Joint Stock Company
For Development of International
Electrical Relations
RAO UES International
Consolidated Financial Statements
for the year ended 31 December 2004

Contents

KPMG Limited

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Independent Auditors' Report

Board of Directors
Joint Stock Company For Development of International Electrical Relations RAO UES International

We have audited the accompanying consolidated balance sheet of Joint Stock Company For Development of International Electrical Relations RAO UES International and its subsidiaries (the "Group") as of 31 December 2004 and the related consolidated statements of income, changes in equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Except as described in the following paragraph, we conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

One entity acquired by the Group in 2003 has not maintained adequate accounting records regarding property, plant and equipment as required by International Financial Reporting Standards IAS 16 *Property, Plant and Equipment*. In addition, the Group has included in its cash flow testing, forming a part of valuation of property, plant and equipment, certain capital expenditures to acquire new assets aimed to improve performance of this entity. This treatment is not in accordance with International Financial Reporting Standards IAS 36 *Impairment of Assets*. It was impracticable to satisfy ourselves as to the fairness of the carrying amount of property, plant and equipment of EUR 16,841 thousand and EUR 1,028 thousand included in the accompanying consolidated balance sheet as at 31 December 2004 and 2003, respectively, and the related depreciation expense in the consolidated income statement and the related effect on the deferred tax balance and deferred tax expense.

Furthermore, as described in note 17 the Group has determined the amortised cost of certain loans with reference to its own internally assessed repayment schedule. International Financial Reporting Standards IAS 39 *Financial Instruments: Recognition and Measurement* requires amortised cost to be calculated based the contractual repayment dates for the loans in the third party loan contracts. Had the Group amortised these loans in accordance with the third party contractual repayment dates, the loans payable would have been increased by EUR 30,642 thousand and EUR 28,121 thousand, deferred tax liabilities would have been decreased by EUR 6,128 thousand and EUR 5,624 thousand, as at 31 December 2004 and 2003, respectively. Furthermore, interest expense would have been increased by EUR 2,521 thousand, net gain on foreign exchange transactions would have been increased by EUR 504 thousand, and net profit would have been decreased by EUR 2,017 thousand for the year ended 31 December 2004. Furthermore, the assessed goodwill as at the date of acquisition of the Georgian entities and related impairment of goodwill would have been increased by EUR 22,497 thousand and net profit for the year ended 31 December 2003 and retained earnings as at 31 December 2004 would have been decreased by EUR 22,497 thousand.

KPMG

One Group entity did not provide for deferred taxation as required by International Financial Reporting Standards IAS 12 *Income Taxes*. The effect of this departure on taxation, net profit and retained earnings as at and for the year ended 31 December 2004 has not been determined.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had it been practicable to obtain sufficient appropriate audit evidence as described in third paragraph, and except for the effect of the matters described in the fourth in fifth paragraphs, the financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2004 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Limited

KPMG Limited
6 December 2005

	Note	2004 '000 EUR	2003 '000 EUR restated
Revenues			
Foreign sales		362,588	281,030
Domestic sales		121,733	65,589
Other		8,002	5,502
Total revenues		**492,323**	**352,121**
Expenses			
Purchased power		(326,788)	(243,967)
Agency fees		(31,936)	(8,156)
Administrative and general expenses		(19,462)	(8,644)
Fuel expenses		(19,350)	(13,080)
Wages and payroll taxes		(16,692)	(6,584)
Transmission fees		(13,194)	(5,169)
Depreciation and amortisation	8,9	(9,153)	(2,290)
Provision for impairment of accounts receivable	13	(6,977)	–
Generation assets maintenance		(6,222)	(3,799)
Taxes other than on income		(3,408)	(299)
Custom taxes		(2,620)	(1,599)
Social expenditures		(283)	(149)
Gain/(loss) on disposal of fixed assets		324	(24)
Impairment of goodwill		–	(35,840)
Other expenses		(5,401)	(9,411)
Total expenses		**(461,162)**	**(339,011)**
Profit from operations		**31,161**	**13,110**
Net financing income	6	8,706	7,430
Profit before tax and minority interest		**39,867**	**20,540**
Income tax expense	7	(14,452)	(13,247)
Profit before minority interest		**25,415**	**7,293**
Minority interest		(519)	(3)
Net profit for the year		**24,896**	**7,290**
Basic and diluted earnings per share	20	41.49 EUR	12.15 EUR

The consolidated financial statements were approved on 6 December 2005:

General Director

Dod E.V.

Chief Accountant

Chesnokova A.O.

The consolidated income statement is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 9 to 38.

	Note	2004 '000 EUR	2003 '000 EUR restated
ASSETS			
Non-current assets			
Property, plant and equipment	8	69,768	51,899
Intangible assets	9	4,129	4,622
Investments	10	39,980	–
Deferred tax assets	11	1,010	839
Other non-current assets		1,692	2,443
		116,579	**59,803**
Current assets			
Investments	10	8,821	–
Inventories	12	7,086	6,112
Trade and other receivables	13	92,458	99,824
Value added tax recoverable		7,465	2,208
Other current assets	14	11,921	8,363
Cash and cash equivalents	15	18,733	13,724
		146,484	**130,231**
Total assets		**263,063**	**190,034**
EQUITY AND LIABILITIES			
Equity			
Share capital	16	1,803	1,803
Revaluation reserve		11,186	–
Foreign currency translation reserve		(3,071)	(2,105)
Retained earnings		27,372	10,852
		37,290	**10,550**
Minority interest		**537**	**18**
Non-current liabilities			
Loans and borrowings	17	35,839	28,910
Deferred tax liabilities	11	24,580	20,797
		60,419	**49,707**
Current liabilities			
Loans and borrowings	17	64,031	10,735
Taxes payable	18	21,072	20,062
Trade and other payables	19	79,714	98,962
		164,817	**129,759**
Total equity and liabilities		**263,063**	**190,034**

The consolidated balance sheet is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 6 to 38.

