



JOINT STOCK COMPANY MADNEULI

Consolidated Financial Statements

*For the year ended 31 December 2006
with Report of Independent Auditors*

JOINT STOCK COMPANY MADNEULI

Consolidated Financial Statements

For the Year Ended 31 December 2006

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INDEPENDENT AUDITORS' REPORT

To the Supervisory Board of the JOINT STOCK COMPANY MADNEULI

We have audited the accompanying consolidated financial statements of JOINT STOCK COMPANY MADNEULI (the "Company") and its subsidiaries (collectively referred to herein as the "Group"), which comprise the consolidated balance sheet as at December 31, 2006, and the consolidated statement of income, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and the fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated 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 control. 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 consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Group as of December 31 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



August 16, 2007

JOINT STOCK COMPANY MADNEULI

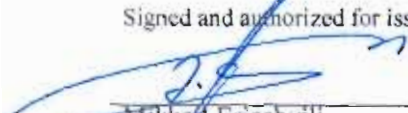
Consolidated Balance Sheet

as at December 31, 2006


(All amounts are in Georgian Laries)

| | Notes | 2006 | 2005 |
|------------------------------------------------------------|-------|--------------------|-------------------|
| ASSETS | | | |
| Non-current assets | | | |
| Property, plant and equipment | 5 | 43,651,387 | 38,239,622 |
| Intangible assets | | 593,829 | 387,257 |
| Prepayments | 6 | 2,975,372 | - |
| Investments in associates | 7 | 18,789,050 | - |
| Deferred tax asset | 13 | 5,285,573 | 4,130,933 |
| | | 71,295,211 | 42,757,812 |
| Current assets | | | |
| Cash and cash equivalents | 8 | 8,259,515 | 2,816,724 |
| Trade receivables | 9 | 12,678,466 | 5,874,646 |
| Prepayments | 6 | 4,050,108 | 883,928 |
| Inventories | 10 | 23,732,563 | 13,603,314 |
| Loan receivable from related party | 4 | 34,929,111 | - |
| Due from associate | 4 | 1,121,137 | 7,465,530 |
| Other current assets | 11 | 10,286,071 | 13,654,101 |
| | | 95,056,971 | 44,298,243 |
| TOTAL ASSETS | | 166,352,182 | 87,056,055 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | |
| Equity attributable to equity holders of the parent | | | |
| Share capital | 19 | 16,037,744 | 16,037,744 |
| Retained earnings | | 82,099,850 | 15,438,878 |
| | | 98,137,594 | 31,476,622 |
| Minority interests | | 513,985 | (228,919) |
| Total shareholders' equity | | 98,651,579 | 31,247,703 |
| Non-current liabilities | | | |
| Rehabilitation provision | 12 | 15,793,928 | 14,570,044 |
| Deferred tax liability | 13 | 7,006,475 | 4,302,155 |
| Other provisions | | 471,397 | 512,966 |
| | | 23,271,800 | 19,385,165 |
| Current liabilities | | | |
| Trade and other payables | 14 | 5,765,358 | 5,122,803 |
| Short-term borrowings | 15 | 15,942,698 | 2,390,543 |
| Advances received | 16 | 12,330,261 | 19,335 |
| Income tax payable | 13 | 4,347,933 | 6,443,598 |
| Other taxes payable | 17 | 2,189,260 | 21,097,580 |
| Payables to related party | 4 | 1,713,500 | - |
| Other current liabilities | 18 | 2,139,793 | 1,349,328 |
| | | 44,428,803 | 36,423,187 |
| Total liabilities | | 67,700,603 | 55,808,352 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | | 166,352,182 | 87,056,055 |

Signed and authorized for issue on behalf of the management of JOINT STOCK COMPANY MADNEULI:


Mikheil Esiashvili
Chief Financial Officer




Koba Nakopia
General Director

August 16, 2007

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

JOINT STOCK COMPANY MADNEULI

Consolidated Statement of Income

for the year ended December 31, 2006

(All amounts are in Georgian Laries)

| | Notes | 2006 | 2005 |
|---------------------------------------------------------------------------|-------|---------------------|-------------------|
| Revenue | | | |
| Sales to third parties | | 132,926,862 | 65,578,486 |
| Sales to associate | 4 | 4,285,762 | 2,400,439 |
| Total revenue | | 137,212,624 | 67,978,925 |
| Cost of sales | 20 | (43,604,020) | (27,868,829) |
| Gross profit | | 93,608,604 | 40,110,096 |
| Operating expenses | | | |
| Selling expenses | 21 | (3,484,951) | (3,229,489) |
| General and administrative expenses | 22 | (24,108,553) | (22,584,956) |
| Other operating expenses | | (1,259,540) | (457,002) |
| Operating profit | | 64,755,560 | 13,838,649 |
| Share of profit of associates | 7 | 18,834,129 | 16,364,567 |
| Currency translation loss | | (1,816,949) | (1,363,630) |
| Interest income | | 1,025,436 | 511,313 |
| Interest expense | | (373,950) | (17,699) |
| Other non-operating income | | 1,338,517 | 1,208,983 |
| Other non-operating expense | | (2,540,287) | (1,747,251) |
| Accretion charge | 12 | (1,223,884) | (1,129,044) |
| Excess of net assets of acquired subsidiaries over the consideration paid | 3 | - | 6,853,557 |
| Profit before tax | | 79,998,572 | 34,519,445 |
| Income tax expense | 13 | (12,594,696) | (9,011,563) |
| Net profit for the year | | 67,403,876 | 25,507,882 |
| Attributable to: | | | |
| Equity shareholders of the parent | | 66,660,972 | 25,567,451 |
| Minority interests | | 742,904 | (59,569) |
| | | 67,403,876 | 25,507,882 |

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

JOINT STOCK COMPANY MADNEULI

Consolidated Statement of Cash Flows

for the year ended December 31, 2006

(All amounts are in Georgian Laries)

| | Notes | 2006 | 2005 |
|---------------------------------------------------------------------------|-------|---------------------|--------------------|
| Operating activities | | | |
| Profit before income tax | | 79,998,572 | 34,519,445 |
| Adjustments to reconcile profit before income tax to net cash flows: | | | |
| Depreciation of property, plant and equipment | 5 | 6,566,702 | 4,657,821 |
| Excess of net assets of acquired subsidiaries over the consideration paid | | - | (6,853,557) |
| Loss on disposal of property, plant and equipment | 5 | 1,034,288 | - |
| Interest income | | (1,025,436) | (511,313) |
| Interest expense | | 373,950 | 17,699 |
| Accretion charge | 12 | 1,223,884 | 1,129,044 |
| Share of profit of associate | 7 | (18,834,129) | (16,364,567) |
| Working capital adjustments: | | | |
| Trade receivables | | (6,803,820) | (5,233,317) |
| Due from associates | | 2,239,632 | - |
| Inventories | | (10,129,249) | (2,909,719) |
| Prepayments | | (3,160,541) | 6,544,858 |
| Other current assets | | 3,368,030 | (1,751,915) |
| Trade and other payables | | (3,729,981) | 2,559,336 |
| Income tax payable | | (627,482) | (303,075) |
| Other taxes payable | | (18,908,320) | (1,949,294) |
| Advances received | | 12,310,926 | (4,341,692) |
| Other current liabilities | | 773,410 | 632,236 |
| Cash generated from operations | | 44,670,436 | 9,841,990 |
| Income tax paid | | (12,513,199) | (1,600,000) |
| Interest paid | | (373,950) | (17,699) |
| Interest received | | 1,645,986 | 94,325 |
| Net cash flows from operating activities | | 33,429,273 | 8,318,616 |
| Investing activities | | | |
| Purchases of property, plant and equipment | | (11,822,164) | (12,881,288) |
| Loan to related party | 4 | (34,270,000) | - |
| Repayment of loan to associate | | 2,819,462 | 413,551 |
| Dividends received from associates | | - | 12,360,255 |
| Investments in associates | | 64,960 | 8,450 |
| Acquisition of subsidiaries, net of cash acquired | 3 | (44,395) | (5,770) |
| Net cash flows used in investing activities | | (43,252,137) | (104,802) |
| Financing activities | | | |
| Proceeds from borrowings from related party | | 1,713,500 | - |
| Proceeds from borrowings | | 13,552,155 | 125 |
| Dividends paid to equity holders of parent | | - | (8,226,221) |
| Net cash from/(used in) financing activities | | 15,265,655 | (8,226,096) |
| Net increase/(decrease) in cash and cash equivalents | | 5,442,791 | (12,282) |
| Cash and cash equivalents at the beginning of year | | 2,816,724 | 2,829,006 |
| Cash and cash equivalents at the end of year | 8 | 8,259,515 | 2,816,724 |

