

Fermaca Pipeline El Encino, S. de R. L. de C. V.
(subsidiary of Fermaca El Encino-La Laguna, S. de R. L. de C. V.,
whose ultimate parent is Fermaca Luxembourg, S. à. r. l.)
Audited Financial Statements
December 31, 2018 and 2017

Fermaca Pipeline El Encino, S. de R. L. de C. V.

(subsidiary of Fermaca El Encino-La Laguna, S. de R. L. de C. V., whose ultimate parent is Fermaca Luxembourg, S. à. r. l.)

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December 31, 2018 and 2017

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Independent Auditor's Report

To the Partners Meeting of Fermaca Pipeline El Encino, S. de R. L. de C. V.:

Opinion

We have audited the financial statements of Fermaca Pipeline El Encino, S. de R. L. de C. V. (the Company), which comprise the statement of financial position as of December 31, 2018, and the related statements of income and comprehensive income, of changes in Partners' equity and of cash flows for the year then ended and the notes to the financial statements, which include a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the Ethics Standards of Mexican Institute of Public Accountants together with other requirements applicable to our audit in Mexico. We have fulfilled our other ethical responsibilities in accordance with those requirements and standards. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and those charged with Governance for the financial statements

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

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

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



Auditors' responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Management.
- Conclude on the appropriateness of Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



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

PricewaterhouseCoopers S. C.

A handwritten signature in black ink, consisting of a large, stylized 'J' followed by 'V' and 'G'.

C.P.C. Julio Valdés García
Audit Partner

Mexico City, May 10, 2019

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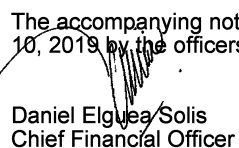
Statements of Financial Position

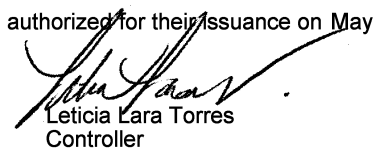
(Notes 1, 2, 3, 4 and 5)

Thousands of US Dollars

		<u>As of December 31,</u>	
<u>Assets</u>	<u>Notes</u>	<u>2018</u>	<u>2017</u>
CURRENT ASSETS:			
Cash (bank deposits)		\$ 53,878	\$ 83
Restricted cash	15	51,812	68,165
Trade receivables	9	32,110	31,959
Tax receivables	12	13,299	27,569
Contract assets		27,319	-
Other current assets		1,134	1,060
Derivative financial Instruments	5 and 10	3,821	481
Total current assets		183,373	129,317
NON-CURRENT ASSETS:			
Receivables from related parties	11	57	52
Derivative financial instruments	5 and 10	-	159
Property, equipment and construction in progress - Net	13	701,537	655,323
Intangible assets	14	35,138	35,091
Total non-current assets		736,732	690,625
Total assets		\$920,105	\$ 819,942
<u>Liabilities and Stockholders' equity</u>			
<u>Liabilities</u>			
CURRENT LIABILITIES:			
Short-term debt	15	\$ 16,685	\$ 570,606
Trade payables		18,262	27,852
Payables to related parties	11	9,165	4,187
Derivative financial instruments	5 and 10	-	-
Other liabilities and accrued expenses		5,257	4,957
Total current liabilities		49,369	607,602
NON-CURRENT LIABILITIES:			
Long-term debt	15	674,865	8,628
Payables to related parties	11	153,478	141,357
Derivative financial instruments	5 and 10	-	44,506
Deferred income tax liabilities	22	24,917	11,615
Total non-current liabilities		853,260	206,106
Total liabilities		902,629	813,708
PARTNERS' EQUITY:			
Social participation	16	26,449	\$ 25,808
Valuation of cash flow hedges	5 and 10	2,672	(30,818)
Cumulative (losses) earnings		(11,645)	11,244
Total partners' equity		17,476	6,234
Total liabilities and partners' equity		\$920,105	\$ 819,942

The accompanying notes are an integral part of these financial statements, which were authorized for their issuance on May 10, 2019 by the officers who signed below.


Daniel Elguea Solis
Chief Financial Officer


Leticia Lara Torres
Controller

Fermaca Pipeline El Encino, S. de R. L. de C. V.

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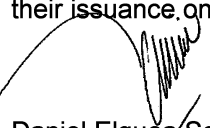
Statements of Income and Comprehensive Income

(Notes 1, 2, 3, 4 and 5)

Thousands of US Dollars

		Year ended on December 31,	
Statements of Income:	Notes	2018	2017
Revenue from contracts with customers	17	\$ 85,403	\$ 55,128
Cost of sales	18	<u>(13,041)</u>	<u>-</u>
Gross profit		<u>72,362</u>	<u>55,128</u>
Project development	19	(3,758)	-
Administrative expenses	19	(1,787)	(1,478)
Other income	20	<u>1,315</u>	<u>4,058</u>
Operating income		<u>68,132</u>	<u>57,708</u>
Finance income	21	2,737	1,363
Finance costs	21	<u>(94,811)</u>	<u>(1,897)</u>
Finance cost - Net	21	<u>(92,074)</u>	<u>(534)</u>
(Loss) profit before income tax		(23,942)	57,174
Deferred Income tax	22	<u>1,053</u>	<u>12,805</u>
Net (loss) income of the year		<u>(\$22,889)</u>	<u>\$ 69,979</u>
Statements of Comprehensive Income (loss):			
Net (loss) income of the year		(\$22,889)	\$ 69,979
Items that may be reclassified to profit or loss:			
Valuation of cash flow hedges	5	47,844	(9,116)
Income tax relating to these items	22	<u>(14,354)</u>	<u>13,207</u>
Other comprehensive income for the period, net of tax		<u>33,490</u>	<u>4,091</u>
Total comprehensive income for the year		<u>\$ 10,601</u>	<u>\$ 74,070</u>

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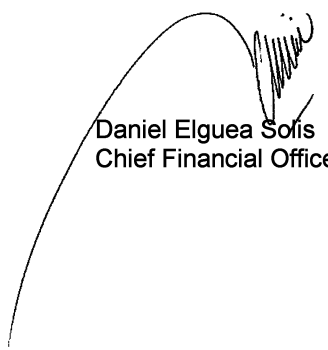
Statements of Changes in Partners' equity

(Notes 1, 2, 3, 4 and 5)

Thousands of US Dollars

	<u>Social participation</u>	<u>Valuation of cash flow hedges</u>	<u>Cumulative earnings (losses)</u>	<u>Total partners' equity</u>
Balances as of January 1, 2017	\$25,808	(\$ 34,909)	(\$ 58,735)	(\$ 67,836)
Net income for the year	-	-	69,979	69,979
Other comprehensive income for the year	-	4,091	-	4,091
Total comprehensive income for the year	-	4,091	69,979	74,070
Balances as of December 31, 2017	<u>25,808</u>	<u>(30,818)</u>	<u>11,244</u>	<u>6,234</u>
Transactions with Partners:				
Increase in social participation (Note 16)	<u>641</u>	-	-	<u>641</u>
Net loss for the year	-	-	(22,889)	(22,889)
Other comprehensive income for the year	-	33,490	-	33,490
Total comprehensive income for the year	-	33,490	(22,889)	10,601
Balances as of December 31, 2018	<u>\$26,449</u>	<u>\$ 2,672</u>	<u>(\$11,645)</u>	<u>\$ 17,476</u>

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Statements of Cash Flows

(Notes 1, 2, 3, 4 and 5)

Thousands of US Dollars

	Year ended on December 31,	
	2018	2017
Operating activities		
(Loss) profit before income tax	(\$ 23,942)	\$ 57,174
Adjustments for reconciling profit (loss) before income tax to:		
Depreciation and amortization (Notes 13 and 14)	11,014	3
Interest income (Note 21)	(333)	(35)
Valuation of derivative financial instruments - swaps (Note 21)	2,201	(1)
Fair value loss on interest rate swaps designated as cash flow hedges – transfer from OCI (Note 21)	53,000	-
Interest expense of bank borrowings	22,942	-
Interest expense with related parties	7,111	119
	71,993	57,260
Changes in working capital increase (decrease)		
Tax receivables	(12,141)	(20,270)
Value added tax recovered	26,411	55,920
Trade receivables	(151)	(31,959)
Contract assets (Note 17)	(27,319)	-
Other assets	399	51
Related parties	153	10,828
Trade payables and other liabilities	(9,290)	6,648
Net cash flows of operating activities	50,055	78,478
Investing activities		
Acquisitions of property, equipment and construction in progress	(38,602)	(117,728)
Intangible assets	(845)	(10,119)
Interest loans payments	(7,996)	(17,677)
Restricted cash	16,353	(63,747)
Net cash flows used in investing activities	(31,090)	(209,271)
Financing activities		
Bank loans obtained (Note 15)	707,253	190,459
Bank loans payment (Note 15)	(609,635)	(61,541)
Interest loans payments	(8,243)	-
Interest received	329	31
Interest rate swaps payments (Note 21)	(55,091)	-
Increase in social participation (Note 16)	641	-
Net cash flows provided by financing activities	35,254	128,949
Foreign exchange gain on cash	(424)	1,905
Net increase of cash (bank deposits)	53,795	61
Cash (bank deposits) at the beginning of the year	83	22
Cash (bank deposits) at the end of the year	\$ 53,878	\$ 83

The main non-cash transactions in 2018 and 2017 are included in Note 13.

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*Amounts expressed in thousands of US Dollars, except amounts expressed
in foreign currencies, number of social participation and exchange rates*

Note 1 - General information:

Fermaca Pipeline El Encino, S. de R. L. de C. V. (the “Company” or “El Encino”) was incorporated on October 29, 2008 and is a subsidiary of Fermaca El Encino-La Laguna, S. de R. L. de C. V., whose ultimate parent is Fermaca Luxembourg, S. à. r. l.

