State Oil Company of the Azerbaijan Republic

Consolidated financial statements prepared under International Financial Reporting Standards

31 December 2018

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Independent auditor's report

To the Management and Management Board 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 2018, 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 2018 and its consolidated financial performance and its consolidated 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 the significance of the Group's oil and gas assets, the high level of subjectivity in respect of assumptions underlying impairment analysis and significant judgements made by management. In addition, volatility in oil prices over the last few years impacts the Group's operations and cash flows and triggers potential impairment.

The key assumptions used by management and results of impairment tests are disclosed in Notes 3, 16 and 29 to the consolidated financial statements.

We evaluated the change in risk profile of the Group's assets and assessed impairment indicators. We involved our internal valuation experts and compared assumptions used in impairment testing such as oil prices forecast, reserves and resources volumes and discount rates with available external data. We checked mathematical accuracy of impairment models and sensitivity analysis. We compared calculated amounts of impairment charge and unsuccessful exploration assets write offs to amounts recorded in the Group's accounting records. We analyzed significant judgement made by management. We analyzed disclosure of impairment in the notes 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.

Information on oil and gas reserves is disclosed in Note 3 to the consolidated financial statements.

We compared the assumptions used by the reserve engineers with the Group's approved budget and historical data. We assessed the underlying assumptions and compared estimates of reserves and resources provided by reserves engineers to the amounts included in the calculation of impairment, depreciation, depletion and amortization and decommissioning provisions. We analyzed disclosure of oil and gas reserves in the notes to the consolidated financial statements.

Other information included in the Group's 2018 Annual Report

Other information consists of the information included in the Group's 2018 Annual Report other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Group's 2018 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.

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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.

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- 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.

31 May 2019

Baku, Azerbaijan

Consolidated statement of financial position

(Amounts presented are in millions of Azerbaijani Manats)

	Note	31 December 2018	31 December 2017
Assets			
Current assets			
Cash and cash equivalents	8	6,640	5,217
Restricted cash	9	276	265
Deposits	8	151	218
Available-for-sale investments		–	174
Trade and other receivables	10	8,395	10,007
Inventories	11	2,979	4,810
Other current assets	12	851	1,614
Total current assets		**19,292**	**22,305**
Non-current assets			
Property, plant and equipment	15	28,259	25,669
Goodwill	39	301	327
Intangible assets other than goodwill	16	714	739
Investments in joint ventures	17	5,301	5,022
Investments in associates	18	4,359	4,571
Deferred tax assets	33	700	905
Other non-current financial assets	14	1,323	685
Other non-current assets	13	1,887	1,124
Total non-current assets		**42,844**	**39,042**
Total assets		**62,136**	**61,347**
Equity			
Charter capital	27	4,147	3,036
Additional paid-in capital	27	5,299	4,541
Retained earnings		7,659	7,357
Other capital reserves		(51)	(6)
Put option on company's shares		(1,310)	(1,310)
Gain on sale/purchase of subsidiary share	27	1,168	1,181
Cumulative translation differences		5,900	5,806
Equity attributable to equity holders of the Group		**22,812**	**20,605**
Non-controlling interests		1,132	1,370
Total equity		**23,944**	**21,975**

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

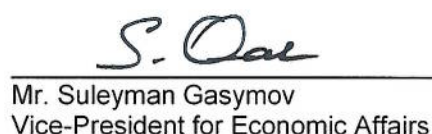
Consolidated statement of financial position (continued)

(Amounts presented are in millions of Azerbaijani Manats)

	Note	31 December 2018	31 December 2017
Liabilities			
Current liabilities			
Trade and other payables	19	11,780	12,450
Short-term and current portion of long-term borrowings	20	4,013	5,998
Taxes payable	21	690	487
Contract liabilities	19	305	–
Deferred acquisition consideration payable	26	157	147
Other provisions for liabilities and charges	23	56	70
Deferred income	24	11	41
Other current liabilities	25	355	653
Total current liabilities		**17,367**	**19,846**
Non-current liabilities			
Long-term borrowings	20	9,659	9,513
Advances received for the sale of interest in PSA	34	4,313	4,076
Put option liabilities	35	2,713	2,719
Deferred tax liabilities	33	1,412	1,209
Asset retirement obligations	22	1,079	1,067
Deferred acquisition consideration payable	26	529	–
Other provisions for liabilities and charges	23	152	94
Deferred income	24	58	63
Other non-current liabilities	25	910	785
Total non-current liabilities		**20,825**	**19,526**
Total liabilities		**38,192**	**39,372**
Total liabilities and equity		**62,136**	**61,347**

Approved for issue and signed on behalf of the Group on 31 May 2019.

Mr. Rovnag Abdullayev
President



Mr. Suleyman Gasymov
Vice-President for Economic Affairs

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

Consolidated statement of profit or loss and other comprehensive income

(Amounts presented are in millions of Azerbaijani Manats)

	Note	2018	2017
Revenue	28	111,198	92,571
Cost of sales	29	(105,468)	(87,352)
Gross profit		**5,730**	**5,219**
Distribution expenses	29	(1,196)	(864)
General and administrative expenses	29	(1,348)	(1,267)
Loss on disposal of property, plant and equipment and intangible assets		(15)	(26)
Social expenses		(105)	(125)
Exploration and evaluation expenses	29	(69)	(38)
Credit loss reversed	29	85	–
Other operating expenses	29	(403)	(1,326)
Other operating income	30	916	949
Operating profit		**3,595**	**2,522**
Finance income	31	212	117
Finance costs	32	(1,126)	(890)
Foreign exchange gains and losses, net		(698)	110
Share of result of joint ventures	17	213	523
Share of result of associates	18	24	134
Profit before income tax		**2,220**	**2,516**
Income tax expenses	33	(996)	(424)
Profit for the year		**1,224**	**2,092**
Other comprehensive loss			
Other comprehensive loss to be reclassified to profit or loss in subsequent periods – currency translation differences		(241)	(620)
Other comprehensive (loss)/gain not to be reclassified to profit or loss in subsequent periods – loss on investments at FVOCI		(74)	44
Other comprehensive loss for the year, net of tax		**(315)**	**(576)**
Total comprehensive income for the year		**909**	**1,516**
Profit is attributable to:			
Equity holders of the Group		1,109	1,748
Non-controlling interests		115	344
		1,224	**2,092**
Total comprehensive (loss)/income attributable to:			
Equity holders of the Group		1,160	1,318
Non-controlling interests		(251)	198
		909	**1,516**

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									
	Note	Charter capital	Additional paid-in capital	Put option on company's shares	Gain on sale / (purchase) of subsidiary share	Other capital reserves	Retained earnings	Currency translation differences	Total	Non-controlling interests	Total equity
Balance at 1 January 2017		**1,802**	**2,159**	**(1,305)**	**1,280**	**(46)**	**6,265**	**6,292**	**16,447**	**1,257**	**17,704**
Profit for the year		–	–	–	–	–	1,748	–	1,748	344	2,092
Other comprehensive income/(loss)		–	–	–	–	40	–	(470)	(430)	(146)	(576)
Total comprehensive income for 2017		–	–	–	–	**40**	**1748**	**(470)**	**1,318**	**198**	**1,516**
Acquisition of non-controlling interest in subsidiary		–	–	–	(113)	–	–	(2)	(115)	44	(71)
Sale of shares to non-controlling shareholder		–	–	–	14	–	–	(14)	–	87	87
Put option reserve		–	–	(5)	–	–	–	–	(5)	5	–
Contribution in charter capital of subsidiaries by non-controlling shareholder		–	–	–	–	–	–	–	–	53	53
Increase in charter capital	27	1,234	(1,234)	–	–	–	–	–	–	–	–
Additional paid-in capital		–	3,616	–	–	–	–	–	3,616	–	3,616
Distribution to the Government	27	–	–	–	–	–	(656)	–	(656)	–	(656)
Dividends declared by subsidiaries		–	–	–	–	–	–	–	–	(274)	(274)
Balance at 31 December 2017		**3,036**	**4,541**	**(1,310)**	**1,181**	**(6)**	**7,357**	**5,806**	**20,605**	**1,370**	**21,975**
Impact of change in accounting policy		–	–	–	–	–	(122)	–	(122)	(2)	(124)
Adjusted Balance 1 January 2018		**3,036**	**4,541**	**(1,310)**	**1,181**	**(6)**	**7,235**	**5,806**	**20,483**	**1,368**	**21,851**
Profit for the year		–	–	–	–	–	1,109	–	1,109	115	1,224
Other comprehensive loss		–	–	–	–	(45)	–	96	51	(366)	(315)
Total comprehensive income for 2018		–	–	–	–	**(45)**	**1,109**	**96**	**1,160**	**(251)**	**909**
Acquisition of non-controlling interest in subsidiary	27	–	–	–	(14)	–	–	–	(14)	14	–
Gain on sale of shares to non-controlling shareholders	27	–	–	–	1	–	–	(2)	(1)	24	23
Additional paid-in capital	27	–	1,869	–	–	–	–	–	1,869	–	1,869
Increase in charter capital	27	1,111	(1,111)	–	–	–	–	–	–	–	–
Contribution in charter capital of subsidiaries by non-controlling shareholder										98	98
Distribution to the Government	27	–	–	–	–	–	(685)	–	(685)	–	(685)
Dividends declared by subsidiaries		–	–	–	–	–	–	–	–	(121)	(121)
Balance at 31 December 2018		**4,147**	**5,299**	**(1,310)**	**1,168**	**(51)**	**7,659**	**5,900**	**22,812**	**1,132**	**23,944**

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

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

	Note	2018	2017
Cash flows from operating activities			
Profit before income tax		2,220	2,516
Adjustments for:			
Depreciation of property, plant and equipment	29	1,391	1,065
Amortisation of intangible assets	16	43	41
Impairment of property, plant and equipment	15	161	468
Impairment of trade and other receivables and other financial assets		(25)	239
Loss on disposals of property, plant and equipment and intangible assets		15	26
Finance income	31	(212)	(117)
Finance costs	32	1,126	890
Foreign exchange rate differences		1,002	26
Share of result of associates and joint ventures	17, 18	(237)	(657)
Other non-cash transactions		(601)	(408)
Operating cash flows before working capital changes		**4,883**	**4,089**
Decrease/(increase) in trade and other receivables		1,027	(1,660)
Decrease in inventories		1,700	222
(Decrease)/increase in trade and other payables and contract liabilities		(402)	2,665
Change in other assets and liabilities		(5)	51
Change in provisions		(19)	(50)
Cash generated from operations		**7,184**	**5,317**
Income taxes paid		(590)	(635)
Interest paid		(885)	(647)
Net cash flows from operating activities		**5,709**	**4,035**
Cash flows from investing activities			
Acquisitions of subsidiary (net of cash acquired)		(1)	13
Additional contribution in associates and joint ventures		(201)	(830)
Purchase of property, plant and equipment		(4,672)	(4,271)
Purchase of intangible assets		(32)	(29)
Withdrawal of deposits		108	813
Interest received		171	117
Dividends received from associates and joint ventures		190	221
Proceeds from sale of property, plant and equipment		112	58
Advances received for sale of interest in PSA	34	237	1,310
Purchase of available-for-sale assets		–	(51)
Change in restricted cash related to construction		–	(129)
Loans received from/(issued to) joint ventures/associates		170	(313)
Loan issued to related parties		(34)	–
Proceeds from sale of disposal group		80	–
Purchase of financial instrument from related parties	7	(161)	–
Loans issued to third parties		–	(6)
Net cash flows used in investing activities		**(4,033)**	**(3,097)**
Cash flows from financing activities			
Proceeds from borrowings		5,601	9,480
Repayment of borrowings		(6,634)	(8,559)
Contribution in subsidiary by non-controlling shareholder		98	26
Proceeds from sale of non-controlling interests	27	23	87
Increase in charter capital and additional paid-in capital	27	1,190	243
Dividends paid to non-controlling interests		(122)	(252)
Distribution to the Government	27	(680)	(656)
Contribution from the Government		578	–
Acquisition of share from non-controlling shareholder		–	(71)
Change in restricted cash related to borrowings		–	(8)
Net cash flows from financing activities		**54**	**290**
Net foreign exchange difference on cash and cash equivalents		(290)	(174)
Expected credit losses ("ECL") for cash and cash equivalents	8	(17)	–
Net increase in cash and cash equivalents		**1,423**	**1,054**
Cash and cash equivalents at the beginning of the year	8	5,217	4,163
Cash and cash equivalents at the end of the year	8	**6,640**	**5,217**

(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 2018	% equity interest 2017
SOCAR Turkey Enerji A.Ş.	Refinery	Turkey	100%	100%
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%	92%
SOCAR Energy Georgia LLC	Sales and Distribution	Georgia	76%	76%
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 LLC	Construction	Azerbaijan	70%	65%
SOCAR Polymer Investments LLC	Chemicals production	Azerbaijan	52%	57%
BOS Shelf LLC	Construction	Azerbaijan	90%	90%

On 28 February 2018 the Group acquired 100 per cent control over four business units, A1, Futura, Pronto and W&G (Austrian business) (Note 39).

2. Basis of preparation and significant accounting policies

Basis of preparation

These consolidated financial statements of SOCAR and its subsidiaries, associates, joint ventures and joint operations (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 2018.

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.

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. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income ("OCI") are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with the Group's accounting policies. 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.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity, while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value. 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.

2. Basis of preparation and significant accounting policies (continued)

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.

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 charge 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.

2. Basis of preparation and significant accounting policies (continued)

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

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.

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 22 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") 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.

2. Basis of preparation and significant accounting policies (continued)

Foreign currency translation (continued)

At 31 December 2018, the principal rate of exchange used for translating foreign currency balances was USD 1 = AZN 1.7000, EUR 1 = AZN 1,9468, CHF 1 = AZN 1.7258, GEL 1 = AZN 0.6367, UAH 1 = AZN 0.0617, TRY 1 = AZN 0.3212, JPY 100 = AZN 1.5366 (2017: USD 1 = AZN 1.7001, EUR 1 = AZN 2.0307, CHF 1 = AZN 1.7374, GEL 1 = AZN 0.6514, UAH 1 = AZN 0.0605, TRY 1 = AZN 0.4499, JPY 100 = AZN 1.5079).

Financial instruments – key measurement terms

Depending on their classification financial instruments are subsequently carried at fair value, or amortized cost as described below. Since the Group started to apply IFRS 9 Financial Instruments after 1 January 2018, the comparative information has not been restated and continues to be reported under IAS 39 *Financial Instruments: Recognition and Measurement*. Therefore, accounting policy under IAS 39 Financial Instruments: Recognition and Measurement which was disclosed in the Group's consolidated financial statements as of 31 December 2017 is not repeated here.

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.

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 allowance for expected credit 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.

2. Basis of preparation and significant accounting policies (continued)

Financial instruments – key measurement terms (continued)

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.

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 asset

Initial recognition and measurement

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through other comprehensive income (OCI), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Group's business model for managing them.

With the exception of trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient, the Group initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs. Trade receivables that do not contain a significant financing component or for which the Group has applied the practical expedient are measured at the transaction price determined under IFRS 15.

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

The Group's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the asset.

Subsequent measurement

For purposes of subsequent measurement, financial assets are classified in four categories:

- Financial assets at amortised cost (debt instruments);
- Financial assets at fair value through OCI with recycling of cumulative gains and losses (debt instruments);
- Financial assets designated at fair value through OCI with no recycling of cumulative gains and losses upon de-recognition (equity instruments);
- Financial assets at fair value through profit or loss.

2. Basis of preparation and significant accounting policies (continued)

Financial asset (continued)

Financial assets at amortised cost (debt instruments)

This category is the most relevant to the Group. The Group measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

The Group's financial assets at amortised cost includes current and deposit accounts as well as restricted accounts at several local and international banks, trade and loan receivables from third parties, loan receivables from associates and long-term deposit accounts classified as other non-current financial assets.

Financial assets at fair value through OCI (debt instruments)

The Group measures debt instruments at fair value through OCI if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

For debt instruments at fair value through OCI, interest income, foreign exchange revaluation and impairment charge or reversals are recognised in the statement of profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in OCI. Upon de-recognition, the cumulative fair value change recognised in OCI is recycled to profit or loss.

The Group's debt instruments at fair value through OCI includes group of trade and other receivables that are hold for both collecting contractual cash flows and selling to manage short-term liquidity needs.

Financial assets designated at fair value through OCI (equity instruments)

Upon initial recognition, the Group can elect to classify irrevocably its equity investments as equity instruments designated at fair value through OCI when they meet the definition of equity under IAS 32 *Financial Instruments: Presentation* and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in the statement of profit or loss when the right of payment has been established, except when the Group benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in OCI. Equity instruments designated at fair value through OCI are not subject to impairment assessment. The Group elected to classify irrevocably its equity investments previously classified as available for-sale investments under this category.

2. Basis of preparation and significant accounting policies (continued)

Financial asset (continued)

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through OCI, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the statement of profit or loss.

This category includes derivative instruments and listed equity investments which the Group had not irrevocably elected to classify at fair value through OCI. Dividends on listed equity investments are also recognised as other income in the statement of profit or loss when the right of payment has been established.

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Group's consolidated statement of financial position) when:

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

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Group continues to recognise the transferred asset to the extent of its continuing involvement. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets

Further disclosures relating to impairment of financial assets are also provided in the following notes:

- Critical accounting estimates and judgments (Note 3);
- Debt instruments at fair value through OCI and trade and other receivables, including contract assets (Note 10).

The Group recognises an allowance for ECLs for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

2. Basis of preparation and significant accounting policies (continued)

Financial asset (continued)

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

For financial assets other than trade receivables and contract assets, the Group applies general approach in calculating ECLs.

For trade and other receivables and contract assets, the Group applies a simplified approach in calculating ECLs. Therefore, the Group does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The Group has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment.

The Group's debt instruments at fair value through OCI comprise solely of trade and other receivables that are held for both collecting contractual cash flows and selling to manage its everyday liquidity needs. For debt instruments at fair value through OCI, the Group applies the same methodology that is applied to financial assets measured at amortized cost.

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

The Group's financial liabilities include trade and other payables, loans and borrowings including bank overdrafts, and derivative financial instruments.

Subsequent measurement

The measurement of financial liabilities depends on their classification, as described below:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are incurred for the purpose of repurchasing in the near term. This category also includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IFRS 9. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

Gains or losses on liabilities held for trading are recognised in the statement of profit or loss.

Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the initial date of recognition, and only if the criteria in IFRS 9 are satisfied. The Group has not designated any financial liability as at fair value through profit or loss.

2. Basis of preparation and significant accounting policies (continued)

Financial liabilities (continued)

Loans, borrowings and payables

This is the category most relevant to the Group. After initial recognition, interest-bearing loans and borrowings and payables are subsequently measured at amortised cost using the EIR method taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process. The EIR amortisation is included as finance costs in the statement of profit or loss.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When 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. The difference in the respective carrying amounts is recognised in the statement of profit or loss.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

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 amount of the loss allowance and the amount initially recognized less, when appropriate, the cumulative amount of income recognized in accordance with IFRS 15.

Derivative financial instruments and hedge accounting

Oil and Gas derivative financial instruments, including paper and physical contracts, are initially measured at fair value on the date on which a derivative contract is entered into and subsequently accounted for at fair value through profit or loss. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

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.

Before 1 January 2018, 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.

2. Basis of preparation and significant accounting policies (continued)

Derivative financial instruments and hedge accounting (continued)

Beginning 1 January 2018, the documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the Group will assess whether the hedging relationship meets the hedge effectiveness requirements (including the analysis of sources of hedge ineffectiveness and how the hedge ratio is determined). A hedging relationship qualifies for hedge accounting if it meets all of the following effectiveness requirements:

- There is 'an economic relationship' between the hedged item and the hedging instrument.
- The effect of credit risk does not 'dominate the value changes' that result from that economic relationship.
- The hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of hedged item.

Hedges that meet all the qualifying criteria for hedge accounting are accounted for, as described below:

Fair value hedges

The change in the fair value of a hedging instrument is recognised in the statement of profit or loss as other expense. The change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item and is also recognised in the statement of profit or loss as other expense.

For fair value hedges relating to items carried at amortised cost, any adjustment to carrying value is amortised through profit or loss over the remaining term of the hedge using the EIR method. The EIR amortisation may begin as soon as an adjustment exists and no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

If the hedged item is derecognised, the unamortised fair value is recognised immediately in profit or loss.

When an unrecognised 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 recognised as an asset or liability with a corresponding gain or loss recognised in profit or loss.

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.

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.

2. Basis of preparation and significant accounting policies (continued)

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 qualifying 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.

Property, plant and equipment

The initial cost of an asset purchased 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. Subsequently, property, plant and equipment are stated at cost as described below, less accumulated depreciation and provision for impairment, where required.

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 charge, if any, is recognized in the statement of profit or loss and other comprehensive income. An impairment charge recognized for an asset or cash generating unit in prior years is reversed if there are indicators that impairment charge 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.

2. Basis of preparation and significant accounting policies (continued)

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.

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 charge.

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.

2. Basis of preparation and significant accounting policies (continued)

Intangible assets

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

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 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).

2. Basis of preparation and significant accounting policies (continued)

Intangible assets (continued)

(e) Development projects

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.

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 liability is provided on taxable temporary differences arising on investments in subsidiaries, joint ventures 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 recognized 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.

Taxes other than corporate income tax

Taxes, other than on income, are recorded within operating expenses.

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).

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.

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.

