MUSCAT CITY DESALINATION COMPANY SAOG (under conversion)

Report and financial statements for the year ended 31 December 2017

Registered and Principal place of business

PO box 1935,
PC 114, Muscat
Sultanate of Oman

MUSCAT CITY DESALINATION COMPANY SAOG

Report and financial statements
for the year ended 31 December 2017

KPMG
4th Floor, HSBC Bank Building
MBD
P.O. Box 641
P.C. 112
Sultanate of Oman
Tel +968 24709181
Fax +968 24700839

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF MUSCAT CITY DESALINATION COMPANY SAOG

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Muscat City Desalination Company SAOG (the Company) set out on pages 5 to 34, which comprise the statement of financial position as at 31 December 2017, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

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 Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Company in accordance with International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the Sultanate of Oman, and we have fulfilled our other ethical responsibilities in accordance with these requirements and 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 financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter – Valuation of derivatives

The Company has derivative financial liabilities carried at fair value in the amount of RO 1.7 million as at 31 December 2017.

Derivative financial instruments are used to manage and hedge interest rate risk. These instruments are designed as cash flow hedges. Valuation of the derivatives is based on valuation models using observable input data.

We have focused on this area because of the level of judgement involved in their measurement, together with the complexity associated.

Our response

We have performed, amongst other audit procedures, the following:

- Obtained an understanding of the risk management policies, as well as accounting policies for recognition and measurement of derivative financial instruments, applied by the Company;

- Tested the design and implementation of controls over measurement of derivatives;

- Reconciled derivative financial instruments recorded values and data to third party confirmations;

- Independently recalculated the fair value of derivative financial instruments with independent and externally available market data using support from our financial risk management specialists; and

- Considered the appropriateness of disclosures in relation to derivative financial instruments.

For further information on derivative financial instrument and hedge accounting please refer note 3 on pages 13 and 14, note 10 on pages 23 and 24 and note 23 on pages 32 and 33.

Other Information

Management is responsible for the other information. The other information comprises the director's report, report on corporate governance and management discussion and analysis.

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

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS and their preparation in compliance with the relevant disclosure requirements of the Capital Market Authority and the applicable provisions of the Commercial Companies Law of 1974, as amended, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

KPMG

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and 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 those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' 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.

Report on Other Legal and Regulatory requirements

We report that the financial statements of the Company as at and for the year ended 31 December 2017, in all material respects, comply with the:

- relevant disclosure requirements of the Capital Market Authority; and
- applicable provisions of the Commercial Companies Law of 1974, as amended.

8 February 2018

Paul Callaghan

MUSCAT CITY DESALINATION COMPANY SAOG

Statement of financial position
as at 31 December

	Notes	**2017**	2016
ASSETS		**RO**	RO
Non-current assets			
Property, plant and equipment	*5*	**93,887,582**	97,106,304
Deferred tax asset	*20*	**356,251**	1,419,528
Total non-current assets		**94,243,833**	98,525,832
Current assets			
Trade and other receivables	*6*	**1,288,767**	1,441,601
Cash and cash equivalents	*7*	**4,471,578**	10,466,554
Total current assets		**5,760,345**	11,908,155
Total assets		**100,004,178**	110,433,987
EQUITY AND LIABILITIES			
Capital and reserves			
Share capital	*8*	**15,555,040**	15,555,040
Legal reserve		**1,513,400**	883,186
Retained earnings	*8*	**669,573**	1,600,333
Cumulative changes in fair values of derivative financial instruments	*10*	**(1,737,893)**	(2,781,873)
Total equity		**16,000,120**	15,256,686
Non-current liabilities			
Non-current portion of term loans	*9*	**62,787,629**	71,968,693
Non-current portion of fair value of derivative financial instruments	*10*	**1,951,937**	3,027,657
Provision for decommissioning obligation	*11*	**330,426**	1,072,755
Deferred tax	*20*	**2,093,654**	1,040,182
Non- current portion of shareholders' loans	*13*	**8,810,579**	5,949,997
End of service benefits	*12*	**8,687**	19,385
Total non-current liabilities		**75,982,912**	83,078,669
Current liabilities			
Current portion of term loans	*9*	**3,024,037**	3,423,156
Current portion of fair value of derivative financial instruments	*10*	**92,643**	133,562
Shareholders' stand – by equity loans	*14*	**837,030**	837,030
Current portion of Shareholders' loans	*13*	**1,583,000**	-
Accruals and other payables	*15*	**2,484,436**	2,738,625
Amount due to related parties	*16*	**-**	4,966,259
Total current liabilities		**8,021,146**	12,098,632
Total liabilities		**84,004,058**	95,177,301
Total equity and liabilities		**100,004,178**	110,433,987

The financial statements on pages 5 to 34 were approved by the Board of Directors on 08/02/2018 and were signed on their behalf by:

Chief Executive Officer **Chairman**

The report of the Independent Auditors is set forth on pages 1-4.

MUSCAT CITY DESALINATION COMPANY SAOG

Statement of profit or loss and other comprehensive income for the year ended 31 December

	Notes	**2017 RO**	2016 RO
Operating revenue		**15,593,486**	12,670,953
Operating costs	*17*	**(9,408,717)**	(8,143,521)
Gross profit		**6,184,769**	4,527,432
Administrative and general expenses	*18*	**(879,248)**	(906,703)
Delay liquidated damages		**-**	988,344
Finance costs	*19*	**(3,561,977)**	(3,310,901)
Net profit for the year before tax		**1,743,544**	1,298,172
Income tax	*20*	**(2,044,090)**	-
Net (loss)/profit for the year		**(300,546)**	1,298,172
Other comprehensive income that is or may be reclassified to profit or loss			
Changes in fair values of derivative financial instruments	*10*	**1,116,639**	916,034
Deferred tax on changes in fair values of derivative financial instruments	*10*	**(72,659)**	(109,924)
Other comprehensive income for the year		**1,043,980**	806,110
Total comprehensive income for the year		**743,434**	2,104,282
(Loss)/earnings per share – basic and diluted	*21*	**(0.002)**	0.008

The attached notes on pages 9 to 34 notes form an integral part of these financial statements.