	2004 '000 EUR	2003 '000 EUR Restated
OPERATING ACTIVITIES		
Profit before tax and minority interest	**39,867**	**20,540**
Adjustments for:		
Depreciation and amortisation	9,153	2,290
Impairment of goodwill	-	35,840
Provision for impairment of accounts receivable	6,977	-
(Gain)/loss on disposal of property, plant and equipment	(324)	24
Loss from change of fair value of derivative financial instruments	-	(6,325)
(Gain)/loss on foreign exchange	(15,872)	2,384
Interest income	(1,355)	(10,994)
Interest expense	8,521	4,661
Other	(261)	289
Operating profit before changes in working capital	**46,706**	**48,709**
Increase in inventories	(974)	(4,798)
Decrease/(increase) in trade and other receivables	389	(80,456)
(Increase)/decrease in value added tax recoverable	(5,257)	353
Increase in other current assets	(3,558)	(1,794)
Decrease/(increase) in other non-current assets	751	(2,111)
(Decrease)/increase in trade and other payables	(19,248)	19,096
(Decrease)/increase in taxes payable other than profit tax	(1,098)	13,293
Cash flows from operations before income taxes	**17,711**	**(7,708)**
Income taxes paid	(12,032)	(9,225)
Cash flows from operating activities	**5,679**	**(16,933)**
INVESTING ACTIVITIES		
Proceeds from disposal of property, plant and equipment	3,040	3
Acquisition of property, plant and equipment	(11,106)	(605)
Acquisition of subsidiaries, net of cash acquired	-	(18,813)
Acquisition of investments	(47,956)	-
Cash flows from investing activities	**(56,022)**	**(19,415)**
FINANCING ACTIVITIES		
Net proceeds from borrowings	70,494	44,976
Interest paid	(6,766)	(3,742)
Dividends paid	(8,376)	-
Cash flows from financing activities	**55,352**	**41,234**
Net increase in cash and cash equivalents	**5,009**	**4,886**
Cash and cash equivalents at beginning of year	13,724	8,838
Effect of inflation on cash and cash equivalents	-	-
Cash and cash equivalents at end of year (note 15)	**18,733**	**13,724**

The consolidated statement of cash flows is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 7 to 38.

'000 EUR	Share capital	Foreign currency translation reserve	Revaluation reserve	Retained earnings	Total
Balance at 1 January 2003	2,006	–	–	3,962	5,968
Net profit for the period as previously reported	–	–	–	39,102	39,102
Restatement (see note 4)	–	–	–	(31,812)	(31,812)
Net profit for the period as restated	–	–	–	7,290	7,290
Foreign currency translation	(203)	(2,105)	–	(400)	(2,708)
Balance at 31 December 2003 as previously reported	**1,803**	**(2,105)**	–	**42,664**	**42,362**
Restatement (note 4)	–	–	–	**(31,812)**	**(31,812)**
Balance at 31 December 2003 as restated	**1,803**	**(2,105)**	–	**10,852**	**10,550**
Net profit for the period	–	–	–	24,896	24,896
Foreign currency translation	–	(966)	–	–	(966)
Revaluation reserve	–	–	11,186	–	11,186
Dividends	–	–	–	(8,376)	(8,376)
Balance at 31 December 2004	**1,803**	**(3,071)**	**11,186**	**27,372**	**37,290**

The consolidated statement of changes in equity is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 8 to 38.

1 Background

(a) Organisation and operations

Joint Stock Company for Development of International Electrical Relations – JSC "RAO UES International" (the "Parent Company") and its subsidiaries (together referred to as the "Group") comprise Russian Federation joint stock companies as defined in the Civil Code of the Russian Federation, and companies located abroad. The Parent Company was established in the Russian Federation on 20 August 1996 in accordance with the decision of its majority shareholder, Russian Open Joint Stock Company for Energy and Electrification Unified Energy System of Russia ("RAO UES").

RAO UES is a holder of certain significant electricity power generation, transmission and distribution assets in the Russian Federation. At 31 December 2004, the state owned 52.7 percent of RAO UES and 100 percent of FGUP "Rosenergoatom". RAO UES and FGUP "Rosenergoatom" own 60 percent and 40 percent, respectively, of the voting ordinary shares of JSC "RAO UES International".

OAO "RAO UES International" performs the following types of business activity:

- Export of electricity, purchased on the domestic market;
- Sales of electricity, purchased abroad, on the Russian market;
- Sales of electricity, purchased abroad, to foreign customers without crossing of the border of the Russian Federation ("Foreign Sales");
- Own production of electricity for further sales on the domestic market and for export.

The Group generates electricity using the Iriklinskaya GRES (a division of OAO Orenburgenergo, an entity controlled by RAO UES), a facility operated under an operating lease. The Group reimburses to JSC Orenburgenergo operational expenses incurred in the course of electricity production on the leased facility.

In October 2002 JSC "RAO UES International" founded RAO Nordic Oy, a wholly owned subsidiary, to operate as a trading company on the Nord Pool (Scandinavian energy exchange). As disclosed in note 4, in 2003 the Group, through RAO Nordic Oy, made several acquisitions of foreign assets.

At 31 December 2004, the number of employees of the Group was 2,901 (2003: 3,016).

The Parent Company's registered office is at 137, Moskovskoe shosse, 302025, Oryol, Russia.

(b) Group's business environment

The government of the Russian Federation directly affects the Group's operations through regulation by the Federal Energy Commission ("FEC"), with respect to energy purchases and sales on the Russian market. The operations of the Georgian and Armenian subsidiaries of the Group are regulated by the Energy Regulatory Commission of each jurisdiction respectively, which regulates the tariffs charged for sale of electricity. As described in note 24, the governments' economic, social and other policies in these countries could have material effects on the operations of the Group.

Russia, Georgia and Armenia have been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. Consequently, operations in Russia, Georgia and Armenia involve risks that typically do not exist in other markets. The accompanying consolidated financial statements reflect management's assessment of the impact of the business environment in these countries on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

2 Basis of preparation

(a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and related interpretations adopted by the International Accounting Standards Board ("IASB").

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that property, plant and equipment is stated at revalued amounts and available for sale investments are stated at fair value.

(c) Measurement and presentation currency

The national currency of the Russian Federation is the Russian Rouble ("RUR"), which is the Parent Company's measurement currency because it reflects the economic substance of the underlying events and circumstances of the Parent Company.

These consolidated financial statements are presented in European Euro ("EUR") since management believes that this currency is more useful for the users of the consolidated financial statements. All financial information presented in EUR has been rounded to the nearest thousand.

The RUR is not a readily convertible currency outside the Russian Federation and, accordingly, any conversion of RUR to EUR should not be construed as a representation that the RUR amounts have been, could be, or will be in the future, convertible into EUR at the exchange rate disclosed, or at any other exchange rate.

(d) Going concern

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realisation of assets and the satisfaction of liabilities in the normal course of business. The accompanying consolidated financial statements do not include any adjustments should the Group be unable to continue as a going concern.

(e) Use of estimates and judgements

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with IFRS. Actual results could differ from those estimates.

In particular, information about significant areas of estimation uncertainty and critical judgments made by management in preparing these consolidated financial statements is described in the following notes:

- Note 4 – Principal subsidiaries and foreign operations; and
- Note 24 - Contingencies.

3 Significant accounting policies

The following significant accounting policies have been applied in the preparation of the consolidated financial statements. These accounting policies have been consistently applied, except for translation of financial statements of foreign subsidiaries which has been performed in accordance with the revised International Financial Reporting Standard IAS 21 *The Effects of Changes in Foreign Exchange Rates*. The change had no effect on financial position or net profit for the year.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are those enterprises controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

(ii) Transactions eliminated on consolidation

Intragroup balances and transactions, and any unrealised gains arising from intragroup transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains except that they are only eliminated to the extent that there is no evidence of impairment.

