



Shamal Az Zour Al Oula For The Building, Execution, Operation, Management, and Maintenance of The First Phase of Az Zour Power Plant KSC (Public) Kuwait

**Independent Auditor's Report And Financial Statements
31 December 2017**



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Shamal Az-Zour Al-Oula K.S.C. (Public)
Directors' Report for the year ended 31 December 2017

Dear Shareholders

On behalf of the Board of Directors of the Company, it gives me great pleasure to present the Board of Directors' Report for the year ended 31 December 2017.

1. Operational performance

Shamal Az-Zour Al-Oula K.S.C. (Public) is the Company established to build, operate and eventually to transfer the power and water facility known as Azzour North Phase 1.

The primary service of the Company under the Energy Conversion and Water Purchase Agreement is to make available exclusively to the off-taker the Ministry of Electricity and Water (MEW) the capacity of the power and water plant and in return the Company will receive capacity payments based upon the demonstrated net dependable capacity. The secondary service of the Company is to sell to MEW (based upon its dispatch instructions) the electrical energy and water generated for a period of 40 years.

The Company is 60% owned by Kuwait public entities: 5% by the Kuwait Investment Authority, 5% by the Public Institution for Social Security and 50% by the Kuwait Authority for Partnership Projects. The remaining 40% is divided between the project sponsors; ENGIE (17.5%), Sumitomo Corporation (17.5%) and A.H. Al Sagar & Bros. (5%).

The operation and maintenance of the plant is carried out by an exclusive sub-contractor, AZN O&M Company (O&M Company) who took over the responsibility for plant operation and maintenance on the Plant Commercial Operation Date of 26 November 2016.

During 2017 the plant completed its first contract year of commercial operation from 26 November 2016 to 26 November 2017.

The plant has met its technical performance expectations in terms of available capacity and electricity generated and water produced.

As with any newly constructed and commissioned plant technical issues that have been found during early operation are being resolved via the Engineering, Procurement and Construction contract warranty process. The warranty will expire in November 2018.

2. Financial performance

The Company generated a net profit, before transfers to reserves, of KD 17.8 million.

No dividends are proposed.

3. Corporate governance

The Company has a Board of Directors with five members. The Board of Directors held ten meetings during 2017. None of the Directors received any remuneration from the Company during the year.

The day to management of the Company has been delegated to the Chief Executive Officer and the Chief Financial Officer.

4. Directors

The current directors of the Company are as follows:

Eng Yousef Mohammad Ali Alhajri – Chairman,

Sheikh Abdullah Jaber Al-Ahmad Al Sabah,

Dr David Barlow,

Mr Eric Maka and

Mr Paul Frain – Chief Executive Officer.

5. Appointment of auditor

The financial statements have been audited by Deloitte and Touche Al-Wazzan & Co. who retire and, being eligible, offer themselves for re-appointment.

6. Future plans

During 2018, the shares currently owned by the Kuwait Authority for Partnership Projects will be sold to Kuwaiti citizens.

The Company and the O&M Company will continue to operate the plant for the benefit of Kuwait in a responsible manner, with a focus on the health and safety of our employees and on minimizing our impact on the environment.

Signed by:

Yousef Mohammad Ali Alhajri
Chairman, Shamal Az-Zour Al-Oula K.S.C. (Public)
13 February 2018

Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of The First Phase of Az Zour Power Plant KSC (Public)

Statement of Financial Position as at 31 December 2017

		Kuwaiti Dinars	
	Note	2017	2016
ASSETS			
Current assets			
Cash and bank balances	3	30,400,748	23,135,419
Trade and other receivables	4	18,211,511	8,496,175
Finance lease receivable	5	10,171,603	9,790,001
		<u>58,783,862</u>	<u>41,421,595</u>
Non-current assets			
Finance lease receivable	5	489,391,262	502,342,137
Property, plant and equipment	6	99,620	-
Total assets		<u>548,274,744</u>	<u>543,763,732</u>
LIABILITIES AND EQUITY			
Liabilities			
Current liabilities			
Trade and other payables	7	10,181,427	26,310,733
Due to related parties	8	1,940,905	1,718,432
Term loans	9	11,897,457	11,692,367
Derivative financial liabilities	16	10,301,753	317,725
		<u>34,321,542</u>	<u>40,039,257</u>
Non-current liabilities			
Provision for staff indemnities		32,160	33,972
Term loans	9	388,062,342	385,062,529
Derivative financial liabilities	16	69,568,572	79,604,217
		<u>457,663,074</u>	<u>464,700,718</u>
Total liabilities		<u>491,984,616</u>	<u>504,739,975</u>
Equity			
Share capital	10	110,000,000	110,000,000
Statutory reserve	10	2,215,095	431,516
Voluntary reserve	10	2,215,095	431,516
Retained earnings		17,638,518	3,369,885
Foreign currency translation reserve		2,927,052	3,114,343
Hedge reserve	16	(78,705,632)	(78,323,503)
		<u>56,290,128</u>	<u>39,023,757</u>
Total liabilities and equity		<u>548,274,744</u>	<u>543,763,732</u>

The accompanying notes 1 to 20 are an integral part of these financial statements.

Eng. Yousef Mohammad Ali Alhajri
Chairman

Andrew Paul Frain
Chief Executive Officer

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SHAMAL AZ ZOUR AL OULA FOR THE BUILDING, EXECUTION, OPERATION, MANAGEMENT AND MAINTENANCE OF THE FIRST PHASE OF AZ ZOUR POWER PLANT KSC (PUBLIC)

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of The First Phase of Az Zour Power Plant KSC (Public) (the "Company"), which comprise the statement of financial position as at 31 December 2017, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2017 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 Financial Statements section of our report. We are independent of the Company 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.