The report of the Independent Auditors is set forth on pages 1-4.

MUSCAT CITY DESALINATION COMPANY SAOG

Statement of changes in equity
for the year ended 31 December

	Share capital	Share premium	Legal reserve	(Accumulated losses) / retained earnings	Cumulative changes in fair values of derivative financial instruments	Total
	RO	RO	RO	RO	RO	RO
At 1 January 2016	15,555,040	84,251	5,185,013	(4,083,917)	(3,587,983)	13,152,404
Total Comprehensive loss						
Profit for the year	-	-	-	1,298,172	-	1,298,172
Other comprehensive loss net of deferred tax	-	-	-		806,110	806,110
Transfers	-	(84,251)	(4,301,827)	4,386,078	-	-
At 31 December 2016	15,555,040	-	883,186	1,600,333	(2,781,873)	15,256,686
At 1 January 2017	**15,555,040**	**-**	**883,186**	**1,600,333**	**(2,781,873)**	**15,256,686**
Total Comprehensive Loss						
Loss for the year	**-**	**-**	**-**	**(300,546)**	**-**	**(300,546)**
Transfer to legal reserve	**-**	**-**	**630,214**	**(630,214)**	**-**	**-**
Other comprehensive income net of deferred tax	**-**	**-**	**-**	**-**	**1,043,980**	**1,043,980**
At 31 December 2017	**15,555,040**	**-**	**1,513,400**	**669,573**	**(1,737,893)**	**16,000,120**

The attached notes on pages 9 to 34 notes form an integral part of these financial statements.

The report of the Independent Auditors is set forth on pages 1-4.

5 Property, plant and equipment *(continued)*

The land on which the plant is constructed has been leased from the Government of the Sultanate of Oman (represented by the Ministry of Housing) for a period of 25 years from 11 February 2013. The lease term can be extended by an additional 25 years at the request of the Company. Lease rentals are paid at the rate of RO 15,045 per annum.

Property, plant and equipment are mortgaged as security for the borrowings of the Company (note 9).

Depreciation charge for the year is recognised as follows:

	2017 RO	2016 RO
Operating costs (note 17)	**2,481,189**	2,142,270
Administrative and general expenses (note 18)	**6,603**	12,638
Cost of capital work in progress	**-**	1,947
	2,487,792	2,156,855

6 Trade and other receivables

	2017 RO	2016 RO
Trade receivables	**1,243,025**	1,397,244
Prepayments and other receivables	**42,992**	42,857
Deposits	**2,750**	1,500
	1,288,767	1,441,601

7 Cash and cash equivalents

	2017 RO	2016 RO
Cash in hand	**102**	227
Cash at bank	**1,203,226**	1,007,242
Short term deposits	**3,268,250**	9,459,085
	4,471,578	10,466,554

The short term deposits are denominated in US Dollars and are with Sumitomo Mitsui Banking Corporation Limited in London with maturities of less than one month. These deposits yield interest at an insignificant rate.

8 Capital and reserves

a) The authorised share capital comprises of 250,000,000 (2016: 250,000,000) ordinary shares of 100 baisa each and the issued share capital comprises 155,550,400 (2016: 155,550,400) fully paid up shares of 100 baisa each.

8 Capital and reserves *(continued)*

The Shareholders of the Company are:

	2017		2016	
	Number of shares	**%**	**Number of shares**	**%**
Summit Water Middle East Company	**50,553,880**	**32.5**	69,997,680	45
Malakoff Oman Desalination Company Limited	**50,553,880**	**32.5**	69,997,680	45
Others	**54,442,640**	**35**	-	-
Cadagua Al Ghubrah UK Limited	**-**	**-**	15,555,040	10
	155,550,400	**100**	155,550,400	100

The two main shareholding companies are registered in Cayman Islands and British Virgin Islands, respectively. None of the other ordinary shareholders owns 10% or more of the Company's paid-up share capital as at 31 December 2017.

Legal reserve

Article 154 of the Commercial Companies Law of 1974 requires that 10% of a company's net profit be transferred to a non-distributable statutory reserve until the amount of the statutory reserve becomes equal to at least one-third of the Company's paid up share capital.

The Company had used the share premium received on the issue of share capital during 2014 and 2015 to fulfil this requirement.

During the year ended 31 December 2016 an amount of RO 4,515,895 was transferred from legal reserve to offset accumulated losses in accordance with the legal opinions and Fatwas (Edicts) issued by the Capital Market Authority. However, for the period ended 31 March 2017, an amount of RO 555,817 was transferred back from retained earnings to legal reserves, so as to adjust retained earnings as on 31 March 2017 to RO Nil to more accurately comply with the legal opinions and Fatwas (Edicts) issued by the Capital Market Authority. A further transfer of RO 74,397 to legal reserve has been made based on the net profit of the Company generated from 1 April 2017 to 31 December 2017.

Dividend

Shareholders at the Ordinary General Meeting ("OGM") held on 27 December 2017 authorised the Board of Directors to determine and distribute cash dividends to the Shareholders of the Company in February 2018 out of the retained earnings as per the audited financial statements for the period ended 30 September 2017, provided that the aggregate amount shall not exceed 3.2% of the paid up share capital of the Company (i.e., 3.2 Baizas per share).