(b) Foreign currencies

Transactions in foreign currencies are translated to the respective measurement currency of each enterprise in the Group at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the measurement currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies that are stated at historical cost are translated to the measurement currency at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the measurement currency at the foreign exchange rate ruling at the dates the fair values were determined. Foreign exchange differences arising on translation are recognised in the income statement.

The assets and liabilities of foreign entities are translated into RUR at the exchange rate at the end of the year. Revenues and expenses are translated into RUR using rates approximating exchange rates at the dates of the transactions. The resulting exchange difference is recorded directly in equity in the foreign currency translation reserve.

The consolidated financial statements have been translated from RUR to EUR as follows:

- Assets, liabilities and equity items as at 31 December 2003 have been translated at the official rate of the Central Bank of the Russian Federation as at 31 December 2003 of RUR 36.8240 to EUR 1.
- Assets and liabilities as at 31 December 2004 have been translated at the official rate of the Central Bank of the Russian Federation as at 31 December 2004 of RUR 37.8104 to EUR°1.
- Equity items, revenues and expenses for the year ended 31 December 2004 have been translated using rates approximating the exchange rates at the dates of the transactions. The resulting exchange difference has been recorded directly in equity in the foreign currency translation reserve.

(c) Property, plant and equipment

(i) Owned assets

Property, plant and equipment is stated at revalued amounts less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads. In prior periods property plant and equipment was stated at cost.

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment.

(ii) Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses.

(iii) Subsequent expenditure

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, is capitalised with the carrying amount of the component being written off. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognised in the income statement as an expense as incurred.

(iv) Revaluation

A revaluation increase on an item of property, plant and equipment is recognised directly in equity except to the extent that it reverses a previous revaluation decrease recognised in the income statement, in which case it is recognised in the income statement. A revaluation decrease on an item of property, plant and equipment is recognised in the income statement except to the extent that it reverses a previous revaluation increase recognised directly in equity, in which case it is recognised directly in equity. When the asset is derecognised the revaluation surplus is transferred directly to retained earnings.

(v) Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. In respect of assets that are accounted for at deemed cost as a part of transition to IFRS in the subsidiaries the depreciation commenced at the transition date to IFRS. Land is not depreciated.

The estimated useful lives are as follows:

- Buildings — 50 years
- High and low voltage stations — 30 years
- Distribution equipment — 15 years.
- Fixtures and fittings — 5 years.

(d) Intangible assets

(i) Goodwill

Goodwill arising on an acquisition represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired.

Goodwill is stated at cost less accumulated amortisation (see below) and impairment losses.

(ii) Other intangible assets

Other intangible assets, which are acquired by the Group and which have finite useful lives, are stated at cost less accumulated amortisation and impairment losses. Expenditure on internally generated goodwill and brands is recognised in the income statement as an expense as incurred.

(iii) Subsequent expenditure

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

(iv) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets. Intangible assets are amortised from the date the asset is available for use.

The estimated useful lives of other intangible assets are 20 years.

(e) Investments

Investments are recognised (derecognised) when the Group obtains (loses) control over the contractual rights inherent in that asset.

Investments are classified as available-for-sale and are stated at fair value, with any resultant gain or loss being recognised in the income statement.

The fair value of available-for-sale investments is their quoted bid price at the balance sheet date. Investments in equity securities that are not quoted on a stock exchange, and where fair value cannot be estimated on a reasonable basis by other means, are stated at cost less impairment losses.

(f) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(g) Trade and other receivables

Trade and other receivables are stated at cost less impairment losses.

(h) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits.

(i) Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amounts are estimated.

An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

(i) Calculation of recoverable amount

The recoverable amount of the Group's held-to-maturity investments, and loans and receivables, is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. Receivables with a short duration are not discounted.

The recoverable amount of other assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(ii) Reversals of impairment

An impairment loss in respect of a held-to-maturity investment, loan or receivable is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

An impairment loss in respect of goodwill is not reversed unless the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(j) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(k) Loans and borrowings

Loans and borrowings are recognised initially at cost. Subsequent to initial recognition, loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

(l) Pension and post retirement benefits

The Group's mandatory contribution to the governmental pension scheme is expensed when incurred.

(m) Provisions

A provision is recognised in the balance sheet when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(n) Trade and other payables

Trade and other payables are stated at cost.

(o) Income tax

Income tax for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: initial recognition of assets or liabilities that affect neither accounting nor taxable profit; and investments in subsidiaries where the Parent Company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

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

(p) Revenues

Revenue from the sale of electricity is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer.

(q) Other expenses

(i) Operating leases

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

(ii) Net financing income

Net financing income comprise interest expense on borrowings, the accretion of interest on provisions, interest income on funds invested, dividend income, foreign exchange gains and losses, and gains and losses on the revaluation and disposal of investments held for trading and available-for-sale.

All interest and other costs incurred in connection with borrowings are expensed as incurred as part of net financing costs.

Interest income is recognised as it accrues, taking into account the effective yield on the asset.

(r) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

(s) Earnings per share

An earnings per share is determined by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

4 Principal subsidiaries and foreign operations

The principal subsidiaries consolidated in the Group's financial statements are disclosed in the table below:

Name	Location	Percent ownership	Principal activity
RAO Nordic Oy	Helsinki, Finland	100%	Electricity trading, holding company
JSC "Rossiyskaya energiya"	Kiev, Ukraine	90%	Electricity trading
JSC "RAO UES International Balkans"	Moscow, Russian Federation	76%	Electricity trading
JSC "MEK"	Yerevan, Armenia	90%	Electricity generation
"Mtkvari" Ltd.	Tbilisi, Georgia	100%	Electricity generation
JSC "Telasi"	Tbilisi, Georgia	75%	Electricity distribution
InterEnergo BV	Amsterdam, Netherlands	67%	Holding company
Silk Road Holdings BV	Amsterdam, Netherlands	100%	Holding company
Gardbani Holdings BV	Amsterdam, Netherlands	100%	Holding company
ES Georgia Holdings BV	Amsterdam, Netherlands	100%	Holding company

In 2003 the Group, through RAO Nordic Oy, has made a series of acquisitions in Armenia and Georgia. In allocating the purchase price, the Group estimated the fair value of the property plant and equipment acquired in Armenia and Georgia using the discounted cash flow method. This was not in compliance with IAS 22 *Business Combinations*, which require property, plant and equipment purchased under business combinations to be accounted for at market value of the individual assets or depreciated replacement cost, when there is no evidence of market value.

In 2005 the Group commissioned "Deloitte and Touche CIS" to independently appraise property, plant and equipment of its subsidiaries in Armenia and Georgia in order to determine the fair values of the acquisitions made in 2003 in compliance with IAS 22 *Business Combinations*. The appraisal has been performed as at the dates of acquisitions and 31 December 2004. The Group has also reassessed the fair value of certain other assets and liabilities of the acquired entities as of the date of acquisition.