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

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

In preparing the financial statements, management is responsible for assessing the Company'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 Company or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SHAMAL AZ ZOUR AL OULA FOR THE BUILDING, EXECUTION, OPERATION, MANAGEMENT AND MAINTENANCE OF THE FIRST PHASE OF AZ ZOUR POWER PLANT KSC (PUBLIC) (Continued)

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

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

Report on Other Legal and Regulatory Requirements

Furthermore, in our opinion proper books of account have been kept by the Company and the financial statements, together with the contents of the report of the Company's Board of Directors relating to these financial statements, are in accordance therewith. We further report that we obtained all the information and explanations that we required for the purpose of our audit and that the financial statements incorporate all the information that is required by the Companies Law No. 1 of 2016 and its Executive Regulations, as amended or by the Company's Memorandum of Incorporation and Articles of Association, that an inventory was duly carried out and that, to the best of our knowledge and belief, no violations of the Companies Law No. 1 of 2016 and its Executive Regulations, as amended or of the Company's Memorandum of Incorporation and Articles of Association, have occurred during the year ended 31 December 2017 that might have had a material effect on the business of the Company or on its financial position.



Bader A. Al-Wazzan
Licence No. 62A
Deloitte & Touche
Al-Wazzan & Co.

Kuwait
13 February 2018

Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of The First Phase of Az Zour Power Plant KSC (Public)

Statement of Profit or Loss and Other Comprehensive Income – year ended 31 December 2017

	Note	Kuwaiti Dinars	
		2017	2016
Revenue	11	46,199,813	9,292,700
Operating costs	12	(14,078,618)	(4,268,954)
Gross profit		32,121,195	5,023,746
Other income		646,290	45,883
Finance costs		(12,051,890)	(751,099)
Staff costs and related expenses		(778,647)	(173,989)
General and administrative expenses		(1,594,099)	(1,334)
Provision for doubtful debts	4	(160,000)	-
Profit before contribution to Kuwait Foundation for the Advancement of Sciences ("KFAS") and Zakat		18,182,849	4,143,207
KFAS	13	(163,646)	(37,289)
Zakat	14	(183,412)	(41,497)
Profit for the year		17,835,791	4,064,421
Other comprehensive income:			
<i>Items that may be reclassified subsequently to profit or loss:</i>			
Foreign currency (loss)/gain		(187,291)	25,588
Change in fair value of cash flow hedge (Note 16)		(382,129)	1,441,236
Total other comprehensive loss		(569,420)	1,466,824
Total comprehensive income for the year		17,266,371	5,531,245

The accompanying notes 1 to 20 are an integral part of these financial statements.

**Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of
The First Phase of Az Zour Power Plant KSC (Public)**

Statement of Changes in Equity – Year ended 31 December 2017

	Kuwaiti Dinars						
	Share capital	Statutory reserve	Voluntary reserve	Retained earnings	Foreign currency translation reserve	Hedge reserve	Total
Balance as at 1 January 2016	110,000,000	17,195	17,195	134,106	3,088,755	(79,764,739)	33,492,512
Total comprehensive income for the year	-	-	-	4,064,421	25,588	1,441,236	5,531,245
Transfer to reserves	-	414,321	414,321	(828,642)	-	-	-
Balance as at 31 December 2016	110,000,000	431,516	431,516	3,369,885	3,114,343	(78,323,503)	39,023,757
Total comprehensive income for the year	-	-	-	17,835,791	(187,291)	(382,129)	17,266,371
Transfer to reserves	-	1,783,579	1,783,579	(3,567,158)	-	-	-
Balance as at 31 December 2017	110,000,000	2,215,095	2,215,095	17,638,518	2,927,052	(78,705,632)	56,290,128

The accompanying notes 1 to 20 are an integral part of these financial statements.

Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of The First Phase of Az Zour Power Plant KSC (Public)

Statement of Cash Flows – Year ended 31 December 2017

	Kuwaiti Dinars	
	2017	2016
Cash flows from operating activities		
Profit before contribution to KFAS and Zakat	18,182,849	4,143,207
Adjustments for:		
Depreciation	24,913	927,271
Finance costs	12,051,890	751,099
Provision for doubtful debts	160,000	-
Increase in trade and other receivables	(9,876,369)	(3,004,178)
Increase in inventories	-	(161,775)
Decrease in finance lease receivables	12,136,399	-
Decrease in trade and other payables	(15,423,976)	(11,572,929)
Increase in due to related parties	222,473	977,468
Provision for staff indemnities	27,497	23,883
Payment of staff indemnities	(29,309)	(17,381)
Net cash from/(used in) operating activities	<u>17,476,367</u>	<u>(7,933,335)</u>
Cash flows from investing activities		
Acquisition of property, plant and equipment	(124,372)	(27,127,758)
Decrease in term deposits	3,586,549	11,549,769
Net cash from/(used in) investing activities	<u>3,462,177</u>	<u>(15,577,989)</u>
Cash flows from financing activities		
Increase in term loans	3,204,903	40,792,367
Payment of finance costs	(13,104,278)	(12,857,514)
Net cash (used in)/from financing activities	<u>(9,899,375)</u>	<u>27,934,853</u>
(Decrease)/increase foreign currency translation reserve	(187,291)	25,588
Net increase in cash and cash equivalents	10,851,878	4,449,117
Cash and cash equivalents		
at beginning of the year	19,548,870	15,099,753
at end of the year (Note 3)	<u>30,400,748</u>	<u>19,548,870</u>

The accompanying notes 1 to 20 are an integral part of these financial statements.

1. Incorporation and activities

Shamal Az Zour Al Oula For The Building, Execution, Operation, Management and Maintenance of The First Phase of Az Zour Power Plant KSC (Public) ("the Company") is a Kuwaiti shareholding company incorporated on 19 August 2013, under trade licence No. 349479 registered at the Ministry of Commerce and Industry on 23 October 2013.

The registered office of the Company is at 6th Floor, Mazaya Tower 2, Khaleed Ibn Al Waleed Street, Block 3, Kuwait City, Kuwait.

In December 2013, the Company signed a Build, Operate and Transfer ("BOT") arrangement ("the Arrangement") with Kuwait's Ministry of Electricity and Water (MEW) for the development, financing, procurement, construction, testing and commissioning of a green field power generation and water desalination plant of 1,500 MWP of power generation capacity, and 102 to 107 Million Imperial Gallons Per Day ("MIGD") of water desalination capacity ("the Plant"), together with associated infrastructure and facilities for 40 years at Az-Zour North, Kuwait. MEW ("the Buyer") will purchase the entire output of the Plant under a 40-year long-term Energy Conversion and Water Purchase Agreement (ECWPA). The Plant was commissioned on 26 November 2016.