In the board of directors meeting dated 8 February 2018, it was resolved to distribute cash dividend of Baizas 2.93 per share, out of the retained earnings as per the audited financial statements for the nine months period ended 30 September 2017 to the shareholders of the Company who are registered in the Company' shareholders' register with the Muscat Clearing & Depository Company SAOC as on 28 February 2018.

9 Term loans

	2017 RO	2016 RO
Term loans	**67,044,178**	76,700,009
Less: deferred finance charges	**(1,232,512)**	(1,308,160)
	65,811,666	75,391,849
Less: current portion of term loans	**(3,024,037)**	(3,423,156)
Non-current portion of term loans	**62,787,629**	71,968,693

Facilities

On 25 July 2013, the Company entered into a long term financing agreement for loan facilities ("the term loans") in the aggregate maximum amount of RO 81,451,616 (USD 211,837,752) with a consortium of international banks.

Facilities drawn down

At 31 December 2017, RO 81,244,505 (USD 211,299,102) had been drawn down (31 December 2016: RO 81,244,505 (USD 211,299,102)) and the remaining undrawn amount has been cancelled.

Facilities repayments

The term loans are due for repayment in 76 quarterly instalments. Instalments totalling RO 9,655,831 (2016: RO 3,166,043) were paid during the year.

Interest

The term loans bear interest at three month USD Libor plus margin. The effective interest rate for the year was 4.47% (31 December 2016: 4.71%).

Security

The term loans are secured by a commercial mortgage over the Company's assets and a legal mortgage over the Company's rights, title and interest in the Usufruct Agreement dated 11 February 2013. In addition, a charge has been created over all of the Company's shares.

Covenants

The facilities agreements contain certain covenants relating to liquidity. These include restrictions on the debt /equity ratio, the debt service coverage ratio and the loan life cover ratio. For the interest period ending on 12 January 2017 and on 12 April 2017, the Company was in breach of the debt service coverage ratio requirement; a waiver from this requirement was obtained from the lenders. For remainder of the period the Company was in compliance with the covenants.

10 Derivative financial instruments

In accordance with the Common Terms Agreement, the Company is required to enter into interest rate hedging agreements to cap the Company's exposure to fluctuating interest rates. This requirement covers the term loans.

As at the reporting date, a principal amount of approximately RO 60,083,570 (USD 156,264,160) (31 December 2016: RO 62,733,622 (USD 163,156,365)) was covered under this agreement for the term loans.

The hedging agreements cap the Company's exposure to fluctuating interest rates. The Company releases a portion of the hedging arrangements in line with the repayment of the term loans.

The hedging arrangement obliges the Company to pay fixed interest at the rate of 2.86% per annum on a quarterly basis for the term loans. These cash flow hedges were assessed as highly effective as at 31 December 2017 (For the year ended 31 December 2016: highly effective).

The fair value movement of RO 1,116,639 (31 December 2016: RO 916,034) has been included in other comprehensive income.

The classification of the fair values of the derivative financial instruments based on the remaining period to maturity from the reporting date is as follows:

	2017	2016
	RO	RO
Less than 1 year	**(92,643)**	(133,562)
1 to 5 years	**(491,786)**	(717,843)
More than 5 years	**(1,460,151)**	(2,309,814)
Total more than 1 year	**(1,951,937)**	(3,027,657)
Cumulative changes in fair value	**(2,044,580)**	(3,161,219)

Cumulative changes in fair value are recognised as follows:

Cumulative changes in fair value	**(2,044,580)**	(3,161,219)
Related deferred tax asset	**306,687**	379,346
Cumulative changes in fair value, net of deferred tax	**(1,737,893)**	(2,781,873)

The table below shows the fair values of the interest rate swaps, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity.

10 Derivative financial instruments *(continued)*

31 December 2017	Fair value RO	Notional amount RO	Notional amounts by term to maturity: 1 - 12 month RO	More than 1 up to 5 years RO	More than 5 years RO
Interest rate swaps	**2,044,580**	**60,083,570**	**2,722,486**	**14,451,991**	**42,909,093**
31 December 2016					
Interest rate swaps	3,161,219	62,733,622	2,650,053	14,245,423	45,838,146

11 Provision for decommissioning obligation

The decommissioning cost represents the present value of management's best estimate of the future cost to remove the facilities and restore the affected area at the Company's leased site to its original condition. The estimate has been made on the basis of an independent report by a professional consultant, discounted at 4.60% to its present value, over the plant's estimated useful life of 40 years.

12 End of service benefits

	2017 RO	2016 RO
1 January	**19,385**	19,065
Provided during the year	**7,950**	10,701
Paid during the year	**(18,648)**	(10,381)
31 December	**8,687**	19,385

13 Shareholders' loans

	2017	2016
Summit Water Middle East Company	**2,864,525**	2,864,525
Malakoff Oman Desalination Company Limited	**2,864,525**	2,864,525
Sumitomo Corporation	**2,128,921**	-
Malakoff International Limited	**2,128,921**	-
Interest accrued	**406,687**	220,947
	10,393,579	5,949,997
Less: current portion of Shareholders' loans	**(1,583,000)**	-
Non-current portion of Shareholder's loans	**8,810,579**	5,949,997

13 Shareholders' loans *(continued)*

Facilities

The Shareholders' loans of RO 1,691,800 (USD 4,400,000) were provided in October 2015. Further Shareholders' loans of RO 4,037,250 (USD 10,500,000) were provided during the year ended 31 December 2016. Further, amounts due to related parties (ultimate shareholders) of RO 4,257,842 (USD 11,073,711) were converted into shareholders' loan in July 2017.