The Company is engaged in the transportation of natural gas through pipeline, including the construction, operation and maintenance of pipeline for transportation of natural gas and other equipment and accessories, in accordance with applicable laws.

On April 30, 2018, the Commercial Operating Date was approved by CFE. Therefore, on May 1, 2018, the capitalization of the El Encino gas pipeline was carried out.

The Company has no employees and all supervisory and administrative services are provided by related parties.

Note 2 - Significant events in the current reporting period:

On December 19, 2014 the Company signed a natural gas transportation agreement with Comisión Federal de Electricidad (CFE) to transport natural gas through a pipeline of approximate 445 kilometer long, 42-inch and a capacity up to 1,500 Million Standard Cubic Feet per Day (MMSCFD) (MPCD by its Spanish acronym) which is being constructed, and will be operated and maintained by the Company. The construction of the pipeline is being constructed in the states of Chihuahua and Durango, Mexico.

The agreement was executed as result of the award issued by CFE in favor of El Encino in connection with the international public bid number LPSTGN-003/14.

On March 10, 2016 the Energy Regulatory Commission (CRE by its Spanish acronym) granted the Company a 30 year permit to transport 1,670 MMSCFD of natural gas. This permit is renewal for half of the original term upon the Company request.

On December 12, 2016, the Company and CFE entered into an amendment agreement, among which December 27, 2017 is set as the new start date for operations, instead of April 1, 2016 previously agreed.

El Encino was in conditions to begin the gas testing required in order to start operations; however, there was no gas available that meets the specifications set by the applicable Mexican Official Norm (NOM by its Spanish acronym). Until such tests were carried out, the Company may not start operations. As the gas availability meeting the NOM is not under El Encino control, delay for starting operations for this matter has not and will not represent any penalty for the Company.

The phase 1 of the pipeline was available as of April 2017, so the revenue started to be recognized and invoiced since that date for the fixed charges tariff for the reserved capacity, considering the capacity was available. See note 4q.

The Commercial Operating Date was approved by CFE is April 30, 2018.

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On the other hand, in 2018, the Encino obtained a new financing to replace the original one. Details on this refinancing are described in Note 15.b.

Note 3 - Basis of preparation:

i. Compliance with IFRS

The financial statements of the Company as of December 31, 2018 and 2017, and for the years then ended, have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the IFRS Interpretations Committee (IFRIC) applicable to companies reporting under IFRS. The financial statements comply with IFRS as issued by the International Accounting Standards Board (IASB).

ii. Historical cost convention

The financial statements have been prepared on the historical cost basis, except for derivative financial instruments and financial liabilities at fair value through profit or loss that one measured at fair value.

Fair value is defined as the price that would be received in the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique.

In addition, fair value measurements are categorized into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1: The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Company is the current bid price. These instruments are included in level 1.
- Level 2: The fair value of financial instruments not traded in an active market (such as over-the-counter derivatives) is determined using valuation techniques which maximize the use of observable market data and rely as little as possible on entity-specific estimates. If all significant inputs required to determine fair value an instrument are observable, the instrument is included in level 2.
- Level 3: If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3. This is the case of unlisted equity securities.

iii. New and amended standards adopted by the Company

- a. The Company has applied the following standards and amendments for the first time for their annual reporting period starting on January 1, 2018:
- IFRS 9 Financial Instruments
 - IFRS 15 Revenue from Contracts with Customers

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- b. The Company had to change its accounting policies following the adoption of IFRS 9 and IFRS 15. The new accounting policies are described in Note 4. Other IFRS amendments or new standards are not listed above either because they are not applicable for the Company or they did not have impact in its financial statement.

Adoption of IFRS 9

Classification and measurement

The Company adopted IFRS 9 “Financial Instrument” since January 1, 2018, the date of initial application and, upon transitional provision under IFRS 9, the Company did not restate prior periods for comparative figures purposes and any difference that might come up as a results of IFRS 9 adoption between previous carrying amounts and the carrying amount at the beginning of the annual reporting period was allocated within the opening retained earnings.

As a result of the implementation strategy towards IFRS 9 adoption and based upon the Classification and Measurement requirements fulfillment, the new categories for financial assets under IFRS 9 are as follows:

<u>Assets</u>	<u>IAS 39 Category</u>	<u>IFRS 9 Category</u>	<u>Change in measurement?</u>
Cash (including restricted cash)	Trade and other receivables	Amortized cost	Not applicable
Trade receivables	Trade and other receivables	Amortized cost	Not applicable
Receivables related parties	Trade and other receivables	Amortized cost	Not applicable
Contract assets	Not applicable	Amortized cost	Not applicable
Other assets	Not applicable	Amortized cost	Not applicable

The adoption of the new Classification and Measurement criteria under IFRS 9 for financial assets had no effect on the Company’s financial statements.

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IAS 39 financial liabilities classification and measurement criteria remains substantially unchanged under IFRS 9, except for the changes in the fair value of financial liabilities designated at fair value with changes recognized through profit or loss for the year, due to the entity credit risk, are classified under other comprehensive income.

Impairment:

The Company has five types of financial assets that are subject to IFRS 9's new expected credit loss model:

- Cash (including restricted cash)
- Trade receivables
- Receivables related parties
- Contract assets
- Other assets

The Company applied the impairment methodology under IFRS 9 for each of those classes of assets. The identified impairment loss was immaterial; mainly due to our main customer (CFE) pay its bills 30 days after the issuance. Furthermore, no late payments have been observed in other customers which also pay its bills 30 days after issuance on average.

Hedge Accounting

IFRS 9 includes new hedge accounting requirements which have a twofold objective: (i) to simplify current requirements, and (ii) to bring hedge accounting in line with risk management, allowing to be a greater variety of derivative financial instruments which may be considered to be hedging instruments. Furthermore, additional breakdowns are required providing useful information regarding the effect which hedge accounting has on financial statements and also on the entity's risk management strategy. The treatment of macro-hedges is being developed as a separate project under IFRS 9. Entities have the option of continuing to apply IAS 39 with respect to accounting hedges until the project has been completed. The Company continued to apply IAS 39 for hedge accounting.

Adoption of IFRS 15

The Company adopted IFRS 15 using the modified retrospective approach. Under this method the financial statements are retrospectively adjusted but the cumulative impact is recognised at the date of initial application (January 1, 2018). Comparatives are not restated and are presented using the amounts determined under IAS 18. Using the modified retrospective approach, The Company did not need to restate any contracts that were completed before the date of initial application.

There was no impact of adoption on January 1, 2018, for the adoption of IFRS 15. However, several changes were made to accounting policies to conform to the requirements of the new standard. See notes 4, 7 and 17 for more details of the new accounting policies, significant judgement and other disclosure requirements of the standard.

iv. New standards and interpretations not yet adopted

Certain new accounting standards and interpretations have been published that are not mandatory for December 31, 2018 and 2017 reporting periods and have not been early adopted by the Company. The Company assessment of the impact of these new standards and interpretations is set out below.

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Below are the results of the assessment:

- IFRS 16 “Leases”- The standard introduces a unique accounting model for lessees which include substantially all leases on the statement of financial position through the recognition of right-of-use assets (presented or disclosed separately from other assets) and lease liabilities (presented or disclosed separately from other liabilities), determining the present value of the future payments of the lease agreement. For the statement of income, IFRS 16 establishes for lessees to recognize amortization of right-of-use assets as well as interest expenses for the lease liabilities. The Company has elected to exclude from the statement of financial position those leases with a maximum possible term of less than 12 months or leases in which the underlying asset met the definition of 'low-value' according to the standard. In addition, IFRS 16 requires to assess service contracts depending on the use of a specific asset to render the service in order to determine the existence of embedded leases. For lessors, accounting for leases is largely unchanged from previous provisions of IFRS (IAS 17 – Leases).

The standard will become effective on January 1, 2019 and supersedes IAS 17 “Leases” and IFRIC 4 “Determining Whether an Arrangement Contains a Lease”. IFRS 16 establishes the principles for recognition, measurement, presentation and disclosure of all leases.

As of December 31, 2018, the Company has performed an analysis to identify the inventory of contracts and potential impacts of adoption. The Company will adopt IFRS 16 using the modified retrospective approach. Under this method, the financial statements will be retrospectively adjusted but the cumulative impact would be recognized at the date of initial application (January 1, 2019). Comparatives will not be restated and will be presented using the amounts determined under IAS 17. The modified retrospective approach includes practical expedients that will be elected. The Company will use the practical expedient to grandfather assessments performed under IFRIC 4 regarding whether a service contract existing at the date of initial adoption contains a lease.

Within the grandfathering as practical expedient, the Company elects to apply the new guidance regarding the definition of a lease only to contracts entered into (or modified) on or after the date of initial application. Existing lease contracts will not need to be reassessed. This expedient will be consistently applied to all the contracts.

The Company has identified that the right of way currently presented as intangible assets will be reclassified as Right of use assets (without recognizing a lease liability as these rights include only one payment made upfront) according to the new standard.

The Company does not expect to have significant impact in the Company results, financial position and financial covenants.

Financial statements authorization

These financial statements and the accompanying notes were authorized for their issuance on May 10, 2019 by Daniel Elguea Solis, Chief Financial Officer and Leticia Lara Torres, Controller.

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Note 4 - Summary of significant accounting policies:

The main accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 7.

a. Foreign currency translation

i. Presentation and functional currency

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the entity operates (functional currency). The financial statements are presented in US dollars, which is the functional and presentation currency of the Company.

ii. Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates in effect at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of comprehensive income and are presented within "Finance income (cost) - Net".