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

JOINT STOCK COMPANY MADNEULI

Consolidated Statement of Changes in Equity

(All amounts are in Georgian Laries, unless otherwise specified)

| | <u>Attributable to equity holders of the parent</u> | | | <u>Minority interests</u> | <u>Total equity</u> |
|-------------------------------------|-----------------------------------------------------|--------------------------|-------------------|---------------------------|---------------------|
| | <u>Share capital</u> | <u>Retained earnings</u> | <u>Total</u> | | |
| Balance at January 1, 2005 | 16,037,744 | (1,902,352) | 14,135,392 | (169,350) | 13,966,042 |
| Net profit for the year | - | 25,567,451 | 25,567,451 | (59,569) | 25,507,882 |
| Dividends declared | - | (8,226,221) | (8,226,221) | - | (8,226,221) |
| Balance at December 31, 2005 | 16,037,744 | 15,438,878 | 31,476,622 | (228,919) | 31,247,703 |
| Net profit for the year | - | 66,660,972 | 66,660,972 | 742,904 | 67,403,876 |
| Balance at December 31, 2006 | 16,037,744 | 82,099,850 | 98,137,594 | 513,985 | 98,651,579 |

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

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements

(All amounts are in Georgian Laries, unless otherwise specified)

1. Corporate information

Joint Stock Company Madneuli (the "Company") was incorporated under the Laws of Georgia on January 31, 1996 where the Government of Georgia owned 97.25% shares and the Company's employees owned remaining 2.75% shares of the Company. The registered office of the Company is Kazreti Settlement, Bolnisi region, Georgia. The Company is licensed for exploration, mining and processing of mineral resources at the Madneuli deposit, within the territory of the Bolnisi region in southern Georgia. The Company's main operations include mining and processing of copper-gold bearing ore. Final products comprise copper-gold concentrate and gold-bearing quartzite.

On November 11, 2005 the Government of Georgia sold all of its shares in the Company to Stanton Equities Corporation ("Stanton") pursuant to the share purchase agreement (the "Agreement"). Stanton is a company organized in British Virgin Islands and 100% owned by Industrial Investors, the independent Russian group established in 1999.

The consolidated financial statements of the Company and of its subsidiaries (collectively referred to as the "Group") for the year ended December 31, 2006 were authorised for issue by the Supervisory Board on August 16, 2007.

2.1. Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for investments and derivative financial instruments that have been measured at fair value. The consolidated financial statements are presented in Georgian Laries ("GEL").

Statement of compliance

The consolidated financial statements of the Company as at December 31, 2006 represent the first complete set of International Financial Reporting Standard ("IFRS") financial statements.

Basis of accounting

The accompanying consolidated financial statements are based on the Company's accounting policies and procedures ("Previous basis of accounting"), with adjustments and reclassifications recorded for the purpose of fair presentation of the Company's financial statements in accordance with IFRS. The principal adjustments relate to consolidation of subsidiaries, business combinations, accounting for investments in associates, expense and revenue recognition, valuation allowances for unrecoverable assets, depreciation and valuation of property plant and equipment, and accounting for income taxes.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its material subsidiaries as at end of each respective year. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognized in assets, are eliminated in full.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.1. Basis of preparation (continued)

Basis of consolidation (continued)

Subsidiaries are those entities in which the Company has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations. Subsidiaries are consolidated from the date on which control is transferred to the Company and are no longer consolidated from the date that control ceases.

Minority interests represent the portion of profit or loss and net assets not held by the Company and are presented separately in the income statement and within equity in the consolidated balance sheet, separately from parent shareholders' equity. Acquisitions of minority interests are accounted for using the parent entity extension method, whereby, the difference between the consideration and the book value of the share of the net assets acquired is recognised as goodwill.

2.2. Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial year because the Company has early adopted those new/revised standards and interpretations mandatory for financial years beginning on or after January 1, 2006 as of January 1, 2005.

The early adoption of below standards effective January 1, 2006 had the significant effect on the disclosures relating to 2005:

- IFRS 6 "Exploration for and Evaluation of Mineral Resources";
- IAS 39 (amended 2005) "Financial Instruments: Recognition and Measurement";
- IFRIC 5 "Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds".

The principal effects of these changes in policies are discussed below.

IFRS 6 "Exploration for and Evaluation of Mineral Resources"

IFRS 6 provides guidance on accounting for exploration and evaluation expenditures, including the recognition of exploration and evaluation assets. The IFRS:

- permitted an entity to develop an accounting policy for exploration and evaluation assets without specifically considering the requirements of paragraphs 11 and 12 of IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors";
- required entities recognising exploration and evaluation assets to perform an impairment test on those assets when facts and circumstances suggest that the carrying amount of the assets may exceed their recoverable amount;
- varied the recognition of impairment from that in IAS 36 "Impairment of Assets" but measured the impairment in accordance with that Standard once the impairment is identified.

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.2. Changes in accounting policies (continued)

IAS 39 (amended 2005) "Financial Instruments: Recognition and Measurement"

The amendment to IAS 39 in 2005:

- required to include financial guarantee contracts issued;
- permitted the foreign currency risk of a highly probable intra-group forecast transaction to qualify as the hedged item in cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the financial statements;
- restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through profit and loss.

IFRIC 5 "Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds"

IFRIC 5 explains how to treat expected reimbursements from funds set up to meet the costs of decommissioning assets or in undertaking environmental restoration or rehabilitation. As the Company does not currently operate in a country where such funds exist, this interpretation has had no impact on the consolidated financial statements.

IFRSs and IFRIC Interpretations not yet effective

The Company has not applied the following IFRSs and IFRIC interpretations applicable to it that have been issued but not yet effective:

- IFRS 7 "Financial Instruments: Disclosures";
- IAS 1 (amended 2005) "Presentation of Financial Statements – Capital Disclosures";
- IFRIC 8 "Scope of IFRS 2";
- IFRIC 9 "Reassessment of Embedded Derivatives".

IFRS 7 "Financial Instruments: Disclosures" replaces the disclosure requirements of IAS 32 "Financial Instruments: Presentation" and must be applied for annual reporting periods that commence on or after January 1, 2007.

The amendment of IAS 1 "Presentation of Financial Statements – Capital Disclosures" requires disclosures regarding an entity's objectives, policies and processes for managing capital. The provisions are effective for reporting periods beginning on or after January 1, 2007.

IFRIC 8 clarifies that IFRS 2 applies to arrangements where an entity makes share-based payments for apparently nil or inadequate consideration. If the identifiable consideration given appears to be less than the fair value of the equity instrument granted, under IFRIC 8 this situation typically indicates that other consideration has been or will be received. IFRS 2 therefore applies. IFRIC 8 becomes effective for financial years beginning on or after May 1, 2006.

IFRIC 9 provides that an entity shall assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. IFRIC 9 becomes effective for financial years beginning on or after June 1, 2006.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.2. Changes in accounting policies (continued)

The Company expects that the adoption of the pronouncements listed above will have no significant impact on the Company's result of operation and financial positions in the period of initial application. The adoption of IFRS 7 will significantly affect the disclosures relating to financial instruments as presented in the notes to the financial statements.

2.3. Significant accounting judgments, estimates and assumptions

Judgments

In the process of applying the Company's accounting policies, management has made the following judgments, apart from those involving estimations, which has the most significant effect on the amounts recognised in the consolidated financial statements:

Determination of material subsidiaries

As mentioned in the principles of consolidation section above, only material subsidiaries are consolidated into the Company's consolidated financial statements. Management determined that immaterial and dormant subsidiaries should not be included in the consolidated financial statements of the Company.

Natural resources taxes associated with quartzite-containing stockpiles

The Company possesses certain quantities of quartzite-containing ore that was initially stockpiled as waste, but subsequently was deemed suitable to be sold as raw material to one of its associates. Natural resources tax arises at the time of extraction of the ore, and management believes that natural resource tax was not applicable at the time the ore was extracted. However, the tax is conservatively accrued and paid at the time when actual sales take place because only then can the taxable quantities of non-ferrous metals be determined reliably.

Deferred tax assets

Management judgment is required for the calculation of current and deferred income taxes. Deferred tax assets are recognized to the extent that their utilization is probable. The utilization of deferred tax assets will depend on whether it is possible to generate sufficient taxable income in respective tax type and jurisdiction. Various factors are used to assess the probability of the future utilization of deferred tax assets, including past operating results, operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that the assessment of future utilization of deferred tax assets must be reduced and this reduction be recognized in profit or loss.

Estimates and assumptions

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the accompanying notes to the financial statements. On an on-going basis, management evaluates their estimates, including those related to contingencies. Management bases their estimates on various market specific assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making assumptions about the carrying values of assets that are not readily apparent from other sources. Actual results may differ significantly from these estimates under different assumptions or conditions.

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.3. Significant accounting judgments, estimates and assumptions (continued)

Estimates and assumptions (continued)

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet 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 discussed below.

Revenue

Due to the specificity of commodity sales contracts, sales prices are determined at future market quotations over the period of three to six months, and the quantities of contained metals are determined by independent assayers and are often not immediately available. Therefore, when there are unsettled sales transactions at the end of each respective year, the Company has made reasonable estimations of unsettled sales transactions based on the quoted futures prices for commodity contracts with similar maturity profile, and has estimated the quantities in own technical laboratory.

Useful life of property, plant and equipment

The Company assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognized in profit or loss.

Impairment of property, plant and equipment

The Company assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Company makes an estimate of the asset's recoverable amount. An asset's recoverable amount is higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. 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 assessment of the time value of money and the risks specific to the assets.