The independent appraisal of the property, plant and equipment and the reassessment of the fair value of certain other assets and liabilities acquired in Armenia and Georgia resulted in the following restatement.

(a) ZAO MEK

In June 2003, RAO Nordic founded ZAO MEK, an entity located in Armenia. RAO Nordic owns a 90 percent interest in this entity. In September 2003, ZAO MEK purchased tangible assets of ZAO Sevan-Hrazdan Cascade ("SHC"), located in Armenia, for a consideration of US$ 25 million (EUR 20 million) payable immediately and EUR 17 million payable along with related interest over a period of 32 years commencing in 2009, together representing a net present value of EUR 22,228 thousand. The Group has set off the US$ 25 million (EUR 20 million) payable by assuming a liability of ZAO Armenian Nuclear Power Plant ("Armenian NPP"), a nuclear power plant owned by the government of Armenia, which is also the ultimate owner of the assets purchased, to the supplier of the nuclear fuel. The assumed liability is payable in equal installments over a period of 5 years, commencing in 2004. The assumed liability was redeemed in 2004 for EUR 15 million.

The assets arising from the acquisition were as follows:

	2003 as previously reported '000 EUR	**Adjustments to fair values**	**2003 as restated '000 EUR**
Property, plant and equipment	21,722	(9,413)	12,309
Inventory	767	–	767
Total assets acquired	22,489	(9,413)	13,076
Offset with receivable from Armenian Nuclear Power Plant cjsc	20,634	–	20,634
Payable to SHC	1,594	–	1,594
Total consideration given	22,228	–	22,228
(Negative goodwill)/Goodwill	(261)	9,413	9,152

The above acquisition was accounted for under the purchase method of accounting. The results of operations of the acquired businesses were included in the consolidated financial statements as of the respective date of acquisition. The purchase price of the foreign acquisition was translated at the exchange rate in effect at the date of acquisition.

(b) JSC Telasi and OOO Mtkvari

In August 2003, the Group acquired 100 percent of the shares of Silk Road Holdings B.V., Gardabani Holdings B.V. and ES Georgia Holdings B.V., all holding companies based in the Netherlands, from the AES Group. In addition, amounts receivable by the AES Group from the above companies amounting to USD 522 million (EUR 417 million), were acquired by the Group. The total consideration paid in cash was USD 23 million (EUR 18 million).

The above holding companies were, in their turn, the owners of shares in the following entities located in Georgia: 75 percent of AO Telasi, an entity which holds electricity distribution assets, and 100 percent of OOO Mtkvari, an entity which holds electricity generation assets and 50 percent of OOO Transenergy, an entity which exports energy from Georgia. ES Georgia Holdings B.V. was also the owner of the management rights of Khramesy 1 and 2 hydrogeneration plants.

The assets and liabilities arising from the acquisition are as follows:

	2003 as previously reported '000 EUR	**Adjustments to fair values**	**2003 as restated '000 EUR**
Property, plant and equipment	35,994	4,405	40,399
Intangible assets	4,954	–	4,954
Accounts receivable and prepayments	10,659	(8,378)	2,281
Other current assets	6,554	(1,205)	5,349
Cash and cash equivalents	869	–	869
Long-term loans and borrowings	–	(209)	(209)
Deferred tax liability	–	(18,771)	(18,771)
Accounts payable and accrued charges	(29,399)	–	(29,399)
Other current liabilities	(13,666)	1,187	(12,479)
Net assets acquired	15,965	(22,971)	(7,006)
Cash paid	19,682	–	19,682
Goodwill	3,717	22,971	26,688

The acquisition was accounted for under the purchase method of accounting. The results of operations of the acquired businesses were included in the consolidated financial statements as of the respective date of acquisition. The purchase price of the foreign acquisition was translated at the exchange rates in effect as the respective date of acquisition.

(c) Prior period adjustments

To account for the full effect of the acquisition accounting the comparative figures for 2003 have been restated.

Accounting for the full effect of the acquisition accounting had the following effect:

	At 31 December 2003 as previously reported EUR'000	**Reassessment of acquisition accounting EUR'000**	**At 1 January 2004 as restated EUR'000**
Balance sheet			
Property, plant and equipment	56,338	(4,439)	51,899
Trade and other receivables	108,202	(8,378)	99,824
Other current assets	9,568	(1,205)	8,363
Retained earnings	42,664	(31,812)	10,852
Long-term loans and borrowings	28,701	209	28,910
Deferred tax liabilities	2,026	18,771	20,797
Short-term loans and borrowings	12,533	(1,798)	10,735
Trade and other payables	98,354	608	98,962
Income statement			
Depreciation and amortisation	(2,601)	311	(2,290)
Impairment of goodwill	(3,717)	(32,123)	(35,840)
Net profit for the year	39,102	(31,812)	7,290

5 Segment reporting

Segment information is presented in respect of the Group's business and geographical segments.

The primary format, geography segments, is based on the Group's management and internal reporting structure.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

(a) Geographical segments

The generation and distribution segments operate in five principal geographical areas, Europe, Russia, Byelorussia, Georgia and Armenia. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets are based on the geographical location of the assets. In presenting the geographical segments in 2004 the Group added new segment – Armenia. The comparative information for geographical segments in 2003 was reclassified to conform with the 2004 presentation.

31 December 2004 '000 EUR	**Europe**	**Russia**	**Byelorussia**	**Georgia**	**Armenia**	**Other**	**Consolidation adjustments**	**Total**
Net revenues	164,395	120,369	52,336	98,476	7,150	60,027	(10,430)	492,323
Segment operating income/(loss)	9,060	15,690	(120)	(4,004)	2,388	4,570	3,577	31,161
Net financing income/(loss)	(857)	(819)	(329)	13,574	(71)	(166)	(2,626)	8,706
Profit/(loss) before tax and minority interest	8,203	14,871	(449)	9,570	2,317	4,404	951	39,867
Income tax expense	(3,105)	(6,008)	–	(3,559)	–	(1,825)	45	(14,452)
Minority interest – share of net result	–	–	–	–	(509)	(10)	–	(519)
Net profit/(loss)	5,098	8,863	(449)	6,011	1,808	2,569	996	**24,896**

31 December 2004 '000 EUR	**Europe**	**Russia**	**Byelorussia**	**Georgia**	**Armenia**	**Other**	**Consolidation adjustment**	**Total**
Segment total assets	48,196	54,959	15,632	127,554	15,045	454,494	(452,817)	263,063
Segment total liabilities	(51,773)	(114,039)	–	(459,457)	(8,039)	(377,974)	785,509	(225,773)
Depreciation	(72)	(122)	–	(8,356)	(553)	(134)	84	(9,153)
Capital expenditure	397	949	–	7,572	493	1,867	(172)	11,106