2. Basis of preparation and significant accounting policies (continued)

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 charge is recorded for the gross amount of the debtor, including VAT where applicable. The related VAT payable 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, Shah Deniz and Absheron PSA provisions, Azerbaijan ACG Limited ("AzACG"), Azerbaijan Shah Deniz Limited ("AzSD") and SOCAR Absheron LLC 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, 3 June 2026 and 22 May 2034, respectively.

Revenue from contracts with customers

The Group started to apply IFRS 15 *Revenue from Contracts with Customers* after 1 January 2018. The comparative information has not been restated and continues to be reported under IAS 11 *Construction Contracts* and IAS 18 *Revenue*. Therefore, accounting policy under previous standards which was disclosed in the Group's consolidated financial statements as of 31 December 2017 is not repeated here.

The Group is in the business of selling ranges of oil and oil products, petroleum products and natural gas as well as providing mainly construction services. Revenue from contracts with customers is recognised when control of the goods or services are transferred to the customer at an amount that reflects the consideration to which the Group expects to be entitled in exchange for those goods or services.

Revenues from sales of crude oil are recognized normally when the oil is loaded into the oil tanker or other transportation facilities. Revenues from sales of petroleum products are recognized 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 construction activities are recognized either at the point of time or overtime basis depending on terms of the contracts with customers.

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

Variable consideration

If the consideration promised in a contract includes a variable amount, the Group shall estimate the amount of consideration to which the Group will be entitled in exchange for transferring the promised goods or services to a customer.

2. Basis of preparation and significant accounting policies (continued)

Variable consideration (continued)

The Group is required to estimate an amount of variable consideration by using either of the following methods, depending on which method the Group expects to better predict the amount of consideration to which it will be entitled:

- The expected value – the expected value is the sum of probability-weighted amounts in a range of possible consideration amounts. An expected value may be an appropriate estimate of the amount of variable consideration if the Group has a large number of contracts with similar characteristics.
- The most likely amount – the most likely amount is the single most likely amount in a range of possible consideration amounts (i.e. the single most likely outcome of the contract). The most likely amount may be an appropriate estimate of the amount of variable consideration if the contract has only two possible outcomes (e.g. the Group either achieves a performance bonus or does not).

The Group selects the method that is best suited, based on the specific facts and circumstances of the contract.

The Group applies the selected method consistently to each type of variable consideration throughout the contract term and updates the estimated variable consideration at the end of each reporting period. It may also be appropriate for the Group to use different methods (i.e. expected value or most likely amount) for estimating different types of variable consideration within a single contract.

Rights of return

Certain contracts provide a customer with a right to return the goods within a specified period. The Group uses the expected value method to estimate the goods that will not be returned because this method best predicts the amount of variable consideration to which the Group will be entitled. The requirements in IFRS 15 on constraining estimates of variable consideration are also applied in order to determine the amount of variable consideration that can be included in the transaction price. For goods that are expected to be returned, instead of revenue, the Group recognises a refund liability. A right of return asset (and corresponding adjustment to cost of sales) is also recognised for the right to recover products from a customer.

Volume rebates

The Group provides retrospective volume rebates to certain customers once the quantity of products purchased during the period exceeds a threshold specified in the contract. Rebates are offset against amounts payable by the customer. To estimate the variable consideration for the expected future rebates, the Group applies the most likely amount method for contracts with a single-volume threshold and the expected value method for contracts with more than one volume threshold. The selected method that best predicts the amount of variable consideration is primarily driven by the number of volume thresholds contained in the contract. The Group then applies the requirements on constraining estimates of variable consideration and recognises Contract liabilities for the expected future rebates.

Significant financing component

For some transactions, the receipt of the consideration does not match the timing of the transfer of goods or services to the customer (e.g. the consideration is prepaid or is paid after the services are provided). When the customer pays in arrears, the Group is effectively providing financing to the customer. Conversely, when the customer pays in advance, the Group has effectively received financing from the customer.

IFRS 15 states that in determining the transaction price, the Group shall adjust the promised amount of consideration for the effects of the time value of money if the timing of payments agreed to by the parties to the contract (either explicitly or implicitly) provides the customer or the Group with a significant benefit of financing the transfer of goods or services to the customer. In those circumstances, the contract contains a significant financing component. A significant financing component may exist regardless of whether the promise of financing is explicitly stated in the contract or implied by the payment terms agreed to by the parties to the contract.

2. Basis of preparation and significant accounting policies (continued)

Contract balances

Contract assets

The Group's right to consideration in exchange for goods or services that the Group has transferred to a customer when that right is conditioned on something other than the passage of time (for example, the Group's future performance).

Contract liabilities

The Group's obligation to transfer goods or services to a customer for which the Group has received consideration (or the amount is due) from the customer.

Assets and liabilities arising from rights of return

Right of return asset

Right of return asset represents the Group's right to recover the goods expected to be returned by customers. The asset is measured at the former carrying amount of the inventory, less any expected costs to recover the goods, including any potential decreases in the value of the returned goods. The Group updates the measurement of the asset recorded for any revisions to its expected level of returns, as well as any additional decreases in the value of the returned products.

Refund liabilities

A refund liability is the obligation to refund some or all of the consideration received (or receivable) from the customer and is measured at the amount the Group ultimately expects it will have to return to the customer. The Group updates its estimates of refund liabilities (and the corresponding change in the transaction price) at the end of each reporting period.

Principal versus agent considerations

The determination of whether the Group is acting as a principal or an agent affects the amount of revenue the Group recognizes. The Group is a principal (and, therefore, records revenue on a gross basis) if it controls a promised good or service before transferring that good or service to the customer. The Group is an agent (and, therefore, records as revenue the net amount that it retains for its agency services) if its role is to arrange for another entity to provide the goods or services.

Accounting for underlift and overlift positions

The Group has shareholding interests in the joint operations. The Group may be in the overlift and underlift position in the mentioned joint arrangements. The Group is in the overlift position, when the Group lifted and sold to a customer more product than its proportionate entitlement based on its share in the joint operation. The Group is in the underlift position, when the Group lifted and sold less product than its proportionate entitlement based on its share in the joint operation.

The Group recognizes revenue from contracts with customers under IFRS 15 based on its actual sales to customers in that period. No adjustments are recorded in revenue to account for any variance between the actual share of production volumes sold to date and the share of production which the Group has been entitled to sell to date.

The Group adjusts production costs to align volumes for which production costs are recognized with volumes sold (for which revenue has been recognized in accordance with IFRS 15).

The Group applies the physical settlement. In case of physical settlement:

- An overlift liability is recorded in accordance with the provisions under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. The overlift liability is recorded at cost.
- An underlift asset gives the Group the right to receive a quantity of product from another participant. This right is equivalent to a prepaid forward commodity purchase or represents a right to additional physical inventory and therefore, IAS 2 *Inventories* is applied. The underlift asset is measured at the lower of cost or net realisable value.

2. Basis of preparation and significant accounting policies (continued)

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 10 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.

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.

2. Basis of preparation and significant accounting policies (continued)

Acquisition of an entity that is not a business

When the Group acquires an entity that is not a business, it allocates the cost of acquisition between the individual identifiable assets and liabilities of the acquired entity as following:

- For identifiable asset and liability initially measured at an amount other than cost, an entity initially measures that asset or liability at the amount specified in the applicable IFRS Standard;
- The entity deducts from the transaction price of the acquired entity the amounts allocated to the assets and liabilities initially measured at an amount other than cost, and then allocates the residual transaction price to the remaining identifiable assets and liabilities based on their relative fair values at the date of the acquisition.

Step-acquisition of subsidiary that is not a business

Step-acquisition of subsidiary which has been previously accounted for as investment in associates and joint ventures ("the investee") are recognized in the amount being the carrying value under the equity method related to the original interest in the investee plus cost of additional investments made by the Group in order to obtain control over the investee ("deemed cost"). Upon obtaining control over the investee it becomes subsidiary of the Group and deemed cost is allocated to the individual identifiable assets and liabilities of the subsidiary applying the same approach used for acquisition of an entity that is not a business.

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 the lower of their carrying amount and fair value less costs to sell.

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.

3. Critical accounting estimates and judgments

The preparation of the Group's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures, and the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods. In the process of applying the Group's accounting policies, management has made judgements, which have the most significant effect on the amounts recognised in the consolidated financial statements.

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Group based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising that are beyond the control of the Group. Such changes are reflected in the assumptions when they occur.

Estimation of oil and gas reserves

Oil and gas reserves are key elements in the Group's investment decision-making process. 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 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.

In addition oil and gas reserves are significant component of testing for impairment of respective CGUs. It is estimated that, if all production were to be reduced by 10 per cent for the next 20 years, this would result in additional impairment charge of AZN 226.

Proved reserves of the SOCAR as of 31 December 2018 were based on reports prepared by independent reservoir engineers in accordance with Petroleum Resources Management System rules. For certain assets proved reserves are based on estimation of internal engineers.

3. Critical accounting estimates and judgments (continued)

Asset retirement obligations

The management makes provision in respect of the Group's legal and constructive obligations 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 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. These costs are expected to be incurred over the useful life of the fields and properties ranging between 9 and 64 years from the reporting date.

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 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. Considering subjectivity of these provisions, there is uncertainty regarding both the amount and estimated timing of incurring such costs. The key assumptions used to measure the amount of the estimated asset retirement obligations and sensitivity analysis, are disclosed in Note 22.

Environmental obligations

The Group records a provision in respect of constructive obligations related to 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.

Considering subjectivity of these provisions, there is uncertainty regarding both the amount and estimated timing of incurring such costs. The key assumptions used to measure the amount of the estimated environmental obligations and sensitivity analysis, are disclosed in Note 23.

Disability provision

The Group records a provision in accordance with Azerbaijan Labour Code and has an obligation to pay compensation for employees damaged at work. 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. Considering subjectivity of these provisions, there is uncertainty regarding both the amount and estimated timing of incurring such costs. The key assumptions used to measure the amount of the estimated disability obligations and sensitivity analysis, are disclosed in Note 23.

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. 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.

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 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 intangible assets with indefinite useful life 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.

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs of disposal and its value in use. The fair value less costs of disposal calculation is based on available data from binding sales transactions, conducted at arm's length, for similar assets or observable market prices less incremental costs of disposing of the asset. The value in use calculation is based on a DCF model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Group is not yet committed to or significant future investments that will enhance the performance of the assets of the CGU being tested. The key assumptions used to determine the recoverable amount for the different CGUs and sensitivity analysis are disclosed in Note 15.

Provision for expected credit losses of financial assets

Trade receivables including contract assets

The Group uses a provision matrix to calculate ECLs for trade receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography, product type, customer type and rating, and coverage by letters of credit and other forms of credit insurance).

The provision matrix is initially based on the Group's historical observed default rates. The Group calibrates the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic product) are expected to deteriorate over the next year which can lead to an increased number of defaults in the manufacturing sector, the historical default rates are adjusted. At every reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analysed.

The assessment of the correlation between historical observed default rates, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and forecast economic conditions. The Group's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future. The information about the ECLs on the Group's trade receivables and contract assets is disclosed in Note 10.

Other financial assets recognized at amortized cost

The Group calculated ECL for other financial assets such as cash and deposit accounts as well as restricted accounts in several local and international banks using the general approach as disclosed in Note 2. The assessment of ECLs is significant estimate considering that it is sensitive to changes in circumstances of counterparties and economic conditions. The information about the ECLs on the Group's bank accounts are disclosed in Note 8 for cash and cash equivalents and Note 9 for restricted cash.

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 amendments to IFRS effective beginning on or after 1 January 2018:

The Group applied IFRS 9 and IFRS 15 for the first time. The nature and effect of the changes as a result of adoption of these new accounting standards are described below.

Several other amendments and interpretations apply for the first time in 2018, but do not have an impact on the consolidated financial statements of the Group. The Group has not early adopted any standards, interpretations or amendments that have been issued, but are not yet effective.

IFRS 9 Financial Instruments

IFRS 9 *Financial Instruments* replaces IAS 39 *Financial Instruments: Recognition and Measurement* for reporting periods beginning on or after 1 January 2018, bringing together all three aspects of the accounting for financial instruments: classification and measurement; impairment; and hedge accounting.

The Group applied IFRS 9 retrospectively choosing not to restate prior year figures. Prior year figures for the assets, which are now within the scope of IFRS 9, were presented in accordance with IAS 39 and will not be comparable to the information related to 2018. Differences arising from the adoption of IFRS 9, have been recognized directly in retained earnings and non-controlling interests (NCI) as of 1 January 2018 and are disclosed below.

(a) Classification and measurement

Under IFRS 9, all debt financial assets that do not meet a "solely payment of principal and interest" (SPPI) criterion, are classified at initial recognition as financial assets at fair value through profit or loss (FVPL). Debt financial assets that meet the SPPI criterion are measured either at fair value through profit or loss, amortized cost or at fair value through other comprehensive income (FVOCI). The classification for the debt financial assets that meets the SPPI criterion is based on the Group's business model for managing these assets:

- Financial assets that are managed under "hold to collect" basis that are measured at amortized cost;
- Financial assets that are managed under "hold to collect and sell" basis that are measured at FVOCI;
- Financial assets that are managed under "held for trading" basis that are measured at FVPL.

The assessment of the Group's business models is made as of the date of initial application, 1 January 2018 and then applies retrospectively to those financial assets that were not derecognised before 1 January 2018. The assessment of whether contractual cash flows on debt instruments are solely comprised of principal and interest is made based on the facts and circumstances not only as at the date of the initial recognition of the assets, but also as at the date of substantial modification.

Upon adoption of IFRS 9, following changes to classification and measurement of financial assets were made:

- Trade and loans receivables and other financial assets (i.e., cash and deposit balances) previously classified as Loans and receivables are held to collect contractual cash flows and give rise to cash flows representing solely payments of principal and interest. These are now classified and measured as Debt instruments at amortised cost.
- Group of trade receivables that were previously classified as Loans and receivables are held both to collect contractual cash flows and sell to meet liquidity needs for the day-to-day trading activities and give rise to cash flows representing solely payments of principal and interest are now classified as Debt instruments at fair value though OCI.
- Equity instruments that were previously classified as AFS financial assets are now classified as Equity instruments at FVOCI upon initial recognition or transition to IFRS 9 since the Group intends to hold such assets for the foreseeable future and irrevocably elected to classify them to be measured at OCI. Equity instruments at FVOCI are not subject to an impairment assessment under IFRS 9. There were no impairment losses recognised in profit or loss for these investments in prior periods.

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

IFRS 9 Financial Instruments (continued)

The classification and measurement of financial liabilities remains largely unchanged from requirements of IAS 39 requirements. Derivatives will continue to be measured at FVPL. However, embedded derivatives are no longer separated from a host financial asset.

(b) Impairment

The adoption of IFRS 9 has fundamentally changed the Group's accounting for impairment charge for financial assets by replacing incurred loss approach of IAS 39 with a forward-looking ECL approach. From 1 January 2018, the Group has been recording the allowance for ECLs for all loans and other debt financial assets not held at FVPL.

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12mECL). The 12mECL is the portion of LTECL that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

The Group has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above process, the Group groups its financial instrument into Stage 1, Stage 2, Stage 3 and POCI, as described below:

Stage 1: When financial instrument is first recognised, the Group recognises an allowance based on 12mECL. Stage 1 financial instrument also include facilities where the credit risk has improved and the financial instrument has been reclassified from Stage 2.

Stage 2: When a financial instrument has shown a significant increase in credit risk since origination, the Group records an allowance for the LTECL. Stage 2 financial instrument also include facilities, where the credit risk has improved and the financial instrument has been reclassified from Stage 3.

Stage 3: Financial instrument considered credit-impaired. The Group records an allowance for the LTECL.

POCI: Purchased or originated credit impaired (POCI) assets are financial assets that are credit impaired on initial recognition. POCI assets are recorded at fair value at original recognition and interest income is subsequently recognised based on a credit-adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the expected credit losses.

The mechanics of the ECL calculations are outlined below and the key elements are as follows:

PD The *Probability of Default* is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.

EAD The *Exposure at Default* is an estimate of the exposure at a future default date.

LGD The *Loss Given Default* is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

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

IFRS 9 Financial Instruments (continued)

Effect of transition to IFRS 9

The following tables set out the impact of adopting IFRS 9 on the statement of financial position and retained earnings as at 1 January 2018 including the effect of replacing IAS 39 incurred credit loss calculations with IFRS 9 ECL:

The effect of adopting IFRS 9 as at 1 January 2018 was as follows:

		IAS 39 measurement		Reclas-sification	Remeasu-rement	IFRS 9 measurement	
	Notes	Category	Amount		ECL	Amount	Category
Financial assets							
Cash and cash equivalents	8	L&R	5,217	–	(21)	5,196	Amortized cost
Restricted cash		L&R	229	–	(1)	228	Amortized cost
Deposits	8	L&R	218	–	(4)	214	Amortized cost
Available-for-sale investments		AFS	174	(174)	–	–	FVOCI
Trade and other receivables		L&R	8,015	(1,580)	(35)	6,400	Amortized cost
Trade and other receivables at FVOCI		L&R	–	1,580	–	1,580	FVOCI
Other current financial assets, including:							
- loan receivables from third parties		L&R	23	–	–	23	Amortized cost
- receivables from PSA parties		L&R	578	–	–	578	Amortized cost
- loan receivable from joint venture		L&R	6	–	–	6	Amortized cost
- derivatives		FVPL	927	–	–	927	FVPL
- other		FVOCI	–	174	–	174	FVOCI
Other long-term financial assets, including:							
- loan receivables from third parties and related parties		L&R	281	–	–	281	Amortized cost
- long-term deposit		L&R	51	–	(3)	48	Amortized cost
- derivative instruments		FVPL	353	–	–	353	FVPL
Total financial assets			16,072	–	(64)	16,008	

	Retained earnings and NCI
Closing balance of retained earnings under IAS 39 (31 December 2017)	**7,357**
IFRS 9 ECL effect on retained earnings	(62)
Restated opening balance under IFRS 9 (1 January 2018)	**7,295**
Closing balance of NCI under IAS 39 (31 December 2017)	**1,370**
IFRS 9 ECL effect on NCI	(2)
Restated opening balance under IFRS 9 (1 January 2018)	**1,368**
Total change in equity	**(64)**

Movement of provision as at 1 January 2018:

	Provision under IAS 39 at 31 December 2017	Re-measurement	ECLs under IFRS 9 at 1 January 2018
Impairment allowance for:			
Cash and cash equivalents	–	21	21
Restricted cash	–	1	1
Deposits	–	4	4
Trade and other receivables	816	35	851
Other non-current financial assets	–	3	3
Total provision on financial assets	**816**	**64**	**880**

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

IFRS 15 Revenue from Contracts with Customers

IFRS 15 supersedes IAS 11 *Construction Contracts*, IAS 18 *Revenue* and related Interpretations and it applies, with limited exceptions, to all revenue arising from contracts with customers. IFRS 15 establishes a five-step model to account for revenue arising from contracts with customers and requires that revenue be 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.

IFRS 15 requires entities to exercise judgement, taking into consideration all of the relevant facts and circumstances when applying each step of the model to contracts with their customers. The standard also specifies the accounting for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract. In addition, the standard requires extensive disclosures.

The Group adopted IFRS 15 using the modified retrospective method of adoption with the date of initial application of 1 January 2018. Under this method, the standard can be applied either to all contracts at the date of initial application or only to contracts that are not completed at this date. The Group elected to apply the standard to new and not completed contracts as at 1 January 2018.

The cumulative effect of initially applying IFRS 15 is recognised at the date of initial application as an adjustment to the opening balance of retained earnings. Therefore, the comparative information was not restated and continues to be reported under IAS 11, IAS 18 and related Interpretations.

Effect of transition to IFRS 15

Transition to IFRS 15 resulted in decrease in retained earnings of the Group by AZN 60 including deferred tax benefit of AZN 20 at 1 January 2018, which is mainly due to change in accounting for overlift liabilities and underlift assets.

Set out below, are the amounts by which each financial statement line item is affected as at and for the year ended 31 December 2018 as a result of the adoption of IFRS 15. The adoption of IFRS 15 did not have a material impact on OCI or the Group's operating, investing and financing cash flows.

Consolidated statements of Profit or Loss for the period ended on 31 December 2018:

		Amounts prepared under		Increase/
	Notes	IFRS 15	Previous IFRS	(decrease)
Revenues	(a)	111,198	111,229	(31)
Cost of sales	(a)	(105,468)	(105,490)	(22)
Gross profit		**5,730**	**5,739**	**(9)**
Profit before tax		**2,220**	**2,229**	**(9)**
Income tax expense	(a)	(996)	(998)	(2)
Profit for the period		**1,224**	**1,231**	**(7)**

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

IFRS 15 Revenue from Contracts with Customers (continued)

Consolidated statements of Financial Position for the period ended on 31 December 2018:

	Notes	Amounts prepared under IFRS 15	Amounts prepared under Previous IFRS	Increase/ (decrease)
Trade and other receivables	(a)	8,395	8,493	(98)
Remaining current assets		10,897	10,897	–
Total current assets		**19,292**	**19,390**	**(98)**
Total non-current assets		**42,844**	**42,844**	**–**
Total assets		**62,136**	**62,234**	**(98)**
Total equity		**23,944**	**24,011**	**(67)**
Trade and other payables	(a), (b)	11,780	12,108	(328)
Contract liabilities	(b)	305	–	305
Other provisions for liabilities and charges	(c)	56	41	15
Remaining current liabilities		5,226	5,226	–
Total current liabilities		**17,367**	**17,375**	**(8)**
Deferred tax liability	(a)	1,412	1,435	(23)
Remaining non-current liabilities		19,413	19,413	–
Total non-current liabilities		**20,825**	**20,848**	**(23)**
Total liabilities		**38,192**	**38,223**	**(31)**
Total liabilities and equity		**62,136**	**62,234**	**(98)**

The nature of the adjustments and the reasons for the significant changes in the statement of financial position as at 31 December 2018 and the statement of profit or loss for the year ended 31 December 2018 are described below:

(a) Accounting for overlift liability and underlift assets

Before adoption of IFRS 15 Group used entitlements method and recognized net revenue reflecting its share in production regardless of actual sales made and invoices issued by PSA participants to customers. This was achieved by adjusting actual sold volume for the production imbalances which is any variance between actual share of production volume sold to date and the share of production which the party has been entitled to sell to date.