The determination of impairments of property, plant and equipment involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a great number of factors, such as changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists. The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods, which require the Company to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the fair value and ultimately the amount of any property, plant and equipment impairment.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.3. Significant accounting judgments, estimates and assumptions (continued)

Reserve estimates

Estimates of recoverable quantities of indicated and inferred mineral reserves reported include judgemental assumptions regarding commodity prices, exchange rates, discount rates and production and transportation costs for future cash flows. It also requires interpretation of complex and difficult geological and geophysical models in order to make an assessment of the size, shape, depth and quality of reservoirs, and their anticipated recoveries. The economic, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact asset carrying values, the rehabilitation provision and the recognition of deferred tax assets, due to changes in expected future cash flows. Reserves are integral to the amount of depreciation, depletion and amortisation charged to the consolidated statement of income and the calculation of inventory.

Rehabilitation provision

The Company reviews the rehabilitation provision at each balance sheet date, and adjusts it to reflect the current best estimate in accordance with IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities". The amount recognized as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Considerable judgment is required in forecasting future site restoration costs. Future events that may affect the amount required to settle an obligation are reflected in the amount of a provision where there is sufficient objective evidence that they will occur.

Litigations

The Company exercises considerable judgment in measuring and recognizing provisions and the exposure to contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the final settlement. Because of the inherent uncertainties in this evaluation process, actual losses may be different from the originally estimated provision. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists, if available, or with the support of outside consultants, such as actuaries or legal counsel. Revisions to the estimates may significantly affect future operating results.

Current taxes

Georgian tax, currency and customs legislation is subject to varying interpretations and changes occurring frequently. Estimates and assumptions made by management in respect of taxes are more fully described in the Note 24.

2.4. Summary of significant accounting policies

Foreign currency transactions

The consolidated financial statements are presented in GEL, which is the Company's functional and presentation currency. Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to profit or loss.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Foreign currency transactions (continued)

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

GEL is not a fully convertible currency outside the territory of Georgia. Within the Georgia, official exchange rates are determined daily by the National Bank of Georgia and are generally considered to be a reasonable approximation of market rates. As at December 31, 2006 the official exchange rate was GEL 1.7925 for one US Dollar ("USD") (as at December 31, 2005 - GEL 1.7135 for one USD). Transactions denominated in foreign currencies are recorded at the official exchange rate on the date of the transaction. At August 16, 2007 the exchange rate was GEL 1.766 for one USD.

Property, plant and equipment

The Company elected to measure property, plant and equipment at the date of transition to IFRS, e.g. January 1, 2005, at their fair value and use that fair value as their deemed cost at that date.

Subsequent to the date of transition to IFRS, property, plant and equipment are recorded at purchase or construction cost, excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. Such cost includes the cost of replacing part of plant and equipment when that cost is incurred if the recognition criteria are met.

Depreciation is calculated on a straight-line basis for common and support property, plant and equipment. Unit-of-production basis of depreciation is calculated for specialized equipment, capitalized acquisition and mine development costs. There were no specialized equipment, capitalized acquisition and mine development costs at each respective balance sheet date. The depreciation periods which represent the estimated useful economic lives of the respective assets depreciated on a straight-line basis are as follows:

| | <u>Number of years</u> |
|----------------------------------|------------------------|
| Buildings | 5-20 |
| Plant and machinery | 2-20 |
| Equipment and motor vehicles | 2-5 |
| Dam and road | 7-8 |
| Capitalized rehabilitation costs | 9 |
| Other | 7-8 |

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised, and the assets replaced are retired. Gains and losses arising from the retirement of property, plant and equipment are included in the consolidated income statement as incurred.

When each major inspection is performed, its cost is recognised as a component in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

The Company includes in its property plant and equipment the rehabilitation provision more fully described later in this note.

2.4. Summary of significant accounting policies (continued)

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is reflected in the income statement in the year in which the expenditure is incurred.

The useful lives of intangible assets are assessed to be either finite or indefinite. The Company has no intangible assets with indefinite useful lives.

Intangible assets with finite lives are amortised 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 each financial year end. 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 treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible asset.

Acquisition of subsidiaries

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Company. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest.

The excess of purchase consideration over the fair value of the Company's share of identifiable net assets is recorded as goodwill. If the cost of the acquisition is less than the fair value of the Company's share of identifiable net assets of the subsidiary acquired the difference is recognized directly in the income statement.

Investments in associates

Associates are entities in which the Company generally has between 20% and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognised at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Company's share of net assets of the associate. The Company's share of its associates' profits or losses is recognised in the consolidated statement of income, and its share of movements in reserves is recognised in equity. However, when the Company's share of losses in an associate equals or exceeds its interest in the associate, the Company does not recognise further losses, unless the Company is obliged to make further payments to, or on behalf of, the associate.

When an associate makes dividend distributions to the Company in excess of the Company's carrying amount, the excess is recognised in net profit for the period. When the associate subsequently returns to profitability, the Company only recognises profits when profits exceed the excess cash distributions recognised in net profit plus any previously unrecognised losses.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Investments in associates (continued)

Unrealised gains on transactions between the Company and its associates are eliminated to the extent of the Company's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

After application of the equity method, the Company determines whether it is necessary to recognise an additional impairment loss of the Company's investment in its associates. The Company determines at each balance sheet date whether there is any objective evidence that the investment in associate is impaired. If this is the case the Company calculates the amount of impairment as being the difference between the fair value of the associate and the acquisition cost and recognises the amount in the income statement.

The reporting dates of the associate and the Company are identical and the associate's accounting policies conform to those used by the Company for like transactions and events in similar circumstances.

Impairment of assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that an asset or a group of assets may be impaired. When indication that an asset may be impaired is evidenced, the asset is measured at its estimated recoverable amount, which is the higher of net selling price or value in use.

Net selling price is the amount obtainable from the sale of an asset in an arms' length transaction between knowledgeable, willing parties, after deducting any direct incremental disposal costs. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. 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.

For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised for the difference between the estimated recoverable amount and the carrying value and is included in the net profit or loss for the period.

An impairment loss is reversed if the subsequent increase in the recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. An impairment loss is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

Borrowings

Borrowings are initially recognised at fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortised cost using the effective interest method; any difference between the initial fair value of the consideration received (net of transaction costs) and the redemption amount is recognised as an adjustment to interest expense over the period of the borrowings.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Fair value of financial instruments

The Company believes the amounts presented as financial instruments in the accompanying consolidated financial statements, consisting of cash and cash equivalents, trade and other accounts receivable, prepayments, VAT recoverable, trade and other accounts payable, short-term loans, and amounts due from/to related parties are reasonable estimates of their fair-value.

The fair value of cash and cash equivalents, accounts receivable and payable and other monetary current assets and liabilities is estimated to approximate carrying value due to their short-term nature.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, gains and losses relating to a financial instrument classified as a liability are reported as expense or income.

Embedded derivatives

Derivatives embedded in the Company's contracts that change the nature of a host contract's risk and are not clearly and closely related to the host contract, are initially recognised at fair value on the date the contract is entered into, with movements reported in the consolidated statement of income.

Natural resource taxes

Natural resources taxes under existing regimes are considered to be production-based taxes and are therefore accrued on the basis of the Company's entitlement to physical production.

Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises raw material, direct labour, other direct costs and related production overheads (based on normal operating capacity) but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

Trade receivables

Trade receivables, which generally have a short term, are carried at original invoice amount less an allowance for any uncollectible amounts. Allowance is made when there is objective evidence that the Company will not be able to collect the debts. Change in the provision is recognised through the consolidated statement of income.

Cash and cash equivalents

Cash and short term deposits in the balance sheet comprise cash at banks and at hand and short term deposits with an original maturity of three months or less. For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Employee benefits

In accordance with the Law on Social Insurance of Georgia, the Company is obligated to contribute to the State Social Protection Fund of Georgia on behalf of its employees that are citizens of Georgia. The Company's contributions represented 20% of the employees' salaries reflected in the statutory records in 2006 and 2005, respectively.

The Company does not have any post-employment compensation plans.

Trade payables and advances received from customers

Trade payables are carried at cost, which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Company.

Advances received from customers represent prepayments for the Company's produce.

Provisions

General

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

Rehabilitation provision

The rehabilitation costs arose on developing an open pit mine in the license area. A corresponding asset is recognised in property, plant and equipment. Rehabilitation costs are provided at the present value of expected costs to settle the obligation using estimated cash flows. The cash flows are discounted at a current pre tax rate that reflects the available borrowing rate. The unwinding of the discount is expensed as incurred and recognised in the income statement as a finance cost. The estimated future costs of rehabilitation are reviewed annually and adjusted as appropriate. Changes in the estimated future costs or in the discount rate applied are added to or deducted from the cost of the asset.