31 December 2003 **'000 EUR**	**Europe**	**Russia**	**Byelorussia**	**Georgia**	**Armenia**	**Other**	**Consolidation adjustments**	**Total**
Net revenues	108,069	66,673	96,261	21,785	6,941	58,274	(5,882)	352,121
Segment income/(loss)	16,449	10,377	3,087	(11,441)	(2,365)	13,078	(16,075)	13,110
Net financing income (unallocated)	–	–	–	–	–	–	–	7,430
Profit before tax and minority interest (unallocated)	–	–	–	–	–	–	–	20,540
Income tax expense (unallocated)	–	–	–	–	–	–	–	(13,247)
Minority interest – share of net result (unallocated)	–	–	–	–	–	–	–	(3)
Net profit	–	–	–	–	–			**7,290**

31 December 2003 **'000 EUR**	**Europe**	**Russia**	**Byelorussia**	**Georgia**	**Armenia**	**Other**	**Consolidation adjustment**	**Total**
Segment total assets	38,348	61,066	21,128	52,740	23,462	6,900	(13,610)	190,034
Segment total liabilities	(34,593)	(39,090)	(10,467)	(83,627)	(3,243)	(17,200)	8,736	(179,484)
Depreciation	(41)	(98)	–	(9,361)	(845)	(205)	8,260	(2,290)
Capital expenditure	167	249	–	103,406	9,564	11,290	(66,352)	58,324

(b) Business segments

The Group comprises the following main business segments:
Generation. The generation of electric power.
Distribution. The distribution of electric power.

31 December 2004 '000 EUR	Generation	Distribution	Other operations	Eliminations	Consolidated
Revenue	92,607	406,230	3,916	(10,430)	492,323
Total assets	234,788	112,394	368,698	(452,817)	263,063

31 December 2003 '000 EUR	Generation	Distribution	Other operations	Eliminations	Consolidated
Revenue	23,437	51,093	338,240	(60,649)	352,121
Total assets	66,261	142,644	120,543	(139,414)	190,034
Total acquisition cost for segment net assets	**22,228**	**19,682**	–	–	–

6 Net financing income

	2004 '000 EUR	2003 '000 EUR
Gain from change in the fair value of derivative instrument	-	3,481
Net gain/(loss) on foreign exchange transactions	15,872	(2,384)
Interest income	1,355	10,994
Interest expense	(8,521)	(4,661)
	8,706	**7,430**

7 Income tax expense

	2004 '000 EUR	2003 '000 EUR
Current tax expense		
Current year	11,721	10,853
Deferred tax expense		
Origination and reversal of temporary differences	1,488	2,394
Derecognition of tax loss carry forwards	1,243	–
	14,452	**13,247**

The Parent Company's applicable tax rate is the corporate income tax rate of 24% (2003: 24%). Income tax rate in Finland is 29% (2003: 29%), in Georgia is 20% (2003: 20%), in Armenia 20% (2003: 20%).

Reconciliation of effective tax rate:

	2004 '000 EUR	%	2003 '000 EUR	%
Profit before tax and minority interest	39,867		20,540	
Income tax at applicable tax rate	9,568	24	4,929	24
Effect of different tax rates	(129)	-	200	-
Net non-deductible/(non-taxable) items	3,641	15	8,118	40
Derecognition of tax loss carry forwards	1,243	(3)	–	–
	14,452	**36**	**13,247**	**64**

8 Property, plant and equipment

'000 EUR	Land and buildings	Plant and equipment	Fixtures and fittings	Construction in progress	Total
Revalued amount					
At 31 December 2003 as previously reported	26,563	29,387	2,935	–	58,885
Reassessment of acquisition accounting	4,644	(11,249)	1,606	5	(4,994)
At 1 January 2004 as restated	31,207	18,138	4,541	5	53,891
Additions	1,622	5,792	3,611	81	11,106
Revaluation	8,243	5,975	1,485	5	15,708
Disposals	–	(2,545)	(464)	–	(3,009)
Transfer	112	12	(101)	(23)	–
Translation difference	2,810	820	306	1	3,937
At 31 December 2004	43,994	28,192	9,378	69	81,633
Depreciation					
At 31 December 2003 as previously reported	(857)	(1,355)	(335)	–	(2,547)
Reassessment of acquisition accounting	684	(61)	(68)	–	555
At 1 January 2004 as restated	(173)	(1,416)	(403)	–	(1,992)
Depreciation charge	(1,326)	(5,367)	(1,523)	–	(8,216)
Revaluation	(342)	(1,186)	(198)		(1,726)
Disposals	–	201	92	–	293
Transfer	(15)	15	–	–	–
Translation difference	(42)	(139)	(43)	–	(224)
At 31 December 2004	(1,898)	(7,892)	(2,075)	–	(11,865)
Net book value					
At 31 December 2003 as previously reported	**25,706**	**28,032**	**2,600**	–	**56,338**
Reassessment of acquisition accounting	5,328	(11,310)	1,538	5	(4,439)
At 1 January 2004 as restated	**31,034**	**16,722**	**4,138**	**5**	**51,899**
At 31 December 2004	**42,096**	**20,300**	**7,303**	**69**	**69,768**

9 Intangible assets

	'000 EUR
Cost amount	
At 1 January 2004	4,693
Additions	771
Translation difference	(251)
At 31 December 2004	5,213
Amortisation	
At 1 January 2004	(71)
Amortisation charge	(937)
Translation difference	(76)
At 31 December 2004	(1,084)
Net book value	
At 1 January 2004	**4,622**
At 31 December 2004	**4,129**

Included in intangible assets as at 31 December 2004 are rights of the Group to manage the hydrogeneration plants Khramesi I and II in Georgia amounting to EUR 3,515 thousand (EUR 4,374 thousand as at 31 December 2003). The Group amortises the rights over their expected useful life of 10 years.

10 Investments

	2004 '000 EUR	2003 '000 EUR
Non-current		
Prepayment to Saint-Guidon Invest BV	36,684	–
Prepayment to Midland Resources Holding LTD	2,197	–
Loans issued to Khramesi I and II	647	
Receivable from Vorotani cjsc non current portion	319	–
Other	133	–
	39,980	–
Current		
Loans issued to "Armenian Nuclear Power Plant" CJSC	4,611	–
Receivable from Vorotani cjsc current portion	3,673	
Loans issued to Khramesi I and II	480	–
Other	57	–
	8,821	–

As at 31 December 2004 the prepayment made to Saint Guidon Invest, NV (Belgium) represents a portion of the future total consideration for the acquisition of 51% of total shares of "Moldavskaya GRES" CJSC (see note 26).

In 2004 the Group signed an agreement with Armenergo and Vorotani Hydroelectristations Compalex (AVH), companies located in Armenia, whereby it transferred the right to collect certain of its assets to AVH.