However, under IFRS 15, revenue shall be recognized based on actually sold volume of products. Therefore, the Group adjusted its cost of sales for production imbalances in order to align with the actually sold volumes.

- Under previous standard the Group measured the overlift liability and underlift asset using the market price of crude oil at the date of lifting at initial recognition. Subsequent measurement of overlift/underlift liabilities and assets depended on the settlement terms of the related operating agreements. If such terms allowed for a cash settlement between parties, the balances were re-measured at fair value at reporting dates subsequent to initial recognition. Production imbalances that are settled through delivery of physical quantities of crude oil were measured at the lower of carrying amount and fair value.

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

IFRS 15 Revenue from Contracts with Customers (continued)

The Group generally applies physical settlement for the production imbalances. Thus, upon transition to IFRS 15 physical settlement terms of the operating agreements of PSAs resulted in following changes in measurement of overlift liabilities and underlift assets:

- Overlift liabilities meets the definition of a provision under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, which requires the provision amount to be the best estimate of the management. Thus the Group applied cost method for measuring its overlift liabilities and adjusted its Cost of Sales figures for the imbalance amount.

  Underlift assets give the joint operation participant the right to receive a quantity of product from another participant. This right would be equivalent to a prepaid forward commodity purchase or may be considered to represent a right to additional physical inventory and therefore, IAS 2 *Inventories* should be applied by analogy. The underlift asset is measured at the lower of cost or net realisable value.

(b) Contract liabilities

A contract liability is the obligation to transfer goods or services to a customer for which the Group has received consideration (or an amount of consideration is due) from the customer. If a customer pays consideration before the Group transfers goods or services to the customer, a contract liability is recognized when the payment is made or the payment is due (whichever is earlier).

Upon adoption of IFRS 15, the Group reclassified amounts received from customers of AZN 305 from Trade and Other Payables to Contract Liabilities line.

(c) Onerous Contracts Presentation

IFRS 15 contains no specific requirements to address contracts with customers that are, or have become, onerous, except for presentation requirements for contract assets and liabilities. The requirements of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* still applies to identification and measurement of onerous customer contracts.

IFRS 15 Revenue from Contracts with Customers

In order to follow the identification and measurement requirements of IAS 37 and presentation requirements of IFRS 15, loss in the amount of AZN 15 was recorded and presented in other provisions for liabilities and charges.

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) on the de-recognition 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 the date of the transactions for each payment or receipt of advance consideration. This Interpretation does not have any impact on the Group's consolidated financial statements.

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. These amendments do not have any impact on the Group's consolidated financial statements.

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

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 Group's accounting policy for cash-settled share based payments is consistent with the approach clarified in the amendments. In addition, the Group has no share-based payment transaction with net settlement features for withholding tax obligations and had not made any modifications to the terms and conditions of its share-based payment transaction. Therefore, these amendments do not have any impact on the Group's consolidated financial statements.

IFRS 4 Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – Amendments to IFRS 4

The amendments address concerns arising from implementing the new financial instruments standard, IFRS 9, before implementing IFRS 17 *Insurance Contracts*, which replaces IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach. These amendments do not have any impact on the Group's consolidated financial statements.

IAS 28 Investments in Associates and Joint Ventures – Clarification that measuring investees at fair value through profit or loss is an investment-by-investment choice

The amendments clarify that an entity that is a venture capital organisation, or other qualifying entity, may elect, at initial recognition on an investment-by-investment basis, to measure its investments in associates and joint ventures at fair value through profit or loss. If an entity, that is not itself an investment entity, has an interest in an associate or joint venture that is an investment entity, the entity may, when applying the equity method, elect to retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries. This election is made separately for each investment entity associate or joint venture, at the later of the date on which: (a) the investment entity associate or joint venture is initially recognised; (b) the associate or joint venture becomes an investment entity; and (c) the investment entity associate or joint venture first becomes a parent. These amendments do not have any impact on the Group's consolidated financial statements.

Annual improvements 2015-2017 cycle

These improvements include:

IFRS 1 First-time Adoption of International Financial Reporting Standards – Deletion of short-term exemptions for first-time adopters

Short-term exemptions stated in IFRS 1 were deleted because they have now served their intended purpose. The amendment is effective from 1 January 2018. This amendment is not applicable to the Group.

IFRS 3 Business Combinations

The amendments clarify that, when an entity obtains control of a business that is a joint operation, it applies the requirements for a business combination achieved in stages, including remeasuring previously held interests in the assets and liabilities of the joint operation at fair value. In doing so, the acquirer remeasures its entire previously held interest in the joint operation.

An entity applies those amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted. These amendments will apply on future transactions of the Group.

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

Annual improvements 2015-2017 cycle (continued)

IFRS 11 Joint Arrangements

A party that participates in, but does not have joint control of, a joint operation might obtain joint control of the joint operation in which the activity of the joint operation constitutes a business as defined in IFRS 3. The amendments clarify that the previously held interest in that joint operation are not remeasured.

An entity applies those amendments to transactions in which it obtains joint control on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted. These amendments are currently not applicable to the Group but may apply to future transactions.

IAS 12 Income Taxes

The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognises the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where the entity originally recognised those past transactions or events.

An entity applies those amendments for annual reporting periods beginning on or after 1 January 2019, with early application is permitted. When an entity first applies those amendments, it applies them to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period. Since the Group's current practises is in line with these amendments, the Group does not expect any effect on its consolidated financial statements.

IAS 23 Borrowing Costs

The amendments clarify that an entity treats as part of general borrowings any borrowing originally made to develop qualifying asset when substantially all of the activities necessary to prepare that asset for its intended use or sale are complete.

An entity applies those amendments to borrowing costs incurred on or after the beginning of the annual reporting period in which the entity first applies those amendments. An entity applies those amendments for annual reporting period beginning on or after 1 January 2019, with early application permitted. Since the Group's current practice is in line with these amendments, the Group does not expect any effect on its consolidated financial statements.

IFRS 3 Business Combinations – Definition of a business

The amendments clarify that to be considered a business, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output. They also clarify that a business can exist without including all of the inputs and processes needed to create outputs. That is, the inputs and processes applied to those inputs must have 'the ability to contribute to the creation of outputs' rather than 'the ability to create outputs'.

The amendments specify that if a set of activities and assets does not have outputs at the acquisition date, an acquired process must be considered substantive only if: (a) it is critical to the ability to develop or convert acquired inputs into outputs; and (b) the inputs acquired include both an organized workforce with the necessary skills, knowledge, or experience to perform that process, and other inputs that the organized workforce could develop or convert into outputs. In contrast, if a set of activities and assets has outputs at that date, an acquired process must be considered substantive if: (a) it is critical to the ability to continue producing outputs and the acquired inputs include an organized workforce with the necessary skills, knowledge, or experience to perform that process; or (b) it significantly contributes to the ability to continue producing outputs and either is considered unique or scarce, or cannot be replaced without significant cost, effort or delay in the ability to continue producing outputs. The amendments narrowed the definition of outputs to focus on goods or services provided to customers, investment income (such as dividends or interest) or other income from ordinary activities.

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

Annual improvements 2015-2017 cycle (continued)

The amendments introduced an optional fair value concentration test to permit a simplified assessment of whether an acquired set of activities and assets is not a business. Entities may elect to apply the concentration test on a transaction-by-transaction basis. The test is met if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or group of similar identifiable assets. If the test is met, the set of activities and assets is determined not to be a business and no further assessment is needed. If the test is not met, or if an entity elects not to apply the test, a detailed assessment must be performed applying the normal requirements in IFRS 3. The amendments must be applied to transactions that are either business combinations or asset acquisitions for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2020. Consequently, entities do not have to revisit such transactions that occurred in prior periods. Earlier application is permitted and must be disclosed. The Group will apply amendment form its effective date.

Amendments to IAS 1 and IAS 8

In October 2018, the IASB issued amendments to IAS 1 *Presentation of Financial Statements* and IAS 8 to align the definition of 'material' across the standards and to clarify certain aspects of the definition. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.' The amendments clarify that materiality will depend on the nature or magnitude of information, or both. An entity will need to assess whether the information, either individually or in combination with other information, is material in the context of the financial statements. The amendments must be applied prospectively. Early application is permitted and must be disclosed. Although the amendments to the definition of material is not expected to have a significant impact on the Group's consolidated financial statements, the introduction of the term 'obscuring information' in the definition could potentially impact how materiality judgements are made in practice, by elevating the importance of how information is communicated and organised in the consolidated financial statements.

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 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 remeasure 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 remeasurement 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.

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

Standards issued but not yet effective (continued)

IFRS 16, which is effective for annual periods beginning on or after 1 January 2019, requires lessees and lessors to make more extensive disclosures than under IAS 17.

Transition to IFRS 16

The Group plans to adopt IFRS 16 from effective date applying the modified retrospective transition method and will elect to apply the practical expedient that permits the entity not to reassess whether a contract is, or contains, a lease at the date of initial application. In addition, the Group will elect to use the exemptions applicable to the standard on lease contracts for which the lease terms end within 12 months as of the date of initial application, and lease contracts for which the underlying asset is of low value. The Group is in the process of impact assessment of IFRS 16.

IFRS 17 Insurance Contracts

In May 2017, the IASB issued IFRS 17 *Insurance Contracts* (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 *Insurance Contracts* (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features. A few scope exceptions will apply. The overall objective of IFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers. In contrast to the requirements in IFRS 4, which are largely based on grandfathering previous local accounting policies, IFRS 17 provides a comprehensive model for insurance contracts, covering all relevant accounting aspects. The core of IFRS 17 is the general model, supplemented by:

- A specific adaptation for contracts with direct participation features (the variable fee approach);
- A simplified approach (the premium allocation approach) mainly for short-duration contracts.

IFRS 17 is effective for reporting periods beginning on or after 1 January 2021, with comparative figures required. Early application is permitted, provided the entity also applies IFRS 9 and IFRS 15 on or before the date it first applies IFRS 17. This standard is not applicable to the Group.

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 and does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments.

The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately;
- The assumptions an entity makes about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates;
- How an entity considers changes in facts and circumstances.

An entity must determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments. The approach that better predicts the resolution of the uncertainty should be followed. The interpretation is effective for annual reporting periods beginning on or after 1 January 2019, but certain transition reliefs are available. The Group will apply interpretation from its effective date. Since the Group operates in a complex multinational tax environment, applying the Interpretation may affect its consolidated financial statements and the required disclosures. In addition, the Group may need to establish processes and procedures to obtain information that is necessary to apply the Interpretation on a timely basis.

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

Standards issued but not yet effective (continued)

Amendments to IFRS 9: Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortised cost or at fair value through other comprehensive income, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the SPPI criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract.

The basis for conclusions to the amendments clarified that the early termination can result from a contractual term or from an event outside the control of the parties to the contract, such as a change in law or regulation leading to the early termination of the contract. The amendments are effective for annual periods beginning on or after 1 January 2019. The Group does not expect any effect of this amendment on its consolidated financial statements.

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

The amendments address the 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.

Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures

The amendments clarify that an entity applies IFRS 9 to long-term interests in associate or joint venture to which the equity method is not applied but that, in substance, from part of the net investment in the associate or joint venture (long-term interests). This clarification is relevant because it implies that the ECL model in IFRS 9 applies to such long-term interest.

The amendments also clarified that, in applying IFRS 9, an entity does not take account of any losses of the associate or joint venture, or any impairment charge on the net investment, recognised as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 *Investment in Associates and Joint Ventures*.

The amendments should be applied retrospectively and are effective from 1 January 2019, with early application permitted. Since the Group does not have such long-term interests in its associate and joint venture, the amendments will not have an impact on its consolidated financial statements.

Amendments to IAS 19 Plan Amendment, Curtailment or Settlement

The amendments to IAS 19 address the accounting when a plan amendment, curtailment or settlement occurs during a reporting period. The amendments specify that when a plan amendment, curtailment or settlement occurs during the annual reporting period, an entity is required to:

- Determine current service cost for the remainder of the period after the plan amendment, curtailment or settlement, using the actuarial assumptions used to remeasure the net defined benefit liability (asset) reflecting the benefits offered under the plan and the plan assets after that event.
- Determine net interest for the remainder of the period after the plan amendment, curtailment or settlement using: the net defined benefit liability (asset) reflecting the benefits offered under the plan and the plan assets after that event; and the discount rate used to remeasure that net defined benefit liability (asset).

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

Standards issued but not yet effective (continued)

The amendments also clarify that an entity first determines any past service cost, or a gain or loss on settlement, without considering the effect of the asset ceiling. This amount is recognised in profit or loss. An entity then determines the effect of the asset ceiling after the plan amendment, curtailment or settlement. Any change in that effect, excluding amounts included in the net interest, is recognised in other comprehensive income. The amendments apply to plan amendments, curtailments, or settlements occurring on or after the beginning of the first annual reporting period that begins on or after 1 January 2019, with early application permitted.

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.

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 2018 is set out below:

	Oil and gas	Refinery	Construc-tion	Sales and distribution	Unalloca-ted (*)	Adjust-ments and elimina-tions (**)	Total
2018							
Revenues							
External customers	3,120	5,021	779	102,135	143	–	**111,198**
Inter-segment	2,495	622	795	27,276	450	(31,638)	–
Total revenue	**5,615**	**5,643**	**1,574**	**129,411**	**593**	**(31,638)**	**111,198**
Other operating income	194	403	26	377	13	(97)	**916**
Finance income	5	148	2	155	1,227	(1,325)	**212**
Foreign exchange (losses)/ gains (net)	(31)	(311)	(4)	15	13	(380)	**(698)**
Raw materials and consumables used	(1,008)	(4,118)	(294)	(126,883)	(84)	30,560	**(101,827)**
Wages, salaries and social security costs	(246)	(320)	(267)	(533)	(267)	123	**(1,510)**
Depreciation of property, plant and equipment	(793)	(154)	(123)	(228)	(105)	12	**(1,391)**
Transportation and vehicle maintenance	(446)	(20)	(153)	(803)	(32)	271	**(1,183)**
Expected credit (loss)/reversal	(153)	(5)	4	80	6	153	**85**
Impairment of property, plant and equipment	(155)	–	–	(7)	1	–	**(161)**
Mining tax	(126)	–	–	–	–	–	**(126)**
Taxes other than on income	(74)	(18)	(3)	(31)	(74)	1	**(199)**
Amortization expense	–	(13)	(1)	(21)	(9)	1	**(43)**
Repairs and maintenance expenses	(301)	(32)	(131)	(44)	(5)	182	**(331)**
Utilities expense	(16)	(276)	(2)	(82)	(3)	5	**(374)**
Change in other provisions for liabilities and charges	(4)	(52)	(21)	(6)	–	–	**(83)**
Other	(518)	(227)	(280)	(437)	(394)	600	**(1,256)**
Loss on disposal of property, plant and equipment and intangible assets	(2)	(11)	(3)	(2)	3	–	**(15)**
Finance costs	(104)	(482)	(26)	(260)	(570)	316	**(1,126)**
Social expenses	(9)	(7)	(2)	(5)	(82)	–	**(105)**
Share of result of joint ventures	13	124	65	–	11	–	**213**
Share of result of associates	–	–	–	(17)	41	–	**24**
Income tax expenses	(612)	(110)	(118)	(82)	(74)	–	**(996)**
Net profit/(loss) for the year	**1,229**	**162**	**243**	**597**	**209**	**(1,216)**	**1,224**

(*) These figures 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.

5. Segment information (continued)

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

	Oil and gas	Refining	Construction	Sales and distribution	Unallocated (*)	Adjustments and eliminations (**)	Total
Investments in associates	–	–	–	4,328	31	–	4,359
Investments in joint ventures	38	4,978	237	4	44	–	5,301
Other reportable segment assets	23,595	11,826	2,650	19,887	19,468	(24,950)	52,476
Total reportable segment assets	**23,633**	**16,804**	**2,887**	**24,219**	**19,543**	**(24,950)**	**62,136**
Total reportable segment liabilities	**(10,372)**	**(8,368)**	**(1,792)**	**(19,896)**	**(15,030)**	**17,266**	**(38,192)**
Capital expenditure (***)							
Additions – business units, JV and associates	1,114	1,540	76	207	59	(18)	2,978
Additions – subsidiaries	1,359	1,352	(9)	217	2	(102)	2,819
Acquisition through business combination (APMT business) (Note 39)	–	–	–	156	–	–	156
Acquisition through business combination (Austrian business) (Note 39)	–	–	–	112	–	–	112
Total capital expenditures	**2,473**	**2,892**	**67**	**692**	**61**	**(120)**	**6,065**

(*) These figures 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.

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 2017 is set out below:

	Oil and gas	Refining	Construction	Sales and distribution	Unallocated (*)	Adjustments and eliminations (**)	Total
2017							
Revenues							
External customers	2,052	4,979	1,000	84,523	17	–	**92,571**
Inter-segment	2,260	583	581	18,815	450	(22,689)	–
Total revenue	**4,312**	**5,562**	**1,581**	**103,338**	**467**	**(22,689)**	**92,571**
Other operating income	472	49	17	359	167	(115)	**949**
Finance income	11	126	–	118	1,467	(1,605)	**117**
Foreign exchange (losses)/gains (net)	(37)	(66)	22	106	187	(102)	**110**
Raw materials and consumables used	(876)	(3,896)	(295)	(100,797)	(87)	21,575	**(84,376)**
Depreciation of property, plant and equipment	(515)	(177)	(116)	(216)	(75)	34	**(1,065)**
Wages, salaries and social security costs	(211)	(313)	(250)	(469)	(241)	113	**(1,371)**
Transportation and vehicle maintenance	(377)	(26)	(133)	(887)	(34)	411	**(1,046)**
Repairs and maintenance expenses	(257)	(12)	(131)	(43)	(9)	174	**(278)**
Impairment of property, plant and equipment	(431)	(1)	(31)	(5)	–	–	**(468)**
Mining tax	(123)	–	–	–	–	–	**(123)**
Utilities expense	(17)	(229)	(2)	(91)	(3)	1	**(341)**
Taxes other than on income	(63)	(27)	(3)	(27)	(79)	1	**(198)**
Amortization expense	(1)	(15)	–	(18)	(8)	1	**(41)**
Impairment of trade and other receivables and other financial assets	(2)	(3)	(1)	(232)	(1)	–	**(239)**
Change in other provisions for liabilities and charges	19	3	3	(1)	(13)	–	**11**
Other	(323)	(183)	(581)	(467)	(180)	422	**(1,312)**
Loss on disposal of property, plant and equipment and intangible assets	42	(11)	(2)	(12)	(43)	–	**(26)**
Finance costs	(91)	(155)	(26)	(231)	(636)	249	**(890)**
Social expenses	(13)	(11)	(3)	(6)	(92)	–	**(125)**
Share of result of joint ventures	9	388	90	3	33	–	**523**
Share of result of associates	–	–	–	135	(1)	–	**134**
Income tax expenses	(221)	(125)	(21)	(85)	28	–	**(424)**
Net profit/(loss) for the year	**1,307**	**878**	**118**	**472**	**847**	**(1,530)**	**2,092**

(*) These figures 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.

5. Segment information (continued)

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

	Oil and gas	Refining	Construction	Sales and distribution	Unallocated (*)	Adjustments and eliminations (**)	Total
Investments in associates	–	–	–	4,555	16	–	**4,571**
Investments in joint ventures	33	4,697	238	4	50	–	**5,022**
Other reportable segment assets	21,582	10,436	2,290	21,637	16,559	(20,750)	**51,754**
Total reportable segment assets	**21,615**	**15,133**	**2,528**	**26,196**	**16,625**	**(20,750)**	**61,347**
Total reportable segment liabilities	**(9,092)**	**(7,437)**	**(1,523)**	**(22,523)**	**(12,840)**	**14,043**	**(39,372)**
Capital expenditure (***)							
Additions – business units, JV and associates	716	1,030	37	339	170	(43)	**2,249**
Additions – subsidiaries	1,062	1,610	58	534	3	–	**3,267**
Acquisition of additional interest in ACG PSA	3,059	–	–	–	–	–	**3,059**
Acquisition of 80 per cent interest in UBEP	506	–	–	–	–	–	**506**
Total capital expenditures	**5,343**	**2,640**	**95**	**873**	**173**	**(43)**	**9,081**

(*) These figures 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.