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and other sales taxes or duty. The following specific recognition criteria must also be met before revenue is recognised:

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Revenue recognition (continued)

Sale of goods

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on dispatch of the goods, using the spot price at the time of shipment for the measurement of the revenue. The final prices are determined by London Metal Exchange ("LME") and London Bullion Market Association ("LBMA") settlement quotations averaged over the quotation period that is usually three to five months following the month of shipment. The price adjustment feature is an embedded derivative that is remeasured to fair value with changes recognised through the statement of income.

Interest income

Revenue is recognised as interest accrues (using the effective interest method that is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

Dividends

Revenue is recognised when the Company's right to receive the payment is established.

Income taxes

Deferred income tax is provided, using the liability method, on all temporary differences at each respective balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred income tax liability arises from goodwill amortisation or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carry-forward of unused tax assets and unused tax losses can be utilised, except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Income taxes (continued)

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at each balance sheet date.

Value added tax

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

Value added tax payable

VAT is payable to tax authorities upon collection of receivables from customers. VAT on purchases, which have been settled at the balance sheet date, is deducted from the amount payable.

In addition, VAT related to sales which have not been collected at the balance sheet date is also included in the balance of VAT payable. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT. The related VAT liability is maintained until the debtor is written off for tax purposes.

Value added tax receivable

VAT receivable relates to purchases, which have not been settled at the balance sheet date. VAT receivable is reclaimable against VAT related to sales upon payment for the purchases.

Equity

Share capital

Ordinary shares with discretionary dividends are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as a share premium.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

2.4. Summary of significant accounting policies (continued)

Equity (continued)

Minority interest

Minority interest represents the interest in subsidiaries not held by the Company. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair value of the identifiable assets and liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented within the shareholders' equity.

Losses allocated to minority interest do not exceed the minority interest in the equity of the subsidiary unless there is a binding obligation of the minority to fund the losses. All such losses are allocated to the Company.

Dividend

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

Related party disclosures

For the purposes of IFRS financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

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 arms' length basis.

3. Business combinations

Acquisitions in 2006

Ecology LLC

In October 2006 the Company acquired the remaining 49% of interest in Ecology LLC, a company involved in cleaning, purifying and extracting heavy metals from the open pit waters of Madneuli mining complex. The Company owned 51% of interest from the establishment of Ecology LLC on September 11, 1996.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

3. Business combinations (continued)

Acquisitions in 2006 (continued)

Ecology LLC (continued)

The fair value of identifiable assets and liabilities of Ecology LLC as at the date of acquisition were:

| | |
|---------------------------------------------------------------------------|----------------|
| Property, plant and equipment | 26,831 |
| Intangible assets | 19,297 |
| Cash and cash equivalents | 20,565 |
| Trade and other receivables | 495,680 |
| | 562,373 |
| Trade and other payables | 429,802 |
| | 429,802 |
| Fair value of net assets | 132,571 |
| Less: previously acquired interest | (67,611) |
| Company's share of the fair value of net assets | 64,960 |
| Excess of net assets of acquired subsidiaries over the consideration paid | - |
| Consideration paid | 64,960 |

The total cost of the combination was GEL 64,960 and was paid entirely in cash. The net cash outflow on acquisition was as follows:

| | |
|-----------------------------------------|---------------|
| Cash paid | 64,960 |
| Less: cash acquired with the subsidiary | (20,565) |
| Net cash outflow | 44,395 |

From the date of the combination, Ecology LLC did not contribute to the net profit of the Company because all sales were made to the Company.

Georgian Lime Plus LTD

On December 20, 2006, the Company contributed 50% of interest in Georgian Lime Plus LTD, a company specialising in extraction and production of lime.

As Georgian Lime Plus LTD was only established at the end of 2006, there was no difference between the acquisition cost to the Company and the Company's share in Georgian Lime Plus LTD's net assets. The total cost of the combination was GEL 1,000 and was paid entirely in cash.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

3. Business combinations (continued)

Acquisitions in 2005

In March 2005 the Company acquired 100% of interest in Belaz Kavkaz Trans Service LLC ("Belaz"), a company specialising in the open-pit hauling services; 100% of interest in Gardi LLC, a company specialising in the open-pit hauling services; and 100% of interest in Trans Petg Mzidi LLC ("TFM"), a company specialising in the open-pit drilling, blasting and excavation services.

The excess of the fair value of Belaz, Gardi LLC and TFM's net assets over the consideration paid by the Company (negative goodwill) was recognised directly in the consolidated statement of income.

From the date of the combination, Belaz, Gardi LLC and TFM did not contribute to the net profit of the Company because all services were provided to the Company.

The fair value of identifiable assets and liabilities of Belaz, Gardi LLC and TFM as at the date of acquisition were:

| | Belaz | Gardi LLC | TFM | Total |
|---------------------------------------------------------------------------|------------------|------------------|-------------------|-------------------|
| Property, plant and equipment | 2,218,239 | 2,779,190 | 10,550,728 | 15,548,157 |
| Cash and cash equivalents | 349 | 1 | 330 | 680 |
| Trade and other receivables | 482,766 | 369 | 645,460 | 1,128,595 |
| Inventories | 213,051 | 3,635 | 455,013 | 671,699 |
| | 2,914,405 | 2,783,195 | 11,651,531 | 17,349,131 |
| Trade and other payables | 2,192,135 | 982,181 | 7,314,808 | 10,489,124 |
| | 2,192,135 | 982,181 | 7,314,808 | 10,489,124 |
| Fair value of net assets | 722,270 | 1,801,014 | 4,336,723 | 6,860,007 |
| Less: minority interests | - | - | - | - |
| Company's share of the fair value of net assets | 722,270 | 1,801,014 | 4,336,723 | 6,860,007 |
| Excess of net assets of acquired subsidiaries over the consideration paid | 720,270 | 1,798,664 | 4,334,623 | 6,853,557 |
| Consideration paid | 2,000 | 2,350 | 2,100 | 6,450 |
| Less: cash acquired with the subsidiary | (349) | (1) | (330) | (680) |
| Net cash outflow | 1,651 | 2,349 | 1,770 | 5,770 |

4. Balances and transactions with related parties

The consolidated financial statements include the financial statements of JSC Madneuli and its subsidiaries/associates listed in the following table:

| Name | % equity interest at | |
|--------------------------------|----------------------|------|
| | 2006 | 2005 |
| <i>Subsidiaries:</i> | | |
| Gardi LLC | 100% | 100% |
| Belaz Kavkaz Trans Service LLC | 100% | 100% |
| Trans Petg Mzidi LLC | 100% | 100% |
| Georgian Mining Company LLC | 100% | 100% |
| Ecology LLC | 100% | 51% |
| <i>Associates:</i> | | |
| Quartzite LTD | 50% | 50% |
| Georgian Lime Plus LTD | 50% | 0% |

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

4. Balances and transactions with related parties (continued)

Transactions with Quartzite LTD

The Company sells stockpile quartzite ore to its 50%-owned associate, Quartzite LTD. In 2006, sales to associate represented 1,766,727 metric tons of quartzite ore amounting to GEL 4,285,762 supplied to Quartzite LTD (2005: 2,025,736 metric tons amounting to GEL 2,400,439).

Accounts receivable due from associates as at December 31, 2006 consists of GEL 634,684 receivable for quartzite ore supplied, GEL 476,598 of unpaid interest on previously settled intercompany loan from the Company, and GEL 9,855 of other current assets (2005: GEL 1,683,671 receivable for quartzite ore supplied, GEL 3,974,477 of intercompany loans receivable, GEL 1,761,897 of unpaid interest, and GEL 45,485 of other current assets).

Transactions with Stanton

In 2006 the Company gave a short-term loan to its ultimate parent, Stanton, in the amount of GEL 34,270,000, bearing an interest of 13.5% per annum which was due as of December 31, 2006 and expires on May 8, 2007. The interest income for 2006 was GEL 659,111.

Transactions with other related parties

In 2006 the Company also borrowed GEL 1,713,500 from related party, Cuento Portfolio Corp, bearing 10% interest. The interest expense for 2006 was GEL 373,950.

Business combination

The Company acquired controlling interest in a number of related companies in 2006 and 2005. Also, the Company acquired a non-controlling interest in an associate. These transactions are detailed in Note 3.

Compensation to key management personnel

Key management personnel comprise members of the Management Board and the Board of Directors of the Company, totalling nine persons as at December 31, 2006 (2005: fourteen). Total compensation to key management personnel included in general and administrative expenses in the consolidated statement of income amounted to GEL 1,330,444 for the year ended December 31, 2006 (2005: GEL 568,967).