Financial statements remeasurement

The Company's financial statements having a recording currency different from the functional currency were translated to the functional currency using the following procedure that would produce the same amounts in the functional currency as would have occurred had all the items been recorded in the functional currency in the first place:

- i. The balances of monetary assets and liabilities at December 31, 2018 and 2017 expressed in Mexican Pesos (MxN), where the functional currency was the US Dollar, were translated at the exchange rate prevailing at such dates, which were: MxN 19.65 in 2018 and MxN 19.73 in 2017, respectively.
- ii. Balances at December 31, 2018 and 2017 of non-monetary assets and liabilities and capital stock and retained earnings were translated at the historical exchange rate at the date of the transaction.
- iii. Income, costs and expenses of the periods presented, expressed in recording currencies (MxN), were translated the date the transaction was recognized in the statement of comprehensive income, except when they arose from non-monetary items in which case the historical exchange rate of the non-monetary items was used.

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- iv. Exchange differences arising in the translation from recording currency to functional currency were recognized in the statement of comprehensive income within “Finance cost - Net” in the period they were originated.

b. Financial assets

i. Classification

From January 1, 2018, the Company classifies its financial assets in the following measurement categories:

- Those to be measured subsequently at fair value (either through OCI or through profit or loss), and,
- Those to be measured at amortized cost.

The classification depends on the entity’s business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the Company has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Company reclassifies debt investments when and only when its business model for managing those assets changes.

ii. Recognition and derecognition

Regular way purchases and sales of financial assets are recognized on trade-date, the date on which the Company commits to purchase or sell the asset. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

iii. Impairment of financial assets carried at amortized cost and fair value through other comprehensive income (FVOCI)

From January 1, 2018, the Company assesses on a forward-looking basis the expected credit losses (ECL) associated with its financial assets carried at amortized cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions

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Financial assets subject to impairment are divided into three categories, based on the stage of each instrument with regard to its level of credit risk:

- Stage 1: financial instruments for which no significant increase in credit risk is identified since its initial recognition. In this case, the impairment provision reflects expected credit losses arising from defaults over the following 12 months from the reporting date.
- Stage 2: if there has been a significant increase in risk since the date of initial recognition but the impairment event has not materialized, the financial instrument is classified as Stage 2. In this case, the impairment provision reflects the expected losses from defaults over the life of the financial instrument.
- Stage 3: a financial instrument is catalogued in this stage when shows effective signs of impairment as a result of one or more events that have already occurred resulting in a loss. In this case, the amount of the impairment provision reflects the expected losses for credit risk over the expected life of the financial instrument.

The Company applies the IFRS 9 simplified approach to measuring expected credit losses, which uses a lifetime expected loss allowance for all trade receivables and contract assets.

c. Cash and restricted cash

Cash includes cash on hand and bank deposits available for operations.

Cash subject to restrictions or intended for a specific purpose is presented separately under current assets. (See Note 15).

As restricted cash consist of cash available for the expenditures for the constructions, is being presented in the cash flows statement within investing activities.

d. Derivative financial instruments and hedging activities

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged.

The Company designates its derivatives as hedges of a particular risk associated with a recognized asset or liability or a highly probable forecast transaction (cash flow hedge).

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

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The fair values of various derivative instruments used for hedging purposes are disclosed in Note 10. Movements on the hedging reserve in shareholders' equity are shown in Statements of Changes in Partner's Equity. The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining hedged item is more than 12 months, and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months.

Cash flow hedge

The effective portion of changes in the fair value of derivatives designated and qualifying as cash flow hedges is recognized in other comprehensive income and accumulated in equity. The gain or loss relating to the ineffective portion is recognized immediately in the statement of comprehensive income within "Finance (cost) - Net".

Amounts accumulated in equity are reclassified to profit or loss in the periods in which the hedged item affects profit or loss (for example, when the forecast sale that is hedged takes place). The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognized as OCI.

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

e. Prepayments to suppliers

Prepayments to suppliers represents expenditures made by the Company where the risks and benefits inherent to the goods to be acquired or services to be received have not been transferred. Prepayments to suppliers are recorded at their cost and are presented in the statement of financial position as current or non-current assets, depending on the destination item. Once the goods and/or services related to advanced payments are received, they should be recognized as an asset in the statement of financial position or as an expense in the statement of comprehensive income, according to their nature.

f. Property, plant, equipment and construction in progress

Property and equipment comprise a natural gas pipeline and compression station, which are currently at historical cost less depreciation. The acquisition and construction cost of the property and equipment requiring a substantial period to be in usage conditions includes: the acquisition cost and the capitalization of the finance cost accrued in such period and attributable at acquisition and construction.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item are likely to flow to the Company and the cost of the item can be reliably measured. The carrying amount of any component accounted for as a separate asset is derecognized when replaced. Repairs and maintenance are recognized in the statement of comprehensive income in the period in which they are incurred. Major improvements are depreciated over the remaining useful life of the related asset.

Depreciation is calculated considering separately each of the asset's components. Land is not subject to depreciation.

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Depreciation is calculated using the straight-line method to allocate cost net of their residual values over estimated useful lives, as follows:

Pipeline	50 years
Compression station	25 years
Furniture and office equipment	10 years
Transportation equipment	4 years
Computer equipment	3 years

Depreciation expense for the years ended December 31, 2018 and 2017 is not significant.

The assets' residual values, useful lives and depreciation method are reviewed, and adjusted if appropriate, at the end of each reporting period. As of December 31, 2018, the Company has not had any changes in this regard.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount exceeds its estimated recoverable amount.

Gains and losses from disposals are determined by comparing the proceeds to the carrying amount and are recognized under 'Other income - Net' in the statement of comprehensive income.

Prepayments to suppliers are recognized as part of fixed asset line item when risks and benefits have been transferred to the Company.

g. Intangible assets

Intangible assets are comprised by rights of way, to obtain the right to access the land on which the pipeline are constructed. Rights of way contracts are for a term of 30 years. These rights can be renovated upon agreement of both parties and if the Company makes the corresponding payment for the renewal.

Rights of way are stated at historical cost less amortization. Amortization is calculated using the straight-line method.

h. Impairment of non-financial assets

Assets that have a finite useful life are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the highest of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are largely independent cash inflows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

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i. Financial liabilities

Liabilities within the scope of IFRS 9 (before IAS 39 except for changes in fair value related to own credit risk) are classified as financial liabilities at fair value through profit or loss or trade payables and other liabilities, as appropriate.

- Trade payables and other liabilities

These amounts represent liabilities for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities unless payment is not due within 12 months after the reporting period (or in the normal operating cycle of the business if longer) if not, they are presented as non-current liabilities. Trade payables and other liabilities are initially recognized at fair value and are subsequently recognized at amortized cost using the effective interest method.

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires.

j. Trade payables and other liabilities

These amounts represent liabilities for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities, unless payment is not due within 12 months after the reporting period (or in the normal operating cycle of the business if longer) if not, they are presented as non-current liabilities. Trade payables and other liabilities are initially recognized at fair value and are subsequently recognized at amortized cost using the effective interest method.

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expired.

k. Debt

Debt is recognized initially at fair value, net of transaction costs incurred. Debt is subsequently carried at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the statement of comprehensive income over the period of the borrowings using the effective interest method.

Fees paid on the establishment of loan facilities are recognized as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalized as a pre-payment for liquidity services and amortized over the period of the facility to which it relates.

Borrowings are removed from the statement of financial position when the obligation specified in the contract is discharged, cancelled or expired.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting period.

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l. Borrowing costs

Specific borrowing costs directly attributable to the acquisition, construction or production of qualifying assets are capitalized during the period required to complete and prepare the asset for its intended use or sale. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale. Generally, assets that take more than one year.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from borrowing costs eligible for capitalization.

All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

m. Current and deferred income tax

The income tax expense or credit for the period is the tax payable on the current period's taxable income, based on the applicable income tax rate for each jurisdiction, adjusted for changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of tax laws enacted or substantively enacted at the statement of financial position date in the countries where the Company and operates and generate taxable income.

The Company evaluates its positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred tax liabilities are not recognized if they arise from the initial recognition of goodwill; deferred income tax is also not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the date of the statement of financial position and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred tax assets are recognized only if it is probable that future taxable amounts will be available to utilize those temporary differences and losses.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax balances relate to the same tax authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Current and deferred tax is recognized in profit or loss, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case, the tax is also recognized in other comprehensive income or directly in equity, respectively.

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n. Provisions

Provisions are recognized when the Company has a present legal or construction obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation at the end of the reporting period. The discount rate used to determine the present value is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognized as interest expense.

o. Asset retirement obligations

Asset retirement obligations represent legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or normal use of the asset. The Company recognize the fair value of a liability for an asset retirement obligation in the period when it is incurred if a reasonable estimate of the fair value can be made. The Company is not able to estimate reasonably the fair value of the asset retirement obligations for portions of its assets, primarily certain pipeline assets, because the settlement dates are indeterminable given the expected continued use of the assets with proper maintenance.

The Company expects its pipeline assets, for which it is unable to estimate reasonably the fair value of the asset retirement obligation, will continue in operation as long as supply and demand for natural gas exists.

p. Partners' equity

The Company's common social parts are classified as partners' equity within equity. Partners' equity is expressed at historical value. Incremental costs directly attributable to the issuance of new social parts are included in equity as a deduction from the consideration received, net of tax.

q. Revenue from contracts with customers (Starting on January 1, 2018)

(1) Transportation of Natural Gas:

The Company is obligated to reserve capacity on its transportation pipeline for customers up to the maximum monthly quantity. The Company is entitled to a capacity reservation fee (charged monthly regardless of the volumes transported) as well a Natural Gas Transportation services fee (charged per volume transported).

