

**WATER USERS  
ASSOCIATION  
DEVELOPMENT SUPPORT  
PROJECT  
IBRD LOAN AGREEMENT  
8039-AZ AND RELEVANT  
FINANCING AGREEMENT  
IDA CREDIT 4913-AZ**

**Special purpose project financial statements  
for the year ended December 31, 2012**

**WATER USERS ASSOCIATION DEVELOPMENT SUPPORT PROJECT  
IBRD LOAN AGREEMENT 8039-AZ AND RELEVANT FINANCING  
AGREEMENT IDA CREDIT 4913-AZ**

**TABLE OF CONTENTS**

---

	<b>Page</b>
STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS	1
INDEPENDENT AUDITOR'S REPORT	2-3
SPECIAL PURPOSE PROJECT STATEMENT OF CASH RECEIPTS AND PAYMENTS	4
SPECIAL PURPOSE PROJECT STATEMENT OF FINANCIAL POSITION	5
NOTES TO THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS	6-10

# **WATER USERS ASSOCIATION DEVELOPMENT SUPPORT PROJECT IBRD LOAN AGREEMENT 8039-AZ AND RELEVANT FINANCING AGREEMENT IDA CREDIT 4913-AZ**

## **STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2012**

---

Project management is responsible for the preparation of the special purpose project financial statements that present fairly the financial position of the Water Users Association Development Support Project (the "Project") as at December 31, 2012, the related cash receipts and payments for the year ended December 31, 2012, in accordance with the International Public Sector Accounting Standards ("IPSAS – Cash Basis").

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

- properly selecting and applying accounting policies;
- presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- stating whether the IPSAS have been followed, subject to any material departures disclosed and explained in the special purpose project financial statements.

Project management is also responsible for:

- designing, implementing and maintaining an effective and sound system of internal controls;
- maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Project, and which enable them to ensure that the special purpose project financial statements of the Project comply with the IPSAS – Cash Basis;
- maintaining statutory accounting records in compliance with Azerbaijani legislation;
- taking those actions as are reasonably available to them to safeguard the assets of the Project; and
- preventing and detecting fraud and other irregularities.

The special purpose project financial statements for the year ended December 31, 2012 were approved by management on June 28, 2013.

On behalf of the Project management:

  
\_\_\_\_\_  
Akil Mustafayev  
Project Director

  
\_\_\_\_\_  
Gulbahar Mammadova  
Chief Accountant

*Baku, the Republic of Azerbaijan  
June 28, 2013*

*Baku, the Republic of Azerbaijan  
June 28, 2013*

## INDEPENDENT AUDITOR'S REPORT

To the Management of the Water Users Association Development Support Project:

We have audited the accompanying special purpose project financial statements of the Water Users Association Development Support Project (the "Project"), financed under the International Bank for Reconstruction and Development ("IBRD") Loan agreement 8039-AZ, between the IBRD and Government of the Republic of Azerbaijan ("GOA") dated October 25, 2011, and relevant financing agreement of International Development Association ("IDA") Credit 4913-AZ agreement, between the IDA and Government of Republic of Azerbaijan ("GOA") dated October 25, 2011, which comprise the special purpose project statement of financial position as at December 31, 2012 and the related special purpose project statement of cash receipts and payments for the year ended December 31, 2012 and cumulatively through December 31, 2012, and a summary of significant accounting policies and other explanatory information (collectively referred to as the "special purpose project financial statements"). The special purpose project financial statement has been prepared by management using the International Public Sector Accounting Standards ("IPSAS – Cash Basis").

### *Management's responsibility for the special purpose project financial statements*

Management is responsible for the preparation and fair presentation of these special purpose project financial statements with the basis of accounting described in Note 2. This includes determining that the IPSAS – Cash Basis of accounting is an acceptable basis for the preparation of the financial statement in the circumstances, and for such internal control as management determines is necessary to enable the preparation of the special purpose project financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' responsibility*

Our responsibility is to express an opinion on these special purpose project financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the special purpose project financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the special purpose project financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the special purpose project financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the special purpose project financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the special purpose project financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

*Opinion*

In our opinion, the accompanying special purpose project financial statements present, in all material respects, the financial position of the Project as at December 31, 2012 and the related cash receipts and payments for the year ended December 31, 2012, in accordance with the IPSAS – Cash Basis, as further detailed in note 2.