Geographical information

Revenues for each individual country are reported separately as follows:

	2018	2017
Switzerland	94,503	78,633
Azerbaijan	6,626	5,382
Turkey	4,972	4,925
UAE	2,352	1,324
Georgia	1,124	1,185
Other	1,621	1,122
Total consolidated revenues	**111,198**	**92,571**

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

5. Segment information (continued)

Set out below is the disaggregation of the Group's revenue from contracts with customers:

Segments	Oil and gas	Refining	Construction	Sales and distribution	Unallocated (*)	Total
Sale of crude oil, net	2,186	–	–	56,275	1	**58,462**
Sale of oil products, net	473	1,459	–	38,161	–	**40,093**
Sale of petrochemicals	–	3,441	–	453	–	**3,894**
Sale of natural gas	227	3	–	2,961	–	**3,191**
Other revenue	234	118	779	4,285	142	**5,558**
Total	**3,120**	**5,021**	**779**	**102,135**	**143**	**111,198**
Switzerland	–	–	–	94,503	–	**94,503**
Azerbaijan	3,120	50	779	2,536	141	**6,626**
Turkey	–	4,971	–	1	–	**4,972**
UAE	–	–	–	2,352	–	**2,352**
Georgia	–	–	–	1,122	2	**1,124**
Other	–	–	–	1,621	–	**1,621**
Total	**3,120**	**5,021**	**779**	**102,135**	**143**	**111,198**
Good transferred at a point in time	3,117	4,993	607	101,509	136	**110,362**
Services transferred over time	3	28	172	626	7	**836**
Total revenue from contracts with customers	**3,120**	**5,021**	**779**	**102,135**	**143**	**111,198**
Revenue						
External customer	3,120	5,021	779	102,135	143	**111,198**
Inter-segment	2,495	622	795	27,276	450	**31,638**
Total	**5,615**	**5,643**	**1,574**	**129,411**	**593**	**142,836**
Adjustment and eliminations	(2,495)	(622)	(795)	(27,276)	(450)	**(31,638)**
Total revenue from contracts with customers	**3,120**	**5,021**	**779**	**102,135**	**143**	**111,198**

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

	2018	2017
Azerbaijan	30,659	27,883
Turkey	8,010	7,595
Switzerland	770	1,030
UAE	555	141
Georgia	524	599
Other	294	204
Total	**40,812**	**37,452**

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, UAH exchange rates, with all other variables held constant, of the Group's post-tax profit:

2018	Change in rates (+/-)	Effect on profit before tax
USD/AZN	14%/-3%	(510)/109
USD/TRY	10.00%/-10.00%	(170)/170
EUR/AZN	14%/-3%	(151)/32
USD/GEL	11.00%/-11.00%	(28)/28
EUR/TRY	10.00%/-10.00%	(15)/15
USD/CHF	7%/-7%	6/(6)

2017	Change in rates (+/-)	Effect on profit before tax
USD/AZN	11.30%/-11.30%	(438)/438
USD/TRY	10.00%/-10.00%	(155)/155
EUR/AZN	13.50%/-13.50%	(111)/111
EUR/USD	12.50%/-7.50%	(50)/30
USD/GEL	13.50%/-9.50%	(38)/27
EUR/TRY	10.00%/-10.00%	(18)/18

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.

6. Financial risk management (continued)

Financial risk factors (continued)

The following sensitivity analysis is based upon derivative price exposures that existed at 31 December 2018, whereby if oil future prices had moved, as illustrated in the table below, with all other variables held constant, pre-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
2018	5%/(5%)	111/(111)	111/(111)
2017	5%/(5%)	126/(126)	126/(126)

(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 and EURIBOR.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates on loans and borrowings, net of loans receivable:

2018	Increase/ decrease in basis points	Effect on profit before tax
Loans and borrowings, net of loans receivable		
USD	+50/-15	25/(7)
EUR	+20/-1	2/(1)

2017	Increase/ decrease in basis points	Effect on profit before tax
Loans and borrowings, net of loans receivable		
USD	+70/-8	34/(4)
EUR	+25/-1	2/(1)

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.

6. Financial risk management (continued)

Credit risk and concentration of credit risk

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

	2018	2017
Cash and cash equivalents excluding cash on hand (Note 8)	6,651	5,205
Restricted cash	201	229
Deposits (Note 8)	155	218
Trade and other receivables	7,372	8,831
Available-for-sale investments	–	174
Other current assets	197	1,175
Other non-current financial assets	485	333
Financial guarantees given (Note 38)	1,105	1,279
Total maximum exposure to credit risk	**16,166**	**17,444**
Financial guarantees – amounts of guarantees of indebtedness of others (Note 38)	(1,044)	(976)
Total exposure to credit risk net of guarantees received	**15,122**	**16,468**

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 2018 was AZN 1,263 (31 December 2017: AZN 1,529). The Group continually monitors the status of the banks where its accounts are maintained. In addition, the Group's restricted cash balance in the amount of AZN 75 (31 December 2017: AZN 36) is placed in Government treasury account.

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 and Azal CJSC 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.

As at 31 December 2018, letters of guarantee and bank guarantees in total amount of AZN 1,044 (TRY 3,252 million) (2017: AZN 976 (TRY 2,169 million)) were received from certain domestic and foreign customers and suppliers of SOCAR Turkey Energy A.Ş ("STEAS").

The Group categorized its financial assets as follows:

31 December 2018	Standard	Sub-standard	Past due but not in default	In default
Cash and cash equivalents excluding cash on hand	5,388	1,263	–	–
Restricted cash	201	–	–	–
Deposits (Note 8)	155	–	–	–
Trade and other receivables	6,143	463	633	133
Other current assets	–	197	–	–
Other non-current financial assets	–	485	–	–
Total	**11,887**	**2,408**	**633**	**133**

6. Financial risk management (continued)

Credit risk and concentration of credit risk (continued)

31 December 2017	Standard	Sub-standard	Past due but not impaired	Individually impaired
Cash and cash equivalents excluding cash on hand	3,676	1,529	–	–
Restricted cash	229	–	–	–
Deposits (Note 8)	218	–	–	–
Trade and other receivables	6,865	170	980	816
Available-for-sale investments	–	174	–	–
Other current assets	–	1,175	–	–
Other non-current financial assets	–	333	–	–
Total	**10,988**	**3,381**	**980**	**816**

For 2018 standard grade includes counterparties with good financial position and good debt service. In addition those financial assets normally have a credit rating on or close to the sovereign credit rating or sufficiently collateralized. Sub-standard grade represented by receivables from other borrowers with good financial position and good debt service which are neither past due nor in default. The Group, generally, considers a financial receivables in default when contractual payments are 90 days past due.

For 2017 standard grade includes counterparties with good financial position and good debt service. In addition those financial assets normally have a credit rating on or close to the sovereign credit rating or sufficiently 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.

The Group's financial liabilities represent both derivative and 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.

The maturity analysis of financial liabilities as of 31 December 2018 and 2017 is as follows:

At 31 December 2018	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Trade and other financial payables	11,642	–	–	–	**11,642**
Deferred acquisition consideration payable	–	157	–	827	**984**
Other current liabilities	–	355	–	–	**355**
Interest bearing borrowings	2,659	1,694	7,086	3,565	**15,004**
Other non-current liabilities	–	–	614	77	**691**
Put option liabilities	–	–	2,713	–	**2,713**
Financial guarantees given	–	–	1,105	–	**1,105**
Total undiscounted financial liabilities	**14,301**	**2,206**	**11,518**	**4,469**	**32,494**

6. Financial risk management (continued)

Liquidity risk (continued)

At 31 December 2017 (reclassified)	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Trade and other financial payables	11,974	–	–	–	**11,974**
Deferred acquisition consideration payable	–	147	–	–	**147**
Other current liabilities	–	653	–	–	**653**
Interest bearing borrowings	4,517	1,884	6,496	5,642	**18,539**
Other non-current liabilities	–	–	492	13	**505**
Put option liabilities	–	–	2,719	–	**2,719**
Financial guarantees given	–	–	1,279	–	**1,279**
Total undiscounted financial liabilities	**16,491**	**2,684**	**10,986**	**5,655**	**35,816**

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:

	2018	2017
Total borrowings (Note 20)	13,672	15,511
Total equity	23,944	21,975
Less: cash and cash equivalents (Note 8)	(6,640)	(5,217)
Total capital under management	**30,976**	**32,269**

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.

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.

6. Financial risk management (continued)

Fair value of financial instruments (continued)

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 2018	
	Carrying amounts	**Fair values**
Cash and cash equivalents (Note 8)	6,640	6,640
Deposits (Note 8)	151	151
Restricted cash	201	201
Trade and other receivables	6,606	6,606
Other current assets	851	851
Other non-current financial assets	1,323	1,282
Total financial assets	**15,772**	**15,731**
Trade and other payables (Note 19)	(11,642)	(11,642)
Other current liabilities (Note 25)	(355)	(355)
Short-term borrowings and current portion of long-term borrowings (Note 20)	(4,013)	(4,013)
Long-term borrowings (Note 20)	(9,659)	(9,629)
Current portion of deferred acquisition consideration payable	(157)	(157)
Non-current portion of deferred acquisition consideration payable	(529)	(529)
Other non-current liabilities	(781)	(671)
Put option liabilities (Note 35)	(2,713)	(2,713)
Total financial liabilities	**(29,849)**	**(29,709)**

	31 December 2017	
	Carrying amounts	**Fair values**
Cash and cash equivalents (Note 8)	5,217	5,217
Deposits (Note 8)	218	218
Restricted cash	229	229
Trade and other receivables	8,015	8,015
Available-for-sale investments	174	174
Other current assets	1,534	1,534
Other non-current financial assets	685	618
Total financial assets	**16,072**	**16,005**
Trade and other payables (Note 19)	(11,974)	(11,974)
Other current liabilities (Note 25)	(653)	(653)
Short-term borrowings and current portion of long-term borrowings (Note 20)	(5,998)	(5,998)
Long-term borrowings (Note 20)	(9,513)	(9,279)
Deferred acquisition consideration payable	(147)	(147)
Other non-current liabilities	(647)	(543)
Put option liabilities (Note 35)	(2,719)	(2,719)
Total financial liabilities	**(31,651)**	**(31,313)**

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

(i) Current financial assets and liabilities fair values 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.

6 Financial risk management (continued)

Fair value hierarchy

The following table provides the fair value measurement hierarchy of the Group's assets and liabilities as at 31 December 2018:

	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 assets at FVPL	**654**	241	413	–
Other non-current financial assets at FVPL	**805**	57	167	581
Liabilities measured at fair value				
Other current liabilities at FVPL	**(355)**	–	(355)	–
Other non-current liabilities at FVPL	**(97)**	(5)	(92)	–
Trade receivables at FVOCI	**1,211**	–	1,211	–
Assets for which fair value are disclosed				
Cash and cash equivalents	**6,640**	6,640	–	–
Restricted cash	**201**	201	–	–
Deposits	**151**	–	151	–
Trade and other receivables	**5,395**	–	–	5,395
Other current assets	**197**	–	–	197
Other non-current financial assets	**477**	–	–	477
Liabilities for which fair values are disclosed				
Trade and other payables	**(11,642)**	–	–	(11,642)
Short-term borrowings and current portion of long-term borrowings	**(4,013)**	–	–	(4,013)
Long-term borrowings	**(9,629)**	(356)	–	(9,273)
Deferred acquisition consideration payable	**(686)**	–	–	(686)
Other non-current liabilities	**(574)**	–	–	(574)
Put option liabilities	**(2,713)**	–	–	(2,713)

6 Financial risk management (continued)

Fair value hierarchy (continued)

The following table provides the fair value measurement hierarchy of the Group's assets and liabilities as at 31 December 2017:

	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 assets	**689**	8	681	–
Available-for-sale investments	**174**	174	–	–
Liabilities measured at fair value				
Other current liabilities	**(593)**	(200)	(393)	–
Other non-current liabilities	**(138)**	–	(138)	–
Assets for which fair value are disclosed				
Cash and cash equivalents	**5,217**	5,217	–	–
Restricted cash	**229**	229	–	–
Deposits	**218**	–	218	–
Trade and other receivables	**8,015**	–	–	8,015
Other current assets	**845**	–	–	845
Other non-current financial assets	**618**	–	–	618
Liabilities for which fair values are disclosed				
Trade and other payables	**(11,974)**	–	–	(11,974)
Other current liabilities	**(60)**	–	–	(60)
Short-term borrowings and current portion of long-term borrowings	**(5,998)**	–	–	(5,998)
Long-term borrowings	**(9,279)**	(318)	–	(8,961)
Deferred acquisition consideration payable	**(147)**	–	–	(147)
Other non-current liabilities	**(405)**	–	–	(405)
Put option liabilities	**(2,719)**	–	–	(2,719)

The Group started to factor its trade and other receivables in order to maintain healthy liquidity position. Thus observable, either directly or indirectly, inputs were available at reporting date for estimating fair values of debt instruments at FVOCI. Accordingly, these instruments were transferred from Level 3 as at 31 December 2017 to Level 2 as at 31 December 2018 in the amount of AZN 1,211.

Financial assets classified under IFRS 9 as of 31 December 2018 as follow:

	Amortized cost	FVOCI	FVPL
Cash and cash equivalents	6,640	–	–
Restricted cash	201	–	–
Deposits	151	–	–
Trade and other receivables	5,395	1,211	–
Other current financial assets	27	100	724
Other long-term financial assets	485	–	838
Total financial assets after ECL	**12,899**	**1,311**	**1,562**

7. Balances and transactions with related parties

Transactions outside the entity's normal course of business

On 9 February 2018 the Group entered into sale and purchase agreement ("SPA") with its associate, Southern Gas Corridor ("SGC") to acquire 7 per cent equity interest in TANAP Doğalgaz İletim A.Ş. Pursuant to SPA, the Group also acquired 7 per cent of loan receivable by SGC due from TANAP Doğalgaz İletim A.Ş. Fair value of total consideration for the purchase of financial assets amounted to AZN 665 (USD 392 million) out of which AZN 161 (USD 95 million) was paid on 22 February 2018. Remaining consideration in the amount of AZN 505 (USD 297 million) was recognized as an interest bearing long-term deferred acquisition consideration payable at the rate of 5.74 per cent per annum. During the period ended 31 December 2018 the Group incurred interest charge in the amount of AZN 24 in respect of long-term deferred acquisition consideration payable.

On the transaction date the Group recognized acquired financial assets at fair value in accordance with IFRS 9 which amounted to AZN 909 (USD 535 million). The Group treated this acquisition as transaction under common control since both parties are ultimately controlled by the Azerbaijan Government. Acquisition of financial assets represents upstream transaction between SOCAR and SGC. Thus unrealized gain amounting to AZN 124 was recognized to the extent of unrelated shareholder's portion within equity as a contribution from ultimate controlling party (Note 27).

At 31 December 2018 the Group accounted for equity interest at fair value and loan receivable at amortised cost in total amount of AZN 969 as other non-current financial assets (Note 14).

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 2018, compensation of key management personnel totalled to AZN 1.282 (2017: AZN 1.153).

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 2018, the outstanding balances with related parties were as follows:

	Note	Government and entities under government control	Associates, joint ventures
Gross amount of trade receivables		113	86
Impairment provisions for trade and other receivables		(41)	(7)
Other receivables		44	62
Other non-current financial assets		–	467
Cash and cash equivalents		1,227	–
Restricted cash		182	–
Deposit		36	–
Advances received		(11)	–
Advances received for the sale of interest in PSA	34	–	(4,313)
Borrowings from IBA (at fixed rates varying from 3 to 4 per cent)		(451)	–
Borrowings from the Ministry of Finance of Azerbaijan Republic		(315)	–
Deferred consideration payable for Methanol Plant		(62)	–
Bond payable to Azerbaijan Investment Company ("AIC")		(163)	–
Trade and other payables		(280)	(851)
Deferred consideration payable to SGC		–	(529)
Taxes payable to State Oil Fund of Azerbaijan Republic ("SOFAZ")	21	(255)	–
Bond payable to SOFAZ		(1,128)	–
Other payables to SOFAZ		(2,870)	–

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

7. Balances and transactions with related parties (continued)

The transactions with related parties for the year ended 31 December 2018 were as follows:

	Government and entities under government control	**Associates, joint ventures**
Sales of natural gas	640	261
Sales of oil products	396	6
Service rendered	3	55
Interest on loans from related parties	(59)	–
Utilities costs	(67)	(5)
Other operating expenses	(40)	(10)
Other operating income	206	–
Social expenses	(19)	–
Transportation expenses	(111)	(336)
Security expenses	(10)	–
Purchases of PPE and inventory	(17,275)	(874)
Dividends received from joint ventures	–	106
Dividends received from associates	–	84

At 31 December 2017, the outstanding balances with related parties were as follows:

	Note	**Government and entities under government control**	**Associates, joint ventures**
Gross amount of trade receivables		151	68
Impairment provisions for trade and other receivables		(99)	(2)
Other receivables		–	13
Other non-current financial assets		–	250
Cash and cash equivalents		1,529	–
Restricted cash		234	–
Advances received		(100)	–
Advances received for the sale of interest in PSA	34	–	(4,076)
Borrowings from IBA (at fixed rates varying from 3 to 4 per cent)		(326)	–
Borrowings from the Ministry of Finance of Azerbaijan Republic		(1,194)	–
Deferred consideration payable for Methanol Plant		(62)	–
Bond payable to Azerbaijan Investment Company ("AIC")		(157)	–
Trade and other payables		(248)	(777)
Taxes payable to State Oil Fund of Azerbaijan Republic ("SOFAZ")	21	(255)	–
Bond payable to SOFAZ		(784)	–
Other payables to SOFAZ		(1,902)	–

7. Balances and transactions with related parties (continued)

The transactions with related parties for the year ended 31 December 2017 were as follows:

	Government and entities under government control	Associates, joint ventures
Sales of natural gas	673	180
Sales of oil products	479	9
Service rendered	3	120
Interest on loans from related parties	(67)	–
Utilities costs	(64)	(3)
Other operating expenses	(28)	(15)
Other operating income	250	–
Social expenses	(29)	–
Transportation expenses	(104)	(292)
Ecology service and environmental security	–	(1)
Security expenses	(10)	–
Purchases of PPE and inventory	(9,069)	(691)
Dividends received from joint ventures	–	132
Dividends received from associates	–	89

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.

As at 31 December 2018 and 2017, outstanding bonds payable balances with related parties were as follows:

Bond Holder	Coupon rate	Maturity date	2018	2017
Azerbaijan Investment Company	LIBOR + 1%	30 December 2027	163	157
SOFAZ	LIBOR + 1%	1 December 2024	430	484
SOFAZ	LIBOR + 1.335%	30 December 2027	286	299
SOFAZ	LIBOR + 4%	31 December 2029	412	–
Total bonds payable			**1,291**	**940**

8. Cash and cash equivalents and short-term deposits

	2018	2017
USD denominated bank balances	5,139	4,167
AZN denominated bank balances	1,076	461
EUR denominated bank balances	273	100
TRY denominated bank balances	48	213
CHF denominated bank balances	45	129
Other denominated bank balances	70	135
Cash on hand	6	12
ECL	(17)	–
Total cash and cash equivalents	**6,640**	**5,217**

Included in AZN denominated bank balances as at 31 December 2018 and 2017 are call deposits in total amount of AZN 35 and AZN 34, respectively, placed with Xalq Bank. Interest rate on these deposits for the year ended 31 December 2018 equalled 3 per cent. Call deposits have original maturity of less than six months.

8. Cash and cash equivalents and short-term deposits (continued)

Deposits

At 31 December 2018, term deposits included placements in the total amount of AZN 155 with maturity of one year, under fixed contractual interest rates ranging from 1 per cent to 1.6 per cent per annum.

At 31 December 2017, term deposits included placements in the total amount of AZN 218 with maturity ranging from six months to one year, under fixed contractual interest rates ranging from 1 per cent to 6 per cent per annum.

At 1 January 2018 and 31 December 2018 the Group recognized ECL on deposits in the amount of AZN 4.

9. Restricted cash

At 31 December 2018 restricted cash was mainly represented by two cash collateral accounts. The Group has restricted cash in the amount of AZN 93 in International Bank of Azerbaijan (31 December 2017: AZN 129) as an irrevocable letter of credits for the foreign purchases related to modernization process of Azerkimya plant. At 31 December 2018 the Group had VAT deposit account in the amount of AZN 75 (31 December 2017: AZN 36) on which the operations are performed associated with receipt, registration and movements of VAT and its payment to state budget. In addition, the Group has restricted cash in the amount of AZN 63 (USD 37 million) in Deutsche Bank (31 December 2017: AZN 63) as a guarantee of minimum return payments payable to Goldman Sachs International ("GSI") according to the Put Option Agreement in relation to 13 percent shares of STEAS (Note 35).

10. Trade and other receivables

	2018	2017
Trade receivables	7,204	8,647
Other receivables	168	184
Less: ECL	(766)	(816)
Total financial receivables	**6,606**	**8,015**
VAT recoverable	885	967
Prepayments	623	771
Taxes receivable	151	119
Underlift oil balance	90	127
Other	40	8
Total trade and other receivables	**8,395**	**10,007**

Trade receivables are mainly represented by receivables from sales of crude oil, oil products and natural gas sold to customers of the Group. At 31 December 2018 financial receivables of 7,016 (31 December 2017: AZN 7,370) were denominated in foreign currencies, mainly in USD.

Trade receivables in the amount of AZN 44 represents government grant as a compensation of losses incurred from sales of natural gas and heating oil for the purpose of meeting local demand.

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.

10. Trade and other receivables (continued)

Set out below is the movement in the allowance for ECL/incurred loss allowance of trade receivables:

	2018	2017
At 31 December 2017	**816**	**588**
Impact of adopting IFRS 9	35	–
At 1 January 2018	**851**	**588**
ECL/incurred loss allowance for current year	19	262
Credit loss/impairment allowance reversed	(54)	(23)
Write-off	(24)	–
Currency translation difference	(26)	(11)
At 31 December	**766**	**816**

At 31 December 2018 financial receivables of AZN 133 were in default under IFRS 9. At 31 December 2017 trade receivables of AZN 980 were past due, but not impaired under IAS 39.