The objectives of the Company are the following:

1. To develop, finance, design, engineer and provide services and build, implement, operate and manage an electricity and power generation plant and a water plant including water desalination plant and related facilities including performing all work directly or indirectly related to or associated with its activities.
2. To carry on all works relating to the building works necessary for the Company to carry on its activity, including construction, purchase and lease of buildings, land, equipment and warehouses necessary for the realization of the objectives of the Company and all the facilities relating thereto.
3. To carry on all works of generation, production, transmission, making, development and sale of electricity and water, or any product relating to any such works in and outside the State of Kuwait.
4. To carry on chemical cleaning, hot oil cleaning works and disinfection for all heat exchangers, and to carry on electrical and civil works necessary for electricity and water sector works (power plants, pipeline and electricity projects for desalination units and petrochemicals), to carry on all maintenance works including those relating to power generation, water, pipeline installations and installation of relay stations and installation of all insulation items.
5. To import and install equipment at electricity and water locations for monitoring and measurement of air pollutants and to use skilled labor specialized in fighting pollution of the environment surrounding water and electricity plants.
6. To purchase materials and equipment and all movable properties and instruments necessary for the Company to realize its objectives, and to maintain the same by all modern means possible, and to import primary materials, equipment and instruments necessary for the Company's objectives.
7. To supply and install security and safety equipment relating to the objectives of the Company.
8. To import all necessary equipment to implement its objects, including but not limited to, install, supply and maintain all types of power cables, electrical cables, water pumps, instruments and equipment relating to the activities of the Company.
9. To register patents relating directly to the Company's experience.
10. To carry out technical research relating to the Company's business with the aim to improve and develop the Company's services in cooperation with specialized parties in and outside the State of Kuwait.
11. To directly participate in infrastructure zones and projects relevant to the objectives of the Company in Build, Operate and Transfer systems (BOT) or in other similar systems including those referred to in Law No. 39 of 2010 (and its amendments), and to manage the facilities established thereby.
12. To invest the Company's funds within the objects and percentages set out by the board of directors.

The Company may carry on the activities listed above in and outside the State of Kuwait, whether as a principal or agent.

Notes to the Financial Statements – 31 December 2017

The Company is permitted to participate in study, finance or implement any project or projects that have been tendered pursuant to Law No. 39 of 2010 (and its amendments) on Establishing Kuwaiti Joint Stock Companies Undertaking Building and Implementation of Electrical Power and Desalination Plants in Kuwait.

In accordance with the ECWPA signed between the Company and MEW on 12 December 2013, the Company is obliged to produce electricity and desalinated water using the Plant and MEW has the ability to restrict the access of others to the economic benefits of the Plant. Furthermore, the ECPWA provides for capacity payments in addition to output payments. Accordingly, the arrangement conveys a right to use the Plant and is classified as a finance lease in accordance with International Financial Reporting Interpretations Committee (IFRIC) Interpretation 4, with the Company as the lessor.

These financial statements have been approved for issue by the Company's Board of Directors on 13 February 2018 and are subject to the approval of the shareholders at their Annual General Meeting.

The Company is deemed to be a subsidiary of Az Zour North One KSCH ("the Parent Company") as it has the ability to direct the relevant activities of the Company, is exposed to variable returns from its involvement with the Company and has the ability to use its power over the Company to affect the amount of its returns.

2. Basis of preparation and significant accounting policies

2.1 Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and the interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC), under the historical cost basis of measurement except for derivative financial instruments measured at fair value.

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. It also requires management to exercise its judgment in the process of applying the accounting policies. The areas involving a high degree of judgment or complexity or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 20.

The shareholders' annual general meeting held on 22 May 2017 approved the audited financial statements of the Company for the year ended 31 December 2016.

The functional currency of the Company is United States Dollars ("USD"). These financial statements are presented in Kuwaiti Dinars ("KD") for the purpose of submission to the Ministry of Commerce and Industry, in the State of Kuwait.

2.2 New standards, interpretations and amendments effective from 1 January 2017

The accounting policies used in the preparation of these financial statements are consistent with those used in the previous financial year. Amendments to IFRSs which were effective for the annual accounting period starting from 1 January 2017 did not have any material impact on the accounting policies, financial position or performance of the Company.

2.3 New standards and interpretations not yet adopted

The following IFRSs and Interpretations have been issued but are not yet effective and have not been early adopted by the Company. The Company intends to adopt them when they become effective.

IFRS 9 Financial Instruments (effective for financial years beginning on or after 1 January 2018).

IFRS 9 'Financial Instruments' replaces IAS 39 Financial Instruments: Recognition and Measurement and is effective for annual periods beginning on or after 1 January 2018. IFRS 9 impacts the classification and measurement of financial assets and financial liabilities, impairment of financial assets and hedge accounting.

The primary impact on the Company relates to the provisioning for future credit losses on its financial assets and the requirement of certain additional disclosures.

Notes to the Financial Statements – 31 December 2017

The Company will adopt IFRS 9 from the effective date of 1 January 2018, apply it retrospectively and recognize on that date any difference between the previous carrying amount and the carrying amount as at 1 January 2018 in opening retained earnings. The Company will not restate prior periods.

Based on currently available information, the Company does not expect the adoption and application of IFRS 9 will have a material impact on the Company. This is subject to change as the Company is continuing to analyze its effects and will disclose the actual impact in its annual financial statements as of 31 December 2018.

IFRS 15 Revenue from Contracts with Customers (effective for financial years beginning on or after 1 January 2018).

In May 2014, the IASB issued IFRS 15 'Revenue from Contracts with Customers', effective for periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognizing revenue arising from contracts with customers and establishes a five-step model for that. Under IFRS 15, revenue will be recognized as goods and services are transferred, to the extent that the transferor anticipates entitlement to consideration in exchange for those goods and services. The standard also specifies a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers.

The Company will adopt IFRS 15 from the effective date of 1 January 2018 and apply the cumulative effect approach by retrospectively adjusting retained earnings on 1 January 2018. The Company will not restate prior periods.