*Paragraph of Emphasis and Limitation of Use*

Without modifying our opinion, we draw your attention to Note 2 to the special purpose project financial statements which describes the basis of accounting. The special purpose project financial statements are prepared to assist the Project to comply with the requirements of IBRD and IDA. As a result, the special purpose project financial statements may not be suitable for other purposes. Our report is intended solely for the use of management of the Project, IBRD, IDA and GOA and should not be distributed or used by anyone other than these specified parties.

*Deloitte Touche*

June 28, 2013  
Baku, the Republic of Azerbaijan


# WATER USERS ASSOCIATION DEVELOPMENT SUPPORT PROJECT IBRD LOAN AGREEMENT 8039-AZ AND RELEVANT FINANCING AGREEMENT IDA CREDIT 4913-AZ

## SPECIAL PURPOSE PROJECT STATEMENT OF CASH RECEIPTS AND PAYMENTS FOR THE YEAR ENDED DECEMBER 31, 2012 AND CUMULATIVE THROUGH THE YEAR ENDED DECEMBER 31, 2012 (in US Dollars)

Note	Direct IDA payments for the year ended December 31, 2012	Direct IDA payments cumulative to December 31, 2012	Total project for the year ended December 31, 2012	Total project cumulative to December 31, 2012	Direct IDA payments for the year ended December 31, 2011	Direct IDA payments cumulative to December 31, 2011	Total project for the year ended December 31, 2011	Total project cumulative to December 31, 2011
<b>FINANCING:</b>								
IDA funds:								
- designated account advances	-	-	3,000,000	3,000,000	-	-	-	-
- designated account replenishment	7	-	4,240,603	4,240,603	-	-	-	-
- SOE reimbursement	6	-	854,785	854,785	-	-	-	-
- direct payments	1,192,424	1,192,424	1,192,424	1,192,424	-	-	-	-
<b>Total IDA funds</b>	<b>1,192,424</b>	<b>1,192,424</b>	<b>9,287,812</b>	<b>9,287,812</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
IBRD funds:								
- front-end fee	-	-	-	8,000	-	-	8,000	8,000
<b>Total IBRD funds</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>8,000</b>	<b>-</b>	<b>-</b>	<b>8,000</b>	<b>8,000</b>
Azerbaijan government funds	-	-	3,325,866	4,643,727	-	-	1,270,236	1,317,861
<b>TOTAL FINANCING</b>	<b>-</b>	<b>-</b>	<b>12,613,678</b>	<b>13,939,539</b>	<b>-</b>	<b>-</b>	<b>1,278,236</b>	<b>1,325,861</b>
<b>LESS PROJECT EXPENDITURES:</b>								
Works, goods, consulting services, training and operating cost	1,192,424	1,192,424	11,750,179	13,069,518	-	-	1,319,339	1,319,339
Front-end fee	-	-	-	8,000	-	-	8,000	8,000
Foreign exchange difference	-	-	1,085	(2,522)	-	-	(3,607)	(3,607)
<b>TOTAL PROJECT EXPENDITURES</b>	<b>1,192,424</b>	<b>1,192,424</b>	<b>11,751,264</b>	<b>13,074,996</b>	<b>-</b>	<b>-</b>	<b>1,323,732</b>	<b>1,323,732</b>
Advances to region support units	-	-	16,265	16,265	-	-	-	-
Excess/(shortage) of financing over expenditures	-	-	846,149	848,278	-	-	(45,496)	2,129

On behalf of the Management:

  
Akif Mustafayev  
Project Director

  
Gulbahar Mammadova  
Chief Accountant

Baku, the Republic of Azerbaijan  
June 28, 2013

Baku, the Republic of Azerbaijan  
June 28, 2013

The notes on pages 6 to 10 form an integral part of these special purpose project financial statements.