11. Inventories

	2018	2017
Goods in transit	1,045	2,526
Finished goods	725	1,129
Raw materials and spare parts	594	547
Crude oil	408	453
Work in progress	142	125
Other	65	30
Total inventories	**2,979**	**4,810**

12. Other current assets

Other current financial assets

At 31 December 2018 and 2017, other current financial assets mainly comprised of loan receivables, derivative instruments and equity investments at FVOCI.

At 31 December 2018, the Group had balances related to margin deposits and financial derivatives in the amount of AZN 691 (31 December 2017: AZN 917).

At 31 December 2018, the Group had equity investments at FVOCI in the amount of AZN 100.

13. Other non-current assets

At 31 December 2018, other non-current assets were mainly represented by long-term prepayments for purchase of property, plant and equipment in the amount of AZN 1,705 (31 December 2017: AZN 1,033), long-term prepaid expenses in the amount of AZN 22 (31 December 2017: AZN 34) and non-current VAT receivable in the amount of AZN 113 (31 December 2017: AZN 3).

14. Other non-current financial assets

At 31 December 2018 and 2017, other non-current financial assets mainly comprised of loan receivables from related parties, equity investment at FVPL and derivative instruments.

At 31 December 2018, other non-current financial assets are represented by fair value of 7 per cent equity interest and loan receivable from TANAP Doğalgaz İletim A.Ş in the amount of AZN 581 and AZN 388, respectively (Note 7).

At 31 December 2018, the Group's loan receivable from its associates is equalled to AZN 70 (31 December 2017: AZN 71).

The Group has entered into a series of commodity swaps, commodity futures and foreign exchange futures to hedge risks. At 31 December 2018 the Group recognized unrealized fair value gains on physical positions in the amount of AZN 224 (2017: AZN 345), which is result of the asset on fair value hedge accounting. 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 2017	3,163	17,270	3,590	473	1,715	2,695	2,832	31,738
Additions	78	1,070	800	322	33	484	1,585	4,372
Acquisition of additional interest in ACG PSA (Note 39)	–	3,059	–	–	–	–	–	3,059
PPE related to 80 per cent interest in UBEP (Note 39)	–	401	–	–	–	–	–	401
Disposals	(63)	(30)	(43)	(4)	(29)	–	(32)	(201)
Transfers	447	285	286	41	(5)	(11)	(1,043)	–
Translation to presentation currency	(99)	(336)	(151)	(20)	(90)	(113)	(80)	(889)
At 31 December 2017	3,526	21,719	4,482	812	1,624	3,055	3,262	38,480
Additions	27	1,726	145	123	51	128	2,382	4,582
Acquisition through business combination (APMT business) (Note 39)	–	–	80	–	17	–	1	98
Acquisition through business combination (Austrian business) (Note 39)	86	–	14	–	1	–	–	101
Disposals	(23)	(35)	(94)	–	(25)	–	(53)	(230)
Transfers	153	3,622	192	28	194	(3,183)	(1,006)	–
Translation to presentation currency	(74)	(18)	(401)	48	(222)	–	(216)	(883)
At 31 December 2018	3,695	27,014	4,418	1,011	1,640	–	4,370	42,148
Depreciation and impairment								
At 1 January 2017	(1,098)	(7,617)	(1,759)	(9)	(744)	–	(395)	(11,622)
Depreciation charge for the year	(134)	(568)	(299)	(37)	(65)	–	–	(1,103)
Disposal	43	25	25	1	25	–	–	119
Impairment (Note 29)	(68)	(394)	–	–	(2)	–	(4)	(468)
Transfers	7	(5)	(1)	–	(1)	–	–	–
Translation to presentation currency	34	143	69	–	17	–	–	263
At 31 December 2017	(1,216)	(8,416)	(1,965)	(45)	(770)	–	(399)	(12,811)
Depreciation charge for the year	(145)	(886)	(292)	(50)	(58)	–	–	(1,431)
Disposal	5	42	47	–	11	–	–	105
Impairment (Note 29)	(25)	(101)	–	(7)	–	–	(28)	(161)
Reversal of impairment	–	187	–	–	–	–	–	187
Transfers	4	(11)	7	–	–	–	–	-
Translation to presentation currency	8	4	192	1	17	–	–	222
At 31 December 2018	(1,369)	(9,181)	(2,011)	(101)	(800)	–	(427)	(13,889)
Net book value								
At 1 January 2017	2,065	9,653	1,831	464	971	2,695	2,437	20,116
At 31 December 2017	2,310	13,303	2,517	767	854	3,055	2,863	25,669
At 31 December 2018	2,326	17,833	2,407	910	840	–	3,943	28,259

15. Property, plant and equipment (continued)

During 2018, the Group capitalized finance costs in the amount of AZN 117 which was mainly attributable to the construction of assets (31 December 2017: AZN 77).

During 2018, the Group acquired assets in the amount of AZN 4,582 (2017: AZN 4,372) excluding property, plant and equipment acquired through business combinations in the amount of AZN 199 (31 December 2017: 3,460).

As at 31 December 2018, the Group's impairment charge is mainly represented by write-down of oil & gas properties and equipment and construction in progress in the amount of AZN 129 (2017: AZN 391) related to investments in the non-profitable oil fields located in the Republic of Azerbaijan. Impairment loss related to oil and gas segment of Group and was recognised within other operating expenses. The Group does not expect future economic benefits from non-profitable fields and recoverable amounts of oil fields were nil as at 31 December 2018 (31 December 2017: nil).

As at 31 December 2018, the reversal of impairment loss of AZN 187 recognized in the oil and gas field located in the Republic of Azerbaijan related to oil and gas segment of the Group. Factors that led to reversal of impairment are increased reserves and improvement in overall economic environment. The Group recognized the reversal of impairment within other operating income. The calculation of value-in-use for the mentioned CGU is most sensitive to the following assumptions:

Discount rate: The pre-tax discount rate applied to the cash flow projections was 16.06 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/lower than management's estimate, this would result in decrease of current impairment reversal amount of AZN 57 and an additional impairment reversal of impairment of AZN 57 respectively.

Natural gas and crude oil prices: Natural gas prices are calculated based on the provisions of long-term sales contracts which are either fixed or variable depending on crude oil prices and other inputs. If the natural gas prices had been 10 per cent higher/lower than management's current estimate, recoverable amount would be AZN 193 higher/lower respectively. Change in recoverable amount would result an additional reversal of impairment by AZN 193 in case of 10 per cent higher prices and impairment charge of AZN 193 in case of 10 per cent lower prices.

Capital expenditures: Capital expenditures necessary to maintain estimated production volumes are based on long-term development plans for particular gas field. If the capital expenditures had been 10 per cent higher/lower than management's current estimate, recoverable amount would be AZN 162 lower/higher respectively. Change in recoverable amount result in an additional reversal of impairment by AZN 162 in case of 10 per cent lower capital expenditures and impairment charge of AZN 162 in case of 10 per cent higher capital expenditures.

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 relation-ship	Licence	Other intangible assets	Total
Cost							
At 1 January 2017	**183**	**191**	**37**	**341**	**–**	**177**	**929**
Additions	–	–	–	–	–	29	**29**
Licence related to 80 per cent interest in UBEP (Note 39)	–	–	–	–	105	–	**105**
Disposal	–	–	–	–	–	(3)	**(3)**
Translation to presentation currency	(18)	(20)	(4)	(14)	–	(1)	**(57)**
At 31 December 2017	**165**	**171**	**33**	**327**	**105**	**202**	**1,003**
Additions	–	–	–	–	–	48	**48**
Acquisitions through business combinations (Austrian Business) (Note 39)	–	–	9	1	–	1	**11**
Acquisitions through business combinations (APMT Business) (Note 39)	–	–	–	–	–	58	**58**
Disposal	–	–	–	–	–	(2)	**(2)**
Translation to presentation currency	(38)	(49)	(10)	(26)	–	(8)	**(131)**
At 31 December 2018	**127**	**122**	**32**	**302**	**105**	**299**	**987**
Amortization and impairment							
At 1 January 2017	**(40)**	**(36)**	**–**	**(87)**	**–**	**(77)**	**(240)**
Amortization charge for the year (Note 29)	(5)	(5)	–	(14)	–	(17)	**(41)**
Disposals amortization	–	–	–	–	–	1	**1**
Translation to presentation currency	4	4	–	4	–	4	**16**
At 31 December 2017	**(41)**	**(37)**	**–**	**(97)**	**–**	**(89)**	**(264)**
Amortization charge for the year (Note 29)	(3)	(3)	(2)	(13)	–	(22)	**(43)**
Translation to presentation currency	9	11	–	11	–	3	**34**
At 31 December 2018	**(35)**	**(29)**	**(2)**	**(99)**	**–**	**(108)**	**(273)**
Net book value							
At 1 January 2017	**143**	**155**	**37**	**254**	**–**	**100**	**689**
At 31 December 2017	**124**	**134**	**33**	**230**	**105**	**113**	**739**
At 31 December 2018	**92**	**93**	**30**	**203**	**105**	**191**	**714**

At 31 December 2018 carrying value of intangible assets included licence of "Umid Babek Exploration and Production Company" ("UBEP") in the amount of AZN 105 (31 December 2017: AZN 105) and trade name of Petkim in the amount of AZN 23 (31 December 2017: AZN 33) acquired through business combination in August 2017 and May 2008, respectively. These intangible assets has indefinite useful life and were tested for impairment as part of recoverability analysis of related CGUs (Note 39).

During 2018, the Group acquired intangible assets through acquisition of 100 per cent interest in APM Terminalleri Liman İşletmeciliği Anonim Şirketi ("APMT") business and Austrian business units in the amount of AZN 58 and AZN 11, respectively.

During 2018, total amortization expense amounting to AZN 43 (2017: AZN 41) have been allocated to general administrative and research and development expenses by AZN 22 (2017: AZN 21), cost of sales by AZN 16 (2017: AZN 15) and distribution expenses by AZN 5 (2017: AZN 5).

17. Investments in joint ventures

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

	2018	2017
Carrying amount at 1 January	**5,022**	**4,555**
Additions to investments in joint ventures	194	592
Share of after tax results of joint ventures	213	523
Dividends received from joint ventures	(117)	(147)
Derecognition of joint ventures	–	(385)
Exchange differences	(30)	(163)
Other	19	47
Carrying amount at 31 December	**5,301**	**5,022**

At 31 December 2018, 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 MI Drilling Fluids	SOCAR AQS	Azerbaijan Rigs	SOCAR CAPE	STYAS
Country of incorporation	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Turkey**
Current assets	64	175	74	379	109	25	904
including cash and cash equivalents	9	28	3	4	3	18	405
Non-current assets	62	20	11	227	1,029	16	12,281
Current liabilities	(36)	(71)	(63)	(241)	(3)	(16)	(704)
including current financial liabilities (except trade and other payables and provisions)	–	–	–	(29)	(8)	(1)	(356)
Non-current liabilities	–	–	–	(68)	(8)	–	(4,456)
including non-current financial liabilities (except other payables and provisions)	–	–	–	(44)	–	–	(4,454)
Net assets	**90**	**124**	**22**	**297**	**1,127**	**25**	**8,025**
Proportion of the Group's ownership	40%	60%	51%	13.4%	10%	51%	60%
Interest in the net assets	**36**	**74**	**11**	**40**	**113**	**13**	**4,815**
Adjustments	2	–	2	–	(1)	–	154*
Carrying value	**38**	**74**	**13**	**40**	**112**	**13**	**4,969**

* *The adjustment includes additional contributions in share capital of Group's joint ventures which is represented by inception-to-date commission paid on letter of credit in the amount of AZN 136. Remaining amount of AZN 18 represents over-financing by the Group since other shareholder did not make capital injections in line with its proportionate shareholding interest.*

	Azgerneft LLC	AZFEN	Azeri MI Drilling Fluids	SOCAR AQS	Azerbaijan Rigs	SOCAR CAPE	STYAS
Revenue	67	512	175	576	89	89	–
Cost of sales	(29)	(397)	(141)	(339)	(41)	(71)	–
including depreciation	(5)	(11)	(1)	(18)	(31)	–	–
General and administrative expenses	–	(6)	(4)	(15)	–	(5)	(65)
Other income	1	–	–	–	–	–	10
Other expense	–	(1)	(13)	(2)	–	–	–
Forex gain (loss)	–	–	–	1	–	–	(25)
Finance income	–	1	–	–	–	–	61
Finance costs	–	–	–	(36)	–	(15)	(12)
Profit/(loss) before tax	**39**	**109**	**17**	**185**	**48**	**(2)**	**(31)**
Income tax (expense)/benefit	(8)	(11)	(8)	(38)	(9)	(1)	235
Profit/(loss) for the year	**31**	**98**	**9**	**147**	**39**	**(3)**	**204**
Group's share of profit for the year	**12**	**59**	**5**	**20**	**4**	**(2)**	**122**

17. Investments in joint ventures (continued)

At 31 December 2018, 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 LLC	18	–	(6)	(3)	2	–	30%	Azerbaijan
Caspian Shipyard Company	2	–	–	–	–	(2)	20%	Azerbaijan
Sarmatia LLC	1	–	(1)	–	–	(1)	27%	Poland
SOCAR Baglan LLC	1	14	(13)	(6)	–	–	51%	Azerbaijan
SOCAR Foster Wheeler Engineering	2	2	(4)	–	12	1	65%	Azerbaijan
SOCAR KBR	56	–	(50)	–	121	6	51%	Azerbaijan
SOCAR Dalgic LLC	5	13	(2)	(16)	9	–	51%	Azerbaijan
AAS – Ekol	4	–	(1)	–	9	3	48%	Azerbaijan
SOCAR Uniper	20	9	(8)	–	40	4	51%	Azerbaijan
SOCAR Fugro	13	1	(8)		33	6	51%	Azerbaijan
SOCAR Construction LLC	1	9	(1)		–	(1)	97%	Azerbaijan
Caspian Innovation Center	12	–	(10)	–	13	1	90%	Switzerland
SOCAR Turkey LNG	15	15	(14)	(2)	26	1	45%	Turkey
Total	**150**	**63**	**(118)**	**(27)**	**265**	**18**		

At 31 December 2017, 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 MI Drilling Fluids	SOCAR AQS	Azerbaijan Rigs	SOCAR CAPE	STYAS
Country of incorporation	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Azerbaijan**	**Turkey**
Current assets	51	235	81	295	205	42	1,011
including cash and cash equivalents	–	69	–	5	54	5	936
Non-current assets	57	30	6	201	891	24	11,208
Current liabilities	(30)	(125)	(45)	(228)	(7)	(20)	(250)
including current financial liabilities (except trade and other payables and provisions)	–	–	–	(12)	–	(5)	(138)
Non-current liabilities	–	–	–	(5)	–	(8)	(4,121)
including non-current financial liabilities (except other payables and provisions)	–	–	–	(5)	–	–	(3,927)
Net assets	**78**	**140**	**42**	**263**	**1,089**	**38**	**7,848**
Proportion of the Group's ownership	40%	60%	51%	13.4%	10%	51%	60%
Interest in the net assets	**31**	**84**	**21**	**35**	**109**	**19**	**4,709**
Adjustments	2	–	2	–	(1)	1	(12)
Carrying value	**33**	**84**	**23**	**35**	**108**	**20**	**4,697**

17. Investments in joint ventures (continued)

	Azgerneft LLC	AZFEN	Azeri MI Drilling Fluids	SOCAR AQS	Azerbaijan Rigs	SOCAR CAPE	STYAS
Revenue	51	796	201	288	–	141	–
Cost of sales	(23)	(545)	(156)	(200)	–	(100)	–
including depreciation	(5)	(9)	(1)	(6)	(1)	–	(3)
General and administrative expenses	–	(6)	(3)	(10)	–	(4)	(35)
Other income	–	–	–	–	–	–	10
Other expense	–	(10)	–	(6)	–	–	–
Forex loss	–	(17)	(2)	–	(1)	–	–
Finance income	–	–	–	5	–	–	28
Finance costs	–	–	–	–	–	(1)	(40)
Profit/(loss) before tax	**28**	**218**	**40**	**77**	**(1)**	**36**	**(37)**
Income tax (expense)/ benefit	(6)	(41)	(8)	(5)	–	(10)	685
Profit/(loss) for the year	**22**	**177**	**32**	**72**	**(1)**	**26**	**648**
Group's share of profit for the year	**9**	**106**	**16**	**37**	**–**	**13**	**389**

At 31 December 2017, 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	–	(6)	(3)	1	(1)	30%	Azerbaijan
Caspian Shipyard Company	4	–	–	–	–	(59)	20%	Azerbaijan
SOCAR Construction LLC	–	11	(1)	–	–	(1)	97%	Azerbaijan
SOCAR Baglan LLC	1	14	(13)	(6)	–	–	51%	Azerbaijan
SOCAR Foster Wheeler Engineering	1	–	(1)	–	4	(1)	65%	Azerbaijan
Sarmatia LLC	1	–	(2)	–	–	(1)	27%	Poland
SOCAR Dalgic LLC	3	16	(1)	(17)	7	–	51%	Azerbaijan
SOCAR KBR	25	–	(25)	–	44	1	51%	Azerbaijan
AAS – Ekol	4	1	(1)	–	10	3	48%	Azerbaijan
SOCAR Fugro	18	1	(14)	–	30	5	51%	Azerbaijan
SOCAR Uniper	1	–	–	–	–	–	51%	Azerbaijan
Total	**75**	**43**	**(64)**	**(26)**	**96**	**(54)**		

During 2018, the Group has made additional contributions in share capital of its joint ventures, SOCAR Turkey Yatırım A.Ş. ("STYAS") and SOCAR Uniper in the amount AZN 152 (2017: AZN 542) and AZN 8 (2017: nil), 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 26 (2017: AZN 28) were recognized as additional investment in STYAS.

18. Investment in associates

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

	2018	2017
Carrying amount at 1 January	**4,571**	**4,442**
Additions to investments in associates	15	238
Share of after tax results of associates	24	134
Dividends received from associates	(99)	(104)
Exchange differences	(32)	(139)
Other	(120)	–
Carrying amount at 31 December	**4,359**	**4,571**

At 31 December 2018, 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:

2018	SCPC	BTC Co	SGC
Country of incorporation	**Cayman Islands**	**Cayman Islands**	**Azerbaijan**
Current assets	228	198	1,438
Non-current assets	9,060	8,770	20,465
Current liabilities	(215)	(941)	(804)
Non-current liabilities	(409)	(752)	(15,293)
Net assets attributable to the Group	**8,664**	**7,275**	**3,523**
Net assets attributable to the NCI	–	–	2,283
Proportion of the Group's ownership	10%	25%	49%
Interest in the net assets	**866**	**1,819**	**1,726**
Adjustments	(15)	–	(77)*
Carrying value	**851**	**1,819**	**1,649**

* *At 31 December 2018, the adjustment includes the amount of AZN 34 which represents over financing to SGC by the Group and AZN 16 represents the Group's share in loss on sale of its additional interests in Shah Deniz PSA to SGC in 2014. In addition, amount of AZN 127 represents elimination of SOCAR's portion of unrealised gain arose from sale of SGC's 7 per cent equity interest in TANAP Doğalgaz İletim A.Ş.*

2018	SCPC	BTC Co	SGC
Revenue	750	1,513	435
Cost of sales	(240)	(859)	(226)
General and administrative expenses	–	–	(76)
Distribution expenses	–	–	(7)
Other income	–	–	34
Finance income	1	1	59
Finance costs	–	(86)	(596)
Forex loss	–	–	(6)
Share of results of associates	–	–	(6)
Profit/(loss) before tax	**511**	**569**	**(389)**
Income tax expense	(77)	–	(10)
Profit/(loss) for the year	**434**	**569**	**(399)**
Loss attributable to NCI	**–**	**–**	**(72)**
Group's share of profit/(loss) for the year	**43**	**142**	**(160)**

18. Investments in associates (continued)

At 31 December 2018, 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
Caspian Geophysical Company	9	(1)	–	(3)	45%	Azerbaijan
AzLab	5	(4)	4	–	50%	Azerbaijan
Cross Caspian Oil and Gas Logistics LLC	3	(2)	4	–	34%	Azerbaijan
Ateshgah Insurance Company	42	(30)	41	(1)	10%	Azerbaijan
Caspian Pipe Coatings LLC	17	(2)	7	1	50%	Azerbaijan
Tankanlagen Mellingen AG ("TAMAG")	13	(3)	–	–	33%	Switzerland
Tanklager Taegerschen AG ("TLT")	2	–	–	–	21%	Switzerland
SOGEP AG	6	(5)	–	–	34%	Switzerland
UBAG AG	7	(5)	–	–	24%	Switzerland
SAPPRO SA	20	(20)	–	–	13%	Switzerland
SARACO SA	38	(32)	–	–	20%	Switzerland
Azerbaijan Gas Supply Company	572	(572)	3,899	–	28%	Cayman Islands
Electrogas Malta	1,128	(1,245)	380	(32)	33%	Malta
Octogone	50	(53)	5	(4)	20%	Benin
CI GNL	2	(31)	–	(10)	26%	Ivory Coast
Total	**1,914**	**(2,005)**	**4,340**	**(49)**		

During 2018, the Group has made additional contributions in share capital of its associates, South Caucasus Pipeline Company (SCPC) in the amount of AZN 15 (2017: AZN 98).