Based on currently available information, the Company does not expect the adoption and application of IFRS 15 will have a material impact on the Company. This is subject to change as the Company is continuing to analyze its effects and will disclose the actual impact in its annual financial statements as of 31 December 2018.

IFRS 16 Leases (effective for financial years beginning on or after 1 January 2019).

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date.

IFRS 16 does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their statement of financial position as lease liabilities, with the corresponding right-of-use assets. Lessees must apply a single model for all recognised leases, but will have the option not to recognise 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognised leases will be similar to today's finance lease accounting, with interest and depreciation expense recognised separately in the statement of profit or loss and other comprehensive income.

Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach. The Company does not anticipate early adopting IFRS 16 and is currently evaluating its impact.

Other new standards or amendments to existing standard are not expected to have a material impact on the financial statements of the Company.

2.4 Financial instruments

In the normal course of business, the Company uses financial instruments, principally cash and bank balances, trade and other receivables, trade and other payables, finance lease receivable, amounts due to related parties and term loans. It also uses derivative financial instruments to manage and reduce its exposure to market risks arising from fluctuations in interest rates. Derivative instruments that it primarily uses are interest rate swaps to convert floating rate debt to fixed rate debt.

Classification

The Company classifies its financial assets as "loans and receivables" and financial liabilities as "other than at fair value through profit or loss".

Recognition/de-recognition

The Company recognizes financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instruments. A financial asset (in whole or in part) is derecognized when the contractual rights to receive cash flows from the financial asset have expired or the Company has transferred substantially all the risks and rewards of ownership. If the Company has retained control, it continues to recognize the financial asset to the extent of its continuing involvement in the financial asset. A financial liability is derecognized when the obligation specified in the contract is discharged, cancelled or expires.

All regular purchases and sales of financial assets are recognized using settlement date accounting. Changes in fair value between the trade date and settlement date are recognized in the statement of profit or loss or in the statement of other comprehensive income in accordance with the policy applicable to the related instrument. Regular purchases or sales are the purchase or sale of financial assets that require delivery of assets within the time frame generally established by regulations or conventions in the market place.

Measurement

Financial instruments

All financial assets and liabilities are initially measured at fair value, which includes transaction costs.

Loans and receivables

These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. This includes trade and other receivables and finance lease receivable. These are subsequently measured and carried at amortized cost using the effective yield method.

Financial liabilities

Financial liabilities "other than at fair value through profit or loss" are subsequently measured and carried at amortized cost using the effective yield method. This includes trade and other payables, amounts due to related parties, term loans and derivative financial instruments.

On initial recognition, any issue or redemption premiums and discounts and issuing costs are added to/deducted from the nominal value of the borrowings concerned. These items are taken into account when calculating the effective interest rate and are therefore recorded in the statement of profit or loss over the life of the borrowings using the amortized cost method.

The debt is subsequently recorded at amortized cost using the effective interest method.

Impairment

A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount. An assessment is made at each statement of financial position date to determine whether there is objective evidence that a specified asset, or a group of similar assets, may be impaired. If such evidence exists, any impairment loss is recognised in the statement of profit or loss.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on assets carried at amortised cost has occurred, the amount of the loss is recognised in the statement of profit or loss at the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. Any subsequent reversal of an impairment loss is recognised in the statement of profit or loss.

Derivative financial instruments and hedge accounting

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognizing the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Company designates its derivatives as hedges of a particular risk associated with a recognized asset or liability.

The Company documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months.

The effective portion of changes in the fair value of derivatives that are designated as hedging instruments and qualify as cash flow hedges is recognized in other comprehensive income and accumulated in equity. Any gain or loss relating to the ineffective portion is recognized immediately in the statement of profit or loss. The gains or losses accumulated in equity are reclassified to the income statement in the same period in which the hedged cash flows affects income.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in other comprehensive income at that time, remains in equity and is recognized when the forecast transaction is ultimately recognized in the statement of profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in other comprehensive income is immediately transferred to the statement of profit or loss.

The fair value of the derivative is the equivalent of the unrealized gain or loss from marking to market the derivative using prevailing market rates or internal pricing models.

Embedded derivatives

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract – with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. This is the case primarily with contracts for the purchase or sale of non-financial assets, whose price is revised based on an index, the exchange rate of a foreign currency or the price of an asset other than the contract's underlying.

Embedded derivatives are separated from the host contract and accounted for as derivatives when:

- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and
- the hybrid (combined) instrument is not measured at fair value with changes in fair value recognised in profit or loss (i.e. a derivative that is embedded in a financial asset or financial liability accounted for at fair value through profit or loss is not separated).

In all other cases embedded derivatives are accounted for in line with the accounting policy for the contract as a whole.

2.5 Cash and cash equivalents

Cash in hand, current accounts and time deposits with banks whose original maturities do not exceed three months from the date of placement are classified as cash and cash equivalents in the statement of cash flows.

Notes to the Financial Statements – 31 December 2017

2.6 Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and accumulated impairment. Property under construction is stated at cost and subsequently transferred to assets when it is available for use and is stated at cost less any accumulated impairment loss. The cost of an item of property, plant and equipment comprises its acquisition costs, borrowing costs and all directly attributable costs of bringing the asset to the working condition for its intended use. Depreciation is computed on the straight-line method, based on estimated useful lives of assets as follows:

	<u>Useful life</u>
Furniture and fixtures	3
Vehicles	3
IT equipment	3

Asset residual values and useful lives are reviewed, and adjusted if appropriate, at each financial position date. The carrying amount of property, plant and equipment is reviewed at each financial position date to determine whether there is any indication of impairment. If any such indication exists, an impairment loss is recognized in the statement of profit or loss.

The carrying amount of property, plant and equipment is derecognised on disposal.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the statement of profit or loss.

2.7 Impairment of non-financial assets

An asset is impaired if its carrying amount exceeds its estimated recoverable amount. The recoverable amount of an asset is the higher of the asset's fair value less cost to sell and value in use. Fair value less cost to sell is the amount obtainable from the sale of an asset in an arm's length transaction. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. An assessment is made at each statement of financial position date to determine whether there is objective evidence that a specific asset, or a group of similar assets, may be impaired. If such evidence exists, an impairment loss is recognised in the statement of profit or loss. Assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units) for the purpose of testing impairment.