**WATER USERS ASSOCIATION DEVELOPMENT SUPPORT PROJECT  
IBRD LOAN AGREEMENT 8039-AZ AND RELEVANT FINANCING  
AGREEMENT IDA CREDIT 4913-AZ**

**SPECIAL PURPOSE PROJECT STATEMENT OF FINANCIAL POSITION  
AS AT DECEMBER 31, 2012  
(in US Dollars)**

	Note	December 31, 2012	December 31, 2011
<b>ASSETS</b>			
Cash at bank:			
IDA designated account	4	55,041	-
Project account		793,237	2,129
Advances to region support units		16,265	-
Cumulative Project Expenditures		13,074,996	1,323,732
<b>TOTAL ASSETS</b>		<b>13,939,539</b>	<b>1,325,861</b>
<b>LIABILITIES AND FUNDS</b>			
Project financing IDA		9,287,812	-
Project financing IBRD		8,000	8,000
Project financing GOA		4,643,727	1,317,861
<b>TOTAL LIABILITIES AND FUNDS</b>		<b>13,939,539</b>	<b>1,325,861</b>

On behalf of the Management:

  
\_\_\_\_\_  
Akif Mustafayev  
Project Director

  
\_\_\_\_\_  
Gulbahar Mammadova  
Chief Accountant

*Baku, the Republic of Azerbaijan  
June 28, 2013*

*Baku, the Republic of Azerbaijan  
June 28, 2013*

The notes on pages 6 to 10 form an integral part of these special purpose project financial statements.

# WATER USERS ASSOCIATION DEVELOPMENT SUPPORT PROJECT IBRD LOAN AGREEMENT 8039-AZ AND RELEVANT FINANCING AGREEMENT IDA CREDIT 4913-AZ

## NOTES TO THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2012 (in US Dollars)

---

### 1. BACKGROUND

The objectives of the Water Users Association Development Support Project (the "Project") are to improve the effectiveness and financial viability of on-farm irrigation water distribution and management of the project area. The Project is financed by the International Bank for Reconstruction and Development ("IBRD") Loan 8039-AZ and relevant financing agreement of International Development Association ("IDA") Credit 4913-AZ (collectively referred to as the "Agreement") between the IBRD, IDA and Government of Republic of Azerbaijan ("GOA") dated October 25, 2011 for USD 3,200,000 and Special Drawing Rights ("SDR") 48,900,000, respectively.

The Project has three components: i) Institutional strengthening and capacity building, ii) On-farm irrigation and drainage rehabilitation, iii) Project management, monitoring and evaluation.

The Institutional strengthening and capacity building provides provision of:

- finance institutional strengthening and capacity building of Azerbaijan Amelioration and Irrigation Open Joint Stock Company ("AIOJSC"), the Central Support Unit, the Region water users associations support units ("WUA"s) in 27 regions, and the regional support centres through the provision of goods, consultants' services;
- capacity building and provision of operational and maintenance equipment and management facilities to eligible WUAs activities pursuant to the Law on "Amelioration and Irrigation" through the provision of goods, consultants' services and training;
- strengthening of the capacity of AIOJSC for the state supervision of the activities of water users associations; and
- preparation of selected studies, research and demonstration pilots in irrigation and drainage, integrated water resource management and related institutional areas.

The On-farm component provides finance on rehabilitation of on-farm irrigation and drainage systems for about 34 eligible WUAs in 15 regions, selected on irrigated area and agricultural production potential through the carrying out of works and the provision of consultants' services.

The Project management, monitoring and evaluation component finances project management and implementation activities, including monitoring and evaluation through the provision of goods, consultants' services and training by a Project implementation unit established within AIOJSC.

According to the contract the expected Project completion date is June 30, 2016.

### 2. BASIS OF PRESENTATION

#### Accounting basis

These special purpose project financial statements are prepared on the cash basis of accounting based on International Public Sector Accounting Standards *Financial Reporting under the Cash Basis of Accounting* issued by the International Public Sector Accounting Standards Board and incorporate the following principal accounting policies, which have been consistently followed in all material respects. Project financing is recognised as a source of project funds when the cash is received. Project expenditures are recognised as a use of project funds when the payments are made.

The reporting currency is United States dollars ("US dollars" or "USD"). Items included in the special purpose project financial statements are measured using the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity (the "functional currency"). The functional currency of the Project is United States dollars ("US dollars" or "USD").