At 31 December 2017, 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:

2017	SCPC	BTC Co	SGC
Country of incorporation	**Cayman Islands**	**Cayman Islands**	**Azerbaijan**
Current assets	212	191	323
Non-current assets	8,450	9,149	18,525
Current liabilities	(299)	(978)	(763)
Non-current liabilities	(389)	(1,256)	(12,446)
Net assets attributable to the Group	**7,974**	**7,106**	**3,886**
Net assets attributable to the NCI	–	–	1,753
Proportion of the Group's ownership	10%	25%	49%
Interest in the net assets	**797**	**1,777**	**1,904**
Adjustments	–	(1)	50*
Carrying value	**797**	**1,776**	**1,954**

* *At 31 December 2017 the adjustment includes the amount of AZN 34 which represents over financing to SGC by the Group 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 2014.*

18. Investments in associates (continued)

2017	SCPC	BTC Co	SGC
Revenue	633	1,595	218
Cost of sales	(172)	(756)	(129)
General and administrative expenses	–	–	(29)
Distribution expenses	–	–	(6)
Other income	–	–	35
Finance income	1	1	34
Finance costs	(1)	(86)	(269)
Forex loss	–	–	(10)
Share of results of associates	–	–	(7)
Profit/(loss) before tax	**461**	**754**	**(163)**
Income tax expense	(106)	–	(19)
Profit/(loss) for the year	**355**	**754**	**(182)**
Group's share of profit/(loss) for the year	**36**	**189**	**(89)**
Adjustments	1	–	(1)
Total	**37**	**189**	**(90)**

At 31 December 2017, 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	43	(30)	41	(2)	10%	Azerbaijan
Azerbaijan Gas Supply Company	501	(500)	2,719	–	28%	Cayman Islands
AzLab	5	–	2	–	50%	Azerbaijan
Caspian Geophysical	12	–	–	(6)	45%	Azerbaijan
Caspian Pipe Coatings LLC	22	(6)	15	3	50%	Azerbaijan
Cross Caspian Oil and Gas Logistics LLC	3	(2)	4	–	34%	Azerbaijan
SCPC Hold Co.	136	(1)	–	–	10%	Cayman Islands
TAMAG	13	(3)	5	–	33%	Switzerland
TLT	2	–	2	–	21%	Switzerland
SOGEP AG	6	(5)	6	–	34%	Switzerland
UBAG AG	38	(32)	26	3	24%	Switzerland
SAPPRO SA	5	(3)	19	–	13%	Switzerland
SARACO SA	19	(16)	22	1	20%	Switzerland
Electrogas Malta	1,279	(1,364)	251	(83)	33%	Malta
Octogone	53	(31)	2	(1)	20%	Benin
CI GNL	15	(30)	–	(14)	26%	Ivory Coast
Total	**2,152**	**(2,023)**	**3,114**	**(99)**		

19. Trade and other payables

	2018	2017
Trade payables	7,242	6,337
Accrued liabilities	3,052	4,607
Other payables	1,348	1,030
Total financial payables	**11,642**	**11,974**
Advances from customers	–	358
Payable to employees	124	108
Liabilities for overlift of oil	14	10
Total trade and other payables	**11,780**	**12,450**

19. Trade and other payables (continued)

Financial payables in the amount of AZN 7,601 (31 December 2017: AZN 7,909) 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 been received yet.

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.

The Group acquired trade and other payables with fair value of AZN 47 and AZN 29 as part of acquisition of 100 per cent interest in APMT and retail service chain network in Austria, respectively (Note 39).

Contract liabilities

As mentioned in Note 4, upon transition to IFRS 15, the Group made reclassifications from "Advances from customer" to "Contract liabilities" as at 31 December 2018. Contract liabilities are mainly represented by advances for sale of goods and services and construction projects in the amount of AZN 155 and AZN 142, respectively.

20. Borrowings

At 31 December 2018, short-term borrowings and current portion of long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate	Maturity	Total borrowed in original currency	Balance as at 31 December 2018
Short-term facilities in USD	2.48-8%	January 2019 – December 2019	**2,174**	2,502
Short-term facilities in TRY	16.5-28.5%	January 2019 – December 2019	**126**	42
Short-term facilities in GEL	12-14%	January 2019 – December 2019	**136**	76
Short-term facilties in other currencies	4.9%-18%	January 2019 – December 2019	**531**	149
Current portion of long-term borrowings			**-**	1,244
Total short-term borrowings and current portion of long-term borrowings			**-**	**4,013**

20. Borrowings (continued)

At 31 December 2018, long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate*	Maturity	Balance as at 31 December 2018	
			Non-current portion	Current portion
USD 1000 million	4.75%	March 2023	1,660	22
USD 750 million	6.95%	March 2030	809	27
USD 500 million	5.88%	January 2023	845	21
USD 489 million	LIBOR + 6.95%	July 2025	682	133
USD 238 million	6M LIBOR + 4%	December 2029	412	–
EUR 251 million	EURIBOR + 3.03%	June 2028	434	55
USD 260 million	LIBOR + 4.3% + 1.25%	December 2022	399	34
EUR 249 million	EURIBOR + 0.95%	June 2028	392	54
AZN 600 million	4%	July 2022	380	71
USD 300 million	LIBOR + 3.25%	March 2022	361	153
USD 212 million	LIBOR + 4.675%	March 2028	321	4
USD 250 million	LIBOR + 2.2%	November 2023	317	2
USD 485 million	LIBOR + 1%	December 2024	294	135
USD 200 million	LIBOR + 1.335%	December 2027	272	14
USD 100 million	5%	October 2021	170	2
USD 78 million	4%	December 2027	163	–
JPY 15,398 million	1.5%	April 2039	157	8
USD 100 million	LIBOR + 3.25%	April 2022	141	30
USD 77 million	4.8%	December 2023	131	–
USD 100 million	LIBOR + 3.25%	February 2022	122	53
USD 68 million	LIBOR + 3%	January 2026	106	9
USD 101 million	LIBOR + 2.8%	April 2022	104	34
AZN 350 million	3%	June 2023	100	50
USD 50 million	4.81%	September 2020	85	–
USD 65 million	LIBOR + 4.95%	December 2024	66	18
USD 29 million	4%	December 2027	61	–
EUR 35 million	LIBOR + 0.063%	December 2026	59	8
USD 100 million	LIBOR + 2.33%	June 2020	57	57
AZN 144 million	0.16% (0.15% + 0.01%)	January 2045	56	6
USD 55 million	LIBOR + 5.25%	September 2024	55	16
EUR 35 million	LIBOR + 0.072%	November 2025	51	8
USD 38 million	4.01%	December 2023	44	10
CHF 22 million	LIBOR + 0.0714% or 0%	July 2020	34	–
EUR 40 million	EURIBOR + 2.25%	December 2020	26	26
USD 100 million	LIBOR + 2.4%	May 2020	25	49
USD 50 million	LIBOR + 2.2%	July 2020	24	25
USD 24 million	4.26%	December 2022	24	8
EUR 20 million	1.64%	October 2023	24	6
EUR 20 million	LIBOR + 0.872%	September 2023	24	6
USD 52 million	6%	January 2020	21	–
CHF 10 million	3%	October 2027	17	–
USD 10 million	5%	October 2020	17	–
USD 20 million	LIBOR + 2%	April 2023	10	–
GEL 46 million	14%	July 2020	9	16
USD 5 million	5%	June 2020	9	–
EUR 12 million	LIBOR + 3%	March 2022	8	3
GEL 61 million	11%	July 2020	8	12
GEL 11 million	11.5%	February 2020	7	–
EUR 7 million	EURIBOR + 1.75%	November 2028	6	1
USD 5 million	4.26%	December 2022	6	2
USD 6 million	4.26%	December 2022	5	2
EUR 7 million	LIBOR + 3%	March 2022	4	2
USD 35 million	LIBOR + 2.35%	April 2020	4	9
USD 4 million	4.26%	December 2022	4	1
GEL 35 million	11.25%	April 2020	4	11
USD 4 million	4.26%	December 2022	4	1
EUR 5 million	LIBOR + 3%	March 2022	3	1
GEL 10 million	5% + ref. rate	November 2020	3	3
GEL 15 million	11.25%	July 2020	3	5
GEL 10 million	14%	October 2020	3	3
Other long-term borrowings			17	18
Total long-term borrowings			**9,659**	**1,244**

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

20. Borrowings (continued)

At 31 December 2017, short-term borrowings and long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate	Maturity	Total borrowed in original currency	Balance as at 31 December 2017
Short-term facilities in USD	1.7%-14%	January 2018 – December 2018	**2,280**	3,864
Short-term facilities in TRY	9.66%-15.35%	January 2018 – December 2018	**617**	275
Short-term facilities in GEL	10.25%-15.5%	January 2018 – December 2018	**108**	58
Short-term facilities in other currencies	0.7%-20%	January 2018 – September 2018	**361**	481
Current portion of long-term borrowings			–	1,320
Total short-term borrowings and current portion of long-term borrowings			–	**5,998**

20. Borrowings (continued)

At 31 December 2017, long-term borrowings of the Group were represented by the following facilities:

Facilities	Interest rate*	Maturity	Balance as at 31 December 2017 Non-current portion	Current portion
USD 1000 million	4.75%	March 2023	1,663	20
USD 750 million	6.95%	March 2030	1,224	27
USD 489 million	LIBOR + 6.95%	July 2025	758	15
USD 300 million	LIBOR + 3.25%	March 2022	502	7
USD 260 million	LIBOR + 4.3% + 1.25%	December 2022	431	–
USD 485 million	LIBOR + 1%	December 2024	353	131
EUR 251 million	EURIBOR + 3.03%	June 2028	308	1
USD 200 million	LIBOR + 1.335%	December 2027	286	14
AZN 378 million	3.5%	October 2024	283	107
EUR 249 million	EURIBOR + 0.95%	June 2028	265	1
AZN 600 million	4%	July 2022	260	66
AZN 350 million	3%	June 2023	250	110
USD 100 million	5%	October 2021	170	2
USD 100 million	LIBOR + 3.25%	February 2022	168	4
USD 100 million	LIBOR + 3.25%	April 2022	167	2
USD 212 million	LIBOR + 4.675%	March 2028	326	34
JPY 15,398 million	1.5%	April 2039	161	8
USD 78 million	4%	December 2027	157	–
USD 101 million	LIBOR + 2.8%	April 2022	138	34
USD 100 million	LIBOR + 2.33%	June 2020	114	57
AZN 98 million	3.5%	December 2028	98	–
USD 50 million	4.81%	December 2019	85	–
AZN 100 million	3.5%	January 2026	80	23
USD 65 million	LIBOR + 4.95%	December 2024	80	19
USD 150 million	LIBOR + 1.8%	November 2019	74	73
USD 150 million	LIBOR + 1.8%	December 2019	74	73
USD 100 million	LIBOR + 2.4%	May 2020	73	49
USD 55 million	LIBOR + 5.25%	September 2024	71	14
EUR 35 million	LIBOR + 0.063%	December 2026	71	–
AZN 70 million	4%	January 2027	63	10
EUR 35 million	LIBOR + 0.072%	November 2025	62	9
USD 29 million	4%	December 2027	59	–
AZN 144 million	0.16% (0.15% + 0.01%)	January 2045	55	8
USD 38 million	4.01%	December 2023	54	10
EUR 40 million	EURIBOR + 2.25%	December 2020	54	27
USD 50 million	LIBOR + 2.2%	July 2020	48	25
CHF 22 million	LIBOR + 0.0714% or 0%	January 2019	38	–
USD 150 million	LIBOR + 2.5%	March 2019	37	74
USD 150 million	LIBOR + 2.2%	May 2019	37	73
USD 24 million	4.26%	December 2022	32	8
EUR 20 million	1.64%	October 2023	31	6
EUR 20 million	LIBOR + 0.872%	September 2023	31	6
USD 52 million	6%	January 2020	30	–
USD 50 million	LIBOR + 1.8%	November 2019	29	29
USD 50 million	LIBOR + 1.8%	December 2019	25	24
GEL 51 million	11%	July 2020	20	13
USD 10 million	5%	October 2020	17	–
USD 35 million	LIBOR + 2.35%	April 2020	13	9
EUR 12 million	LIBOR + 3%	March 2022	11	3
USD 20 million	LIBOR + 2%	April 2023	10	–
USD 5 million	5%	Jun 2020	9	–
USD 6 million	4.26%	December 2022	7	2
USD 5 million	4.26%	December 2022	7	2
EUR 7 million	LIBOR + 3%	March 2022	7	2
USD 4 million	4.26%	December 2022	6	1
USD 6 million	4.01%	February 2020	5	5
USD 4 million	4.26%	December 2022	5	1
EUR 5 million	LIBOR + 3%	March 2022	5	1
USD 150 million	LIBOR + 2.5%	November 2018	–	73
Other long-term borrowings			16	8
Total long-term borrowings			**9,513**	**1,320**

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

21. Taxes payable

	2018	2017
Payable to SOFAZ	255	255
Corporate income tax payable	219	98
Social security contributions	3	2
Other taxes payable	213	132
Total taxes payable	**690**	**487**

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 2009-2018.

Taxpayers components of the Group 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 VAT, property tax, 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	2018	2017
Carrying amount at 1 January		**1,067**	**968**
Additions		87	77
Acquisition of additional interest in ACG PSA		–	293
Unwinding of the present value discount	32	65	61
Effect of change in estimates		(140)	(306)
Exchange differences		–	(26)
Carrying amount at 31 December		**1,079**	**1,067**

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.

The maximum costs in respect of asset retirement obligations of the Group mainly represented by the following oil and gas exploration, evaluation and development fields in the Azerbaijan Republic.

The maximum estimated cost to Azneft PU to abandon the production facilities employed was AZN 1,913 as at 31 December 2018 (31 December 2017: AZN 1,924). The Company used 8.47 per cent rate to discount this obligation (2017: 8.02 per cent).

The maximum estimated cost to AzACG to abandon the production facilities employed in ACG project was AZN 1,629 as at 31 December 2018 (31 December 2017: AZN 1,582). The Company used 6.41 per cent rate to discount this obligation (2017: 5.66 per cent).

The maximum estimated cost to AzSD to abandon the production facilities employed in Shah Deniz project was AZN 500 as at 31 December 2018 (31 December 2017: AZN 469). The Company used 6.26 per cent rate to discount this obligation (2017: 5.66 per cent).

The maximum estimated cost to the Group to abandon the production facilities employed in Absheron PSA project was AZN 147 as at 31 December 2018 (31 December 2017: AZN 89). The Company used 6.26 per cent rate to discount this obligation (2017: 5.66 per cent).

22. Asset retirement obligations (continued)

The maximum estimated cost to the Group to abandon the production facilities employed in SOCAR Umid RSA project was AZN 90 as at 31 December 2018 (31 December 2017: nil). The Company used 6.26 per cent rate to discount this obligation.

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 461 at 31 December 2018 (31 December 2017: AZN 477) are included in the cost of oil and gas properties and equipment.

Asset retirement obligations are measured by the Group using the present value of the estimated future costs of decommissioning of the assets. Management determines discount rates that reflect current market assessments of the time value of money and where appropriate, the risks specific to the liability. Discount rates are reviewed at each reporting date and used for discounting abandonment and site restoration costs. The discount rate used as at 31 December 2018 was in range of 6.26-8.47 per cent (31 December 2017: 5.66-8.02 per cent).

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 139 lower / AZN 201 higher, respectively.

The following inflation rates were applied in calculation of discounted cash flows in respect of abandonment and site restoration costs:

Year	2019	2020	2021	2022	2023	2024 and later
Inflation rate	3.82%	4.20%	3.90%	3.80%	3.75%	4.00%

If the estimated inflation rates 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 128 higher / 75 AZN lower, respectively.

23. Other provisions for liabilities and charges

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

	Note	Environmental obligations	Disability payments	Total
Carrying amount at 1 January 2017		**76**	**117**	**193**
Effect of change in utilization date		(7)	–	**(7)**
Disposals		–	(6)	**(6)**
Utilisation		(17)	(16)	**(33)**
Unwinding of the present value discount	32	6	9	**15**
Effect of change in estimates		–	2	**2**
Carrying amount at 31 December 2017		**58**	**106**	**164**
of which:				
Current		55	15	**70**
Non-current		3	91	**94**
Carrying amount at 1 January 2018		**58**	**106**	**164**
Additions/(Disposals)		99	3	**102**
Unused amount reversed		(29)	–	**(29)**
Utilisation		(24)	(16)	**(40)**
Unwinding of the present value discount	32	4	8	**12**
Effect of change in estimates		–	(1)	**(1)**
Carrying amount at 31 December 2018		**108**	**100**	**208**
of which:				
Current		41	15	**56**
Non-current		67	85	**152**

23. Other provisions for liabilities and charges (continued)

Environmental obligation

Subsequent to the Presidential Decree numbered 1697 dated 28 September 2006, the Group started to recognize constructive obligations, prepared and approved Action Plans (2014-2018) for Environmental Restoration with respect to the damage and contamination caused to the environment as a result of the Group's activities within Absheron area.

In 2018, the Management approved new Action Plan (2019-2023) to estimate the Group's obligations in respect of environmental restoration related to expected damage and contamination caused to the environment as a result of activities within Absheron area. The management estimated the Group's environmental obligations based on historic trend of respective expenses and estimated production profile of the Group.

Environmental obligations are measured by the Group using the present value of the estimated future costs of environmental restorations. Management determines discount 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. Discount rates used for discounting environmental remediation costs. The Group calculated the present value of the environmental obligation using a discount rate of 7.97 per cent (2017: 8.27 per cent).

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 environmental provision would have been AZN 2 lower / AZN 2 higher, respectively.

Disability payment

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 and salaries paid to current similar positions. The Group calculated the present value of the disability payments to employees using a discount rate of 8.32 per cent (2017: 7.94 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.

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 6 lower / AZN 7 higher, respectively.

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

24. Deferred income

	2018	2017
Carrying amount at 1 January	**104**	**172**
Offset with tax overpayments	(29)	–
Released to the consolidated statement of profit or loss	(6)	(68)
Carrying amount at 31 December	**69**	**104**
of which:		
Current	11	41
Non-current	58	63

Current

As at 31 December 2018, current portion of deferred income represents government grants for the compensation of losses expected to be incurred from sale of natural gas and heating oil for the purpose of meeting local demand in the country.

Non-current

As at 31 December 2018, 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:

	2018	2017
Liabilities under carried interest arrangements	566	479
Derivative liabilities	445	791
Long-term payables to related party	83	–
Other liabilities	56	41
Total other financial liabilities	**1,150**	**1,311**
of which:		
Current	355	653
Non-current	795	658
Provision for employment termination benefits	57	66
Other liabilities	58	61
Total other non-current non-financial liabilities	**115**	**127**
Total other liabilities	**1,265**	**1,438**

Derivative liabilities

The Group has financial liabilities related to margin calls and funds held on trading in the amount of AZN 47 (31 December 2017: AZN 50), unrealized losses on paper positions in the amount of AZN 228 (2017: AZN 565) and unrealized losses on physical positions in the amount of AZN 170 (2017: AZN 176). Current portion of these liabilities as of 31 December 2018 was AZN 355 (31 December 2017: AZN 653).

Liabilities under carried interest arrangements

In February 2017, exploration and evaluation stage of Absheron PSA was completed successfully and the Group started to recognize liability with respect to its participating interest Absheron Offshore 2 PSA ("Absheron PSA") which was carried by other parties under the carried arrangement until the commencement of development stage. Pursuant to Absheron PSA, at 31 December 2018 the Group's carried liability under Absheron PSA was AZN 412 (31 December 2017: AZN 334).

Provision for employment termination benefits

Under *Turkish Labour 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). 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:

	2018	2017
Discount rate (per cent)	5.00	4.39
Probability of retirement (per cent)	100	100

25. Other current and non-current liabilities (continued)

Provision for employment termination benefits (continued)

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:

	2018	2017
Carrying amount at 1 January	**66**	**76**
Actuarial loss and service cost	13	12
Payments during the year	(10)	(13)
Return on plan assets	(4)	(10)
Other	3	5
Translation to presentation currency	(11)	(4)
Carrying amount at 31 December	**57**	**66**

26. Deferred acquisition consideration payable

At 31 December 2018, the Group has deferred consideration payable in the amount of AZN 529 (31 December 2017: nil) for the acquisition of 7 per cent equity interest and 7 per cent of SGC's loan receivable from TANAP Doğalgaz İletim A.Ş. (Note 7).

Additionally, the Group has deferred consideration payable in the amount of AZN 65 (31 December 2017: AZN 65) and AZN 65 (31 December 2017: AZN 65) for the purchase of remaining 49 per cent shares of SOCAR Petroleum CJSC and acquisition of SOCAR Trading, respectively.

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 1,111 in charter capital was registered during 2018 and accordingly the amount was reclassified from additional paid in capital to charter capital (2017: AZN 1,234).

Additional paid-in capital ("APIC")

During 2018 the Government contributed to the charter capital of the Group in the amount of AZN 1,190 (31 December 2017: AZN 243).

During 2018 the Government transferred PPE to the Group for free amounting to AZN 20. Transferred PPE was recognized at fair value within APIC.

As a result of acquisition of 7 per cent equity interest in TANAP Doğalgaz İletim A.Ş and 7 per cent of SGC loan receivable from TANAP Doğalgaz İletim A.Ş, the Group recognized AZN 124 within APIC as a contribution from ultimate controlling party (Note 7).