Impairment losses for cash-generating units reduce first the carrying amount of any goodwill allocated to that cash-generating unit. Any remaining impairment loss is charged pro rata to the other assets in the cash-generating unit. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognised may no longer exist. An impairment charge is reversed if the cash-generating unit's recoverable amount exceeds its carrying amount.

2.8 Provisions for liabilities

Provisions for liabilities are recognized when, as a result of past events, it is probable that an outflow of economic resources will be required to settle a present legal or constructive obligation and the amount can be reliably estimated.

2.9 Post-employment benefits

The Company provides post-employment benefits to its expatriate employees. The entitlement to these benefits is based upon the employee's final salary and length of service subject to the completion of a minimum service period. The expected cost of these benefits are accrued over the period of employment.

With respect to its national employees, the Company makes contributions to a government scheme calculated as a percentage of the employee's salary. The Company's obligations are limited to these contributions, which are expensed when due.

2.10 Borrowing costs

The interest on borrowings specifically incurred to finance the construction of property, plant and equipment is capitalized as part of their cost during the period that is required to complete the construction. All other interest cost is recognized as an expense of the period in which it is incurred.

Notes to the Financial Statements – 31 December 2017

2.11 Leases

Accounting for arrangements that contain a lease

"IFRIC Interpretation 4: Determining whether an Arrangement contains a Lease" deals with the identification of services and take-or-pay sales or purchasing contracts that do not take the legal form of a lease but convey rights to customers/suppliers to use an asset or a group of assets in return for a payment or a series of fixed payments. Contracts meeting these criteria are identified as either operating leases or finance leases.

Where the Company determines a long term electricity conversion and water purchase agreement to be or to contain a lease and where the buyer has the principal risks and rewards incidental to the ownership of the related plant through its contractual arrangements with the Company, the arrangement is considered to be a finance lease where the Company is acting as lessor and its customer the lessee and a finance receivable is recognized to reflect the financing deemed to be granted by the Company.

As disclosed in note 2.12 capacity payments covering the fixed capital component are apportioned on the basis of their relative fair values between minimum lease payments (comprising capital repayments relating to the provision of the Plant and finance income) and service income representing those payments which are not included within minimum lease payments. The finance income is recognized as revenue using a market rate of interest to give a constant periodic rate of return on the net investment in each period.

Lease classification

Leases are classified as finance leases or operating leases. A finance lease is defined as a lease, which transfers substantially all the risks and rewards incidental to the ownership of the related asset to the lessee. All leases, which do not comply with the definition of a finance lease, are classified as operating leases. The main factors considered by the Company to assess if a lease transfers substantially all the risks and rewards incidental to ownership are whether the lessor transfers ownership of the asset to the lessee by the end of the lease term, the lessee has an option to purchase the asset and if so, the conditions applicable to exercising that option, the lease term is for the major part of the economic life of the asset, the asset is of a highly specialized nature and the present value of minimum lease payments amounts to at least substantially all of the fair value of the leased asset.

Finance lease – where the Company is the lessor

At inception of the lease, a finance lease is recorded at an amount equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments.

Operating lease - where the Company is the lessee

Leases of assets under which all the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the statement of profit or loss on a straight-line basis over the period of the lease.

2.12 Revenue recognition

Revenue is measured at the fair value of consideration received or receivable and comprises the following items:

- Capacity payments for power and water consisting of a fixed capital component and a fixed operation and maintenance component
- Electrical and water output payments consisting of a fuel adjustment component and a variable operation and maintenance component

The relevant revenues are:

- Finance income where the Company is the lessor and service income
- Income relating to operating and maintenance activities

Finance income where the Company is the lessor and service income

Capacity payments covering the fixed capital component are apportioned on the basis of their relative fair values between minimum lease payments (comprising capital repayments relating to the provision of the Plant and finance income) and service income. The finance lease interest income for fixed capital component recognized in the statement of profit or loss and other comprehensive income is part of the minimum lease payment and is recognized as disclosed in note 2.11. Service income is recognized in the period it is earned at the fair value of the Company's performance under the contract in each period.

Income relating to operating and maintenance activities

The revenue from capacity payments for power and water covering fixed operation and maintenance charges and from electrical and water output payments covering the fuel adjustment and variable operation and maintenance charges is recognized on an accrual basis of accounting when the services have been rendered and/or the risks and rewards have been transferred, the amounts of revenue and related costs can be reliably measured, and it is probable that the economic benefits associated with the transaction will flow to the Company.

2.13 Fair values

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 by the Company.

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 Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized 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 - inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;

Level 2 - inputs, other than quoted prices included within Level 1, that are observable for the asset or liability either directly or indirectly; and

Level 3 - unobservable inputs for the asset or liability.

For financial instruments quoted in an active market, fair value is determined by reference to quoted market prices. Bid prices are used for assets and offer prices are used for liabilities.

For unquoted financial instruments fair value is determined by reference to the market value of a similar investment, discounted cash flows, other appropriate valuation models or brokers' quotes.

For financial instruments carried at amortised cost, the fair value is estimated by discounting future cash flows at the current market rate of return for similar financial instruments.

For investments in equity instruments, where a reasonable estimate of fair value cannot be determined, the investment is carried at cost.

The fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

Notes to the Financial Statements – 31 December 2017

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Company 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.

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

2.14 Foreign currency transactions

The functional currency of the Company is US Dollars and the presentation currency is the Kuwaiti Dinars. Though the primary economic environment in which the Company operates is the State of Kuwait, the functional currency is the US Dollar as it is the currency that mainly dictates the Company's operations.

Foreign currency transactions are translated into US Dollars at the rates prevailing on the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into US Dollars at the rates of exchange ruling at the financial position date. Resultant gains or losses are taken to the statement of profit or loss and other comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Assets and liabilities were translated into presentation currency using the closing rate at the date of the statement of financial position. The income and expenses are translated using the average exchange rate during the year. All the resulting exchange differences are recognized in statement of profit or loss and other comprehensive income.

2.15 Taxation

Tax on the profit or loss for the period comprises current and deferred tax. Tax is recognized in the income statement except to the extent that it relates to items recognized directly within equity, in which case it is recognized within the statement of other comprehensive income.