The exchange rates used by the Project management in the preparation of the financial statements as at year-end are as follows:

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
AZN/1 USD	0.7850	0.7865
SDR/1 USD	1.5361	1.5305

### **3. ACCOUNTING POLICIES**

#### **Reporting entity**

The special purpose project financial statements are only for the Water Users Association Development Support Project financed under the International Bank for Reconstruction and Development ("IBRD") and International Development Association ("IDA").

#### **Cash**

Cash comprises cash on the Designated and Project Accounts. The Designated account is a disbursement account of the Project maintained in US Dollars at the International Bank of the Republic of Azerbaijan.

The Project Account is maintained by the Project in local currency (Azerbaijan Manat) and to be used for financing the Government contribution to the Project's expenditures.

#### **Recognition of funding and expense**

Project financing is recognized as a source of funds when the cash is received. Project expenditure is recognized as a use of funds when payment is made.

#### **Foreign currency translation**

Transactions in other currencies are converted to US dollars at the exchange rate prevailing at the date of the transaction. Cash balances in other currencies are converted to US dollars at the period end exchange rate. The resulting foreign exchange gain/losses are recorded separately in the special purpose statement of cash receipts and payments.

### **4. FINANCING AND EXPENDITURES THROUGH THE DESIGNATED ACCOUNT**

#### **Financing**

Financing consists of the contributions made by the IBRD and IDA either in the form of direct payments made to the contractors, suppliers and consultants or in the form of designated account replenishments. The Project periodically requests withdrawal of loan proceeds through submission of a statement indicating expenditures for certain items referred to in the Agreement.

#### **Expenditures**

Payments out of the designated account are made for eligible expenditures in accordance with the provisions of the Agreement. Disbursements from designated account are made either for direct payments or to reimburse for project expenditures already paid by the Project. The IDA then replenishes the designated bank account on the basis of appropriate withdrawal applications submitted for these disbursements as described in the preceding paragraph.

The designated account is a disbursement account for the Project, denominated in US dollars, maintained at the International Bank of Azerbaijan (Account # 33318028409330119120 USD, address: 67 Nizami street, Azerbaijan, Baku AZ1005) during the year ended December 31, 2012, so as to ensure the payment of eligible expenditures, as defined by the Agreement.

The summary of the movements of the designated account were as follows:

**Balance as at January 1, 2012**

**ADD receipts:**

- Designated account advance	3,000,000
- Advance replenishments (Note 7)	3,515,716
- SOE reimbursements (Note 6)	611,929

**Total cash receipt** **7,127,645**

**DEDUCT disbursements:**

Amount of eligible expenditures paid	(7,059,104)
Advances to region support units	(13,500)

**Balance as at December 31, 2012** **55,041**

No withdrawal on International Bank for Reconstruction and Development ("IBRD") Loan 8039-AZ and relevant financing agreement of International Development Association ("IDA") Credit 4913-AZ agreement was made from the start of project activities till January 1, 2012 (Note 6, 7).

**5. BUDGET AND BASIS OF FUNDING**

According to the terms of the Agreement with the IBRD and IDA, the Project is financed by proceeds received from different sources of finance as follows:

IBRD loan agreement 8039-AZ:

Category	Description	Budget, USD	% financed by IBRD Loan
1	Works, Goods, Consultants' services including Audit, Training and Operating Costs	3,192,000	83%
2	Front-end fee	8,000	-
<b>TOTAL</b>		<b>3,200,000</b>	

IDA credit 4913-AZ:

Category	Description	Budget, USD*	% financed by IDA Loan
1	Works, Goods, Consultants' services including Audit, Training and Operating Costs	77,301,120	83%
<b>TOTAL</b>		<b>77,301,120</b>	

\* Total budget of the Project finance comprises SDR 48,900,000 equivalent of USD 77,301,120 as at agreement date October 25, 2011 per official exchange rate as of Central Bank of Azerbaijan USD/1 SDR 1.5808.