As at 31 December 2004 the prepayment made to Midland Resources Holding, LTD (Gurnsey) represents a portion of the future total consideration for acquisition of 100% of total shares of "Electric Networks of Armenia" CJSC (see note 26).

11 Deferred tax assets and liabilities

(a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following items:

'000 EUR	Assets		Liabilities		Net	
	2004	2003	2004	2003	2004	2003
Property, plant and equipment	33	–	(8,970)	(5,682)	(8,937)	(5,682)
Investments	194	–	–	–	194	–
Intangible assets	54	106	–	–	54	106
Deferred expenses	–	240	–	–	–	240
Trade and other receivables	2,705	1,360	(204)	–	2,501	1,360
Other current assets	20	66	(406)	–	(386)	66
Loans and borrowings	6	74	(17,072)	(16,099)	(17,066)	(16,025)
Trade and other payables	275	–	(982)	(1,936)	(707)	(1,936)
Other current liabilities	133	122	–	–	133	122
Tax loss carry-forwards	644	1,791	–	–	644	1,791
Tax assets/(liabilities)	4,064	3,759	(27,634)	(23,717)	(23,570)	(19,958)
Set-off tax	(3,054)	(2,920)	3,054	2,920	–	–
Net tax assets/(liabilities)	**1,010**	**839**	**(24,580)**	**(20,797)**	**(23,570)**	**(19,958)**

(b) Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of a Group entity located in Georgia and applicable to the following items:

	2004 '000 EUR	2003 '000 EUR
Deductible temporary differences	10,745	15,237
Tax loss carry-forwards	15,264	21,478
	26,009	**36,715**

The tax losses expire in 2007. The deductible temporary differences do not expire under current tax legislation. Deferred tax assets have not been recognised in respect of these items because it is not probable that the future taxable profit will be available in the respective Group entity against which the Group can utilise the benefits.

(c) Movement in temporary differences during the year

'000 EUR	At 31 December 2003 as previously reported	Reassessment of acquisition accounting	At 1 January 2004 as restated	Recognised in income	Recognised in equity	Translation difference	31 December 2004
Property, plant and equipment	(90)	(5,592)	(5,682)	(1,687)	(2,796)	1,228	(8,937)
Investments	–	–	–	205	–	(11)	194
Intangible assets	106	–	106	(52)	–	–	54
Deferred expenses	240	–	240	(246)	–	6	-
Trade and other receivables	353	1,007	1,360	1,185	–	(44)	2,501
Other current assets	66	–	66	(475)	–	23	(386)
Loans and borrowings	74	(16,099)	(16,025)	297	–	(1,338)	(17,066)
Trade and other payables	(1,936)	–	(1,936)	(715)	–	1,944	(707)
Other current liabilities	–	122	122	–	–	11	133
Tax loss carry-forwards	–	1,791	1,791	(1,243)	–	96	644
	(1,187)	**(18,771)**	**(19,958)**	**(2,731)**	**(2,796)**	**1,915**	**(23,570)**

12 Inventories

	2004 '000 EUR	2003 '000 EUR
Fuel production stock	898	1,613
Other inventories	6,188	4,499
	7,086	**6,112**

13 Trade and other receivables

	2004 '000 EUR	2003 '000 EUR restated
Accounts receivable – trade	135,255	138,092
Advances given to suppliers	14,707	9,186
Other receivables	5,567	8,620
	155,509	155,898
Provision for impairment for accounts receivable	(63,051)	(56,074)
	92,458	**99,824**

Provision for impairment

	2004 '000 EUR	2003 '000 EUR
At 1 January	56,074	1,764
Net increase in provision	6,977	54,310
At 31 December	**63,051**	**56,074**

14 Other current assets

	2004 '000 EUR	2003 '000 EUR restated
Taxes receivable	10,979	6,958
Deferred expenses	910	963
Income tax receivable	32	–
Other current assets	–	442
	11,921	**8,363**

15 Cash and cash equivalents

	2004 '000 EUR	2003 '000 EUR
Foreign currency bank accounts	10,233	10,834
Cash at bank and in hand	8,500	2,890
	18,733	**13,724**

16 Equity

(a) Share capital

The authorised, issued and fully paid share capital as at 31 December 2004 consisted of 600,000 ordinary shares (2003: 600,000) with nominal value of RUR 100 per share (2003: RUR 100).

In 2004 the Group additionally authorised issue of 4,400,500 shares with nominal value of 100 RUR per share.

(b) Dividends

In accordance with Russian legislation the Parent Company's distributable reserves are limited to the balance of accumulated retained earnings recorded in the Parent Company's statutory financial statements. As of 31 December 2004 the Parent Company had cumulative retained earnings, including the profit for the current year, of EUR 37,678 thousand (RUR 1,454,617) (2003: EUR 26,981 thousand (RUR 993,532 thousand)).

Dividends in relation to 2004 were declared on 29 June 2005 and amounted to EUR 8,728 thousand - EUR 14.50 per ordinary share (2003: EUR 8,376 thousand – EUR 13.96 per ordinary share).

17 Loans and borrowings

This note provides information about the contractual terms of the Group's loans and borrowings.

	2004 '000 EUR	2003 '000 EUR Restated
Non-current		
Secured loans and borrowings	33,025	–
Unsecured loans and borrowings	2,523	28,699
Notes payable	269	–
Finance lease obligation	22	211
	35,839	**28,910**
Current		
Secured loans and borrowings	57,691	–
Unsecured loans and borrowings	5,781	10,159
Current portion of finance lease obligation	559	576
	64,031	**10,735**

Terms and debt repayment schedule

'000 EUR	Total	Under 1 year	1-5 years	Over 5 years
Secured loans and borrowings:				
USD 45,000 thousand – variable at Libor + 3.75% (a)	33,025	–	33,025	–
USD 30,000 thousand – fixed at 9.5% (a)	22,017	22,017		
USD 40,000 thousand – variable at 3 month Libor + 4.25% (b)	29,465	29,465	–	–
RUR 234,750 thousand – fixed at 8% (a)	6,209	6,209	–	–
Unsecured loans and borrowings:				
Payable to KfW (c)	2,302	–	–	2,302
USD 54,000 thousand – fixed at 7% payable to the World Bank (d)	100	–	–	100
USD 14,000 thousand – fixed at 8.2% payable to EBRD (d)	40	–	–	40
EUR 36,360 thousand – fixed at 0.75% payable to KfW (d)	81	–	–	81
USD 4,000 thousand – fixed at 16%	2,969	2,969	–	–
USD 2,150 thousand – fixed at 18%	1,595	1,595	–	–
EUR 1,205 thousand - fixed at 0.75%	1,217	1,217	–	–
Finance lease liabilities:				
USD 750 thousand – fixed at 22% (e)	556	556	–	–
EUR 736 thousand – fixed at 3-32% (e)	25	3	22	–
Notes payable (f)	269	–	–	269
	99,870	**64,031**	**33,047**	**2,792**

(a) The loans are secured over the cash flows from the operating activities of the Group.