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Revenue from the transportation of natural gas includes two performance obligations: Reserve Capacity and natural gas transportation services. Reserved capacity is a stand ready obligation that is generally recognized on a straight-line basis over the contracted period. Billings to clients might differ from revenue recognized, and therefore, a contract asset or contract liability is recognized for the difference between revenue recognized and amounts billed to clients. When the Company performs the service before having the right to bill the client, a contract asset is recognized as it represents the Company's right to consideration in exchange for the service that the Company has already transferred to the client. On the other hand, when the Company bills the clients based on tariffs agreed in contracts that do not represent the right to consideration for performance completed to date, a contract liability is recognized.

The Natural Gas Transportation services are associated with the volume of natural gas transported. Revenue for this performance obligation is recognized over time when the volumes are being transported. The Company uses the right-to-invoice practical expedient to measure progress and recognize revenue under IFRS 15 based on the amounts invoiced to customer, since the Company has the right to consideration from a customer in an amount that corresponds directly with the value to the customer of the Company's performance completed to date.

The Company includes in the transaction price estimated variable considerations such as discounts taking into consideration the revenue constraints provided for in the IFRS 15, since revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur.

(2) Financing components:

The Company has contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. The recognition of financing component is applicable in those cases as a finance costs (when there is a contract liability) or as a finance income (when there is a contract asset).

r. Operating leases

Leases in which a significant portion of the risks and rewards relating to the leased property are not transferred to the Company as lessee are classified as operating leases. Payments made under operating leases (net of incentives received from the lessor) are charged to the statement of comprehensive income, based on the straight-line method over the lease term.

The respective leased assets are included in the statements of financial position based on their nature.

s. Rounding of amounts

All amounts disclosed in the financial statements and notes have been rounded off to the nearest thousand currency units unless otherwise stated.

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Accounting policies applied until December 31, 2017:

Financial assets

a. Classification

The Company classifies its financial assets in the category of trade and other receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

- Trade and other receivables

Trade receivables represent amounts due from customers that are generated by services provided in the normal course of the Company's operations. Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. If collection of the amounts is expected in one year or less they are classified as current assets.

If not, they are presented as non-current assets. Trade receivables are generally due for settlement within 30 days and therefore are all classified as current. The Company's trade and other receivables comprise trade receivables, receivables related parties, other current assets in the consolidated statement of financial position.

b. Recognition and measurement

Trade and other receivables are initially recognized at fair value plus transactions costs and are subsequently carried at amortized cost using the effective interest method.

c. Impairment of financial assets carried at amortized cost

The Company assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets are impaired. An impairment loss is recognized if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and provided that the loss event (or events) has an impact on the estimated future cash flows arising from the financial asset or group of financial assets that can be reliably estimated.

As of December 31, 2018 there is no evidence of impairment.

For loans and receivables, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognized in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the reversal of the previously recognized impairment loss is recognized in profit or loss.

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Revenue recognition

i. Revenue from natural gas transportation:

Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are gross.

Revenue is recognized when the amount of revenue can be measured reliably, when it is probable that the economic benefits associated with the transaction will flow to the entity, the stage of completion of the transaction at the end of the reporting period can be measured reliably; and when the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

The Company recognizes revenue from the natural gas transportation service and the operation of third party pipeline through Supervisory Control and Data Acquisition System (SCADA system). The transportation operations generally consist of tariff -based activities associated with transporting natural gas through pipeline. Revenues from pipeline tariffs are associated with the transportation of natural gas at an agreed tariff, as well as revenues associated with agreements for committed capacity on the pipeline. Tariff revenues are recognized either at the point of delivery or at the point of receipt pursuant to specifications outlined in the contractual agreements. Part of the pipeline tariff revenues are based on actual volumes.

The Company has certain agreements that require counterparties to ship a minimum volume over an agreed upon period. Revenue is recognized as a stand-ready obligation accomplished when the counterparty's ability to make up the minimum volume has expired.

Note 5 - Financial risk management:

The Company's activities expose it to the following financial risks: market risk (foreign exchange risk and cash flow and fair value interest rate risk), credit risk and liquidity risk. The overall risk management program of the Company focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the financial performance of the Company. The objective of the financial risk management is to protect the financial performance of the business.

a. Market risk

i. Foreign exchange risk

At December 31, 2018 and 2017, the Company's exposure to foreign currency risk (MxN pesos) at the end of the reporting period, expressed in thousands of US dollars, was as follow:

	<u>2018</u>	<u>2017</u>
Assets:	\$ 14,015	\$ 28,327
Liabilities:	<u>(11,657)</u>	<u>(20,932)</u>
Net short position:	<u>\$ 2,358</u>	<u>\$ 7,395</u>

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At December 31, 2018 and 2017, the exchange rates were MxN19.65 and MxN19.74 per US dollar, respectively.

At the date of issuance of the financial statements, the exchange rate was MxN19.26 per US dollar.

Following is a summary of the main foreign currency transactions (MXN pesos) recognized in profit or loss by the Company during the years ended December 31, 2018 and 2017 (excluding the acquisition or sale of property and equipment for its own use), together with the related service expense and net interest expense (amounts are expressed in thousands of US dollars):

	<u>2018</u>	<u>2017</u>
Expenses	<u>\$ 1,715</u>	<u>\$ 1,186</u>

ii. Cash flow and fair value interest rate risk

The Company's interest rate risk arises from long-term borrowings with variable rates, which expose the Company to cash flow interest rate risk. Company policy is to maintain borrowings at fixed rates using interest rates swaps to achieve this when necessary. As of December 31, 2018 and 2017, the Company maintained approximately 98.4% and 90.39%, respectively, of its borrowings in fix rate instruments. During 2018 and 2017, the Company's borrowings at variable rate were denominated in US dollars and Mexican pesos.

As at the end of the reporting period, the Company had the following outstanding variable rate borrowings and interest rate swap contracts:

	<u>December 31, 2018</u>		<u>December 31, 2017</u>	
	<u>Balance</u>	<u>% of total loans</u>	<u>Balance</u>	<u>% of total loans</u>
Credit facility - Syndicated (Note 15)	\$ 236,474	34%	\$ 570,541	98%
Credit facility - VAT (Note 15)	-	0%	8,693	2%
Interest rate swaps (notional principal amount)	<u>(240,416)</u>		<u>(426,249)</u>	
Net exposure to cash flow interest rate risk	<u>(\$ 3,942)</u>	(1%)	<u>\$ 152,985</u>	26%

An analysis of maturities is provided in section c. of this note. The percentage of total loans shows the proportion of loans that are currently at variable rates in relation to the total amount of borrowings.

During the year, the following gains were recognized in profit or loss and other comprehensive income in relation to interest rate swaps.

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	<u>2018</u>	<u>2017</u>
Gain (loss) recognized in other comprehensive income	\$47,844	(\$9,116)
(Loss) / Gain on valuation of derivatives (ineffective portion) (See note 21)	(2,201)	1
(Loss) / Gain reclassified from other comprehensive income - fair value loss on interest rate swaps designated as cash flow hedge - transfer from OCI to loss (Note 21)	(53,000)	-

Sensitivity

If interest rates during the year ended December 31, 2018 and 2017 of borrowings denominated in US dollars, would have been 10% higher (with all the other variables constant), the profit after tax corresponding to each period would had been \$8,247 and \$25,522 higher/lower, respectively, mainly as a result of a higher/lower interest payment in connection with the variable rate borrowings.

b. Credit risk

Credit risk arises from cash, derivative financial instruments and deposits in banks and financial institutions, as well as credit exposures to customers.

As concerns banks and financial institutions, only independently rated parties with a minimum rating of "A" are accepted.

CFE (the National Energy Company, with a rating of AAA) is the Company's main customer. Credit risk is monitored by the finance area. As of December 31, 2018 and 2017, the Company recognized revenue per fixed charge per capacity.

The Company believes that revenue concentration risk posed by having a reduced number of counterparts is offset by the creditworthiness of the said customers, however, if the Company's customers, particularly CFE, fail to perform or become unable to meet their contractual obligations on a timely basis, or if any of these agreements is prematurely terminated, it would have a material adverse effect on the financial condition and results of operations of the Company.

No credit limits were exceeded during the reporting period, and Management does not expect any losses from non-performance by these counterparties.

c. Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash to meet payment obligations when they fall due. The finance department manages liquidity and flexibility in funding by monitoring forecast and actual cash flows and the maturity profile of financial assets and liabilities. Such forecasting takes into consideration the Company's debt financing plans and covenant compliance.

The tables below summarizes the Company's financial liabilities into relevant maturity groupings based on the remaining period at the statement of financial position date to the contractual maturity date.

The amounts disclosed in the table below are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

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For interest rate swaps the cash flows have been estimated using forward interest rates applicable at the end of the reporting period.

<u>As of December 31, 2018:</u>	<u>Less than 1 year</u>	<u>From 1 to 2 years</u>	<u>From 2 to 5 years</u>	<u>Over 5 years</u>	<u>Total</u>	<u>Carrying amount</u>
Debt (Note 15) ⁽¹⁾	\$ 11,740	\$ -	\$ 317,150	\$ 590,778	\$ 919,668	\$ 691,550
Related parties (Note 11)	9,165	-	-	153,478	162,643	162,643
Trade and other payables	<u>23,519</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>23,519</u>	<u>23,519</u>
	<u>\$ 44,424</u>	<u>\$ -</u>	<u>\$ 317,150</u>	<u>\$ 744,256</u>	<u>\$ 1,105,830</u>	<u>\$ 877,712</u>

<u>As of December 31, 2017:</u>	<u>Less than 1 year</u>	<u>From 1 to 2 years</u>	<u>From 2 to 5 years</u>	<u>Over 5 years</u>	<u>Total</u>	<u>Carrying amount</u>
Debt (Note 15) ⁽¹⁾	\$ 596,729	\$ 1,758	\$ 9,661	\$ -	\$ 608,148	\$ 579,234
Derivative financial instruments (Note 10)	-	-	-	44,506	44,506	44,506
Related parties (Note 11)	4,187	-	-	141,357	145,544	145,544
Trade and other payables	<u>32,809</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>32,809</u>	<u>32,809</u>
	<u>\$ 633,725</u>	<u>\$ 1,758</u>	<u>\$ 9,661</u>	<u>\$ 185,863</u>	<u>\$ 831,007</u>	<u>\$ 802,093</u>

⁽¹⁾ Amounts before commissions and issuance costs.