## 6. STATEMENT OF EXPENDITURES WITHDRAWAL SCHEDULE

The IDA has disbursed advance payments to the Designated Account of the Project of USD 3,000,000 for the year ended December 31, 2012. The following funds were disbursed through the Statement of Expenditures ("SOE"):

For the year ended December 31, 2012:

Application #	SOE reimbursement	Works, goods, consulting services, training and operating cost	Reimbursed expenditures (Note 4)	Balance
4	103,872	103,872	(103,872)	-
6	101,761	101,761	(101,761)	-
9	152,741	152,741	(152,741)	-
10	102,177	102,177	(102,177)	-
11	151,378	151,378	(151,378)	-
12	72,930	72,930	-	72,930*
14	211,619	211,619	-	211,619*
<b>Total</b>	<b>896,478</b>	<b>896,478</b>	<b>(611,929)</b>	<b>284,549</b>

\* Applications # 12 and 14 were submitted for expenditures occurred and paid in year 2012 and reimbursed subsequent to reporting period in year 2013.

For the year ended December 31, 2011:

Application #	SOE reimbursement	Works, goods, consulting services, training and operating cost	Reimbursed expenditures	Balance
1	222,830	222,830	(222,830)**	-
3	20,026	20,026	(20,026)**	-
<b>Total</b>	<b>242,856</b>	<b>242,856</b>	<b>(242,856)**</b>	<b>-</b>

\*\* Applications # 1 and 3 were submitted for expenditures occurred and paid in year 2011 from funds obtained from the Government of Republic of Azerbaijan and subsequently reimbursed in 2012 by IDA through Project Account in AZN.

## 7. DESIGNATED ACCOUNT EXPENDITURE REPLENISHMENT SCHEDULE

The following funds for expenditures were disbursed through replenishment of Designated account for the year ended December 31, 2012:

Application #	Designated account expenditure reimbursement	Works, goods, consulting services, training and operating cost	Reimbursed expenditures (Note 4)	Balance
4	396,104	396,104	(396,104)	-
6	546,530	546,530	(546,530)	-
9	844,967	844,967	(844,967)	-
10	822,276	822,276	(822,276)	-
11	905,839	905,839	(905,839)	-
12	837,117	837,117	-	837,117*
14	1,809,793	1,809,793	-	1,809,793*
<b>Total</b>	<b>6,162,626</b>	<b>6,162,626</b>	<b>(3,515,716)</b>	<b>2,646,910</b>

\* Applications # 12 and 14 were submitted for expenditures occurred and paid in year 2012 and reimbursed subsequent to reporting period in year 2013.

For the year ended December 31, 2011:

Application #	Designated account expenditure reimbursement	Works, goods, consulting services, training and operating cost	Reimbursed expenditures	Balance
1	665,695	665,695	(665,695)**	-
3	59,192	59,192	(59,192)**	-
<b>Total</b>	<b>724,887</b>	<b>724,887</b>	<b>(724,887)**</b>	<b>-</b>

\*\* Applications # 1 and 3 were submitted for expenditures occurred and paid in year 2011 from funds obtained from the Government of Republic of Azerbaijan and subsequently reimbursed in 2012 by IDA through Project Account in AZN.

#### 8. TOTAL AMOUNTS PAID BY IDA

The total direct disbursements by IDA on behalf of the Project were USD 1,192,424 for the year ended December 31, 2012. Payments controlled and paid by IDA to the Project for the year ended December 31, 2012 were USD 8,026,847.

#### 9. OPERATING ENVIRONMENT

##### Country risk

Emerging markets such as Azerbaijan are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. Laws and regulations affecting businesses in Azerbaijan continue to change rapidly, tax and regulatory frameworks are subject to varying interpretations. The future economic direction of Azerbaijan is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment.

Because Azerbaijan produces and exports large volumes of oil and gas, its economy is particularly sensitive to the price of oil and gas on the world market.

#### 10. EVENTS SUBSEQUENT TO THE SPECIAL PURPOSE PROJECT FINANCIAL STATEMENTS DATE

Subsequent to balance sheet date IDA reimbursed applications # 12 and 14 in amount of USD 910,047 and USD 2,021,412, respectively (Note 6, 7).

As of June 20, 2013 the Project raised additional funds from IDA and Government of the Republic of Azerbaijan in amount of USD 9,571,506 and USD 2,878,804, respectively. Amount of expenditures increased by USD 11,626,828.

The only asset of the Entity is cash, which is not subject to fair value review and write down as the fair value of cash is its book value.

#### 10. APPROVAL OF FINANCIAL STATEMENTS

These special purpose project financial statements were authorised for issue by the Management of the Project on June 28, 2013.