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

5. Property, plant and equipment

Property, plant and equipment comprised of the following:

| Cost/deemed cost: | Land and Buildings | Plant and machinery | Equipment and motor vehicles | Dam and road | Capitalised rehabilitation provision | Other | Total |
|----------------------------------|--------------------|---------------------|------------------------------|------------------|--------------------------------------|----------------|-------------------|
| As at January 1, 2005 | 1,344,302 | 7,868,753 | 623,990 | - | 13,441,000 | 24,099 | 23,302,144 |
| Additions | 24,646 | 1,607,652 | 352,632 | - | - | 223,602 | 2,208,532 |
| Acquisitions of a subsidiary | - | 17,309,891 | 76,876 | - | - | - | 17,386,767 |
| As at December 31, 2005 | 1,368,948 | 26,786,296 | 1,053,498 | - | 13,441,000 | 247,701 | 42,897,443 |
| Additions | 307,884 | 8,572,749 | 1,248,468 | 1,875,628 | - | 1,008,026 | 13,012,755 |
| Disposals | (86,623) | (789,072) | (89,462) | - | - | (702,233) | (1,667,390) |
| As at December 31, 2006 | 1,590,209 | 34,569,973 | 2,212,504 | 1,875,628 | 13,441,000 | 553,494 | 54,242,808 |
| Accumulated depreciation: | | | | | | | |
| As at January 1, 2005 | - | - | - | - | - | - | - |
| Charge for the year | 115 | 2,966,583 | 169,022 | - | 1,493,444 | 28,657 | 4,657,821 |
| As at December 31, 2005 | 115 | 2,966,583 | 169,022 | - | 1,493,444 | 28,657 | 4,657,821 |
| Charge for the year | 40,125 | 4,290,298 | 345,102 | 243,832 | 1,493,444 | 153,901 | 6,566,702 |
| Disposals | (11,261) | (518,496) | (103,345) | - | - | - | (633,102) |
| As at December 31, 2006 | 28,979 | 6,738,385 | 410,779 | 243,832 | 2,986,888 | 182,558 | 10,591,421 |
| Net Book Value: | | | | | | | |
| As at December 31, 2006 | 1,561,230 | 27,831,588 | 1,801,725 | 1,631,796 | 10,454,112 | 370,936 | 43,651,387 |
| As at December 31, 2005 | 1,368,833 | 23,819,713 | 884,476 | - | 11,947,556 | 219,044 | 38,239,622 |

As permitted by IFRS 1, the Company estimated the fair value of the property, plant and equipment as at January 1, 2005 of the Company and its material subsidiaries, and used that basis as deemed cost (except Ecology LLC, which did not have significant property, plant and equipment). Fair value was determined by reference to market-based evidence, which is the amount for which the assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arms' length transaction as at the valuation date. The excess of fair value over the net book value of GEL 3,124,618 as a result of revaluation of property, plant and equipment was charged to equity as at January 1, 2005.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

6. Prepayments

Prepayments as at December 31, 2006 consist of current prepayments totalling GEL 4,050,108 (2005: GEL 883,928) representing advances paid to materials and services suppliers, and non-current prepayments totalling GEL 2,975,372 (2005: nil) representing prepayments for purchases of equipment.

7. Investments in associates

The Company's principle associates are listed in Note 4. The movements in investment in associate were as follows:

| | 2006 | 2005 |
|------------------------------------------------------------------------------|-------------------|--------------|
| Investment in associates | | |
| Balance as at January 1 | - | 21,385,835 |
| Share of profit of associate | 18,834,129 | 10,305,206 |
| Excess of dividends distribution over the share of associates results | - | 6,059,361 |
| Elimination of unrealized gains on intercompany sales | (45,079) | (65,647) |
| Amounts charged directly to associates' equity (dividends declared and paid) | - | (37,684,755) |
| Balance as at December 31 | 18,789,050 | - |

The following table illustrates summarised financial information of Quartzite LTD, the Company's most significant associate, as at December 31:

| | 2006 | 2005 |
|------------------------------------------------|--------------------|--------------|
| Aggregated assets and liabilities of associate | | |
| Current assets | 32,306,704 | 35,064,230 |
| Non-current assets | 24,276,291 | 17,470,392 |
| Current liabilities | (22,038,583) | (56,778,770) |
| Non-current liabilities | (3,938,394) | (2,818,092) |
| Net assets | 30,606,018 | (7,062,240) |
| Aggregated revenue and profit of associate | | |
| Revenue | 85,932,410 | 56,763,593 |
| Profit | 37,668,258 | 20,610,412 |

8. Cash and cash equivalents

Cash and cash equivalents were denominated in the following currencies as at December 31:

| | 2006 | 2005 |
|---------------|------------------|-----------|
| Georgian Lari | 163,340 | 139,893 |
| US Dollars | 8,096,175 | 2,676,831 |
| | 8,259,515 | 2,816,724 |

The above cash and cash equivalents mainly consist of cash at banks.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

8. Cash and cash equivalents (continued)

Included in cash and cash equivalents as at December 31, 2006 is restricted deposit at bank representing an escrow account of GEL 8,060,500 opened on December 28, 2006 to secure an acquisition of a new entity. The restriction was released subsequent to year-end due to cancellation of the transaction.

9. Trade receivables

Trade receivables as at December 31, 2006 mainly represent amounts due from customers for the sales that are pending the determination of final invoice amount at the end of each respective quotation period ranging from one to four months from year-end (2005: three months). Sales terms specify that 90% of the preliminary balance is to be paid upon shipment, and the remainder to be settled based on the final prices determined at the end of the specified quotation periods. The receivables are adjusted on December 31 of each respective year to futures prices.

10. Inventories

inventories consist of the following as at December 31:

| | <u>2006</u> | <u>2005</u> |
|------------------------------------------|-------------------|-------------------|
| Raw materials (at cost) | 12,000,612 | 2,457,463 |
| Work in progress (at cost) | 927,769 | 442,619 |
| Finished goods (at net realisable value) | <u>10,804,182</u> | <u>10,703,232</u> |
| | <u>23,732,563</u> | <u>13,603,314</u> |

11. Other current assets

Other current assets comprised of VAT receivable totalling GEL 10,002,336 and prepayments for other taxes totalling GEL 283,735 as at December 31, 2006 (2005: GEL 13,654,101 and nil, respectively). VAT receivable represents amounts payable or paid to suppliers which is recoverable from the tax authorities via offset against VAT payable to the tax authorities on the Company's revenue or against other tax liabilities. Management periodically reviews the recoverability of the balance of VAT.

12. Rehabilitation provision

The capitalised rehabilitation provision represents the costs of restoring site damage. The Company made necessary assessment for determination of rehabilitation costs and established detailed reclamation plan. The provision for undiscounted costs of land rehabilitation comprised GEL 27,777,768 at each respective balance sheet date. Based on the best estimate of future costs and the economic lives of the facilities the Company calculated a net present value of the rehabilitation provision by using the average market borrowing rate of 14%. As a result, discounted rehabilitation provision was GEL 15,793,928 as at December 31, 2006 and GEL 14,570,044 as at December 31, 2005. The accretion charge for the year ended December 31, 2006 and December 31, 2005 was GEL 1,223,884 and GEL 1,129,044, respectively. These expenses are expected to be incurred at the end of the next eight years.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

13. Income tax

Income tax expense consisted of the following for the year ended December 31:

| | 2006 | 2005 |
|--------------------------------|-------------------|------------------|
| Income tax expense | 10,601,397 | 9,532,641 |
| Deferred tax expense/(benefit) | 1,993,299 | (521,078) |
| Income tax expense | 12,594,696 | 9,011,563 |

The Company was subject to income tax of 20% in 2006 and 2005 on taxable income as determined under the laws of Georgia. Georgia was the only tax jurisdiction in which the Company's income was subject to taxation.

The Company recognized deferred tax asset which was mainly due to temporary differences between rehabilitation provision and investment in associates balances per IFRS and tax records. Management believes that the Company will generate sufficient profits in future periods to utilize its deferred tax asset in accordance with IAS 12.

The Company recognized deferred tax liability which was mainly due to temporary differences between fixed assets balances per IFRS and tax records. Management believes that the Company will generate enough profit in future periods to utilize its deferred tax asset in accordance with IAS 12.

The following is a reconciliation of the income tax expense to the amount that would arise by applying 20% to the profit before income taxes reported in the accompanying consolidated financial statements for the year ended December 31:

| | 2006 | 2005 |
|------------------------------------------------------------------------------------|--------------------|------------------|
| Profit before income tax | 79,998,572 | 34,519,445 |
| Statutory tax rate | 20% | 20% |
| Income tax expense at enacted statutory rate | 15,999,714 | 6,903,889 |
| Tax effect of items which were not deductible or assessable for taxation purposes: | | |
| Non-deductible expenses | 361,808 | 2,423,016 |
| Non-taxable income from associates | (3,766,826) | (315,342) |
| Income tax expense reported in the statement of income | 12,594,696 | 9,011,563 |

Deferred income tax assets and liabilities related to the following as at December 31:

| | 2006 | 2005 |
|----------------------------------|--------------------|--------------------|
| Deferred income tax liabilities: | | |
| Property, plant and equipment | (5,912,708) | (3,441,755) |
| Long term loans | (1,093,767) | (860,400) |
| Deferred tax liabilities | (7,006,475) | (4,302,155) |
| Deferred income tax assets: | | |
| Inventories | 801,366 | 717,584 |
| Rehabilitation provision | 3,158,786 | 2,914,009 |
| Other taxes payable | 475,000 | 475,000 |
| Trade and other payables | 850,421 | 24,340 |
| Deferred tax assets | 5,285,573 | 4,130,933 |

The Company's income tax liabilities were GEL 4,347,933 as at December 31, 2006 (2005: GEL 6,443,598).