Note 6 - Capital management

Risk management

The Company's objectives in capital management are to safeguard its ability to continue as ongoing business in order to provide yields to partners as well as to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Company may adjust dividends paid to partners, return capital to partners, issue new social parts or sell assets to reduce debt.

Consistent with others in the industry, the Company monitors capital on the basis of the gearing ratio, which is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including "current and non-current borrowings" as shown in the statement of financial position) less cash. Total capital is calculated as 'equity', as shown in the statement of financial position plus net debt.

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The gearing ratio at December 31, 2018 and 2017 was:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Total debt (Note 15)	\$ 691,550	\$ 579,234
Less: cash (including restricted cash)	<u>(105,690)</u>	<u>(68,248)</u>
Net debt	585,860	510,986
Total equity	<u>17,476</u>	<u>6,234</u>
Total capital	<u>\$ 603,336</u>	<u>\$ 517,220</u>
Gearing ratio	<u>97%</u>	<u>99%</u>

Note 7 - Critical accounting estimates and judgments:

The preparation of financial statements requires the use of accounting estimates which, by definition, seldom equal actual results. Management also needs to exercise judgment in applying the Company's accounting policies. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

This note provides an overview of areas involving a higher degree of judgment or complexity, and of items which are more likely to be materially adjusted due to estimates and assumptions that turn out to be wrong. Estimates and projections that have a significant risk of material adjustments on assets and liabilities recognized during the following year are detailed below:

Significant accounting judgements

a. Recognition of deferred tax assets

Recognition of deferred tax assets is based upon whether it is more likely than not that there will be sufficient and suitable taxable profits in the relevant legal entity against which to utilize the assets in the future. Judgment is required when determining probable future taxable profits, which are estimated using the latest available profit forecasts. Prior to recording deferred tax assets for tax losses, relevant tax law is considered to determine the availability of losses to offset against future taxable profits.

Embedded leases

Natural gas transportation service contracts were considered to be outside the scope of IAS 17 "Leases". The Company performed analyses following the guidance on IFRIC 4 in order to conclude if the transportation contracts contained embedded leases that had to be recognized under IAS 17. The conclusion of those analyses was that those contracts did not contain a lease and, therefore, revenue related to those contracts are to be evaluated and recognized under IFRS 15.

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b. Revenue from contracts with customers

a) Timing of satisfaction of performance obligations:

i) Performance obligations satisfied over time

For natural gas transportation services, revenue is recognized using the right to invoice practical expedient, measuring progress and recognizing revenue for the amounts invoiced to customer. This represents a faithful depiction of the transfer because the Company has the right to consideration from a customer in an amount that corresponds directly with the value to the customer of the Company's performance completed to date.

For reserved capacity, revenue is recognized ratably throughout the contract and the Company has a "stand-ready" obligation. Billings to clients might differ from revenue recognized because the milestones and tariffs agreed upon in the service contract might not faithfully depict the transfer of the value to the customer and performance completed to date. Therefore, a contract asset or a contract liability is recognized for the difference between revenue recognized or deferred and amounts billed to clients.

b) Identification of separate performance obligations:

The Company has identified two performance obligations for its Transportation Services that are satisfied over time: Reserve Capacity and natural gas transportation. Even though both performance obligations might be considered as one performance obligation in some cases, the occurrence of the actual natural gas transportation (volume) might not be required by clients during some months even when there are nominated capacities. The transaction price is also separated since the requirement of capacity is not dependent on the transportation of volumes of gas. Transaction price includes two charges:

- Fixed charge - corresponds directly with the reserved capacity performance obligation, and
- Variable charge - with the transportation of natural gas service.

Transaction price is allocated between the performance obligations taking into consideration the stand-alone selling price of each one.

For all contracts, variable considerations, such as discounts, are taken into consideration, and are included in the transaction price to the extent that it is highly probable that a significant reversal will not occur.

c) Costs to obtain or fulfil a contract with a customer

Costs to obtain a contract with customers are recognized as an asset if the Company expects to recover those costs. However, the incremental costs of obtaining a contract are expensed as incurred when the amortization period of the asset that the Company otherwise would have recognised is one year or less. The Company has not identified costs to obtain a contract for current contracts.

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Costs to fulfil a contract are recognized if they are related to a contract with customer, generate resources that will be used in satisfying performance obligations, are expected to be recovered and are not within the scope of another standard (other than IFRS 15). The Company has identified costs related to the reserved capacity and transportation of natural gas such as rights of way and design, engineering, construction and testing of the pipeline, however the Company has determined that those costs are within IAS 38 “Intangible Assets” and IAS 16 “Property, plant and equipment”, respectively. In that sense, those costs are accounted for using those standards.

Further information is provided in Note 17.

Estimates:

a. Fair value of derivatives

The fair value of financial instruments that are not traded in an active market (such as over-the-counter derivatives) is determined by using valuation techniques. The Company uses its judgment to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

b. Gas pipeline useful life

The gas pipeline is depreciated over its estimated at useful life of 50 years, based on Management’s judgment, expertise and best practices in the natural gas transportation industry. Its residual value is considered non-significant.

When Management identifies that actual useful economic lives differ materially from the estimates used to calculate depreciation, the charge of depreciation expense is adjusted prospectively.

c. Fair value of derivatives

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

The sensitivity analysis of derivatives is within the Note 5.

d. Impairment

The Company applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables and contract assets.

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Note 8 - Financial instruments:

The Company holds the following financial instruments:

a. Financial instruments by category:

December 31, 2018					
	Trade and other receivables	Derivate used for hedging		Other financial liabilities at amortized cost	Derivatives used for hedging
Financial assets:			Financial liabilities:		
Cash			Trade payables		
(including restricted cash)	\$ 105,690	\$ -		\$ 18,262	\$ -
Contract assets	27,319	-			
Receivable from related parties	57	-	Payable to related parties	162,643	-
Trade receivables	32,110	-	Debt	691,550	-
Other assets	1,134	-			
Derivate financial instrument	-	3,821	Derivative financial instruments	-	-
Total financial assets	<u>\$ 166,310</u>	<u>\$3,821</u>	Total financial liabilities	<u>\$ 872,455</u>	<u>\$ -</u>
December 31, 2017					
	Trade and other receivables	Derivate used for hedging		Other financial liabilities at amortized cost	Derivatives used for hedging
Financial assets:			Financial liabilities:		
Cash			Trade payables		
(including restricted cash)	\$ 68,248	\$ -		\$ 27,852	\$ -
Receivable from related parties	52	-	Payable to related parties	145,544	-
Trade receivables	31,959	-			
Other assets	1,060	-	Debt	579,234	-
Derivate financial instrument	-	640	Derivative financial instruments	-	44,506
Total financial assets	<u>\$ 101,319</u>	<u>\$ 640</u>	Total financial liabilities	<u>\$ 752,630</u>	<u>\$44,506</u>

Note 9 - Trade receivables:

As of December 31, 2018 and 2017, short term accounts receivable are as follows:

	December 31,	
	2018	2017
CFE ⁽¹⁾	<u>\$ 32,110</u>	<u>\$ 31,959</u>
	<u>\$ 32,110</u>	<u>\$ 31,959</u>

⁽¹⁾ Natural gas transportation client; see description of the contract in Notes 17 and 23.

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Fair value of trade receivables is equal to their carrying amount. The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivables mentioned above.

As of December 31, 2018 and 2017, there are no past-due or impairment balances.

Note 10 - Derivative financial instruments:

Derivatives are only used for economic hedging purposes and not as speculative investments. However, where derivatives do not meet the hedging criteria, they are classified as 'held for trading' for accounting purposes.

i. The Company holds the following derivative financial instruments:

	<u>2018</u>	<u>2017</u>
Interest rate swaps - cash flow hedge		
Assets - current	\$ 3,821	\$ 481
Assets - non-current	<u>-</u>	<u>159</u>
	<u>3,821</u>	<u>640</u>
Interest rate swaps - cash flow hedge		
Liabilities - current	-	-
Liabilities - non-current	<u>-</u>	<u>(44,506)</u>
	<u>-</u>	<u>(44,506)</u>
Total financial instruments	<u>\$ 3,821</u>	<u>(\$ 43,866)</u>

- a. On July 24, 2015 the Company entered into a credit agreement with several financial institutions as described in Note 15.

This credit agreement was issued at variable rates. At the same dates, the Company entered into interest rate swaps agreements that have the economic effect of converting debt from floating rates to fixed rates.

The interest rate swaps have the follow fixed rates: 1.588% for the due dates in 2018 and 3.1206%, 3.115% and 3.13% for due dates in 2039, depending on the corresponding financial institution.

The interest rate swaps were entered with the following financial institutions: : 1) Banco Santander, S. A. (Santander); 2) Banco Nacional de México, S. A. (Banamex); 3) ING Bank N. V. (ING); 4) Norddeutsche Landesbank Girozentrale (Nord LB); 5) Banco Sabadell, S. A. (Sabadell), and 6) SCS Goldman Sachs Inc. Paris et Cie. (GS).

On June 21, 2018, this credit agreement was liquidated as well as the interest rate swaps related with it by an amount of \$53 million and it was reclassified to Statements of Income.

The ineffective portion recognized in the profit or loss that arises from fair value hedges amounts to a loss of \$2,201 in 2018 and a gain of \$1 in 2017.

- b. On June 12, 2018, the Company, entered into a credit agreement with several banks, described in Note 15.