(b) Russian Open Joint Stock Company for Energy and Electrification Unified Energy System of Russia has provided guarantee for this loan.

(c) The long-term payable to KfW is stated at amortised cost. The Group used the contractual repayment dates and an effective interest rate of 18% to determine the amortised cost of the loan.

(d) The loan payable to the World Bank is in relation to the rehabilitation of Gardabani Thermal Power Station. The loan matures in 2027 and the parties to the loan contract are JSC Tbilsresi and the Ministry of Finance of Georgia.

The loan payable to EBRD is in relation to the rehabilitation of Gardabani Thermal Power Station. The loan matures in 2010 and the Ministry of Finance of Georgia is a party to the loan contract.

The loan payable to KfW is in relation to the rehabilitation of Gardabani Thermal Power Station. The loan matures in 2036 and the parties to the loan contract are the National Bank of Georgia, Ministry of Finance of Georgia and Ministry of Fuel and Energy of Georgia.

All three loans have common provisions in relation to setting priority for the repayment of the loans, as follows:

(i) First, the entity is required to cover all current operational costs.

(ii) Second, the entity is required to repay a principal and related interest of the loan payable to the parent company only up to a maximum aggregate principal amount of USD 50 million.

(iii) Third, the entity is required to repay the "Subordinated Liabilities", i.e. the loans to the World Bank, EBRD and KfW stipulated above.

(iv) Fourth, the entity is required to repay all principal and interest repayments due on the loans payable to the parent company above the USD 50 million aggregate principal cap set out in point (ii) above.

The Group considered the ability to settle existing and future liabilities of this entity in accordance with the above repayment priority and concluded that the repayment of these three loans will start not earlier than in 2028 with the last payment to be made in 2066. The fair value of these loans has been calculated by taking into account the future cash flows associated with the repayment of these loans, as assessed by the Group, and discounting them at a rate of 20%, approximating the equivalent market yield on loan borrowings by the entity at the date of inception of these loans.

(e) As of 31 December 2004, the Group had a number of long-term notes payable denominated in GEL. The fair value of these notes payable has been calculated by discounting them at a rate of 17.8%, approximating the equivalent yield on loan borrowings in the Georgian market, as follows:

Note	Face value	Fair value 2005	Date of maturity
'000 EUR			
Sakenergo	54,533	–	2098
Ortachela	159	–	2098
Zahesi	48	–	2098
Satskhenisi	30	–	2098
SSS Telasi	20	–	2098
Orbi	4	–	2098
Elektrogadatsema	856	269	2022
	55,650	**269**	

(f) Finance lease liabilities are payable as follows:

		2004			2003	
'000 EUR	**Payments**	**Interest**	**Principal**	**Payments**	**Interest**	**Principal**
Less than one year	588	29	559	847	271	576
Between one and five years	45	23	22	241	30	211
	633	**52**	**581**	**1,088**	**301**	**787**

For more information about the Group's exposure to interest rate and foreign currency risk, see note 21.

18 Taxes payable

	2004 '000 EUR	2003 '000 EUR
VAT	12,853	13,951
Income tax	1,973	2,284
Other taxes	6,246	3,827
	21,072	**20,062**

19 Trade and other payables

	2004 '000 EUR	2003 '000 EUR restated
Accounts payable – trade	63,535	44,488
Advances received	7,172	4,561
Provisions	5,760	522
Payable to Nordic Development Limited and Sevan-Hrazdan Cascade	–	17,520
Other payables	3,247	31,871
	79,714	**98,962**

20 Earnings per share

The calculation of basic earnings per share at 31 December 2004 was based on the net profit for the year and a weighted average number of ordinary shares (see note 16(a)) outstanding during the year.

In thousands of shares	**2004**	**2003**
Weighted average number of ordinary shares at 31 December	600	600
Net profit for the year, in EUR'000	24,896	7,290
Income per ordinary share – basic and diluted, in EUR	41.49	12.15

The Group has no potential dilutive ordinary shares.

21 Financial instruments

Exposure to credit, interest rate and currency risk arises in the normal course of the Group's business.

(a) Credit risk

The Group does not require collateral in respect of financial assets. Credit evaluations are performed on all customers, other than related parties, requiring credit over a certain amount.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

(b) Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of issuing new debt management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

(c) Foreign currency risk

The Group incurs foreign currency risk on sales, purchases and borrowings that are denominated in a currency other than RUR. The currencies giving rise to this risk are primarily USD, Georgian Lari and Armenian Dram. Management does not hedge the Group's exposure to foreign currency risk.

(d) Fair values

Fair value has been determined either by reference to the market value at the balance sheet date or by discounting the relevant cash flows using market interest rates for similar instruments. As a result of this exercise management believes that the fair value of its financial assets and liabilities approximates their carrying amounts.

22 Operating leases

Non-cancellable operating lease rentals are payable as follows:

	2004 '000 EUR	2003 '000 EUR
Less than one year	1,934	505
Between one and five years	3,658	
	5,592	**505**

The Group leases office premises in Moscow and power plant facilities of Iriklinskaya GRES (a division of OAO Orenburgenergo, an entity controlled by RAO UES).

The leases typically run for an initial period of one or five years (five years for premises rent), with an option to renew the lease after that date.

During the current year EUR 1,918 thousand (2003: EUR 505 thousand) was recognised as an expense in the income statement in respect of operating leases.

23 Commitments

(a) Investment commitments

In accordance with the agreement between the Group and the Government of Georgia, the Group has the following investment commitments which are denominated in millions US Dollars:

Year	Upgrade Investments USD million
2004	4
2005	7
2006	5.5
2007	5.5
2008	5.5

"Upgrade Investments" are any expenditure, expenses or investments of any kind related to the rehabilitation, or upgrade of the business infrastruture, including, without limitation, the rehabilitation, replacement, or upgrade of the transformers, cables, lines, fuses, vehicles, fault detection equipment, relay protection and automating substations.

(b) Sales commitments

The Group has entered into a contract with TOO Kazenergoresource, a contract with Belenergo and two contracts with TPK Sirius.

The contract with TOO Kazenergoresource specifies the supply of 1.44 million MWh of electricity per year. The price for electricity supplied was USD 22 per MWh for the period 1 July 2004 to 31 December 2004 and USD 24.7 per MWh from 1 January 2005. The contract shall be executed in USD or RUR as agreed with the supplier. The contract expires in March 2008.

The contract with Belenergo specifies the supply of 5,5 million MWh of electricity in 2005 and 4,5 million MWh of electricity in 2006 and 2007 each year. The price for electricity supplied is USD 20,3 per MWh. The contract shall be executed in USD or RUR. The contract expires in December 2007.