Current tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the financial position date, and any adjustment to tax payable in respect of previous periods.

Taxable profit differs from the profit on ordinary activities before tax as reported in the statement of profit or loss because it excludes items of income or expense that are taxable or deductible in other periods. This includes the effect of tax allowances and excludes items that are never taxable or deductible.

Deferred tax

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax is measured on a non-discounted basis using tax rates enacted or substantively enacted at the financial position date and that are expected to apply in the period when the deferred tax asset is realized or the deferred tax liability is settled.

Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized only to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be used.

Deferred tax assets and deferred tax liabilities are offset when there is a legally enforceable right to set off tax assets against tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

2.16 Contingencies

Contingent assets are not recognised as an asset until realization becomes virtually certain. Contingent liabilities are not recognized as a liability unless as a result of past events it is probable that an outflow of economic resources will be required to settle a present, legal or constructive obligation and the amount can be reliably estimated.

Notes to the Financial Statements – 31 December 2017

3. Cash and bank balances

	Kuwaiti Dinars	
	2017	2016
Cash in hand	889	8,671
Cash with banks	466,725	19,540,199
Deposits	29,933,134	3,586,549
Cash and bank balances	30,400,748	23,135,419
Less: Deposits with original maturity over three months	-	(3,586,549)
Cash and cash equivalents as per statement of cash flows	<u>30,400,748</u>	<u>19,548,870</u>

The short-term deposits are denominated in USD and placed with a foreign bank at an effective interest ranging from 1.33% to 1.63% (2016: 0.40% to 0.90%) per annum.

4. Trade and other receivables

	Kuwaiti Dinars	
	2017	2016
Trade receivables	10,325,077	1,260,972
Provision for doubtful debts	(160,000)	-
	10,165,077	1,260,972
Unbilled revenue	5,148,396	5,471,398
Deferred tax asset	1,597,406	1,598,439
Insurance claim receivable	642,442	-
Prepaid expenses	326,444	-
Advance lease rent to MEW	92,622	104,284
Other receivables	239,124	61,082
	<u>18,211,511</u>	<u>8,496,175</u>

The average credit period granted to the customer is 60 days. No interest is charged on the overdue trade receivables.

As of 31 December 2017, trade receivables of KD 5,043,966 (2016: KD 1,260,972) were neither past due nor impaired. Trade receivables amounting to KD 5,121,111 (2016: Nil) were past due but not impaired, ageing less than three months. As at 31 December 2017, trade receivables amounting to KD 160,000 (2016: Nil) were impaired and fully provided. All the trade receivables are denominated in KD and are located in the State of Kuwait. The maximum exposure to credit risk at the statement of financial position date is disclosed in note 15 to these financial statements.

The deferred tax charge relating to current year is recognized in other comprehensive income.

The advance lease rent represents the total operating lease cost for the lease of the land on which the Plant is built and is being amortised over the lease period of forty years.

5. Finance lease receivable

Finance lease for which the Company acts as lessor.

This lease falls within the scope of the IFRIC 4 guidance on the interpretation of IAS 17 and applies to the ECWPA on the basis that it is an energy conversion and sale contract that conveys an exclusive right to use a production asset. The Company has recognized a finance lease receivable as follows:

	Kuwaiti Dinars	
	Minimum lease receipts	Present value of minimum lease receipts
	2017	2017
Amounts receivable under finance lease		
Within one year	37,408,001	36,303,095
Year 2 to 5 inclusive	150,292,570	120,293,463
After year 5	712,045,470	342,966,307
Undiscounted future minimum lease payments	899,746,041	499,562,865
Unearned finance income	(400,183,176)	-
Net investment in finance lease at 31 December 2017	<u>499,562,865</u>	<u>499,562,865</u>

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Notes to the Financial Statements – 31 December 2017

	Kuwaiti Dinars	
	Minimum	Present value
	lease receipts	of minimum
	2016	2016
Amounts receivable under finance lease		
Within one year	37,719,097	38,782,536
Year 2 to 5 included	188,744,826	155,150,741
After year 5	716,006,869	318,198,861
Undiscounted future minimum lease payments	942,470,792	512,132,138
Unearned finance income	(430,338,654)	-
Net investment in finance lease at 31 December 2016	<u>512,132,138</u>	<u>512,132,138</u>

Included in the statement of financial position:

	Kuwaiti Dinars	
	2017	2016
Current portion	10,171,603	9,790,001
Non-current portion	489,391,262	502,342,137
	<u>499,562,865</u>	<u>512,132,138</u>

The interest rate implicit in the finance lease is 5.5% (2016: 5.5%) per annum.

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Notes to the Financial Statements – 31 December 2017

6. Property, plant and equipment

	Kuwaiti Dinars				
	Assets under construction	Plant and equipment	IT equipment	Vehicles	Furniture and fixtures
Cost					
As at 1 January 2016	385,555,587	79,602,444	215,850	96,602	8,629
Additions for the year	40,307,961	-	-	-	-
Disposal	-	-	(1,541)	-	-
Foreign currency translation Transfers	(1,703,546)	(363,669)	(988)	(441)	(40)
	(424,160,002)	(79,238,775)	(213,321)	(96,161)	(8,589)
As at 31 December 2016	-	-	-	-	-
Additions for the year	-	-	1,926	122,446	-
Foreign currency translation	-	-	3	199	-
As at 31 December 2017	-	-	1,929	122,645	-
Accumulated depreciation					
As at 1 January 2016	-	1,393,286	-	-	-
Charge for the year	-	927,271	-	-	-
Foreign currency translation Transfer	-	(5,033)	-	-	-
	-	(2,315,524)	-	-	-
As at 31 December 2016	-	-	-	-	-
Charge for the year	-	-	252	24,661	-
Foreign currency translation	-	-	-	41	-
As at 31 December 2017	-	-	252	24,702	-
Carrying amount					
As at 31 December 2017	-	-	1,677	97,943	-
As at 31 December 2016	-	-	-	-	-

Assets under construction relates to the Plant as of 1 January 2016, constructed on land leased from MEW and includes interest capitalized KD 14,981,376 during 2016. On the completion of the Plant and the commencement of the finance lease in 2016, the Company derecognized its property, plant and equipment and recognized a finance lease receivable.