In 2018, APIC decreased by AZN 145 is represented by income tax related to settlement of receivable from ACG PSA contractor parties as per amended and restated ACG PSA Agreement in 2017 (Note 33).

In 2018 according to the order of Cabinet of Ministers of Azerbaijan Republic, borrowing amounting to AZN 680 due to Ministry of Finance was converted to the charter of the Group (31 December 2017: nil). As of 31 December 2018, AZN 680 was registered as charter capital.

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 2018 such direct cash transfers to the Government, financing (made in the form of payments to sub-contractors of governmental entities) and distribution of property, plant and equipment amounted to AZN 675, AZN 5 and AZN 5 respectively (31 December 2017: AZN 567, AZN 89 and nil, respectively), mainly for repair and reconstruction of existing, as well as construction of new recreational, transport, educational and medical infrastructure of the Azerbaijan Republic.

Sale of shares to non-controlling shareholder

On 10 August 2018, the Group sold its 4.42 per cent shares of SOCAR Polymer Investments LLC for consideration in the amount of AZN 23 (USD 13) to non-controlling shareholder and recognized gain directly in equity in the amount of AZN 1. As a result, the Group's controlling ownership in SOCAR Polymer Investments LLC decreased from 56.57 per cent to 52.15 per cent.

Acquisition of non-controlling interest in subsidiary

On 8 January 2018 the Group increased its ownership in Baku Shipyard LLC by 5.21 per cent through injection of capital and recognized loss in the amount of AZN 14 directly in equity. As a result, the Group's controlling ownership in Baku Shipyard LLC increased from 65 per cent to 70.21 per cent.

28. Analysis of revenue by categories

	2018	2017
Crude oil, net	58,462	56,592
Oil products, net	40,093	24,808
Petrochemicals	3,894	3,881
Natural gas	3,191	2,670
Rent income	249	124
Other revenue	5,309	4,496
Total revenue	**111,198**	**92,571**

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 levied amount is transferred to the State Budget.

Revenue from oil product sales is stated net of excise tax of AZN 456 (2017: AZN 440).

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	2018	2017
Raw materials and consumables used		101,827	84,376
Wages, salaries and social security costs		1,510	1,371
Depreciation of property, plant and equipment		1,391	1,065
Transportation and vehicle maintenance		1,183	1,046
Utilities expense		374	341
Repairs and maintenance expenses		331	278
Taxes other than on income		199	198
Impairment of property, plant and equipment	15	161	468
Mining tax		126	123
Change in other provisions for liabilities and charges		83	(11)
Amortization expense	16	43	41
Expected credit loss (reversal)/impairment under IAS 39		(85)	239
Other		1,256	1,312
Total cost of sales, exploration and evaluation, distribution, general and administrative, ECL and other operating expenses		**108,399**	**90,847**

In 2018, the Group recovered written off cash balance in bank which was declared insolvent in 2016. Accordingly, the Group received cash in the amount of AZN 60 from respective liquidator of the bank.

30. Other operating income

	Note	2018	2017
Government grant		214	68
Gain on reversal of impairment charge		187	23
Gain on termination of operation agreement	39	170	–
Fair value gain on equity instrument at FVPL		142	–
Settlement of pre-existing relationship	39	51	–
Subsidy received from the Government		–	250
Gain on re-measurement to fair value of investment in JV	39	–	257
Gain on release of liabilities under carry arrangements		–	54
Sales of other goods and services rendered		–	35
Other		152	262
Total other operating income		**916**	**949**

31. Finance income

	2018	2017
Interest income on time deposits and bank accounts	126	71
Other	86	46
Total finance income	**212**	**117**

32. Finance costs

	Note	2018	2017
Interest expenses		1,049	814
Provisions for asset retirement obligations: unwinding of the present value discount	22	65	61
Environmental provision: unwinding of the present value discount	23	4	6
Provision for disability payments: unwinding of the present value discount	23	8	9
Total finance costs		**1,126**	**890**

33. Income taxes

Income tax expense comprises the following:

	2018	2017
Current tax expense	612	500
Deferred tax (benefit)/charge	384	(76)
Income tax expense reported in the statement of profit or loss	**996**	**424**
Deferred tax charged to OCI	**-**	**(10)**

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

	2018	2017
Profit before tax	**2,220**	**2,516**
Theoretical tax charge at statutory rate of 20 per cent	**444**	**503**
Effects of different tax rates for certain subsidiaries (25 and 27 per cent)	65	35
Tax effect of items which are not deductible or assessable for taxation purposes:		
- Income which is exempt from taxation	(61)	(255)
- Non-deductible expenses	189	111
Deferred tax asset not recognized	172	104
Current income tax on non-resident dividends (overseas subsidiaries)	19	6
Recognition of previously unrecognized deferred tax asset	(2)	(45)
Unused investment incentives on which deferred income tax assets recognized	(19)	(25)
Potential income tax on retained profit of subsidiaries, associates and joint ventures	3	(38)
Other	186	28
Income tax expense reported in the statement of profit or loss	**996**	**424**

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. Deferred tax asset not recognized mainly relates to the current year tax losses of the Group's subsidiaries which are not expected to utilize these losses.

At 31 December 2018, cumulative balance of unrecognized deferred tax asset is AZN 1,435 (31 December 2017: AZN 1,265).

At 31 December 2018, 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 2018, benefits arising from previously unrecognized deferred tax assets were used during the year to reduce current tax and deferred tax expenses by the amount of AZN 2 (2017: AZN 26) and nil (2017: AZN 19), respectively.

As at 31 December 2018, the Group has not recognised deferred tax liability in the amount of AZN 56 (31 December 2017: AZN 56) 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.

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 2018	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	31 December 2018
Tax effect of deductible/(taxable) temporary differences				
Carry forward tax losses	98	(39)	(8)	51
Investments in associates and joint ventures	(1)	–	–	(1)
Trade and other payables	27	(15)	–	12
Trade and other receivables	33	(11)	–	22
Inventory	9	(4)	(1)	4
Property, plant and equipment	520	(66)	(11)	443
Provisions for liabilities and charges	75	(8)	1	68
Unused investment incentives	113	(33)	(5)	75
Employment termination benefits	9	–	(2)	7
Other	22	(3)	–	19
Deferred tax assets	**905**	**(179)**	**(26)**	**700**

	1 January 2018	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	Acquisition through business combination (Note 39)	Effect of transition to IFRS 15	31 December 2018
Tax effect of deductible/ (taxable) temporary differences						
Accruals	(4)	21	–	–	–	17
Investments in associates and joint ventures	(101)	3	(4)	–	–	(102)
Intangible assets	(41)	2	–	(3)	–	(42)
Trade and other payables	13	(7)	–	–	–	6
Trade and other receivables	(53)	(47)	1	–	20	(79)
Inventory	(22)	(16)	–	–	–	(38)
Property, plant and equipment	(903)	(166)	10	(25)	–	(1,084)
Provisions for liabilities and charges	133	–	3	–	–	136
Other	(231)	5	–	–	–	(226)
Deferred tax liabilities	**(1,209)**	**(205)**	**10**	**(28)**	**20**	**(1,412)**

	1 January 2017	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	31 December 2017
Tax effect of deductible/(taxable) temporary differences				
Carry forward tax losses	80	23	(5)	98
Investments in associates and joint ventures	1	(2)	–	(1)
Trade and other payables	(5)	16	16	27
Trade and other receivables	60	(23)	(4)	33
Inventory	16	(7)	–	9
Property, plant and equipment	443	73	4	520
Provisions for liabilities and charges	73	2	–	75
Unused investment incentives	129	(2)	(14)	113
Employment termination benefits	8	–	1	9
Other	36	(14)	–	22
Deferred tax assets	**841**	**66**	**(2)**	**905**

33. Income taxes (continued)

	1 January 2017	Credited/ (charged) to profit or loss	Credited/ (charged) to OCI	31 December 2017
Tax effect of deductible/(taxable) temporary differences				
Accruals	(2)	(4)	2	(4)
Investments in associates and joint ventures	(101)	(3)	3	(101)
Intangible assets	(43)	2	–	(41)
Trade and other payables	6	7	–	13
Trade and other receivables	(38)	(16)	1	(53)
Inventory	(25)	2	1	(22)
Property, plant and equipment	(895)	(52)	44	(903)
Provisions for liabilities and charges	137	8	(12)	133
Other	(311)	66	14	(231)
Deferred tax liabilities	**(1,272)**	**10**	**53**	**(1,209)**

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 was not explicitly defined as a contractor party in the ACG PSA. As a result, its tax-payer status was not clearly determinable. During 2018, AzACG accrued and paid its income tax at the rate of 25 per cent in accordance with ACG PSA provisions. This assumption was based on communication with relevant tax authorities according to which management concluded that AzACG carries a tax-payer status under the provision of ACG PSA. On 14 September 2017, AzACG, SOCAR and ACG PSA Contractor parties amended and restated ACG PSA. As part of this agreement, ACG PSA Contractor parties also amended ACG PSA Joint Operation Agreement according which AzACG is defined as a new contractor party starting from effective date of amended ACG PSA, 1 January 2018.

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 2018 and 2017.

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 2018 and 2017, therefore, no corporate income tax related to Shah Deniz project was recognized for 2018 and 2017. At 31 December 2018 and 2017, 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 22 per cent as of 31 December 2018. According to new amendments on tax legislation of Turkey, 22 per cent corporate tax rate is applied to the profits of the companies related to 2018 and will be applied to 2019 and 2020 tax periods. Corporate income taxes are payable quarterly. Besides that there are many exemptions in Corporate Tax Law of Turkey regarding corporations including investment incentives which give right to the corporations to deduct some portion (22.2%-50%) of capital expenditures against taxable profit. In accordance with the tax legislation of Turkey dividends paid to overseas corporations located outside Turkey, which have a place of business in Turkey are not subject to withholding tax that is 15 per cent.

33. Income taxes (continued)

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

Deferred tax effect of transition to IFRS 15 was AZN 20 that was recognized directly in opening balance of retained earnings.

In 2017, as a result of increase of Group's participating interest in ACG PSA from 11.65 per cent to 25 per cent, the Group recognized receivables from ACG PSA Contractor Parties in the amount of AZN 578 (USD 339 million) as contribution from government within equity. In 2018, the Group received cash from contractor parties that was subject to statutory tax charge amounting to AZN 145 (Note 27) and it was recognized within equity.

34. Advances received for sale of interest in PSA

In July 2014, the Group signed a Deferred Sales Purchase Agreement ("DSPA") to sell SOCAR's 10 per cent interest in Shah Deniz PSA and 10 per cent interest in SCPC (together referred as "Interest"). 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. In addition, DSPA specifies certain progress payments related to acquisition consideration payable annually till the end of 2020. As of 31 December 2018, total consideration received for the interest in Shah Deniz PSA and SCPC amounted AZN 4,313 (USD 2,537 million) (2017: AZN 4,076 (USD 2,398 million)).

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 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. As at 31 December 2018, carrying value of put option liability over 13 per cent STEAS shares equals to AZN 2,205 (31 December 2017: AZN 2,209).

The Group also has put option liability in the amount of AZN 508 (USD 300 million) (31 December 2017: AZN 510 (USD 300 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.

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:

	Note	2018	2017
Non-cash investing and financing activities			
Transfer of loan to the charter of the Group	27	680	–
Offsetting of Group's loan with tax overpayments		220	–
Investment addition to TANAP Doğalgaz İletim A.Ş. by SGC on behalf of the Group		61	–
Capital expenditures under carried interest arrangement		46	475
Capitalized decommissioning costs		–	70
Purchase of PPE through long-term loans		–	60
Transfer of loan to charter by NCI		–	27
Purchase of PPE through finance lease		–	16
Other non-cash capital expenditures		58	–
Non-cash investing and financing activities		**1,065**	**648**

37. Changes in liabilities arising from financing activities

	1 January 2018	Cash flows	Finance cost	Foreign exchange movement	Acquisition of new business	Other	31 December 2018
Short-term interest bearing borrowings	5,998	(1,853)	232	(138)	–	(226)	4,013
Non-current interest bearing borrowings	9,513	89	600	99	32	(674)	9,659
Put option liabilities	2,719	–	–	(6)	–	–	2,713
Dividend payable to NCI	22	(122)	–	–	–	121	21
Total liabilities from financing activities	**18,252**	**(1,886)**	**832**	**(45)**	**32**	**(779)**	**16,406**

The "Other" column of borrowings includes effect of conversion of loan to charter transaction executed by Ministry of Finance in the amount AZN 680 (Note 27). Remaining amount of AZN 220 represents utilization of loan payable against Group's tax overpayments.

The "Other" column of dividend payable includes dividend declared amount to non-controlling shareholders during 2018.

Changes in liabilities arising from financing activities as at 31 December 2017 were as follows:

	1 January 2017	Cash flows	Finance cost	Foreign exchange movement	Other	31 December 2017
Short-term interest bearing borrowings	6,717	(666)	197	(145)	(105)	5,998
Non-current interest bearing borrowings	8,210	1,083	462	(275)	33	9,513
Put option liabilities	2,832	–	–	(113)	–	2,719
Dividend payable to NCI	–	(252)	–	–	274	22
Total liabilities from financing activities	**17,759**	**165**	**659**	**(533)**	**202**	**18,252**

38. Contingences, commitments and operating risks

Operating environment

Azerbaijan

The Group's operations are mainly conducted in the Azerbaijan Republic. Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of the Azerbaijan economy is largely dependent upon these reforms and the effectiveness of economic, financial and monetary measures undertaken by the government as well as crude oil prices and stability of Azerbaijani Manat.

The Azerbaijan economy has been negatively impacted by decline of oil prices and devaluation of Azerbaijani Manat during 2015. This resulted in reduced access to capital, a higher cost of capital, inflation and uncertainty regarding economic growth. In response to these challenges, Azerbaijani government announced plans to accelerate reforms and support financial system. On 6 December 2016 President of the Azerbaijan Republic approved "Strategic road maps for the national economy and main economic sectors of Azerbaijan". The road maps cover 2016-2020 development strategy, long-term outlook up to 2025 and vision beyond.

Furthermore, during 2018 the government continued its monetary policy with respect to stability of Azerbaijani Manat as well as allocated foreign currency resources which stabilized Azerbaijani Manat. This policy is expected to continue in 2019 with the aim of maintaining macroeconomic stability.

The Group's management is monitoring changes in macroeconomic environment and taking precautionary measures it considers necessary in order to support the sustainability and development of the Group's business in the foreseeable future.

International credit rating agencies regularly evaluate credit rating of the Azerbaijan Republic and the Group. Fitch evaluated rating of the Group and rating of the Azerbaijan Republic as "BB+", however, S&P evaluated the Azerbaijan Republic with "BB+" and the Group with "BB-". Moody's Investors Service set "Ba2" credit rating for Azerbaijan and for the Group.

Turkey

The Group's activities in Turkey were affected by the instability of Turkish economy during 2018. Such instability was followed by significant inflation and devaluation of local currency against major foreign currencies, such as, USD and EUR by 40 per cent and 33 per cent, respectively.

While management believes it is taking appropriate measures to support the sustainability of 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.

Ukraine

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.

The Ukrainian economy while deemed to be of market status continues to display characteristics consistent with that of an economy in transition. These characteristics include, but are not limited to, certain structural imbalances, low capital market liquidity, relatively high inflation and a significant level of domestic and foreign state debt.

Following the significant decline in 2014-2016, the Ukrainian economy started to demonstrate certain signs of recovery and growth. Main risks affecting the sustainability of the emerging economic trends are represented by the continuing tensions in geopolitical relations with the Russian Federation; lack of the clear consensus as to the directions of the institutional reforms, including public administration, judiciary system and reforms in core sectors of the economy; acceleration of labor emigration and low level of capital inflow.

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

38. Contingences, commitments and operating risks (continued)

Operating environment (continued)

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 2018 and 2017 no provision for potential tax liabilities had been recorded.

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 (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.

38. Contingences, commitments and operating risks (continued)

Compliance with financial covenants

At 31 December 2018, the Group had loans payable in total amount of AZN 13,672 which were received for financing its investing and operating activities. 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 2018 and 2017 the Group was in compliance with all applicable financial covenants.

Guarantees received and given by STEAS

The following table demonstrates guarantees received and given by the Group at 31 December 2018:

	2018	2017
Guarantees received		
Bank guarantees within the context of direct order collection system (DOCS)	304	285
Receivable Insurance	258	142
Letters of guarantee received from customers	182	203
Letters of credit received	130	173
Letters of guarantee received from suppliers	127	94
Other	43	79
Total guarantees received	**1,044**	**976**
Guarantees given		
Letters of guarantee given	175	268
Total guarantees given	**175**	**268**
Collaterals, pledges and mortgages (CPMs) given by Petkim		
CPMs given by Petkim on Petlim loan*	324	361
CPMs given for Petkim	665	542
Total CPMs given by Petkim	**989**	**903**

* During 2015, Petlim Limancılık Ticaret A.Ş, where the Group subsidiary Petkim owns 70 per cent shares, has signed a project finance credit agreement with a financial institution in the amount of USD 212 million (AZN 360) 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 47) and a mortgage amounting to USD 350 million (AZN 595) as a guarantee for the loan repayment. The project has financial covenants that are valid during the operating period.

Ongoing cases against Petkim

On 25 August 2017, Petkim was notified by Turkish Tax Authority about the additional VAT charge and fine which was calculated based on Special Consumption Tax ("SCT") regime as a result of the investigation related to pyrolysis gasoline ("pygas") consumption during 2014. Three ongoing legal cases with respect to the application of SCT regime for pygas, have been recently resulted in favour of the Petkim. Accordingly the management and its legal consultants believe the base for noted fine will be deemed as invalid, and so no financial exposure is deemed probable.

Black Sea Terminal tax case

In 2018 Black Sea Terminal – subsidiary of the Group was inspected by the Revenue Service ("RS") which covered the period starting from 1 January 2015 up to 1 January 2018 for corporate income tax and personnel income tax / withholding tax. As a result of inspection, RS accrued additional WHT and respective fines and sanctions in total amount of AZN 106 (GEL 158 million). The Group did not agree with results of the inspection and appealed to Ministry of Finance for further investigation. The management believes that there will be no material outflow in this regard.

38. Contingences, commitments and operating risks (continued)

Bank guarantees of Azfen

At 31 December 2018 Azfen had bank guarantees given in favour of third parties in the aggregate amount of USD 155 million (AZN 264) (31 December 2017: USD 130 million (AZN 221)). The Group's share of commitments as of 31 December 2018 was USD 93 million (AZN 158) (31 December 2017: USD 78 million (AZN 137)).

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 Azerbaijan Republic, 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 expenditures related to remaining gasification in the country will continue to be financed by the Government through contributions into capital.

As at 31 December 2018 gasification was completed by 95.7 per cent and management believes that remaining portion will be completed by the end of 2019.

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 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.

SOCAR – AGSC Gas sales agreement

The Group is obliged under the agreement signed with AGSC to purchase minimum annual quantity of gas during the period September 2019 – June 2020 (with earlier termination or possible extension of the agreement in accordance with provisions of the agreement) at a price which is stipulated in the contract.

Participating interest in ACG PSA

Azerbaijan International Operating Company, the Operator of the ACG PSA has entered into a number of capital commitments as at 31 December 2018. The Group estimated its 25 per cent (31 December 2017: 25 per cent) share of these commitments to be USD 373 million (AZN 634) (31 December 2017: USD 411 million (AZN 699)).

Commitments related to participating interest in Shah Deniz

BP Exploration Shah Deniz Limited, the Operator of the Shah Deniz PSA has entered into a number of capital commitments as at 31 December 2017. The Group estimated its 13.27 per cent share of these capital commitments through its subsidiary and associate to be USD 516 million (AZN 877) (31 December 2017: USD 764 million (AZN 1,299)).

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 13.27 per cent share of the following commitments relating to AGSC's activity:

BOTAS SPA 1

AGSC is obliged under the gas contract signed with BOTAS to make available a maximum of approximately 6.6 billion Contract Cubic Meters ("BCcm") of gas annually until the expiry of the contract at a price calculated based on a formula established by the gas contract. Agreement will be terminated in 2019.

38. Contingences, commitments and operating risks (continued)

Commitments related to participating interest in AGSC (continued)

BOTAS SPA 2

On 25 October 2011 the Group and BOTAS executed a gas Sale and Purchase Agreement ("BOTAS SPA 2") with respect to the sale by the Group to BOTAS of certain volumes of Shah Deniz Stage 2 Gas (2 BCcm first year, 4 BCcm second year, 6 BCcm plateau period). In December 2012 the Group transferred and assigned the rights and obligations under the Stage 2 SPA to AGSC. The commencement date under BOTAS SPA 2 was 30 June 2018.

BOTAS contract for BTC fuel gas (BIL GSA)

AGSC is obliged under the agreement with BOTAS to make available 0.15 BCcm of gas annually at a price which is calculated based on a formula established in the contract.

Georgian Supplemental Gas SPA with GOGC

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 annually in 2019 and onwards, at a price which is calculated based on a formula established in the contract. Agreement will be terminated by the end of 2023.

Sale and purchase agreement with OptionCo

AGSC is obliged under the agreement signed with OptionCo to make available gas during each contract year a maximum of five percent of the volumes transported in the previous calendar years by AGSC via the SCP pipeline through territory of Georgia, at a price which is calculated based on a formula established in the contract.