Facilities repayments

The Shareholders' loans are due for repayment subject to the consent of the term loan lenders which is dependent on cash flows.

Interest

The Shareholders' loans carry interest at the rate of 2% per annum.

Security

The Shareholders' loans are unsecured.

14 Shareholders' stand – by equity loans

	2017	2016
	RO	RO
Summit Water Middle East Company	**376,664**	376,664
Malakoff Oman Desalination Company Limited	**376,664**	376,664
Cadagua Al Ghubrah UK Limited	**83,702**	83,702
	837,030	837,030

Facilities

The Shareholders' stand – by equity loans of RO 837,031 (USD 2,176,932) were provided in November 2015.

Facilities repayments

The Shareholders' stand – by equity loans are due for repayment on demand subject to the consent of the term loan lenders which is dependent on cash flows.

Interest

The Shareholders' stand – by equity loans are interest free.

Security

The Shareholders' stand – by equity loans are unsecured.

15 Accruals and other payables

	2017 RO	2016 RO
Accruals and other payables	**2,484,436**	2,738,625

Accruals and other payables include an amount of RO 637,987 (31 December 2016: RO 660,719), due to Muscat City Desalination Operation and Maintenance Company LLC, a related party.

16 Related party transactions

Related parties comprise the shareholders, directors, key management personnel and any business entities in which these parties have the ability to control or exercise significant influence. The Company maintains significant balances with these related parties which arise in the normal course of business. The terms and conditions of related party transactions are mutually agreed.

Significant related party transactions during the year are as follows:

	2017 RO	2016 RO
Mobilisation and delay fees to Muscat City Desalination Operation and Maintenance Company LLC	**-**	122,500
Operation and maintenance and other cost to Muscat City Desalination Operation and Maintenance Company LLC	**3,657,840**	3,203,367
Net receipts under Shareholders' loans	**-**	4,037,250
Interest expense on Shareholders' loans	**185,740**	220,947
Key management compensation	**254,471**	198,402
Amount due to related parties		
Sumitomo Corporation / Cadagua S.A. / Malakoff International Limited	**-**	4,966,259

This amount relates to initial project costs paid by the related parties which has not yet been reimbursed to the related parties and has been capitalised under property, plant and equipment as it relates directly to the construction of the plant. An amount of RO 4,257,842 was converted into shareholders' loan in July 2017.

For additional disclosure of related party balances and transactions refer notes 13, 14 and 15.

17 Operating costs

	2017 RO	2016 RO
Operation and maintenance cost	**3,630,431**	3,203,367
Electricity charges	**3,297,097**	2,797,884
Depreciation	**2,481,189**	2,142,270
	9,408,717	8,143,521

18 Administrative and general expenses

Employee costs	**344,840**	253,923
Arbitration cost	**-**	212,653
Insurance	**238,067**	198,808
Legal and professional expenses	**150,802**	76,477
Exchange differences – net	**11,150**	(14,887)
Lease rental	**15,045**	-
Depreciation	**6,603**	12,638
Others	**112,741**	167,091
	879,248	906,703

Employees related expenses comprise the following:

	2017 RO	2016 RO
Salaries	**250,916**	205,643
End of service benefit	**7,950**	10,701
Other Employee Benefits	**85,974**	37,579
	344,840	253,923

The number of employees as at 31 December 2017 was 6 (2016: 6)

19 Finance costs (net)

Interest expense on term loans and interest swaps	**3,234,276**	2,922,640
Interest expense on Shareholders' loan	**185,740**	190,768
Amortisation of deferred finance cost	**75,648**	242,715
Interest income on term deposits	**(53,759)**	(45,222)
Agency fees	**39,605**	-
Other finance costs	**80,467**	-
	3,561,977	3,310,901

20 Income tax

The Company is liable to income tax at the rate of 15% (31 December 2016: 12%). The effective tax rate for the Company for the year is nil (31 December 2016: nil). No provision for income tax has been made for the year ended 31 December 2017 in view of the taxable losses for the year.

a) Recognised in the statement of comprehensive income

	2017 RO	2016 RO
Deferred tax		
- Current period	**1,262,602**	155,931
- Prior period	**781,488**	(155,931)
	2,044,090	-

The reconciliation of income tax expense is as follows:		
Profit / (loss) for the period	**1,743,544**	1,298,172
Income tax at standard rate	**261,532**	155,781
Non - deductible expenses	**29,137**	150
Effect of change in tax rate	**227,863**	-
Deferred tax asset not recognised	**744,070**	-
Prior period deferred tax	**781,488**	(155,931)
	2,044,090	-

b) Deferred tax assets and liabilities represent origination and reversal of temporary differences and comprise:

	Asset / (liability) as at 1 January 2017 RO	Recognised in profit or loss and other comprehensive income RO	**Asset / (liability) as at 31 December 2017 RO**
Property, plant and equipment- Deferred tax liability:	(1,040,182)	(1,053,472)	**(2,093,654)**
Carried forward tax losses	911,451	(911,451)	**-**
Provision for decommissioning obligation	128,731	(79,167)	**49,564**
Change in fair value of derivative financial instrument (through other comprehensive income)	379,346	72,659	**306,687**
Deferred tax assets	1,419,528	(917,959)	**356,251**

20 Income tax *(continued)*

Deferred tax arises on account of tax losses and temporary differences between the tax base of assets and liabilities and their carrying values in the statement of financial position. No deferred tax asset on losses has been recognised as management does not consider it probable that sufficient taxable income may arise prior to their expiry to obtain the benefits therefrom.