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

14. Trade and other payables

Trade and other payables as at December 31, 2006 and 2005 represent the amounts owed to suppliers of fuel, spare parts and equipment.

15. Short-term borrowings

Short-term borrowings are comprised of the following as at December 31:

| | Effective interest rate % | Maturity | 2006 | 2005 |
|----------------------|------------------------------|---------------|-------------------|------------------|
| Bank of Georgia | 13%-13.5% | November 2007 | 12,687,280 | 125 |
| United Georgian Bank | - | March 2005 | 2,390,418 | 2,390,418 |
| TBC Bank overdraft | 14% | January 2007 | 865,000 | - |
| | | | 15,942,698 | 2,390,543 |

The Company's 50% interest in Quartzite LTD was pledged under the terms of loan agreements signed with the Bank of Georgia.

According to the court resolution, the liability to United Georgian bank was fixed at GEL 2,390,418, including interest, and was payable by March 2005. Negotiations regarding the settlement of this debt are in progress.

The Company has not entered into any hedging arrangements in respect of its foreign currency obligations or interest rate exposures.

All the borrowings bear fixed interest rate.

The carrying amounts of the Company's short-term borrowings are denominated in the following currencies as at December 31:

| | 2006 | 2005 |
|---------------|-------------------|------------------|
| Georgian Lari | 3,255,418 | 2,390,543 |
| US Dollars | 12,687,280 | - |
| | 15,942,698 | 2,390,543 |

16. Advances received

Advances received as at December 31, 2006 of GEL 12,330,261 represent prepayments made by customers. Sales terms specify that 90% of the preliminary balance is to be paid upon shipment, and the remainder to be settled based on the final prices determined at the end of the specified quotation periods. The drop in market prices between 2006 and periods subsequent to December 31, 2006 resulted in the Company's refunding to the buyer the excess part of the provisional payment, recognized as liability - advances received. Advances received balance as at December 31, 2005 totalling GEL 19,335 is minor due to increasing cooper concentrate prices between 2005 and 2006.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

17. Other taxes payable

Other taxes payable are comprised of the following as at December 31:

| | 2006 | 2005 |
|----------------------|------------------|-------------------|
| Natural resource tax | 747,276 | 11,453,351 |
| Social tax | 302,542 | 6,391,888 |
| Personal income tax | 238,194 | 985,141 |
| VAT | 503,939 | - |
| Other taxes | 397,309 | 2,267,200 |
| | <u>2,189,260</u> | <u>21,097,580</u> |

During the years prior to November 11, 2005, the date of signing the Agreement, the Company had certain disputed tax liabilities. The Company accrued for all its liabilities for taxes as part of the agreement between Stanton and the government of Georgia. According to this agreement the total tax liabilities of GEL 20,272,200 were settled by December 31, 2006.

18. Other current liabilities

| | 2006 | 2005 |
|---------------------------|------------------|------------------|
| Due to employees | 314,566 | 135,929 |
| Due to injured persons | 135,263 | 156,273 |
| Accrued liabilities | 553,939 | 228,593 |
| Salaries | 657,489 | 346,808 |
| Other current liabilities | 478,536 | 481,725 |
| | <u>2,139,793</u> | <u>1,349,328</u> |

Dues to injured persons include the Company's obligation to pay lifetime compensation to employees or their family who suffered a severe injury or death as a result of their employment. The obligation was estimated using statistical average life expectancy in Georgia and the fixed compensation level for each injured employee as established by management's one-off decision to grant such a benefit, discounted using the average market borrowing rate of 14%. The non-current portion of this obligation amounts to GEL 471,397 as of December 31, 2006 (2005: GEL 512,966).

19. Equity

Share capital

The authorised number of ordinary shares of the Company is 12,830,195, with a nominal value per share of USD 1 (GEL equivalent being 16,037,744). All authorised shares have been issued and fully paid as at December 31, 2006 and 2005.

Dividends

A dividend was declared by the Company in 2005 in respect of 2004 to holders of ordinary shares totaling GEL 8,226,221.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

20. Cost of sales

Cost of sales was comprised of the following for the year ended December 31:

| | <u>2006</u> | <u>2005</u> |
|------------------------------------|--------------------------|--------------------------|
| Cost of sales – copper concentrate | 39,938,966 | 27,496,767 |
| Cost of sales – cement copper | 3,080,293 | - |
| Other | 584,761 | 372,062 |
| | <u>43,604,020</u> | <u>27,868,829</u> |

The components of cost of sales comprised of the following for the year ended December 31:

| | <u>2006</u> | <u>2005</u> |
|-------------------------------|--------------------------|--------------------------|
| Materials and components | 24,651,507 | 16,758,186 |
| Production overheads | 7,321,029 | 847,792 |
| Labour costs | 7,334,981 | 6,400,891 |
| Depreciation and amortization | <u>4,296,503</u> | <u>3,861,960</u> |
| | <u>43,604,020</u> | <u>27,868,829</u> |

21. Selling expenses

Selling expenses comprised of the following for the year ended December 31:

| | <u>2006</u> | <u>2005</u> |
|-------------------------------|-------------------------|-------------------------|
| Transportation and storage | 2,402,615 | 2,226,493 |
| Materials | 552,552 | 512,048 |
| Labour | 229,574 | 212,745 |
| Depreciation and amortization | 70,830 | 65,638 |
| Other | 229,380 | 212,565 |
| | <u>3,484,951</u> | <u>3,229,489</u> |

22. General and administrative expenses

General and administrative expenses comprised of the following for the year ended December 31:

| | <u>2006</u> | <u>2005</u> |
|---------------------------------------------------|--------------------------|--------------------------|
| Taxes other than income tax | 4,418,222 | 2,396,863 |
| Labour costs | 9,500,542 | 6,241,619 |
| Depreciation and amortization expenses | 1,566,267 | 730,223 |
| Materials | 382,466 | 1,784,255 |
| Business travel and other representative expenses | 2,980,560 | 6,268,892 |
| Other | <u>5,260,496</u> | <u>5,163,104</u> |
| | <u>24,108,553</u> | <u>21,584,956</u> |

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

23. Group reconciliation of equity and profit and loss

For all periods up to and including the year ended December 31, 2005, the Company prepared its statutory financial statements in accordance with the Previous basis of accounting. These consolidated financial statements for the year ended December 31, 2006 are the first the Company has prepared in accordance with IFRS.

Accordingly, the Company has prepared consolidated financial statements which comply with IFRS applicable for periods beginning on or after January 1, 2005 as described in the accounting policies. In preparing these consolidated financial statements, the Company opening consolidated balance sheet was prepared as at January 1, 2005, the Company's date of transition to IFRS. This note explains the principal adjustments made by the Company in restating its Previous basis of accounting balance sheet as at January 1, 2005 and its Previous basis of accounting financial statements for the year ended December 31, 2005.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

23. Group reconciliation of equity and profit and loss (continued)

Group reconciliation of equity as at December 31, 2005:

| | Notes | Previous basis of accounting (unaudited) | Remeasurements | IFRS |
|------------------------------------------------------------|-------|------------------------------------------------|--------------------|-------------------|
| ASSETS | | | | |
| Non-current assets | | | | |
| Property, plant and equipment | A | 24,487,689 | 13,751,933 | 38,239,622 |
| Intangible assets | | 387,257 | - | 387,257 |
| Investments in associates | | 50,236 | (50,236) | - |
| Deferred tax asset | B | 2,629,422 | 1,501,511 | 4,130,933 |
| Total non-current assets | | 27,554,604 | 15,203,208 | 42,757,812 |
| Current assets | | | | |
| Cash and cash equivalents | | 2,816,724 | - | 2,816,724 |
| Trade receivables | C | 9,430,504 | (3,555,858) | 5,874,646 |
| Prepayments | | 937,476 | (53,548) | 883,928 |
| Inventories | D | 18,268,436 | (4,665,122) | 13,603,314 |
| Due from associate | C | 2,819,462 | 4,646,068 | 7,465,530 |
| Other current assets | | 15,840,443 | (2,186,342) | 13,654,101 |
| Total current assets | | 50,113,045 | (5,814,802) | 44,298,243 |
| TOTAL ASSETS | | 77,667,649 | 9,388,406 | 87,056,055 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | |
| Equity attributable to equity holders of the parent | | | | |
| Share capital | | 16,037,744 | - | 16,037,744 |
| Retained earnings | E | 22,608,401 | (7,398,442) | 15,209,959 |
| Total shareholders' equity | | 38,646,145 | (7,398,442) | 31,247,703 |
| Non-current liabilities | | | | |
| Rehabilitation provision | F | - | 14,570,044 | 14,570,044 |
| Deferred tax liability | B | - | 4,302,155 | 4,302,155 |
| Long-term loans | K | 6,294,016 | (6,294,016) | - |
| Other provisions | | - | 512,966 | 512,966 |
| Total non-current liabilities | | 6,294,016 | 13,091,149 | 19,385,165 |
| Current liabilities | | | | |
| Trade and other payables | | 4,769,599 | 353,204 | 5,122,803 |
| Short-term borrowings | K | 125 | 2,390,418 | 2,390,543 |
| Advances received | | 19,335 | - | 19,335 |
| Income tax payable | G | 26,881,304 | (20,437,706) | 6,443,598 |
| Other taxes payable | G | - | 21,097,580 | 21,097,580 |
| Other current liabilities | | 1,057,125 | 292,203 | 1,349,328 |
| Total current liabilities | | 32,727,488 | 3,695,699 | 36,423,187 |
| Total liabilities | | 39,021,504 | 16,786,848 | 55,808,352 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | | 77,667,649 | 9,388,406 | 87,056,055 |