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 (DEPA, Bulgargaz Shell, Uniper, Axpo, ENGIE, Gas Natural Fenosa, Enel, Hera) and in December 2013 the GSA were assigned to AGSC until Shah Deniz PSA expiry with re-assignment to the Group. The commencement date will be firmed up through funnelling mechanism as defined in the GSA.

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. 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

A fully-termed Framework Agreement related to the novation of long-term GSAs and transfer of GTA capacity from AGSC to SOCAR after 2036 was executed on 19 October 2015 and further amended and restated on 28 September 2018.

Trans Anatolian Pipeline Gas Transportation Agreement (TANAP GTA)

AGSC is a party to TANAP GTA with annual reserved capacity as defined in the contract. The start date will be set through a funnelling mechanism.

Trans Adriatic Pipeline Gas Transportation Agreement (TAP GTA)

AGSC and SOCAR is a party to TAP GTA with annual capacity as defined in the contract. The planned commencement date is between 1 January 2020 – 31 December 2020.

38. Contingences, commitments and operating risks (continued)

BOTAS Gas Transportation Agreement (BOTAS GTA)

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

Societa Nazionale Metanodotti GTA (SNAM GTA)

AGSC is a party to SNAM GTA with annual reserved capacity as defined in the contract. The planned commencement date will be set through a funnelling mechanism.

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

AGSC is obliged under an agreement signed with BTC Co to make available 0.16 bcm in 2019 and during the following years until the termination of the contract subject to the right of BTC Co to reduce annual off-take, at a price which is calculated based on the formula established in the contract.

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.

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 not 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 Baku Shipyard LLC

As at 31 December 2018, the Group had capital commitments to third parties in the amount of AZN 50 (31 December 2017: AZN 46) in respect of construction contracts.

Commitments of SOCAR Switzerland

The Group has number capital commitments for the next years. The Group estimated its capital commitments to be CHF 42 million (AZN 72) (31 December 2017: CHF 9 million (AZN 15)).

Commitments of SOCAR Head Office

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

38. Contingences, commitments and operating risks (continued)

Commitments of SOCAR Head Office

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 2018 was USD 454 million (AZN 772) (31 December 2017: USD 514 million (AZN 874)).

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 Group's share in the SCP Expansion remaining construction budget through its subsidiary and associate at 31 December 2018 was USD 20 million (AZN 34) (31 December 2017: USD 103 million (AZN 175)).

Construction of TANAP

At the financial statement date, the Group has capital commitment to fund the construction of TANAP system. The Group's share in the remaining budget for construction of TANAP system through its associate at 31 December 2018 was USD 240 million (AZN 408) (31 December 2017: USD 795 million (AZN 1,351)).

Construction of TAP

At the financial statement date, the Group has capital commitment to fund the construction of TAP system. In late 2018 TAP AG reached financial close under the project financing, provided by a large group of financial institutions. The Group acts as one of the guarantors of the loan facilities for the 9.8% shares that it holds in TAP AG and continues to provide required equity financing to TAP AG pro-rata to its equity share. The Group's share in the remaining budget for construction of TAP system through its associate at 31 December 2018 was USD 25 million (AZN 42) (31 December 2017: USD 242 million (AZN 412)).

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 throughout the Carry Period (as defined in the Funding Agreement).

SOCAR Gas Transportation Agreement (SOCAR GTA)

Based on this GTA, from and including the start date 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.

38. Contingences, commitments and operating risks (continued)

Operating lease commitments

The Group's certain joint operations and subsidiaries have entered into number of operating lease agreements which created commitments. At 31 December 2018, The Group has following operating lease commitments:

31 December 2018	Within one year	After one year but no later than five years	More than five years
Shah Deniz PSA	58	101	2
ACG PSA	45	39	–
SOCAR Switzerland	23	59	123
SOCAR Trading	20	36	12
CDC	46	–	–
Total	**192**	**235**	**137**

At 31 December 2017, The Group has following operating lease commitments:

31 December 2017	Within one year	After one year but no later than five years	More than five years
Shah Deniz PSA	30	39	–
ACG PSA	55	39	–
SOCAR Switzerland	21	48	106
SOCAR Trading	84	50	12
Total	**190**	**176**	**118**

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life

Acquisition of 100 per cent interest in APMT

According to "Operation Agreement" signed between the Group and APM Terminalleri Liman İşletmeciliği Anonim Şirketi ("APMT") in 2013, the latter was appointed as the operator of Petlim port. APMT was responsible for providing services in accordance with the terms and conditions set out in the operation agreement. The agreement provided APMT with the right to use the infrastructure and maintain, manage and repair the port. On 27 December 2018, APMT terminated Operation Agreement which triggered penalty payment to the Group by ultimate shareholder of APMT. The Group and former owner ("Owner") of APMT negotiated exit route and potential settlement options of penalty amount. As a result, parties agreed to determine penalty amount as fair value of APMT business and settle penalty by transferring APMT to the Group. Thus, the Group recognized penalty receivable of AZN 170 (Note 30) at transaction date.

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

Acquisition of 100 per cent interest in APMT (continued)

This transaction was recognized as an acquisition of new business in accordance with IFRS 3. At the date of acquisition, the Group applied provisional accounting and the fair values of identifiable assets and liabilities arising from the acquisition were identified as following:

	Note	Provisional fair value recognized for transferred asset and liabilities
		AZN
Assets		
Property, plant and equipment	15	98
Intangible assets	16	58
Cash		55
Trade and other receivables		23
		234
Liabilities		
Trade and other payables	19	(47)
Deferred tax liabilities	33	(17)
		(64)
Total net assets at fair value		**170**
Purchase consideration transferred		**(170)**

The transactions resulted in net cash inflow in the amount of AZN 55. The cash outflow as a result of acquisition was nil.

Prior to acquisition, the Group recognized deferred income balance of AZN 51 with APMT regarding the right of use of the port for the future years. At the date of acquisition, deferred income was released to profit or loss statement of the Group as a settlement of pre-existing relationship (Note 30).

Acquisition of 100 per cent shares in retail service chain network in Austria

On 28 February 2018 the Group acquired 100 per cent control over four business units which are network of gas and petrol stores located in Austria. The Group considered this acquisition as an opportunity to expand its petrol station network into an adjacent geography at an attractive rate of return.

This transaction was recognized as acquisition of new business in accordance with IFRS 3. As a result of purchase price allocation fair value of net identifiable assets of acquired business units was determined as equal to the consideration transferred for this acquisition of AZN 56.

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

Acquisition of 100 per cent shares in retail service chain network in Austria (continued)

The fair values of the assets and liabilities as at the date of acquisition are presented below:

	Notes	Fair value recognized on acquisition of control over new business units
Assets		
Property, plant and equipment	15	101
Intangible assets	16	11
Inventories		7
Trade and other receivables		15
Other current financial assets		3
Total assets		**137**
Liabilities		
Long-term borrowings		(32)
Deferred tax liabilities	33	(11)
Trade and other payables	19	(29)
Other current financial liabilities		(9)
Total liabilities		**(81)**
Total net assets at fair value		**56**
Purchase consideration transferred		**(56)***

* *There was cash outflow in the amount of AZN 56 as a result of acquisition.*

From the date of acquisition, newly acquired business units have contributed AZN 303 of revenue and AZN 2 loss to the net profit before tax from the continuing operations of the Group. If the acquisition had taken place at the beginning of the year, the Group's revenue from continuing operations would have been AZN 111,255 and the profit before tax from continuing operations for the period would have been AZN 2,219.

Acquisitions in 2017

Acquisition of 10 per cent interest in Absheron PSA

On 23 June 2017, contractor parties to Absheron PSA, the Group, TOTAL Absheron and Engie signed Deed of Assignment whereby Engie withdrew from PSA and assigned its 20 per cent participating interest to other parties for free of charge. As a result of transaction the Group's participating interest increased to 50 per cent. The Group applied acquisition method to accounting for the increase in participating interest in Absheron PSA which constitutes a business. As a result of provisional purchase price allocation, the Group recognized acquired oil and gas property at fair value of AZN 48 and respective gain within other operating income.

On October 2018, the valuation was completed and the acquisition date fair value of acquired oil and gas property did not differ from provisional value which was used in financial statements as of 31 December 2017.

Accounting of 80 per cent shares in UBEP

SOCAR Umid LLC ("Umid" or "JV") was joint venture between the Group and Nobel Oil with ownership interest of 80 per cent and 20 per cent, respectively. Main objective of Umid was exploration, development and production of Umid field. Despite of the commencement of production phase, Umid did not have licence for sale of gas and condensate.

Shareholders of Umid decided to restructure joint venture and establish joint operation that would be party to Risk Service Agreement ("RSA") dated on 12 January 2017, which was ratified by the Parliament on 2 May 2017.

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

Accounting of 80 per cent shares in UBEP (continued)

On 7 August 2017, based on Share Swap Agreement, parties transferred all assets and liabilities of Umid (except for property, plant and equipment) to the Group. PPE of JV was transferred for use of UBEP. SOCAR and Nobel Oil continued their operations in UBEP with ownership interest 80 per cent and 20 per cent, respectively.

This transaction was recognized as "acquisition of joint operation that is business" in accordance with IFRS 3 and IFRS 11. Excess amount of fair value of net identifiable assets of UBEP over fair value of assets transferred was recorded as a gain on bargain transaction in the amount of AZN 84.

	Note	Fair value of 80 per cent shares in UBEP
Assets		
Group's share in property, plant and equipment	15	401
Group's share in intangible asset – licence	16	105
Total identifiable net assets at fair value		**506**
Fair value of assets transferred		
Fair value of acquirer's previously held equity interest in JV		561
Less: fair value of assets and liabilities of JV transferred to the Group		(139)
Total transferred assets at fair value		**422**
Gain on bargain transaction		**84**

There were no cash outflows as a result mentioned transactions and the transactions resulted in cash inflow in the amount of AZN 13.

As mentioned above, according to the Share Swap Agreement, all assets and liabilities of Umid, except for property plant and equipment, transferred to the Group. The Group accounted for this transfer at fair value as an adjustment to transferred assets.

The Group re-measured previously held equity interest in Umid to fair value and recognized it as part of assets transferred:

	Note	
Fair value of investment in JV at transaction date		561
Carrying value of investment in JV at transaction date		304
Gain on re-measurement to fair value of investment in JV	30	**257**

Acquisition of additional shares in ACG PSA

Up to 20 November 2017, AzACG managed SOCAR's 11.65 per cent participating interest in the Agreement on the Joint Development and Production Sharing for the Azeri and Chirag Fields and the Deep Water Portion of the Gunashli Field in the Azerbaijan Sector of the Caspian Sea (the "ACG PSA"), which was enacted by the legislature of the Azerbaijan Republic giving it the full force of law in the Azerbaijan Republic and which became effective on 12 December 1994 with a 30-year validity.

On 20 November 2017, ACG PSA was amended and restated whereby AzACG's interest in the PSA increased by 13.35 per cent which became effective from 1 January 2018. No consideration was paid by the Group for the acquired shares.

ACG PSA Contractor Parties signed ATD on 14 September 2017 and agreed to compensate the Group for the difference between its initial participating interests of 11.65 per cent and adjusted participating interests of 25 per cent related to 2017 activities. As a result, the Group has a right to 25 per cent share of revenue and is liable for 25 per cent of expenses for the period from 1 January 2017 to 31 December 2017. The Group recognized receivables from ACG PSA Contractor Parties in the amount of AZN 578 (USD 339 million).

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

Acquisition of additional shares in ACG PSA (continued)

As per amended and restated ACG PSA agreement, increase in participation interest of the Group to 25 per cent was to the detriment of participation interest of ACG PSA Contractor Parties. The right to extension of the PSA was granted to ACG PSA Contractor Parties by the Government and effectively, the Group's interest in PSA increased. Ultimately the Group acquired additional interest in ACG PSA in the transaction under common control of the Government without transfer of any consideration. The Group's accounting policy is to account for such transactions at fair value with difference between consideration amount and fair value of acquired asset recognized within equity as APIC.

Fair values of the assets and liabilities related to, acquired 13.35 per cent interest in ACG PSA are presented below:

	Note	Fair value recognized on acquisition of additional interest in ACG PSA
Assets		
Property, plant and equipment	15	3,059
Receivable from contractor parties		578
Inventory		84
Trade and other receivables		2
		3,723
Liabilities		
Trade and other payables		(57)
Asset retirement obligations		(293)
		(350)
Total net assets at fair value		**3,373**

Goodwill and intangible assets with indefinite useful lives

For impairment testing goodwill acquired through business combinations and intangible assets with indefinite useful lives were allocated to CGUs at 31 December 2018 and 2017 as following:

	SOCAR Trading		SOCAR Switzerland		Petkim		UBEP		Other	
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Goodwill	106	106	115	116	63	88	–	–	17	17
Trade name	–	–	7	–	23	33	–	–	–	–
Licence	–	–	–	–	–	–	105	105	–	–

Movement in the carrying amount of goodwill was as follows:

	2018	2017
Carrying amount at 1 January	**327**	**342**
Translation difference	(26)	(15)
Carrying amount at 31 December	**301**	**327**

The carrying amounts of goodwill as of 31 December 2018 and 2017 include an accumulated goodwill impairment of AZN 3.

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

Testing of the carrying value of goodwill and trade name related to Petkim

The carrying value of the goodwill and Petkim trade name at 31 December 2018 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined in the amount of AZN 3,539 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 10-year period. Cash flows for 10-year period are based on existing long-term contracts with duration until 2028. Cash flow projections beyond 10-year period are extrapolated by the terminal growth rates of 2 per cent and then discounted to their net present value. The following key assumptions were used for impairment test of the goodwill:

The valuation exercises are highly sensitive to the WACC, which was taken into account by the Group as 11.4 per cent during forecasted period of 10 years.

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 175 lower / AZN 192 higher, respectively;
- If the terminal growth rate used in the calculation had been 1 per cent higher/lower than management's estimate, the value in use would have been AZN 151 higher / AZN 134 lower, respectively.

As a result of the sensitivity analysis, no impairment charge was identified.

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

The carrying value of the goodwill at 31 December 2018 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 Switzerland GmBH and its subsidiaries as AZN 853 as of 31 December 2018. 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 terminal growth rates of 1.5 per cent and then discounted to their net present value, applying WACC, used as a discount rate of 6 per cent. As a result of the test performed, no impairment has been identified. Valuation exercise is highly sensitive to WACC and terminal growth rate.

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 155 lower / AZN 245 higher, respectively.

If the terminal growth rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the value in use would have been AZN 42 higher / AZN 37 lower, respectively.

As a result of the sensitivity analysis, no impairment charge was 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 2018 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 1,050 as of 31 December 2018. 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. The following key assumptions were used for impairment test of the goodwill:

- Valuation exercise is sensitive to the WACC, which was 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.

39. Business combination, acquisition of non-controlling interests, acquisition of subsidiary which is not a business, goodwill and intangible asset with indefinite useful life (continued)

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

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

If the estimated discount rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the value in use would have been AZN 23 lower / AZN 24 higher, respectively.

If the terminal growth rate used in the calculation had been 0.25 per cent higher/lower than management's estimate, the value in use would have been AZN 10 higher / AZN 10 lower, respectively.

As a result of the sensitivity analysis, no impairment charge was identified.

Testing of the licence related to UBEP

The license of UBEP gives right to the Group to produce and sell natural gas and condensate of Umid field and exploit Babek field. Carrying value of license at 31 December 2018 has been tested for impairment through comparison with its recoverable amount. Recoverable amount has been determined based on the value-in-use calculations of UBEP as AZN 828 as of 31 December 2018. Cash flow projections used for this purpose are based on production profile of the field which is 24 years. As a result of the test performed, no impairment was identified.

The valuation exercises are sensitive to the change in WACC, which was taken into account by the Group, as 14.24 per cent throughout the projection period.

If WACC used in the calculation had been 1 per cent higher/lower than management's estimate, the value in use would have been AZN 28 lower / AZN 30 higher, respectively. As a result of the sensitivity analysis, no impairment was identified.

40. Material partly-owned subsidiaries

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

Proportion of equity interest held by non-controlling interests:

Name	Country of incorporation	Country of operation	2018	2017
Petkim	Turkey	Turkey	49%	49%
Star Gulf FZCO	UAE	Azerbaijan	20%	20%

Accumulated balances of material non-controlling interests:

Name	2018	2017
Petkim	927	1,255
Star Gulf FZCO	18	33

Profit allocated to material non-controlling interests:

Name	2018	2017
Petkim	132	299
Star Gulf FZCO	11	49

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

40. Material partly-owned subsidiaries (continued)

Summarised statement of profit or loss and other comprehensive income for 2018:

	Petkim	Star Gulf FZCO
Revenue	3,358	110
Cost of Sales	(2,815)	(58)
General and administrative expenses	(93)	(1)
Distribution expenses	(28)	–
Other operating income	169	10
Other operating expense	(189)	–
Finance income	868	–
Finance costs	(941)	–
Foreign exchange loss	–	(4)
Profit before tax	**329**	**57**
Income tax expense	(60)	(4)
Profit for the year from continuing operations	**269**	**53**
Other comprehensive loss to be reclassified to profit or loss in subsequent periods – currency translation differences	(743)	(26)
Total comprehensive (loss)/income	**(474)**	**27**
Attributable to non-controlling interests	(233)	5
Dividends declared to non-controlling interests	95	20

Summarised statement of profit or loss and other comprehensive income for 2017:

	Petkim	Star Gulf FZCO
Revenue	3,474	223
Cost of Sales	(2,636)	(69)
General and administrative expenses	(101)	(1)
Distribution expenses	(28)	–
Other operating income	131	91
Other operating expense	(84)	–
Finance income	306	–
Finance costs	(322)	–
Foreign exchange gain	–	6
Profit before tax	**740**	**250**
Income tax expense	(128)	(7)
Profit for the year from continuing operations	**612**	**243**
Other comprehensive loss to be reclassified to profit or loss in subsequent periods – currency translation differences	(279)	(10)
Total comprehensive income	**333**	**233**
Attributable to non-controlling interests	162	47
Dividends declared to non-controlling interests	138	101

40. Material partly-owned subsidiaries (continued)

Summarised statement of financial position as at 31 December 2018:

	Petkim	Star Gulf FZCO
Current assets	**2,571**	**226**
including:		
Cash and cash equivalents	967	130
Trade and other receivables	385	49
Inventories	366	2
Other current assets	853	45
Non-current assets	**2,145**	**7**
including:		
Property, plant and equipment	1,759	6
Intangible assets	232	1
Other non-current assets	154	–
Current liabilities	**(1,240)**	**(145)**
including:		
Short-term borrowings and current portion of long-term borrowings	(480)	–
Trade and other payables	(760)	(145)
Non-current liabilities	**(1,582)**	**–**
including:		
Long-term borrowings	(1,383)	–
Deferred income	(57)	–
Other provisions for liabilities and charges	(34)	–
Deferred tax liabilities	(108)	–
Total equity	**1,894**	**88**
Attributable to:		
Equity holders of parent	966	70
Non-controlling interests	928	18

Summarised statement of financial position as at 31 December 2017:

	Petkim	Star Gulf FZCO
Current assets	**1,895**	**336**
including:		
Cash and cash equivalents	657	226
Trade and other receivables	790	48
Inventories	404	2
Other current assets	44	60
Non-current assets	**2,588**	**8**
including:		
Property, plant and equipment	2,083	7
Intangible assets	333	1
Other non-current assets	172	–
Current liabilities	**(1,056)**	**(181)**
including:		
Short-term borrowings and current portion of long-term borrowings	(362)	–
Trade and other payables	(694)	(181)
Non-current liabilities	**(866)**	–
including:		
Long-term borrowings	(607)	–
Deferred income	(61)	–
Other provisions for liabilities and charges	(46)	–
Deferred tax liabilities	(152)	–
Total equity	**2,561**	**163**
Attributable to:		
Equity holders of parent	1,306	130
Non-controlling interests	1,255	33

40. Material partly-owned subsidiaries (continued)

Summarised cash flow information for year ended 31 December 2018:

	Petkim	Star Gulf FZCO
Operating	478	80
Investing	(888)	(3)
Financing	832	(168)
Net foreign exchange difference on cash and cash equivalents	137	–
Net increase/(decrease) in cash and cash equivalents	**559**	**(91)**

Summarised cash flow information for year ended 31 December 2017:

	Petkim	Star Gulf FZCO
Operating	553	304
Investing	(361)	39
Financing	(95)	(394)
Net foreign exchange difference on cash and cash equivalents	(5)	–
Net increase/(decrease) in cash and cash equivalents	**92**	**(51)**

41. Events after reporting date

New loans

Subsequent to reporting period, the Group obtained new long-term and short-term loans in the amount of AZN 726 (USD 427 million) and AZN 60 (GEL 97 million), respectively from international banks.

Loan repayments

During subsequent period, the Group repaid its outstanding loans in the amount of AZN 150 (USD 88 million) and AZN 88 (GEL 142 million) to several international banks.

Additional Paid In Capital

During subsequent period, additional paid in capital was increased in the amount of AZN 254 of which AZN 80 was registered to charter capital.

Change in tariff

According to the decree of Tariff Committee of the Azerbaijan Republic dated 30 April 2019, gas limit for population group was raised from 1700 m3 to 2200 m3.

Letter of Credit

During subsequent period, the Group acquired a new letter of credit in the amount of AZN 213 (USD 125 million).

Business acquisition

On 29 January 2019, share and purchase agreement was signed between STEAS and EWE Aktiengesellschaft in relation to the acquisition of 100 per cent shares in EWE Turkey Holding Anonim Şirketi.