
Carrying amount at 1 January	275	177
Translation difference	67	98
Carrying amount at 31 December	342	275

The carrying amount of goodwill as of 31 December 2016 and 2015 includes an accumulated goodwill impairment of AZN 3.

Allocation of goodwill by CGUs at 31 December 2016 and 2015 were as following:

	2016	2015
SOCAR Switzerland	116	105
SOCAR Trading	110	48
Petkim	98	104
Other	18	18
Carrying amount at 31 December	342	275

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

38 Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business and goodwill (continued)

Testing of the carrying value of goodwill related to acquisition of Petkim

The carrying value of the goodwill at 31 December 2016 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined in the amount of AZN 3,291 based on the value-in-use calculations of Petkim. Pre-tax cash flows projections used for this purpose are based on financial budgets approved by management covering 5-year period. Cash flows for 5-year period are based on existing long-term projects with duration until 2021. Cash flow projections beyond 5-year period are extrapolated by the expected growth rates and then discounted to their net present value.

The valuation exercises are highly sensitive to the range of EBITDA / Net Sales and the WACC, which were taken into account by the Group as 11.7 per cent – 17.4 per cent and 9.1 per cent between 2017 and 2021, respectively.

As a result of the test performed, no impairment has been identified.

A sensitivity analysis is conducted by changing the assumptions used in the estimation of Petkim carrying amount of the value in use in relation to the key parameters that are described below:

- ▶ If the estimated discount rate used in the calculation had been 0.4 per cent higher/lower than management's estimate, the value in use would have been AZN 201 lower / AZN 229 higher, respectively;
- ▶ If the terminal growth rate used in the calculation had been 0.5 per cent higher/lower than management's estimate, the carrying amount of the value in use would have been AZN 240 higher / AZN 204 lower, respectively.

As a result of the sensitivity analysis no impairment losses were identified.

Testing of the carrying value of goodwill related to acquisition of SOCAR Switzerland

The carrying value of the goodwill at 31 December 2016 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined based on the value-in-use calculations of SOCAR Energy Holdings AG and its subsidiaries as AZN 879 as of 31 December 2016. Pre-tax cash flows projections used for this purpose are based on annual business plan approved by management covering 5-year period. Management believes that the underlying cash flows projections represent accurate and reliable forecast. Cash flow projections beyond 5 year period are extrapolated by expected growth rates of 1.5 per cent p.a. and then discounted to their net present value, applying WACC, used as a discount factor of 6 per cent p.a.

As a result of the test performed, no impairment was identified.

If the estimated discount rate used in the calculation had been 1 per cent higher/lower than management's estimate, the value in use would have been AZN 161 lower / AZN 253 higher, respectively.

If the terminal growth rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the carrying amount of the value in use would have been AZN 43 higher / AZN 38 lower, respectively.

As a result of the sensitivity analysis no impairment losses were identified.

Testing of the carrying value of goodwill related to acquisition of SOCAR Trading

The carrying value of the goodwill attributable to the acquisition of SOCAR Trading at 31 December 2016 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined based on the value-in-use calculations of SOCAR Trading and its subsidiaries as AZN 1,153 as of 31 December 2016. Cash flow projections used for this purpose are based on financial forecast approved by management covering 5-year period. Cash flows for that period are based on existing and new projects and discounted to their net present value. Management believes that these cash flow projections represent accurate and realistic forecast. Cash flow projections beyond 5-year period have terminal growth rate of 1 per cent.

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

38 Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business and goodwill (continued)

Testing of the carrying value of goodwill related to acquisition of SOCAR Trading (continued)

The following key assumptions were used for impairment test of the goodwill:

- ▶ Valuation exercise is sensitive to the range WACC, which were taken into account by the Group, as 12 per cent;
- ▶ Valuation is also sensitive to terminal growth rate which is taken into account by the Group as 1 per cent.

As a result of the test performed, no impairment had been identified.

If the estimated discount rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the carrying amount of the value in use would have been AZN 23 lower / AZN 23 higher, respectively.