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7. Trade and other payables

	Kuwaiti Dinars	
	2017	2016
Accounts payable	1,310,188	2,514,986
Retentions payable	2,730,939	16,328,988
Accruals and other payables	6,140,300	7,466,759
	<u>10,181,427</u>	<u>26,310,733</u>

8. Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include entities over which the Company exercises significant influence, major shareholders, directors and key management personnel of the Company. The Company has a related party relationship with entities over which certain shareholders and directors are able to exercise significant influence. The Company ensures that prices and terms for these transactions are such that the Board of Directors of the Company would consider them comparable with those from unrelated third parties.

Amounts due to related parties are interest free and have no fixed maturity.

The related party transactions and balances included in these financial statements are as follows:

	Kuwaiti Dinars	
	2017	2016
Statement of financial position		
Due from related parties (included in other receivables)	213,280	56,977
Due to related parties	1,940,905	1,718,432
Retentions payable	2,115,136	1,354,935
Statement of profit or loss		
Operating costs	14,101,490	3,201,484
General and administrative expenses	302,340	92,448

9. Term loans

	Kuwaiti Dinars	
	2017	2016
Current portion	11,897,457	11,692,367
Non-current portion	388,062,342	385,062,529
	<u>399,959,799</u>	<u>396,754,896</u>
	Kuwaiti Dinars	
	2017	2016
USD 645 million facility from Japan Bank for International Cooperation that bears a floating interest rate of Libor plus 1.25% per annum.	179,981,910	178,539,703
USD 283 million facility from various lenders under Nippon Export and Investment Insurance covered facilities agreement that bears a floating interest rate of Libor plus 1.1% - 1.3% per annum.	78,992,060	78,359,092
USD 505 million facility from various lenders under the Commercial facilities agreement that bears a floating interest rate of Libor plus 1.7% - 2.55% per annum.	140,985,829	139,856,101
	<u>399,959,799</u>	<u>396,754,896</u>

As at 31 December 2017, the Company has undrawn loan facilities amounting to KD Nil (2016: KD 53 million) and working capital facilities amounting to KD 14 million (2016: 14 million). The loans are repayable in quarterly instalments with the final maturity in November 2036.

The loan agreements provide for the borrowings to be secured by assignment of receivables and residual rights under the ECWPA as well as the pledge of the Company's shares. Loan financial covenants include contribution of equity of at least 20% of the total project cost on the project commercial operation date and a debt service coverage ratio of 1.05:1 after that.

10. Equity

Share capital

The Company's authorized and issued share capital comprises of 1,100,000,000 shares of 100 Kuwaiti fils (2016: 1,100,000,000 shares of 100 Kuwaiti fils) (KD 110,000,000) each, fully paid up in cash.

Statutory reserve

In accordance with the Companies Law and the Company's Articles of Association, 10% of the net profit has been transferred to statutory reserve and must be done annually until the reserve reaches a minimum of 50% of the paid up share capital. This reserve can be utilized only for distribution of a maximum dividend of 5% in years when retained earnings are inadequate for this purpose.

Voluntary reserve

In accordance with the Company's Articles of Association, 10% of the net profit has been transferred to the voluntary reserve until the shareholders decide to discontinue the transfer. There are no restrictions on distributions from the voluntary reserve.

11. Revenue

	Kuwaiti Dinars	
	2017	2016
Finance lease interest income	27,729,526	2,339,165
Fixed operation and maintenance income	11,952,821	2,020,527
Electrical and water output income	984,544	3,680,908
Supplemental receipts and service income	5,532,922	1,252,100
	<u>46,199,813</u>	<u>9,292,700</u>

12. Operating costs

The principal operating costs are the operating and maintenance costs of the Plant.

13. Contribution to KFAS

This represents the contribution to the Kuwait Foundation for the Advancement of Science ("KFAS") computed at 1% of profit for the year after the transfer to statutory reserve.

14. Zakat

Zakat represents the tax payable to Kuwait's Ministry of Finance under Zakat Law No.46 of 2006, computed at 1% of profit for the year after the transfer to statutory reserve.

15. Financial instruments – fair value and risk management

Fair value

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

The Company uses the level 2 hierarchy inputs to measure the fair value of derivative financial instruments and the level 3 hierarchy for determining and disclosing the fair values of financial instruments carried at amortized cost. The carrying values are not materially different from their fair values.

The carrying amounts of financial assets and financial liabilities that are liquid or have a short-term maturity are approximately equal to their fair value. This estimate is based on Level 3 inputs with the discount rate that reflects the credit risk of counterparties being the most significant input.

Notes to the Financial Statements – 31 December 2017

Financial risk factors

The Company's use of financial instruments exposes it to a variety of financial risks such as credit risk, liquidity risk and market risk. The Company continuously reviews its risk exposures and takes measures to limit them to acceptable levels. The significant risks that the Company is exposed to are discussed below:

(a) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Financial assets, which potentially subject the Company to credit risk, consist principally of short notice bank deposits, trade and other receivables and the finance lease receivable. The Company manages credit risk by placing funds with financial institutions of high credit rating and transacting its principal business with counterparties of repute. Credit risk with respect to trade receivables is limited as all the trade receivables are due from MEW.

(b) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company manages liquidity risk by confirming on a regular basis that sufficient funds are available to meet maturing commitments and by mainly availability of funding. The Company measures liquidity risk by projecting the availability of future cash flows using historical and other related data.

The table below analyses the Company's financial liabilities into relevant maturity groupings based on the remaining period at the statement of financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
	Kuwaiti Dinars			
At 31 December 2017				
Trade and other payables	10,181,427	-	-	-
Due to related parties	1,940,905	-	-	-
Term loans	23,260,958	51,772,606	79,618,852	371,488,441
Derivative financial liabilities	11,979,744	9,814,090	21,680,640	49,339,300
At 31 December 2016				
Trade and other payables	26,310,733	-	-	-
Due to related parties	1,718,432	-	-	-
Term loans	20,432,797	43,839,723	120,197,853	323,388,248
Derivative financial liabilities	317,725	3,755,043	7,542,847	96,725,377

(c) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market price risk comprises of three types of risk – currency risk, interest rate risk and other price risk.