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The credit agreement was issued at variable rates. At the same date, the Company entered into interest rate swaps agreements that have the economic effect of converting debt from floating rates to fixed rates.

The interest rate swaps has 2.627% as fixed rate with the due date in 2032.
The interest rate swaps were entered with the following institutions: 1) BNP Paribas Securities Corp. (BNP); 2) ING Bank N.V. (ING); 3) Norddeutsche Landesbank Girozentrale New York Branch (Nord LB) y 4) Mizuho Bank, LTD (Mizuho) and 5) Banco Sabadell, S. A. (Sabadell).

ii. Classification of derivatives

Derivatives are only used for economic hedging purposes and not as speculative investments. Derivatives are presented as current assets or liabilities if they are expected to be settled within 12 months after the end of the reporting period.

iii. Fair value measurement

Interest rate swaps recognized used for hedging were classified in level 2, by valuation method.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. Changes in the fair value of the financial instrument are accounted for in the statement of comprehensive income, within Finance cost - net. See Note 21.

There were no transfers between levels during the years presented.

Note 11 - Related parties:

The Company is a subsidiary of Fermaca El Encino-La Laguna, S. de R. L. de C. V., whose ultimate parent is Fermaca Luxembourg, S. à r. l.

a. The main balances at December 31, 2018 and 2017 with related parties are as follows:

	<u>December 31,</u>	
<u>Receivables</u>	<u>2018</u>	<u>2017</u>
Long-term:		
<u>Affiliated Companies:</u>		
Fermaca Pipeline Anáhuac, S. de R. L. de C. V.	\$ <u>57</u>	\$ <u>52</u>

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	<u>December 31,</u>	
<u>Payables</u>	<u>2018</u>	<u>2017</u>
Short-term loans:		
<u>Affiliated Companies:</u>		
Tejas Gas de Toluca, S. de R. L. de C. V. (TGT)	\$ 1,039	\$ 945
Tarahumara Pipeline, S. de R. L. de C. V. (TP)	507	460
Fermaca Enterprises, S. de R. L. de C. V. (FE)	<u>363</u>	<u>330</u>
	<u>1,909</u>	<u>1,735</u>
 <u>Payables</u>		
Short-term:		
<u>Other:</u>		
Fermaca New Projects, S. A. de C. V. (FNP)	\$ 6,295	\$ 1,952
Bcysa Servicios Industriales, S. A. de C. V. (Bcysa)	531	-
Fermaca Pipeline La Laguna, S. de R. L. de C. V. (La Laguna)	332	330
Others	<u>98</u>	<u>170</u>
	<u>7,256</u>	<u>2,452</u>
	<u>\$ 9,165</u>	<u>\$ 4,187</u>
 <u>Long-term loans:</u>		
<u>Affiliated Companies:</u>		
Herbodem, S. A. de C. V. SOFOM E. N. R. (Herbodem)	<u>153,478</u>	<u>141,357</u>
	<u>\$ 162,643</u>	<u>\$ 145,544</u>

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- b. During the years ended December 31, 2018 and 2017 the Company carried out the following operations with related parties:

	Years ended December 31,	
<u>Revenue:</u>	<u>2018</u>	<u>2017</u>
Interest income	\$ <u>4</u>	\$ <u>4</u>
<u>Expenses:</u>		
Interest expenses ^{(1) (c.iii)}	\$10,594	\$ 9,710
Construction and supervision services ^{(2) (c.i) (c.ii)}	2,999	7,496
Other expenses ⁽³⁾	<u>1,038</u>	<u>2,275</u>
	<u>\$14,631</u>	<u>\$19,481</u>

- ⁽¹⁾ In 2018 \$3,483 (\$9,591 in 2017) of accrued interest with related parties was capitalized as part of construction of the gas pipeline (See Note 21).
- ⁽²⁾ During 2018 and 2017, the amount of construction supervision services was capitalized as part of construction of the gas pipeline.
- ⁽³⁾ In 2018 and 2017, other expenses include rents, administrative expenses and reimbursements to FNP for the fees paid to Banco Nacional de Comercio Exterior, related to the letter of credit. (See Note 21).

- c. The Company entered into the following agreements with its related parties:
- Supervisory services and administration of the project agreement between the Company and BCYSA (an entity wholly-owned by some directors and indirect partners of the Company), mainly for supervision and advice of the new projects. These agreements are entered to for each project in which BCYSA is working on. BCYSA provide supervisory activities related to GDI Sicim Pipelines, S. A. de C. V. (Company supplier); inspection and coordination services related to the Pipe Supply agreement; and obtaining negotiating and formalizing Rights-of-Way.
 - An operations, maintenance and management's agreement was celebrated between the Company and TGT, which covers the supervisory services of TGT of the efficiency, safe and cost - effective of the operation.
 - On December 17, 2015, the Company and Herbodem entered into a credit agreement for \$118.7 million, which matures on the first business day of January 2046. The credit is subject to interest of 8.05% and 8.80% (starting month 25).

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d. During the year the Company had the following loans (from) to related parties:

Name of entity	Incorporation date ^(*)	Principal	% Interest from January to May	% Interest from June to December	Balance as of December 31, 2018
Anahuac	23/05/2014	\$ 46	9%	10%	\$ 57
Enterprises	23/05/2014	(287)	9%	10%	(363)
Tarahumara	27/12/2013	(413)	9%	10%	(507)
TGT	21/03/2014	(805)	9%	10%	(1,038)
Herbodem ⁽ⁱⁱⁱ⁾	17/12/2015	(118,743)	8.80%	8.80%	(153,478)
		<u>(\$120,202)</u>			<u>(\$155,329)</u>

(*) With no specific maturity date, except for Herbodem which maturity date is January 2, 2046.

<u>Loans (from) to affiliated companies:</u>	<u>2018</u>	<u>2017</u>
As of January 1	(\$ 143,169)	(\$ 131,846)
Interest charged	(10,590)	(9,706)
Currency exchange	<u>(1,570)</u>	<u>(1,617)</u>
	<u>(\$155,329)</u>	<u>(\$ 143,169)</u>

Note 12 - Tax receivables:

Tax receivables are comprised as follows:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Value added tax ^{(1) (2)}	\$ 13,164	\$ 27,436
Income tax	<u>135</u>	<u>133</u>
	<u>\$ 13,299</u>	<u>\$ 27,569</u>

⁽¹⁾ During 2018, the Company received VAT refunds of \$26,412 (the amounts returned includes restatement for inflation), which was used to pay off the loan from Banco Nacional de Comercio Exterior, S. N. C.

⁽²⁾ At December 31, 2017, the Company has received VAT refunds of \$55,920 (the amounts returned includes restatement for inflation).

During 2018, the Company generated favorable balances of VAT to be recovered.

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Note 13 - Property, equipment and construction in progress - Net:

Properties, equipment and constructions in progress at December 31, 2018 and 2017 are shown below:

At January 1, 2018

	<u>Land</u>	<u>Pipeline</u>	<u>Others</u>	<u>Construction in progress</u>	<u>Total ⁽¹⁾</u>
Opening balance	\$ 3,903	\$ -	\$ 11	\$ 651,409	\$ 655,323
Additions	-	-	540	55,890	56,430
Transfer	-	707,299	-	(707,299)	-
Depreciation of the year	-	(10,202)	(14)	-	(10,216)
Carrying amount at December 31, 2018	<u>\$ 3,903</u>	<u>\$697,097</u>	<u>\$ 537</u>	<u>\$ -</u>	<u>\$ 701,537</u>

At January 1, 2017

	<u>Land</u>	<u>Pipeline</u>	<u>Others</u>	<u>Construction in progress</u>	<u>Total ⁽¹⁾</u>
Opening balance	\$ 1,844	\$ -	\$ 3	\$513,046	\$ 514,893
Additions	2,059	-	11	138,363	140,433
Depreciation of the year	-	-	(3)	-	(3)
Carrying amount at December 31, 2017	<u>\$ 3,903</u>	<u>\$ -</u>	<u>\$ 11</u>	<u>\$651,409</u>	<u>\$ 655,323</u>

⁽¹⁾ In order to guarantee the timely payment and compliance of the obligations with the banks, the Company has guaranteed debt with all assets in a trust with Deutsche Bank México, S. A., Multiple Banking Institution (Fiduciary).

Depreciation expense of \$10,216 in 2018 and \$3 in 2017 has been charged in cost of services and administrative expenses, in the statement of comprehensive income.

During 2018, the Company capitalized borrowing costs in the amount of \$11,479 (\$32,528 in 2017). See Note 19.

As of December 31, 2018, there were non-cash transactions (pending payments for the acquisition of construction material for the pipeline and interest payable) related to property and equipment for the amount of \$12,391 (\$23,086 in 2017).

Construction in progress:

In December 2014, the Company was awarded the Encino-La Laguna project. That gas pipeline will cover the demand for natural gas at the CFE generating plants located in Chihuahua and Durango, as well as in the Central and Western regions of Mexico. The 42 inch diameter pipeline is 414 km in length, running from El Encino in the state of Chihuahua and ending in Lerdo in the state of Durango.

As of December 31, 2018, this project includes design, engineering, supply, construction, operation and maintenance of the gas pipeline, which has the capacity to transport 1,670 MMSCFD.

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The Commercial Operating Date was approved by CFE is April 30, 2018. Therefore, the capitalization of the El Encino gas pipeline was carried out.

Note 14 - Intangible assets - Net:

At December 31, 2018, and 2017, intangible assets are comprised of rights of way as follows:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Opening balance	\$ 35,091	\$ 24,972
Additions ⁽¹⁾	845	10,119
Accumulated amortization ⁽²⁾	<u>(798)</u>	<u>-</u>
Carrying amount	<u>\$ 35,138</u>	<u>\$ 35,091</u>

⁽¹⁾ The rights of way began to be amortized as of May 1, 2018, the date on which the capitalization of the Company's gas pipeline was completed.