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

23. Group reconciliation of equity and profit and loss (continued)

Group reconciliation of profit and loss for the year ended December 31, 2005:

| | Notes | Previous basis of accounting (unaudited) | Remeasurements | IFRS |
|------------------------------------------------------------------------------|-------|------------------------------------------------|--------------------|-------------------|
| Revenue | | | | |
| Sales to third parties | | 64,488,274 | 1,090,212 | 65,578,486 |
| Sales to associate | | 2,565,679 | (165,240) | 2,400,439 |
| Total revenue | | 67,053,953 | 924,972 | 67,978,925 |
| Cost of sales | L | 25,485,132 | 2,383,697 | 27,868,829 |
| Gross profit | | 41,568,821 | (1,458,725) | 40,110,096 |
| Selling expenses | | 3,229,489 | - | 3,229,489 |
| General and administrative expenses | II | 19,812,896 | 2,772,060 | 22,584,956 |
| Other operating expenses | | 457,002 | - | 457,002 |
| Operating profit | | 18,069,434 | (4,230,785) | 13,838,649 |
| Share of profit of associates | C, II | - | 16,364,567 | 16,364,567 |
| Currency translation gain | | (1,363,630) | - | (1,363,630) |
| Interest income | | 631,384 | (120,071) | 511,313 |
| Interest expense | | (17,699) | - | (17,699) |
| Extraordinary loss | M | (12,776,208) | 12,776,208 | - |
| Other non-operating income | C | 26,524,740 | (25,315,757) | 1,208,983 |
| Other non-operating expense | M | (2,263,273) | 516,022 | (1,747,251) |
| Accretion charge | | - | (1,129,044) | (1,129,044) |
| Excess of net assets of acquired subsidiaries over the consideration paid | I | 266,672 | 6,586,885 | 6,853,557 |
| Profit before tax | | 29,071,420 | 5,448,025 | 34,519,445 |
| Income tax expense | B | (8,785,392) | (226,171) | (9,011,563) |
| Net profit for the year | | 20,286,028 | 5,221,854 | 25,507,882 |

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

23. Group reconciliation of equity and profit and loss (continued)

Group reconciliation of equity as at January 1, 2005:

| | Notes | Previous basis of accounting (unaudited) | Remeasurements | IFRS |
|------------------------------------------------------------|-------|------------------------------------------------|---------------------|-------------------|
| ASSETS | | | | |
| Non-current assets | | | | |
| Property, plant and equipment | A | 15,541,443 | 7,760,701 | 23,302,144 |
| Intangible assets | | 247,711 | - | 247,711 |
| Investments in associates | I | 48,236 | 21,337,599 | 21,385,835 |
| Deferred tax asset | B | 3,581,991 | 600,742 | 4,182,733 |
| Total non-current assets | | 19,419,381 | 29,699,042 | 49,118,423 |
| Current assets | | | | |
| Cash and cash equivalents | | 2,829,006 | - | 2,829,006 |
| Trade receivables | C | 8,632,046 | (7,990,717) | 641,329 |
| Prepayments | | 8,097,501 | (668,715) | 7,428,786 |
| Inventories | D | 15,050,113 | (4,356,518) | 10,693,595 |
| Due from associate | C | - | 7,462,093 | 7,462,093 |
| Other current assets | | 14,277,185 | (2,374,999) | 11,902,186 |
| Total current assets | | 48,885,851 | (7,928,856) | 40,956,995 |
| TOTAL ASSETS | | 68,305,232 | 21,770,186 | 90,075,418 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | |
| Equity attributable to equity holders of the parent | | | | |
| Share capital | | 14,828,051 | 1,209,693 | 16,037,744 |
| Retained earnings | E | 11,791,888 | (13,863,590) | (2,071,702) |
| | | 26,619,939 | (12,653,897) | 13,966,042 |
| Non-current liabilities | | | | |
| Rehabilitation provision | F | - | 13,441,000 | 13,441,000 |
| Deferred tax liability | B | - | 2,847,943 | 2,847,943 |
| Long-term borrowings | K | 4,380,000 | (4,380,000) | - |
| Other provisions | | 133,488 | 431,991 | 565,479 |
| Total non-current liabilities | | 4,513,488 | 12,340,934 | 16,854,422 |
| Current liabilities | | | | |
| Trade and other payables | | 2,563,467 | - | 2,563,467 |
| Short-term borrowings | K | 1,992,016 | 398,402 | 2,390,418 |
| Advances received | I | 14,620,369 | (10,259,342) | 4,361,027 |
| Income tax payable | G | 17,444,075 | (16,602,953) | 841,122 |
| Other taxes payable | G | - | 23,046,874 | 23,046,874 |
| Payables to associates | I | - | 25,324,500 | 25,324,500 |
| Other current liabilities | | 551,878 | 175,668 | 727,546 |
| Total current liabilities | | 37,171,805 | 22,083,149 | 59,254,954 |
| Total liabilities | | 41,685,293 | 34,424,083 | 76,109,376 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | | 68,305,232 | 21,770,186 | 90,075,418 |

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

23. Group reconciliation of equity and profit and loss (continued)

Restatement of equity from Previous basis of accounting to IFRS

A – The Group and material associates elected to measure property, plant and equipment at the date of transition to IFRS, i.e. January 1, 2005, at their fair value and use that fair value as their deemed cost at that date. The measurement resulted in a write-up of fixed assets balances. In addition, rehabilitation provision was capitalized (see **F**).

B – The various transitional adjustments lead to different timing differences. According to the accounting policies in Note 2 the Company has to account for such differences. In order to calculate the deferred tax amount a tax rate of 20% has been applied.

C – Amounts due from associates were reclassified from trade receivables into a separate category for IFRS reporting purposes.

D – The Company wrote off certain obsolete and damaged inventory for IFRS reporting purposes.

E – The difference represents the cumulative effect of prior period adjustments.

F – The Company has not accrued a rehabilitation provision in Previous basis of accounting financial statements. The provision was recognized for IFRS reporting purposes.

G – For IFRS reporting purposes, profit taxes payable were reclassified from other taxes payable into a separate category. Net difference at January 1, 2005 is due to tax adjustments.

H – For IFRS reporting purposes, business travel and representative expenditures were reclassified from non-operating into general and administrative expenses.

I – Under Previous basis of accounting the Company accounts for its associates at cost. The IFRS treatment of associates is different. The related difference in the statement of income represents dividends from associates reversed to reflect the investment in associate in accordance with IFRS.

K – For IFRS reporting purposes, part of the long-term loans was reclassified as short-term borrowings, and another part was released.

L – Natural resource tax was allocated from general and administrative expenses to cost of sales for IFRS reporting purposes. The treatment under the Previous basis of accounting is different.

M – Extraordinary loss including tax penalties, sponsorship and similar expenditures were reclassified to other non-operating expenses for IFRS reporting purposes.

24. Contingencies and commitments

Operating environment of the Company

The Company's operations are conducted in Georgia. As an emerging market, at the present time Georgia does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature market economy. However, there have been a number of developments that positively affect the overall investment climate of the country.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

24. Contingencies and commitments (continued)

Operating environment of the Company (continued)

While operations in Georgia may involve risks that are not typically associated with those in developed markets (including the risk that the GEL is not freely convertible outside of the country and undeveloped debt and equity markets), over the last few years the government of Georgia has made significant progress in implementing the reforms necessary to create banking, judicial, taxation and regulatory systems. In management's view, these steps contribute to mitigate the risks of doing business in Georgia. However, entities operating in Georgia, including the Company, could be affected for the foreseeable future by existing risks and their consequences.

The accompanying 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.

Taxation matters

Georgian tax, currency and customs legislation is subject to varying interpretations and changes occurring frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company may not coincide with that of management. As a result, tax authorities may challenge transactions and the Company may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for six calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As at December 31, 2006 and 2005 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company's tax, currency and customs positions will be sustained.

Share purchase agreement (the "Agreement")

On November 11, 2005 sales and purchase agreement was signed between the Ministry of Economic Development of Georgia and Stanton. According to this agreement Stanton agreed to pay USD 36,010,000 for acquisition of 97.25% of the Company, 50% interest in Quartzite LTD, and 50% in Trans Georgian Resources LLC. In addition, Stanton agreed to pay USD 16,000,000 for settlement of old tax debts of the Company and its associate Quartzite LTD.

On October 14, 2005 Stanton also acquired the remaining 50% interest of Quartzite LTD and Trans Georgian Resources LLC, becoming the ultimate owner of 100% interest in both companies.