As at 31 December 2016, based on the best estimates available deferred tax asset on losses in the amount of RO 911,451 was recognised. At the end of the current year the management revisited the estimates and, accordingly, fully reversed the deferred tax asset as management does not consider it probable that sufficient taxable income may arise prior to their expiry to obtain the benefits therefrom.

21 (Loss)/earnings per share

	2017	2016
(Loss) /profit for the year (RO)	**(300,546)**	1,298,172
Weighted average number of shares outstanding during the year	**155,550,400**	155,550,400
(Loss) /earnings per share (basic and diluted)	**(0.002)**	0.008

22 Lease commitments

The land which the plant occupies has been leased from the Government of the Sultanate of Oman (represented by the Ministry of Housing) for a period of 25 years from 11 February 2013. The lease term can be extended by an additional 25 years at the request of the Company. Lease rental is paid at the rate of RO 15,045 per annum.

At 31 December 2017, future minimum lease commitments under non-cancellable operating leases are as follows:

	2017	2016
	RO	RO
Less than one year	**15,045**	15,045
Between one and five years	**60,180**	60,180
More than five years	**225,675**	240,720
	300,900	315,945

23 Financial instruments

This note presents information on the risks arising from the Company's use of financial instruments, namely; credit risk, liquidity risk and market risk to which the Company is exposed, its objectives, policies and processes for measuring and managing risk and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework.

Risk management policies and systems are reviewed regularly to ensure that they reflect any changes in market conditions and the Company's activities. The Company, through its induction and training program, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's deposits with banks.

The exposure to credit risk is monitored on an on-going basis and therefore the Company considers the credit risk to be minimal.

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

	2017	2016
	RO	RO
Trade receivables	**1,243,025**	1,398,744
Bank balances	**4,471,476**	10,466,327
	5,714,501	11,865,071

The exposure to credit risk for trade receivables at the reporting date by type of customer is:

Oman Power and Water Procurement Co. SAOC	**1,328,662**	1,397,244

Trade and other receivables at the end of the reporting period are not overdue or impaired. Cash at bank and deposits with the bank are placed with financial institutions with a credit rating of at least BAA3.

23 Financial instruments *(continued)*

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company uses cash flow forecasting methods which assist it in monitoring cash flow requirements and optimising its cash flow cycle. The Company ensures that it has sufficient cash available to meet its expected operational expenses, including the servicing of financial obligations.

The maturities of Company's financial liabilities after adding back deferred finance charges at the reporting date are shown below

31 December 2017	**Carrying amount**	**Total**	**Less than 1 year**	**1 to 5 Years**	**More than 5 years**
		----------------Contractual Cash flows----------------			
	RO	**RO**	**RO**	**RO**	**RO**
Non derivative financial liabilities					
Term loans	**67,044,178**	**97,144,150**	**6,273,005**	**24,132,370**	**66,738,775**
Shareholders' stand – by equity loans	**837,030**	**837,030**	**837,030**	**-**	**-**
Shareholders' loans	**10,393,579**	**12,592,947**	**1,870,607**	**1,457,460**	**9,264,880**
Accruals and other payables	**2,484,436**	**2,484,436**	**2,484,436**	**-**	**-**
	80,759,223	**113,058,563**	**11,465,078**	**25,589,830**	**76,003,655**

31 December 2016	Carrying amount	Total	Less than 1 year	1 to 5 Years	More than 5 years
		----------------Contractual Cash flows----------------			
	RO	RO	RO	RO	RO
Non derivative financial liabilities					
Term loans	76,700,009	111,768,360	6,747,947	26,205,313	78,815,100
Shareholders' stand – by equity loans	837,030	837,030	837,030	-	-
Shareholders' loans	5,949,997	6,866,645	-	6,866,645	-
Due to related parties	4,966,259	4,966,259	4,966,259	-	-
Accruals and other payables	2,738,625	2,738,625	2,738,625	-	-
	91,191,920	127,176,919	15,289,861	33,071,958	78,815,100

23 Financial instruments *(continued)*

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

Currency risk
The Company is not exposed to foreign currency risk on its bank deposits designated in US Dollars as the Omani Rial is effectively pegged to the US Dollar and the US Dollar exchange rate has remained unchanged since 1986.

Interest rate risk
The Company's interest rate risk arises principally from medium and long term borrowings. Borrowings issued at variable rates expose the Company to cash flow interest rate risk.

Borrowings issued at fixed rates expose the Company to fair value interest rate risk. The Company's policy is to maintain approximately 100% of its borrowings in fixed rate or hedged instruments.

Cash flow sensitivity analysis for variable rate instruments
A change of 100 basis points in interest rates at the reporting date would have increased / (decreased) equity by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

31 December 2017	**100 bp increase RO**	**100 bp decrease RO**
Fair value of derivative financial instruments	**4,475,818**	**(4,475,819)**
31 December 2016		
Fair value of derivative financial instruments	5,019,899	(5,019,899)

Capital risk management

The Board of Directors' policy is to maintain a strong capital base so as to maintain investor and creditor confidence and to sustain future development of the business.

The Company is not subject to externally imposed capital requirements except those under the Commercial Companies Law of 1974, as amended.

23 Financial instruments *(continued)*

Capital risk management *(continued)*

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

In order to maintain the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders or issue new shares.

Fair value

Financial assets consist of cash and bank balances and receivables. Financial liabilities consist of term loans, Shareholders' loans, shareholders' stand – by equity loans and payables. Derivatives consist of interest rate swap arrangements. The fair values of financial instruments are not materially different from their carrying values.