⁽²⁾ Amortization expense of \$798 in 2018 has been charged in cost of services in the statement of comprehensive income.

Note 15 - Debt:

Debt is comprised as follows:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
<u>Short-term:</u>		
Notes Purchase Agreement	\$ 10,247	\$ -
Credit facility - Syndicated ^{(a) (b)}	6,438	570,541
Credit facility - VAT ^(c)	<u>-</u>	<u>65</u>
Total short-term	<u>16,685</u>	<u>570,606</u>
<u>Long-term:</u>		
Notes Purchase Agreement	444,829	-
Credit facility - Syndicated ^{(a) (b)}	230,036	-
Credit facility - VAT ^(c)	<u>-</u>	<u>8,628</u>
Total long-term	<u>674,865</u>	<u>8,628</u>
Total debt	<u>\$ 691,550</u>	<u>\$ 579,234</u>

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(a) On July 24, 2015, the Company entered into a credit facility in an aggregate principal amount not exceeding \$603,925 with ING Bank N.V., Dublin Branch, Nord LB, NY Branch, Goldman Sachs Bank USA, Sabadell Capital, S. A. de C. V. Sofom, E. N. R. (Sabadell), Banco Santander (México) S. A. (Santander) and Banco Nacional de México, S. A. (Banamex).

On September 30, 2015 Sabadell, GS and Nord LB with the consent of El Encino assigned a portion of their credit principal amount to Kreditanstalt für Wiederaufbau (KfW). The final maturity date was December 31, 2018. The payments of principal are made semiannually starting from June 2017.

The loans are subject to LIBOR interest plus the applicable margin.

As of December 31, 2017, the Company has withdrawn \$570 million at nominal value.

During 2017, the Company has made payments to the principal amount for \$7,451 (MxN 140,039). On June 21, 2018, the Company made payment for the total of debt by an amount of \$587 million (including interest) and signed a new credit agreement which is described in the item b. The original expiration date was on December 31, 2018.

The loans establish the following covenants:

- Not engage in any business or activity other than the development and operation of the Project.
- Not contract, create, incur, become liable for, assume or permit to subsist any indebtedness.
- Not agree to create, incur, assume, suffer to occur or permit to subsist any lien upon or with respect to any of its property, revenues or assets.
- Not agree to enter into any hedging program or hedging agreements other than Permitted Hedging Agreements.
- Not make or instruct any relevant person to make any investments of any person, except to acquire and hold Permitted Investments.
- The Borrower will not make any loans or advances to any Person except trade credit.
- Not form, own or have any subsidiaries or otherwise own beneficially an ownership interest in any person.
- Not incur operating expenses in excess of 115% of the operating expenses set forth in the operating budget for such financial year without the prior written consent of the Administrative Agent.
- Not incur capital expenditures except for capital expenditures which are consistent with the operating budget for such financial year and less than \$1 million in the aggregate for all capital expenditures.
- Not establish or maintain any bank accounts other than the project accounts and any other accounts permitted to be established or maintained pursuant to the Security and Depositary Agreement.

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- Not sponsor, maintain or contribute to any pension plan or multiemployer plan.
- Not issue any equity interests or any other security convertible into any other equity interests in the Borrower's capital to any Person other than to the Sponsor and the Equity Holder.

The Company satisfactorily complied with the covenants above mentioned during the terms of the contract.

As of December 31, 2017, the Company has recognized restricted cash by an amount of \$68,165, which is obtained through debt and consists of cash available for the construction of the "El Encino - La Laguna" pipeline.

As of December 31, 2018, the Company has recognized restricted cash by an amount of \$51,812, which is obtained through debt and consists of cash available for the interest payment of the same.

(b) On December 26, 2017, the Company executed a hybrid financing composed of:

a. 14 year term loan with the following Financial Institutions as Lenders:

1. BNP Paribas Securities Corp.
2. ING Capital LLC
3. Norddeutsche Landesbank Girozentrale, New York Branch
4. Mizuho Bank, Ltd.
5. Sabcapital, S. A. de C. V. S.O.F.O.M. E.R.

Term Loan:	\$	255,000
Debt Service Reserve Letter of Credit:		30,000
Transportation Agreement Letter of Credit:		79,800

The Company executed a Note Purchase Agreement in the international market amounting \$450,000, net of transaction costs incurred amounting to \$5,258 maturing on April 30, 2041. Interest on the Note Purchase Agreement are payable semi-annually at a fixed rate of 5.465% per annum (effective interest rate of 5.5659%) starting on July 31, 2018. The net proceeds from the issuance of the Note Purchase Agreement and Credit Agreement were used to repay in full the previously Credit Facility Syndicated and interest rate SWAPS contracted. (See Note 10).

On June 12, 2018, the Company executed an amended and restated credit agreement and note purchase agreement. The funding of Credit and Notes was done on June 21, 2018. The net proceeds of the funds were used to repay in full the previous Credit Facility and interest rate SWAPS (Note 10). As part of this prepayment, it was paid a penalty of \$65 recognized as finance cost in the income statement.

Under The Mexican Income Tax Law, payments of interest made in respect of the Credit Agreement and Notes (including original issue discount are deemed to be interest) to a Non-Mexican holder will be subject to a withholding tax rate from 4.9% to 10% under certain conditions. Interest paid is subject to a withholding tax rate of 4.9%.

During 2018, the Company has made a payment to the principal by an amount of \$14,584.

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(c) On May 29, 2015, the Company entered into a credit facility in an aggregate principal amount not exceeding MXP 1,600 million (\$81 million) with Banco Nacional de Comercio Exterior, Sociedad Nacional de Crédito, Institución de Banca de Desarrollo (Bancomext) to finance the VAT related to the expenditures for the construction of the “El Encino-La Laguna” pipeline. The Company agreed to pay the entire balance of the VAT credit, at the latest on the due date (5 years from the first disposition). As of September 29, 2018, the Company had withdrawn MXP 1,616 million (\$82 million). As of December 31, 2017, the Company had withdrawn MXP 1,302 million (\$66 million) (at nominal value).

On December 15, 2017, the Company signed an amendment agreement, where it was agreed an extraordinary withdrawn for Section B, for an amount of MXP 52 million (\$3 million).

The Company agreed to pay this loan with the VAT reimbursements, for which a refund request has been filed with the tax authority (VAT generated during the construction of all the investments involved in the project work and expenses) by the Company. The aforementioned loan established certain positive and negative covenants, which were duly met by the Company.

As of December 31, 2017, the Company has withdrawn MXP 1,249 million (\$63.5 million), at nominal value and made payments to the principal by an amount of MXP 1,067 million (\$54 million).

On September 26, 2018, this credit facility was liquidated by the total amount.

Fair value

For the majority of the borrowings, the fair values are not materially different to their carrying amounts, since the interest payable on those borrowings is either close to current market rates or the borrowings are of a short-term nature. Material differences are identified only for the following borrowings:

	<u>December 31, 2018</u>		<u>December 31, 2017</u>	
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Carrying amount</u>	<u>Fair value</u>
Note Purchase Agreement	\$ 455,076	\$ 476,133	\$ -	\$ -
Credit facility - Syndicated	236,474	231,026	570,541	574,385
Credit facility - VAT	-	-	8,693	8,624
Total	<u>\$ 691,550</u>	<u>\$ 707,159</u>	<u>\$ 579,234</u>	<u>\$ 583,009</u>

Reconciliation of financing activities:

<u>December 31, 2018:</u>	<u>Note Purchase Agreement</u>	<u>Credit Facility Syndicated</u>	<u>Credit Facility VAT</u>	<u>Total</u>
Net debt as at January 1, 2018	\$ -	\$ 570,541	\$ 8,693	\$ 579,234
Cash flows Acquisitions	444,829	246,430	15,993	707,252
Principal payments	-	(585,014)	(24,621)	(609,635)
Interests	13,120	17,004	814	30,938 ⁽¹⁾
Interest payments	(2,873)	(12,487)	(879)	(16,239)
Ending balance December 31, 2018	<u>\$ 455,076</u>	<u>\$ 236,474</u>	<u>\$ -</u>	<u>\$ 691,550</u>

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⁽¹⁾ In 2018, \$7,996 of accrued interest was capitalized as part of construction of the gas pipeline. (See Note 21).

Note 16 - Partners' equity:

a. Social participation

During 2018, the Partner's meeting approved the following resolutions:

- On September 10, 2018, approved an increase of the variable portion of social participation by an amount of \$641.

After the increase and previous resolutions, the social participation as of December 31, 2018 and 2017 is integrated as follows:

At December 31, 2018

	<u>Social units</u>	<u>Fixed portion of social participation Series "A"</u>	<u>Variable portion of social participation Series "B"</u>	<u>Total</u>
Fermaca El Encino-La Laguna, S. de R. L. de C. V. ^(a)	2	\$ -	\$ 26,449	\$ 26,449
Fermaca LNG del Caribe, S. de R. L. de C. V.	<u>1</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>3</u>	<u>\$ -</u>	<u>\$ 26,449</u>	<u>\$ 26,449</u>

At December 31, 2017

	<u>Social units</u>	<u>Fixed portion of social participation Series "A"</u>	<u>Variable portion of social participation Series "B"</u>	<u>Total</u>
Fermaca El Encino-La Laguna, S. de R. L. de C. V. ^(a)	1	\$ -	\$ 25,808	\$ 25,808
Fermaca LNG del Caribe, S. de R. L. de C. V.	<u>1</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>2</u>	<u>\$ -</u>	<u>\$ 25,808</u>	<u>\$ 25,808</u>

As of December 31, 2018 and 2017, the fixed portion of social participation has not been paid.