If the terminal growth rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the carrying amount of the value in use would have been AZN 18 higher / AZN 18 lower, respectively.

As a result of the sensitivity analysis no impairment losses were identified.

39 Material partly-owned subsidiaries

Financial information of subsidiaries that have material non-controlling interests is provided below:

The Group's subsidiaries with material non-controlling interests are Petkim Petrokimya Holding A.Ş and Star Gulf FZCO. Country of incorporation and operation of Petkim is Turkey. Country of incorporation and operation of Star Gulf FZCO is United Arab Emirates (UAE) and Azerbaijan, respectively.

Proportion of equity interest held by non-controlling interests:

Name	Country of incorporation	Country of operation	2016	2015
Petkim	Turkey	Turkey	48%	41%
Star Gulf FZCO	UAE	Azerbaijan	20%	20%

Accumulated balances of material non-controlling interests:

Name	2016	2015
Petkim	1,206	1,061
Star Gulf FZCO	87	32

Profit allocated to material non-controlling interests:

Name	2016	2015
Petkim	161	84
Star Gulf FZCO	79	21

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

39 Material partly-owned subsidiaries (continued)

The summarised financial information of these subsidiaries, based on amounts before inter-company eliminations, is provided below:

Summarised statement of profit or loss for 2016:

	Petkim	Star Gulf FZCO
Revenue	2,392	506
Cost of Sales	(1,924)	(95)
General and administrative expenses	(82)	(1)
Distribution expenses	(23)	–
Other operating income	117	10
Other operating expense	(139)	–
Finance income	200	–
Finance costs	(179)	–
Foreign exchange loss	–	(4)
Profit before tax	362	416
Income tax expense	(26)	(22)
Profit for the year from continuing operations	336	394
Other comprehensive (loss)/income to be reclassified to profit or loss in subsequent periods – currency translation differences	(148)	41
Total comprehensive income	188	435
Attributable to non-controlling interests	90	92
Dividends paid to non-controlling interests	114	37

Summarised statement of profit or loss for 2015:

	Petkim	Star Gulf FZCO
Revenue	1,706	196
Cost of Sales	(1,464)	(85)
General and administrative expenses	(52)	(1)
Distribution expenses	(12)	–
Other operating income	49	2
Other operating expense	(70)	–
Finance income	159	–
Finance costs	(137)	–
Foreign exchange loss	–	(4)
Profit before tax	179	108
Income tax benefit/(expense)	25	(7)
Profit for the year from continuing operations	204	101
Other comprehensive income to be reclassified to profit or loss in subsequent periods – currency translation differences	871	59
Total comprehensive income	1,075	160
Attributable to non-controlling interests	441	29

*(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)***39 Material partly-owned subsidiaries (continued)**

Summarised statement of financial position as at 31 December 2016:

	Petkim	Star Gulf FZCO
Current assets	1,340	484
including:		
<i>Cash and cash equivalents</i>	637	281
<i>Trade and other receivables</i>	354	201
<i>Inventories</i>	307	2
<i>Other current assets</i>	42	–
Non-current assets	2,949	19
including:		
<i>Property, plant and equipment</i>	2,188	18
<i>Intangible assets</i>	383	1
<i>Other non-current assets</i>	378	–
Current liabilities	(903)	(66)
including:		
<i>Short-term borrowings and current portion of long-term borrowings</i>	(260)	–
<i>Trade and other payables</i>	(643)	(66)
Non-current liabilities	(873)	–
including:		
<i>Long-term borrowings</i>	(589)	–
<i>Deferred income</i>	(65)	–
<i>Other provisions for liabilities and charges</i>	(50)	–
<i>Deferred tax liabilities</i>	(169)	–
Total equity	2,513	437
Attributable to:		
Equity holders of parent	1,307	350
Non-controlling interests	1,206	87

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

39 Material partly-owned subsidiaries (continued)

Summarised statement of financial position as at 31 December 2015:

	Petkim	Star Gulf FZCO
Current assets	1,486	246
including:		
<i>Cash and cash equivalents</i>	719	176
<i>Trade and other receivables</i>	436	62
<i>Inventories</i>	197	1
<i>Other current assets</i>	134	7
Non-current assets	2,705	36
including:		
<i>Property, plant and equipment</i>	2,073	35
<i>Intangible assets</i>	419	1
<i>Other non-current assets</i>	213	–
Current liabilities	(849)	(121)
including:		
<i>Short-term borrowings and current portion of long-term borrowings</i>	(194)	–
<i>Trade and other payables</i>	(655)	(121)
Non-current liabilities	(754)	–
including:		
<i>Long-term borrowings</i>	(490)	–
<i>Deferred income</i>	(36)	–
<i>Other provisions for liabilities and charges</i>	(48)	–
<i>Deferred tax liabilities</i>	(180)	–
Total equity	2,588	161
Attributable to:		
Equity holders of parent	1,527	129
Non-controlling interests	1,061	32

Summarised cash flow information for year ended 31 December 2016:

	Petkim	Star Gulf FZCO
Operating	244	195
Investing	(214)	3
Financing	(164)	(118)
Net foreign exchange difference on cash and cash equivalents	95	–
Net (decrease)/increase in cash and cash equivalents	(39)	80

Summarised cash flow information for year ended 31 December 2015:

	Petkim	Star Gulf FZCO
Operating	324	122
Investing	(277)	(4)
Financing	120	(16)
Net foreign exchange difference on cash and cash equivalents	73	–
Net increase in cash and cash equivalents	240	102

(Amounts presented are in millions of Azerbaijani Manats, unless otherwise stated)

40 Events after reporting date

Increase in Additional Paid in Capital

On 3 February 2017 the Group's additional paid in capital was increased by the Government of the Azerbaijan Republic in the amount of AZN 143.

New Loans

During subsequent period, the Group obtained new long-term loans in the amount of AZN 798 (USD 457 million), AZN 186 (EUR 101 million) and AZN 254 (GEL 368 million) from local and international banks. In addition, the Group obtained new short-term loan in the amount of AZN 140 (USD 82 million) from local bank.

Bond repayment

On 6 February 2017 the Group fully repaid AZN 185 (USD 97 million) of its outstanding 5.45 per cent senior unsecured notes (with original balance of USD 500 million) due on 9 February 2017.

Issue of notes

On 10 March 2017 the Group's associate – SGC issued AZN 1,720 (USD 1 billion) senior unsecured notes guaranteed by the Azerbaijan Republic ("Notes") bearing interest rate of 6.875 per cent per annum with maturity due on 24 March 2026.

Declaration of dividends by associate

During subsequent period the Group's associate - BTC Co declared dividends in the amount of AZN 72 (USD 42 million) that were fully paid to the Group.

Investments

During subsequent period the Group has made additional investment in its associate – SGC and joint venture – Azerbaijan Rigs LLC in the amount of AZN 140 and AZN 19, respectively.

On 29 May 2017 the Group purchased 16.34 per cent shares of SOCAR Energy Georgia for the consideration in the amount of AZN 58 (USD 34 million). As a result, the Group's controlling ownership in SOCAR Energy Georgia increased from 51 per cent to 67.34 per cent.

Sale of Petkim's shares

On 8 March 2017, the Group sold its 1.32 per cent shares of Petkim Petrokimya Holding A.Ş for consideration in the amount of AZN 42 (TRY 88 million) and as a result, the Group's controlling ownership in Petkim Petrokimya Holding A.Ş decreased from 52.32 per cent to 51 per cent.

Prepayment for acquisition of Methanol Plant

During subsequent period the Group signed an agreement with related party for acquisition of methanol production assets (the Plant) in the amount of AZN 810. According to the agreement the Group has made AZN 394 prepayment to the seller. The control over the Plant was not transferred to the Group.

Government Grant

According to the decree of National Assembly dated 30 June 2017, the Group will receive government grant in the amount of AZN 250 in 2017 as a compensation of losses incurred from sale of natural gas and heating oil for the purpose of meeting local demand in the country.