Fair value hierarchy

The Company uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique.

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data

	2017	2016
	RO	RO
Interest rate swaps – *Level 2 (nominal amounts)*	**60,083,570**	62,733,622

The Company had no financial instruments in level 1 or level 3. During the year ended 31 December 2017, there were no transfers of financial instruments between the levels for fair value measurement.

24 Cash flows from financing activities

Reconciliation of movement liabilities/equity to cash flows arising from financing activities is as follows:

	Term loans	Accrued interest	Amount due to related parties	Total
Balance at 1 January 2017	75,391,849	750,460	4,966,259	**81,108,568**
Changes form financing cash flows				
Repayment of term loan	(9,655,831)	-	-	**(9,655,831)**
Finance cost paid	-	(3,372,530)	-	**(3,372,530)**
Repayment of amount due to a related parties	-	-	(708,417)	**(708,417)**
Total changes from operating cash flows	**(9,655,831)**	**(3,372,530)**	**(708,417)**	**(13,736,778)**
Other changes				
Interest expense for the year	-	3,300,589	-	**3,300,589**
Amount due to related parties converted to shareholders' loan	-	-	(4,257,842)	**(4,257,842)**
Amortisation of deferred finance cost	75,648	-	-	**75,648**
Total liabilities / equity - related other changes	**75,648**	**3,300,589**	**(4,257,842)**	**(881,605)**
Balance at 31 December 2017	**65,811,666**	**678,519**	**-**	**66,490,185**

25 Comparative figures

Certain comparative figures for corresponding period have been represented to conform to the presentation adopted in the current year.

5 Property, plant and equipment

	Civil and structural works RO	Plant and machinery RO	Pipelines RO	Decommission-ing asset RO	Spares RO	Furniture, fixtures & office equipment RO	Motor vehicles RO	Total RO
Cost								
1 January 2017	31,325,719	46,357,456	19,908,264	1,072,755	576,006	25,739	38,734	99,304,673
Additions	-	11,110	-	-	-	289	-	11,399
Adjustment	-	-	-	(742,329)	-	-	-	(742,329)
31 December 2017	**31,325,719**	**46,368,566**	**19,908,264**	**330,426**	**576,006**	**26,028**	**38,734**	**98,573,743**
Accumulated Depreciation								
1 January 2017	676,220	1,000,705	429,754	23,157	12,434	21,982	34,117	2,198,369
Charge for the year	783,206	1,159,120	497,707	26,756	14,400	1,986	4,617	2,487,792
31 December 2017	**1,459,426**	**2,159,825**	**927,461**	**49,913**	**26,834**	**23,968**	**38,734**	**4,686,161**
Carrying value								
31 December 2017	**29,866,293**	**44,208,741**	**18,980,803**	**280,513**	**549,172**	**2,060**	**-**	**93,887,582**

5 Property, plant and equipment *(continued)*

	Civil and structural works RO	Plant and machinery RO	Pipelines RO	Decommissi-oning asset RO	Spares RO	Furniture, fixtures & office equipment RO	Motor vehicles RO	Capital work-in-progress RO	Total RO
Cost									
1 January 2016	-	-	-	-	-	24,625	38,734	95,401,338	95,464,697
Additions	-	-	-	1,072,755	-	1,114	-	2,766,107	3,839,976
Transfers	31,325,719	46,357,456	19,908,264	-	576,006	-	-	(98,167,445)	-
31 December 2016	31,325,719	46,357,456	19,908,264	1,072,755	576,006	25,739	38,734	-	99,304,673
Accumulated Depreciation									
1 January 2016	-	-	-	-	-	17,080	24,434	-	41,514
Charge for the year	676,220	1,000,705	429,754	23,157	12,434	4,902	9,683	-	2,156,855
31 December 2016	676,220	1,000,705	429,754	23,157	12,434	21,982	34,117	-	2,198,369
Carrying value								-	
31 December 2016	30,649,499	45,356,751	19,478,510	1,049,598	563,572	3,757	4,617	-	97,106,304

MUSCAT CITY DESALINATION COMPANY SAOG

Statement of cash flows
for the year ended 31 December

	Note	2017 RO	2016 RO
Operating activities			
Net profit for the year before tax		**1,743,544**	1,298,172
Adjustment for:			
Depreciation		**2,487,792**	2,156,855
Finance cost		**3,561,977**	3,310,901
Provision for end of service benefits		**7,950**	10,701
Cash flows from operating activities before working capital changes		**7,801,263**	6,776,629
Change in trade and other receivables		**152,834**	10,789,165
Change in accruals and other payables		**(182,248)**	(16,334,172)
End of service benefit paid		**(18,648)**	(10,381)
Net cash generated from operating activities		**7,753,201**	1,221,241
Investing activity			
Additions to property, plant and equipment		**(11,399)**	(2,737,042)
Net cash used in investing activity		**(11,399)**	(2,737,042)
Financing activities			
Proceeds from shareholders' loans		**-**	4,037,250
Amount due to related parties		**(708,417)**	-
Receipts of term loans		**-**	8,230,473
Repayment of term loans		**(9,655,831)**	(3,166,043)
Finance cost paid		**(3,372,530)**	(2,837,233)
Net cash (used in) / generated from financing activities		**(13,736,778)**	6,264,447
Net change in cash and cash equivalents		**(5,994,976)**	4,748,646
Cash and equivalents at the beginning of the year		**10,466,554**	5,717,908
Cash and cash equivalents at the end of the year		**4,471,578**	10,466,554

The attached notes on pages 9 to 34 notes form an integral part of these financial statements.

The report of the Independent Auditors is set forth on pages 1-4.