(i) Currency risk

Currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchanges rates.

A 10% weakening/strengthening of the functional currency against other major currencies does not have a material impact on the financial position of the Company.

(ii) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Company's interest rate risk arises from short-term bank deposits and long term-borrowings. Borrowings issued at variable rates expose the Company to cash flow interest rate risk. The Company's borrowings at variable rates are denominated mainly in US Dollars.

Notes to the Financial Statements – 31 December 2017

The Company manages this risk by hedging its long-term borrowings using floating to fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating to fixed rate and therefore the exposure to cash flow interest rate risk is limited.

At 31 December 2017, if interest rates at that date had been 0.5% higher/lower with all other variables held constant, other comprehensive income would have been lower/higher by KD 2,249,485 (31 December 2016: KD 2,349,555).

(iii) Other price risk

Other price risk is the risk that the value of the financial instrument will fluctuate as a result of changes in equity market prices, whether caused by factors specific to an individual investment, issuer or all factors affecting all instruments traded in the market. The Company is not exposed to this risk, as it has no equity investments.

16. Hedge reserve account and derivative financial liabilities

In the ordinary course of business, the Company uses derivative financial instruments in the form of interest rate swaps to manage its exposure to fluctuations in interest rates. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in the price of one or more underlying financial instruments, reference rates or indices. Interest rate swaps are contractual agreements between two parties to exchange interest based on notional value in a single currency for a fixed period.

In accordance with the Common Terms Agreement signed with the lenders, the Company is required to swap the floating rate interest due on its borrowings to fixed rate interest through interest rate swaps. Accordingly, the Company entered into a number of forward starting interest rate swaps from January 2014 to August 2036 to hedge variable rate interest payments on its outstanding debt and future debt issuances. These swaps have been classified as cash flow hedges. The increase in the fair value of the outstanding interest rate swaps as of 31 December 2017 amounting to KD 382,129 (2016: KD 1,441,236) has been taken to other comprehensive income and classified as hedge reserve in equity net of the related deferred tax. This fair value decline will be released to the statement of profit or loss in the same periods during which the hedge item affects the statement of profit or loss.

The table below shows the fair values of derivative financial instruments, together with the notional amounts analyzed by the term to maturity. Notional amounts represent amounts to which a rate or price is applied to determine the amounts of cash flows to be exchanged and do not represent the potential gain or loss associated with the market or credit risk of such instruments.

All derivative contracts are fair valued based on observable market data.

Derivatives held for hedging:

Cash flow hedges - Interest rate swaps
Notional amount:
At 31 December

Kuwaiti Dinars	
2017	2016
399,306,592	398,982,311

Derivatives held for hedging:

Cash flow hedges - Interest rate swaps
Negative fair value:
Short term
Long term

Kuwaiti Dinars	
2017	2016
(10,301,753)	(317,725)
(69,568,572)	(79,604,217)
(79,870,325)	(79,921,942)
1,597,406	1,598,439
(432,713)	-
(78,705,632)	(78,323,503)

Deferred tax asset
Foreign exchange translation impact

Notes to the Financial Statements – 31 December 2017

17. Capital risk management

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

Consistent with others in the industry, the Company monitors capital based on the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents. Total capital is calculated as equity, excluding the hedge reserve (as shown in the statement of financial position) plus net debt.

	Kuwaiti Dinars	
	2017	2016
Total borrowings	399,959,799	396,754,896
Less: cash and cash equivalents	(30,400,748)	(19,548,870)
Net debt	369,559,051	377,206,026
Total equity (excluding hedge reserve)	134,995,760	117,347,260
Total capital	504,554,881	494,553,286
Gearing ratio	73%	76%

Borrowings are defined as term loans and are disclosed in note 9.

18. Commitments

Operation and maintenance commitments

The Company has an operation and maintenance agreement (O&M) with AZN O&M Company WLL who operate and maintain the Plant, for which the Company has agreed to pay fixed and variable operating fees, to be adjusted based on price indices.

Under the O&M, the minimum future payments due are as follows;

	Kuwaiti Dinars	
	2017	2016
Within one year	14,394,262	14,173,327
Year 2 to 5 inclusive	76,810,316	75,598,492
After year 5	338,399,731	356,395,881
	429,604,309	446,167,700

19. Embedded derivatives

The ECWPA and the O&M contain embedded derivatives in the form of price adjustments for inflation based on price indices.

These embedded derivatives are not separated from the host contracts and are not accounted for as stand-alone derivatives under IAS 39, as management believes that the economic characteristics and risks associated with the embedded derivatives are closely related to those of the host contracts.

20. Critical accounting judgments and estimates

The preparation of financial statements in conformity with IFRSs requires management to make estimates and assumptions that may affect amounts reported in these financial statements. Actual results could differ from those estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a high degree of judgment or areas where assumptions and estimates have the most significant effect on the amounts recognized in these financial statements are as follows:

Impairment of non-financial assets and financial assets

The Company reviews its assets to assess whether a provision for impairment should be recorded in the statement of profit or loss. Considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of any provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty.

Notes to the Financial Statements – 31 December 2017

Fair value of derivatives

The fair value of financial instruments that are not traded in an active market (for example derivative liability as disclosed in note 16) is determined by using valuation techniques. The Company uses its judgment to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

Minimum lease payments

Minimum lease payments from the ECWPA are estimated based on projections of available net electricity and water capacity, US producer price indices and Kuwaiti consumer price indices over a period of twenty five years.

Determining whether an arrangement contains a lease and lease classification

Management has applied the guidance in IFRIC 4, 'Determining whether an arrangement contains a lease'. Based on management's evaluation, the ECWPA with MEW is considered as a lease within the context of IFRIC 4 and has been classified as a finance lease under IAS 17 since significant risks and rewards of ownership were transferred to MEW on the Project Commercial Operation Date which is the date of commencement of the lease term. The primary basis for this conclusion is that the ECWPA is for the substantial portion of the life of the Plant and the present value of minimum lease payments substantially equates to the fair value of the Plant at the inception of the lease.