^(a) As of December 31, 2018 and 2017, two social parts and a social part, respectively, are pledged as collateral to Deutsche Bank México, S. A., in connection with the bank debt (Note 15). These social parts are deposited in a Trust created for this purpose, which is managed by Deutsche Bank Mexico (Fiduciary).

- b. Net income is subject to the legal provision requiring that at least 5% of the income for each year is set aside to increase the legal reserve until it is equal to a fifth of the amount of capital paid. At December 31, 2018, the legal reserve has not been created.

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- c. Dividends to be paid will be free from income tax if they come from Net Tax Profit Account (CUFIN, by its Spanish acronym). Any dividends paid in excess of CUFIN will cause a tax equivalent to 42.86%. The current tax is payable by the Company and may be credited against its income tax of the year or the following two years. Dividends paid coming from profit previously taxed by income tax are not subject to tax withholding or additional tax payment. As of 2013, Income Tax Law sets the obligation of keeping CUFIN with profit generated up to December 31, 2013, and starting another CUFIN with profit generated from January 1, 2014.

Note 17 - Revenue from contracts with customers:

Our revenue from contracts with customers are mainly related to our natural gas transportation agreement. The revenue from contracts with customers for the years ended December 31, 2018 and 2017 is shown below:

a. Revenue from contracts with customers

	<u>2018</u>	<u>2017</u>
Reserved capacity and Natural gas transportation services	<u>\$ 85,403</u>	<u>\$ 55,128</u>

b. Unsatisfied long-term contracts

As of December 31, 2018, the aggregate amount of the transaction price of the unsatisfied performance obligations resulting from reserved capacity by an amount of \$2,079,956 (with remaining period of 25 years).

The amount showed before include a financing component, which will be recognized as financing expense or financing income in accordance with its nature year after year.

As of December 31, 2017, as permitted under the transitional provisions in IFRS 15, the transaction price of the unsatisfied performance obligations is not disclosed.

Management expects that transaction price allocated to the unsatisfied contracts as of December 31, 2018 will be recognized as revenue during the next reporting period by an amount of \$85,403. The remaining will be recognized after the 2019 financial year ratably over the corresponding years by an amount of \$1,994,553.

As permitted under IFRS 15, the transaction price of the unsatisfied contracts where the right to invoice practical expedient is applicable, is not disclosed.

c. Assets and liabilities related to contracts with customers

The Company has recognized an asset related to contracts with customers by an amount of \$27,319.

In addition to the contract balance disclosed above, the Company has not had an asset in relation to costs to fulfil a long-term contract.

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Note 18 - Cost of services:

Following is an analysis of the most relevant cost of services for the years ended December 31, 2018 and 2017, classified by function in the statement of comprehensive income:

	<u>2018</u>	<u>2017</u>
Depreciation and amortization	\$ 11,000	\$ -
Pipeline maintenance	1,553	-
Insurance	<u>488</u>	<u>-</u>
	<u>\$ 13,041</u>	<u>\$ -</u>

Note 19 - Administrative expenses:

Following is an analysis of the most relevant development and administrative expenses for the years ended December 31, 2018 and 2017, classified by function in the statement of comprehensive income:

	<u>2018</u>	<u>2017</u>
Project development ^(a)	<u>\$ 3,758</u>	<u>\$ -</u>
Fees	\$ 1,059	\$ 883
General expenses ^(b)	652	565
Other expenses	41	13
Leases	21	17
Depreciation	<u>14</u>	<u>-</u>
	<u>\$ 1,787</u>	<u>\$ 1,478</u>

^(a) Non-capitalizable costs for the development of the project.

^(b) General expenses are mainly composed of administrative services, subscriptions and expenses for the operation.

Note 20 - Other Income:

Other incomes for the years ended December 31, 2018 and 2017, is comprised as follows:

	<u>2018</u>	<u>2017</u>
Inflation adjustment of VAT reimbursed	\$ 1,315	\$ 3,942
Other	<u>-</u>	<u>116</u>
	<u>\$ 1,315</u>	<u>\$ 4,058</u>

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Note 21 - Finance incomes and (costs):

An analysis of the finance income and (costs) for the years ended December 31, 2018 and 2017 is shown as follows:

<u>Finance costs:</u>	<u>2018</u>	<u>2017</u>
Interest expense:		
Bank borrowings (Note 15)	(\$ 30,938)	(\$ 22,937)
Related parties (Note 11)	<u>(10,594)</u>	<u>(9,710)</u>
	(41,532)	(32,647)
Fair value loss on interest rate swaps designated as cash flow hedges - transfer from OCI (Notes 5 and 10)	(53,000)	-
Loss on valuation of derivatives (Notes 5 and 10)	(2,612)	-
Other finance costs (*)	<u>(9,146)</u>	<u>(1,778)</u>
Total finance costs	(106,290)	(34,425)
Less: amounts capitalized on qualifying assets	<u>11,479</u>	<u>32,528</u>
Finance costs in the statement of comprehensive income	<u>(\$ 94,811)</u>	<u>(\$ 1,897)</u>
<u>Finance income:</u>		
Gain on valuation of derivatives	\$ 411	\$ 1
Interest income on short-term bank deposits	329	31
Interest income on loans to related parties (Note 11)	4	4
Foreign exchange income	<u>1,993</u>	<u>1,327</u>
Finance income in the statement of comprehensive income	<u>2,737</u>	<u>1,363</u>
Finance cost - Net	<u>(\$ 92,074)</u>	<u>(\$ 534)</u>

(*) Commissions for use of letters of credit

Note 22 - Income taxes:

- a. Income tax of the year is calculated by applying a 30% rate on the taxable profit. In 2018, the Company determined a tax loss of \$25,879 (tax profit of \$84,292 in 2017). Tax income differs from accounting income, mainly due to items accumulating over time a deducted different for accounting and tax proposes, such as recognition of the effects of inflation for tax purposes, as well as items affecting only the accounting or the tax income.
- b. The income tax provision is analyzed as follows:

	<u>Year ended on</u> <u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Deferred income tax benefit	<u>\$ 1,053</u>	<u>\$ 12,805</u>

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- c. At December 31, 2018 the Company had cumulative tax losses carry forwards for a total of \$110,744 whose right to be amortized against future taxable income expires according to the following schedule:

<u>Year of loss</u>	<u>Restated Amount</u>	<u>Year of expiration</u>
2016	\$ 84,060	2026
2018	<u>26,684</u>	2028
Total	<u>\$ 110,744</u>	

Deferred income tax assets are recognized for tax loss carry-forwards (NOL's) to the extent that realization of the tax benefit related to future tax benefits is probable.

- d. At December 31, 2018 and 2017, the main temporary differences on which the deferred income tax asset (liability) was recognized are analyzed as follows:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Property and equipment	(\$ 145,928)	(\$ 162,690)
Revenue from contract assets	(27,319)	-
Prepaid expenses	(16,841)	-
Derivative financial instruments	(3,821)	44,025
Tax losses carry forwards	110,744	79,873
Other items	<u>107</u>	<u>73</u>
	(83,058)	(38,719)
Income tax payable rate	<u>30%</u>	<u>30%</u>
Deferred tax liabilities	<u>(\$ 24,917)</u>	<u>(\$ 11,615)</u>

Following is the deferred income tax recognized outside the results of the period, in the other comprehensive loss:

	<u>2018</u>	<u>2017</u>
Derivative financial instruments	<u>(\$ 1,146)</u>	<u>\$ 13,209</u>

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e. Following is the reconciliation between income tax payable and the effective rate:

	<u>2018</u>	<u>2017</u>
(Loss) profit before income tax	(\$23,942)	\$ 57,174
Income tax legal rate	<u>30%</u>	<u>30%</u>
Income tax at legal rate	(7,183)	17,152
Plus (less) effect of the following items on the income tax:		
Non-deductible expenses	9	65
Annual inflation adjustment	10,833	12,170
Valuation of financial instruments (ineffective portion of the hedge (Note 10)	(8,863)	(1,271)
Tax losses	-	(24,882)
Derivative financial instruments	1,146	(13,207)
Other items	<u>3,005</u>	<u>(2,832)</u>
Deferred Income tax	<u>(\$ 1,053)</u>	<u>(\$12,805)</u>

Note 23 - Commitments and contingencies:

a. Commitments

In January 2015, El Encino entered into a Transportation Service Agreement with CFE that sets forth the basis for a long term “Ship or Pay” agreement under the following conditions:

Duration: 25 years.

Minimum Reserved Capacity: 1,500 MCFD.

Current Monthly revenue: \$3,000 increasing over time according to rate.

On April 30, 2018, the Commercial Operating Date was approved by CFE. Therefore, on May 1, 2018, the capitalization of the El Encino gas pipeline was carried out.

The start of operations has changed based on the events described in Note 2. As indicated in said note, as a force majeure event was documented and confirmed as provided in the agreement, El Encino has not and will not incur in any penalty for this matter.

As of December 31, 2017, the Company has contracted a letter of credit with Banco Nacional de Comercio Exterior, S. N. C., in guarantee of the obligations resulting from the natural gas transportation services contract with CFE, in the amount of \$90,000. The letter of credit is renewable annually.

As of December 31, 2018 was modified to \$ 79,800. The letter of credit is contracted with BNP, Mizuho and ING and was issued by Santander.

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b. Contingencies:

- i. During the normal course of its operations, the Company has taken no uncertain or aggressive tax positions. Likewise, the Company does not anticipate that significant unrecognized tax benefits will be recognized over the next 12 months. The Company is not currently subject to any tax audit process.
- ii. The Company's activity is natural gas transportation, which requires the corresponding permit issued by the CRE. Changes in the regulatory environment could affect the operation of the Company.

Note 24 - Events after the financial statements:

In the first quarter of 2019, the Company has received VAT refunds equivalent to \$3,714. (Includes the corresponding updates).



Daniel Elguea Solis
Chief Financial Officer



Leticia Lara Torres
Controller