1. Legal status and principal activities

Muscat City Desalination Company SAOG, under conversion (the “Company”) is a public joint stock company and is registered in the Sultanate of Oman. The Company was incorporated on 19 January 2013. The Company’s principal activity is the production and sale of desalinated water. The Company commenced commercial production of potable water on 19 February 2016. The Company was listed on the Muscat Securities Market, and conversion to an “SAOG” was completed, on 2 January 2018.

1.1 Key agreements

Water Purchase Agreement
On 11 February 2013 the Company signed a long term Water Purchase Agreement (“WPA”) with Oman Power and Water Procurement Company SAOC for the supply of 42 million imperial gallons of water per day. The agreement expires 20 years after the Scheduled Commercial Operation Date of 12 October 2014, subject to any extension period or early termination arising under the terms of the agreement.

Engineering, Procurement and Construction Contract
The Company entered into an agreement for the construction of a desalination plant with a capacity of 42 million imperial gallons of water per day with International Water Treatment LLC (“the EPC Contractor”) on a turnkey basis which was completed during 2016.

2 New standards and interpretation not yet effective

A number of relevant new standards and amendments to standards are effective for annual periods beginning after 1 January 2018.

- IFRS 9 Financial Instruments, replaces the existing guidance in IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and de-recognition of financial instruments from IAS 39. IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. This standard will affect the rules relating to hedge accounting, as well as accounting policy for recognition and measurement of financial instruments, as well as regarding impairment of financial assets.

- IFRS 15 Revenue from Contracts with Customers establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. This standard will require additional qualitative and quantitative disclosures.

- IFRS 16 Leases replaces the existing guidance in IAS 17 Leases and will be effective from 1 January 2019 and deals with recognition, measurement and classification of leases.

2 New standards and interpretation not yet effective *(continued)*

The Company has completed the assessment of the potential impact on its financial statements resulting from the application of IFRS 9 and IFRS 15. As per management, the implementation of IFRS 9 and IFRS 15 is not expected to have a significant impact on the financial statements. However, the implementation of these standards is underway and, accordingly, the expected impact cannot yet be determined with certainty.

3 Summary of significant accounting policies

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The financial statements also comply with the relevant Rules and Guidelines on Disclosure by Issuers of Securities and Insider Trading, with the relevant Rules for Disclosure and Proforma issued by the Capital Market Authority and with the applicable requirements of the Commercial Companies Law of 1974, as amended.

Basis of preparation

These financial statements have been prepared under the historical cost convention except for certain financial assets and liabilities measured at fair value.

Functional and presentation currency

The accounting records are maintained in Omani Rial which is the functional and presentation currency for these financial statements.

Following are the significant accounting policies applied by the Company consistently to all the years presented.

Foreign currencies

Any currency other than the functional currency is considered as a foreign currency. Transactions in foreign currencies are translated to Omani Rials at the rates of exchange prevailing on the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to Omani Rials using the exchange rate at the reporting date.

Non-monetary assets and liabilities measured at historical cost are translated using the exchange rate at the date of the transaction whereas those measured at fair value are translated using the exchange rate at the date when fair value was determined. An exchange difference on settlement of monetary items or on translation is generally recognised in profit or loss.

Property, plant and equipment

Recognition and measurement
Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses, if any. Cost includes the amount of cash and cash equivalents paid or the fair value of other consideration given to acquire an asset at the date of acquisition or construction. Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, including major inspection and overhaul expenditure, is capitalised.

3 Summary of significant accounting policies *(continued)*

Property, plant and equipment *(continued)*

The cost of self-constructed assets includes the cost of materials, direct labour, borrowing costs and an appropriate proportion of overheads. Gains and losses on disposal of property, plant and equipment are determined by reference to their carrying amount and are taken into account in determining profit or loss. Repairs and renewals are charged to profit or loss when the expense is incurred.

Subsequent costs
The Company recognises in the carrying amount of property, plant and equipment the cost of major inspections and the cost of replacing part of such an item when the cost is incurred, if it is probable that the future economic benefits embodied in the item will flow to the Company and the cost of the item can be measured reliably. All other costs are recognized as an expense as incurred.

Depreciation
Depreciation is calculated so as to write off the cost of property, plant and equipment, other than capital work-in-progress, over their estimated economic useful lives, using the straight line method, from the date that the asset is brought into use.

Where components of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment. Major repairs are depreciated over the remaining useful life of the related asset, or up to the date of the next major repair, whichever is shorter.

The estimated useful lives for the current year are as follows:

	Years
Civil and structural works	40
Plant and machinery	40
Pipelines	40
Decommissioning asset	40
Spares	40
Furniture, fixtures and office equipment	4
Motor vehicles	4

The useful lives, depreciation method, and residual values of property, plant and equipment are assessed by the management at reporting date and adjusted if appropriate.

Capital work-in-progress
Capital work-in-progress is stated at cost less any impairment losses.

Earnings per share

Basic earnings per share is calculated by dividing the net profit for the year by the weighted average number of shares outstanding during the year.

3 Summary of significant accounting policies *(continued)*

Impairment

Financial assets
A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognised in profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost the reversal is recognised in profit or loss.

Non-financial assets
The carrying amounts of the Company's non-financial assets, other than inventories, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognised if the carrying amount of an asset exceeds its estimated recoverable amount. Impairment losses are recognised in the statement of comprehensive income. Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Employees' end of service benefits

Termination benefits are expensed at the earlier of when the Company can no longer withdraw the offer of those benefits. If benefits are not expected to be settled wholly within 12 months of the reporting date, then they are discounted.