The Agreement stipulates a number of commitments for Stanton which indirectly affect the Company and its subsidiaries/associates. The main requirements of the agreement were the followings:

- Maintain the same scope of activities for the period of at least three years from the date of purchase;
- Maintain at least the same salary levels for the period of at least three years from the date of purchase;
- Maintain the same number of employees for the period of at least three years from the date of purchase (842 persons as at July 2005);
- In case of the Company, Stanton will carry out environmental protection activities to comply with the licensure requirements applicable to ore extraction and processing, and will undertake maximum effort to eliminate the existing cases of non-compliance;
- In addition, Stanton will present to the Ministry of Environmental Protection in three months from execution of the agreement a plan of measures to address the atmosphere, water, waste pollution prevention, ecologic disaster contingency recovery plan and ecologic management; the program would need to be implemented in 21 months from the date of approval by the Ministry.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

24. Contingencies and commitments (continued)

Share purchase agreement (the "Agreement") (continued)

Another subsidiary of Madneuli JSC, Georgian Mining Company, was obliged to explore 20% of the license area every year starting from 2005.

Environmental liability

In accordance with terms of the Agreement, Stanton is not liable for any environmental matters of the Company that arose before the acquisition date.

According to Georgian legislation all companies conducting the processing of minerals should hold environmental protection permit. Since the Company was established before the adoption of Law of Georgia on Environmental Protection Permit, it does not have such permit. However, according to the local legislation the companies carrying out mineral processing activities established before the adoption of this law are obligated to get such a permit till January 1, 2009. The management is planning to get this permit by the date required.

Whilst management is of the opinion that the Company met the government's requirements concerning environmental matters, there can be no assurances that contingent liabilities did not exist.

Mineral licenses

According to Georgian legislation, exploration and extraction of precious, non-ferrous and rare metals are subject to licensing. At present the Ministry of Environmental Protection and Natural Resources of Georgia is the only governmental body authorized for issuance of Entrails Use Licenses. Furthermore the License on usage of entrails is the only official document proving the right of usage of entrails of the earth within mountain, geological and land allotment.

The following Group companies hold the following production and exploration licenses:

- The Company holds entrails use license issued by the Ministry of Environmental Protection and Natural Resources of Georgia with respect to research and extraction of gold, copper, barites and polymetals in Bolnisi administrative area.
- Georgian Mining Company LTD holds entrails use license issued by the Ministry of Environmental Protection and Natural Resources of Georgia with respect to research and extraction of precious, non-ferrous and rare metals on the territories of Bolnisi, Dmanisi, Tetrtskaro and Marneuli administrative regions.

These licenses are valid till 2014.

Quartzite LTD carries out the processing of gold-bearing secondary quartzite ore on the basis of mining license given to the Company. According to the minutes No.11 (dated May 16, 1997) of the meeting of the interdepartmental council of experts on licensing under the Ministry of Environmental Protection and Natural Resources of Georgia, Quartzite LTD was entitled for the processing of secondary quartzite ore in the capacity of the Company's business partner.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

24. Contingencies and commitments (continued)

Natural resource tax

The Company holds quartzite-containing stockpiles extracted back in the 80th that were previously thought to be waste, but later analysis confirmed that the content of quartzite is sufficient for heap leaching operations, so the Company started selling the ore from those stockpiles to Quartzite LTD. When the ore was sold, the Company recognized full profit on sales and the related profit tax and natural resource tax payable. Natural resource tax liability was recognized and paid only to the extent the ore was sold to Quartzite LTD. Hence there is a possible risk, that the tax authorities may impose the natural resource tax on the whole stockpile since the extraction. No accrual was made because it is not probable that economic outflows will take place as a result of this transaction. The range of possible tax liabilities is approximately GEL 15.6 million and GEL 17.1 million, as at December 31, 2006 and 2005, respectively.

Other commitments and contingencies

The subsidiaries of the Company provide transportation/hauling, drilling/blasting and similar services to the parent. Some of them are not profit-making, so they often request financial support from the parent to pay salaries and other ongoing operating expenditures. Although there is no contractual commitment, there is a constructive commitment to pay/lend to subsidiaries on demand.

Insurance policies

The Company holds no insurance policies in relation to its assets, operations, or in respect of public liability or other insurable risks, with the exception of insurance policies covering export shipments.

Legal proceedings

During the year, the Company was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Company and which have not been accrued or disclosed in these consolidated financial statements.

There are also certain claims related to the Company's activities prior to Stanton's acquisition. As those claims arose after the list of creditors and claimants was published in the public tender announcement, and the Agreement warrants that the list is exhaustive, management believes those claims have no ground and that there is no significant risk of loss to the Company.

25. Financial risk management

Credit risk

Financial assets, which potentially subject the Company to credit risk, consist principally of cash and cash equivalents, trade receivables, VAT receivable and prepayments (included in other current assets). The carrying amount of prepayments represents the maximum amount exposed to credit risk. Although the provision of services under prepayments made could be influenced by economic factors, management believes that there is no significant risk of loss to the Company.

The Company manages the credit risk by depositing the majority of available cash and cash equivalents with well known banks in Georgia. The management of the Company continually monitors the status of the banks where deposits are maintained.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Laries, unless otherwise specified)

25. Financial risk management (continued)

Credit risk (continued)

The carrying amount of trade receivables, net of provision for doubtful debts, represents the maximum amount exposed to credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Company beyond the provision already recorded.

The carrying amount of VAT receivable represents the maximum amount exposed to credit risk. The Company has a track of successful negotiations with the tax authorities whereas VAT receivable was offset against VAT payable and other tax liabilities. Management believes that there is no significant risk of loss to the Company arising from this risk.

Interest rate risk

The Company's income and operating cash flows are substantially independent of changes in market interest rates. As at December 31, 2006 the Company had two short-term borrowings taken from the Bank of Georgia and TBC with a fixed interest rates as disclosed in Note 15. The Company has no significant exposure to interest rate risk.

Foreign exchange risk

The Company exports production to European countries and attracts substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated assets (see Note 9) and liabilities (see Note 16) give rise to foreign exchange risk exposure.

The Company does not have formal arrangements to mitigate foreign exchange risks of the Company's operations. However, management believes that the Company is secured from foreign exchange risks as foreign currency denominated sales are used to cover repayment of foreign currency denominated borrowings.

The Company does not hedge accounts payable and borrowings denominated in foreign currencies since management does not believe the foreign exchange risk is significant.

26. Post balance sheet events

Change of Stanton's name

On April 5, 2007 Stanton, the ultimate owner of the Company, has changed its name to GeoProMining LTD.

Deutsche Bank Guarantee

Subsequent to December 31, 2006, the Company and its associate, Quartzite LTD (collectively referred to as "Guarantors"), guaranteed the performance of its related party, Karlou B.V. (the "Borrower"), under the loan agreement with Deutsche Bank AG, Amsterdam Branch (the "Bank") for the amount of USD 180 million. The Guarantors irrevocably and unconditionally jointly and severally guarantee to the Bank punctual performance by the Borrower of all the Borrower's obligations under the terms of the loan agreement; undertake with the Bank that whenever the Borrower does not pay any amount when due under or in connection with any terms of the loan agreement, that the Guarantors shall immediately on demand pay that amount as if it were the principal obligor; and indemnify the Bank immediately on demand against any cost, loss or liability suffered by the Bank if any obligation guaranteed by them or become unenforceable, invalid or illegal. The amount of the cost, loss or liability shall be equal to the amount which the Bank would otherwise have been entitled to recover.

JOINT STOCK COMPANY MADNEULI

Notes to the Consolidated Financial Statements (continued)

(All amounts are in Georgian Lari's, unless otherwise specified)

26. Post balance sheet events (continued)

Deutsche Bank Guarantee (continued)

In July 2007 Karlou B.V. drew down USD 140,000,000 under this loan facility and provided a loan to the Company in the amount of USD 116,885,000 for the period of 4 years with an interest rate of LIBOR + 3.05%. The Company made a decision to sub-loan USD 84,670,000 to GeoProMining LTD for the same period of time and interest rate of LIBOR + 3.55%.

Share repurchase

Subsequent to December 31, 2006, Stanton repurchased 1.9% of the minority interest held by the company employees and other individuals.

Liquidation of subsidiaries

The Company has formally liquidated three of its subsidiaries (Gardi LLC, Belaz and Ecology LLC), however the Company has not received an official confirmation from the State tax authorities. The Company plans to liquidate TFM LLC in late 2007. However, all operations of these subsidiaries were continued by the Company and the Company purchased all assets of the liquidated subsidiaries. Thus, those assets were not presented in the consolidated financial statements as held for disposal in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

Changes in debt

The Company also increased its credit line with BOG by USD 8 million (secured by 11.4% of the Company shares) and opened a new credit line of USD 5 million (unsecured) with TBC Bank. In June, 2007, the Company signed a new agreement with BOG where the Company unpledged its 11.4% shares as well as its pledged interest in Quartzite and agreed to reduce the loan to USD 6.5 millions (unsecured).

Declaration of dividends

Effective May 8, 2007 Stanton, as the majority shareholder, issued a resolution to appropriate GEL 67,290,000 of retained earnings as dividends to shareholders.