With respect to its Omani employees, the Company makes contributions to the Public Authority for Social Insurance under Royal Decree 72/91 calculated as a percentage of the employees' salaries. The Company's obligations are limited to these contributions, which are expensed when due. Provision for non-Omani employee terminal benefits under an unfunded defined benefit

3 Summary of significant accounting policies *(continued)*

Employees' end of service benefits *(continued)*

retirement plan, is made in accordance with Omani Labour Laws and is calculated by estimating the amount of future benefits that employees have earned in return for their service in the current and prior years.

Provisions

A provision is recognised in the statement of financial position when the Company has a legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and the amount can be reliably estimated. The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flow estimated to settle the present obligation, the carrying amount is the present value of those cash flows.

Equity

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity, net of any tax effects.

Revenue

Revenue comprises water capacity and water output charges calculated in accordance with the agreement with Oman Power and Water Procurement Company SAOC for sale of desalinated water. Revenue is recognised when water passes through the flow meter installed in the Company premises.

Finance expenses

Finance costs comprise interest on term loans, interest rate swaps and interest on shareholders' loan. Borrowing costs, net of interest income, which are directly attributable to the acquisition or construction of qualifying assets such as items of property, plant and equipment are capitalised as part of the cost of property, plant and equipment. All other interest expenses are recognised as an expense in profit or loss using the effective interest rate method.

Financial instruments

i) Non-derivative financial instruments

Non-derivative financial instruments comprise receivables, cash and cash equivalents, loans and trade and other payables and amount due to related parties.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured at amortised cost using the effective interest rate method.

3 Summary of significant accounting policies *(continued)*

Financial instruments *(continued)*

ii) Derivative financial instruments

The Company holds derivative financial instruments to hedge its interest rate risk exposures. Derivatives are initially recognised at fair value at the date the derivative contract is entered into and are subsequently measured at their fair value at the end of each reporting period. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which case the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

A derivative with a positive fair value is recognised as a financial asset; a derivative with a negative fair value is recognised as a financial liability. A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Hedge accounting
The Company designates the hedging instrument as cash flow hedges. At the inception of the hedge relationship, the Company documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Company documents whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item.

Cash flow hedges
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss, as is any gain or loss on any hedging that exceeds 100% of the associated liability.

Amounts previously recognised and accumulated in equity are reclassified to profit or loss in the years when the hedged item is recognised in profit or loss.

Hedge accounting is discontinued when the Company revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting.

Income tax

Income tax expense comprises current and deferred tax. It is recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

3 Summary of significant accounting policies (continued)

Income tax *(continued)*

Current tax
Income tax is calculated as per the fiscal regulations of the Sultanate of Oman. Current tax is the expected tax payable on the taxable income for the year, using the tax rates ruling at the reporting date.

Deferred tax
Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax is calculated on the basis of the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. The tax effects on the temporary differences are disclosed under current or non-current liabilities as deferred tax.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the unused tax losses can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash in hand and bank balances with an original maturity of less than three months.

Operating Segment

An operating segment is a component of the Company that engages in activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components, whose operating results are reviewed regularly by the Chief Executive Officer (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess their performance, and for which discrete financial information is available.

The Company's only activity is the sale of desalinated water to OPWP, being the only customer, hence the chief operating decision maker considers the business of the Company as one operating segment.

Water sales and other activities all take place in the Sultanate of Oman.

3 Summary of significant accounting policies *(continued)*

Leases

At inception of an arrangement, the Company determines whether the arrangement is or contains a lease.

At inception or on reassessment of an arrangement that contains a lease, the Company separates payments and other consideration required by the arrangement into those for the lease and those for other elements on the basis of their relative fair values. If the Company concludes for a finance lease that it is impracticable to separate the payments reliably, then an asset and a liability are recognised at an amount equal to the fair value of the underlying asset; subsequently, the liability is reduced as payments are made and an imputed finance cost on the liability is recognised using the Company's incremental borrowing rate.

Leased assets
Leases of property, plant and equipment that transfer to the Company substantially all of the risks and rewards of ownership are classified as finance leases. The leased assets are measured initially at an amount equal to the lower of their fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the assets are accounted for in accordance with the accounting policy applicable to that asset.

Assets held under other leases are classified as operating leases and are not recognised in the Company's statement of financial position.

Lease payments
Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

4 Critical accounting judgements and key sources of estimation uncertainty

In the application of the Company's accounting policies, which are described in note 3, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and in future periods, if the revision affects both current and future periods.

4 Critical accounting judgements and key sources of estimation uncertainty *(continued)*

Key sources of estimation uncertainty

The following are the key assumptions concerning the future 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.

Impairment of property, plant and equipment
Property, plant and equipment is stated at cost. Management considers that there are no indications of impairment considering that the plant has successfully started commercial operations and expects to comply with the requirement of the WPA and sell potable water to OPWP.

Useful life of property, plant and equipment
The estimation of the useful life of the property, plant and equipment has a significant impact on the financial statements. The useful life has been determined to be 40 years on the strength of an independent consultant's report and the comprehensive maintenance and replacement programme in place.

Provision for decommissioning
The expected cost of decommissioning has been determined on the basis of a study by an independent consultant and discounted over 40 years using a discount factor of 4.60%.

Application of IFRIC 4 and IFRIC 12
Judgement is required to ascertain whether the WPA agreement with OPWP contains a lease as per IFRIC 4: Determining Whether an Arrangement contains a Lease, or a service concession arrangement as per IFRIC 12: Service Concession Arrangements. If the agreement contains a lease, judgement is required to classify the lease as an operating lease or a finance lease as per IAS 17: Leases. The lease has been classified as an operating lease.