Two contracts with TPK Sirius specify the supply of 16.52 million MWh of electricity for the period 26 May 2004 to 31 December 2013. The price for electricity supplied was USD 18 for the period 26 May 2004 to 31 December 2004. According to the contracts terms the price of the actually supplied electrical power shall increase, if the actual hourly capacity and the quantity of the electrical power differ by more than 10% from the agreed figures. The price of the electrical power to be supplied is determined annually on the basis of the supplementary agreements. The contracts will be executed in USD.

(c) Purchase commitments

The Group concluded agreements with its electricity suppliers Ekibastuzskaya GRES-2 and OAO Elektricheskie Stantsii.

In August 2003 the Group concluded the agreement with its electricity supplier, Ekibastuzskaya GRES-2, for the period 2003-2007. The quantity of electricity to be supplied is 6 million MWh per annum. The price for the period September 2004 to December 2005 is fixed in the amount of RR 276 per MWh. The average price for the period 1 January 2006 to 31 December 2007 will be defined by an additional agreement, but the average price will not vary by more than 10 percent from the latest price.

The agreement with OAO Elektricheskie Stantsii specifies the supply of 1.5 million MWh per annum. The price is USD 6 per MWh. According to the contract terms the price may increase by not more than 10% per year, price revision is possible two times per year. The contract shall be executed in USD. The contract expires in December 2008.

24 Contingencies

(a) Political environment

The operations and earnings of the Group continue, from time to time and in varying degrees, to be affected by political, legislative, fiscal and regulatory developments, including those related to environmental protection, in Russia, Georgia and Armenia.

(b) Insurance

The insurance industry in Russia, Georgia and Armenia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

(c) Litigation

In the normal course of business the Group may be a party to legal actions. Other than as presented below, management of the Group is unaware of any actual, pending or threatened claims as at the signing date of these financial statements, which would have a material impact on the Group.

	2004 '000 EUR	2003 '000 EUR
Litigation with the State of Georgia	38,228	33,045
Customer complaints	506	1,050
Other	2,885	391
	41,619	**34,486**

The litigation with the State relates to the incorrect calculation of electricity consumption at one of the metering points. The Group has fully provided for the portion of the claim amounting to EUR 2,990 thousand. In relation to the remaining part of the overall claim of EUR 35,238 and EUR 2,885 thousand of other claims, the Group cannot reliably assess the outcome of the litigation process.

(d) Taxation contingencies

(i) Russia and CIS

The taxation system in the Russia and CIS countries is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

These circumstances may create tax risks in Russia and other CIS countries that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian and other CIS countries' tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these preliminary consolidated IFRS financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

The subsidiaries in Georgia and Armenia have various transactions with other related parties, where the pricing is determined in conjunction with other companies within the Shareholder Group. The pricing policy could give rise to transfer pricing risks. In management's opinion, the Group is in substantial compliance with the tax laws of Georgia and Armenia. However, relevant authorities could take different positions with regard to interpretive issues or court practice could develop adversely to positions taken by the Group and the effect could be significant.

(e) Existence of receivables from the state

A Group Company has recalculated a receivable from the state of EUR 2 million in relation to subsidies applicable to the 1999 financial year. However, due to the lack of documentation the state has not confirmed the amount as of the date of finalizing these consolidated financial statements and accordingly the receivable was not recognised in these consolidated financial statements.

25 Related party transactions

(a) Transactions with management and close family members

Total remuneration paid to the members of the Board of Directors for the year ended 31 December 2004 was EUR 173 thousand (2003: EUR 333 thousand).

(b) Transactions with other related parties

Related parties comprise the shareholders of the Parent Company and all other companies in which those shareholders, either individually or together, directly or indirectly, have a controlling interest. Sales with related parties for the year were as follows:

	2004 '000 EUR	2003 '000 EUR
Sales of electricity	**114,381**	**90,930**

Purchases of raw materials and services from related parties for the year were as follows:

	2004 '000 EUR	2003 '000 EUR
Purchased power	138,988	145,339
Agency fees	28,998	7,158
Generation assets maintenance	3,650	7,599
Transmission fees	2,183	–
Other expenses	80	–
	173,889	**160,096**

Related party transactions in relation to investing activities were as follows:

	2004 '000 EUR	2003 '000 EUR
		–
Non-current investments	647	–
Current investments	5,091	–
Interest income	1,047	–
Interest expense	(1,128)	–

Trade and other receivables owed by related parties at the end of the year were as follows:

	2004 '000 EUR	2003 '000 EUR
Trade and other receivables current	16,022	16,080
Other receivables	4,247	–
Advances paid	52	179
	20,321	**16,259**

Trade and other payables owed to related parties at the end of the year were as follows:

	2004 '000 EUR	2003 '000 EUR
Trade and other payables	**14,704**	**18,222**

(c) Pricing policies

Related party transactions are based on market prices or on prices determined by relevant state authorities in the CIS countries.

26 Events subsequent to the balance sheet date

In February 2005 a Group entity, established together with the Government of the Republic of Tadjikistan the company OAO Sangtudinskaya GES-1, whereby the Group was allocated a 75 percent interest in the OAO Sangtudinskaya GES-1 (75 ordinary shares at par value of USD 1,000). OAO Sangtudinskaya GES-1 has been created in accordance with the Inter-governmental Agreement between the Russian Federation and the Republic of Tadjikistan for construction of Sangtudinskaya GES-1 in the Republic of Tadjikistan. In December 2005 the Government of the Russian Federation approved an Inter-governmental Protocol between the Government of Russian Federation and the Government of Republic of Tadjikistan on the issue of shares of OAO Sangtudinskaya GES-1. In accordance with this Protocol, the Group was allocated 1,000 ordinary shares at par value of USD 1,000 thereby reducing the interest of the Group in OAO Sangtudinskaya GES-1 to 0.4%.

During 2005 the Group entered into a series of transactions resulting in acquisition of 51% of the share capital of "Moldavskaya GRES" CJSC – a hydro power plant located in Moldova for a net purchase consideration of EUR 35 million.

In December 2004 the Group, through its subsidiary Interenergo B.V., signed a share purchase agreement with Midland Resources Holding Ltd to purchase 100% shares of "Electrical Armenia Network" CJSC (a power distribution network located in Armenia).

On 23 June 2005 Midland Resources Holding Ltd issued a declaration of trust according to which 100% of the shares in "Electrical Armenia Network" CJSC, registered in the name of Midland Resources Holding Ltd (as well as distribution of dividends and/or any distributions received by Midland Resources Holding Ltd), are held by Midland Resources Holding Ltd in trust for Interenergo B.V., incorporated under the laws of the of the Netherlands, with its registered office in Amsterdam. Management of the Group expects that ownership of the shares will be received by the Group before the end of 2005. In accordance with the share purchase agreement, the purchase consideration to be paid is USD 74 million (EUR 54 million). As of the date of finalisation of these financial statements the ownership rights have not yet been transferred to the Group.

In July 2005 the Group acquired 6,059,026 ordinary shares of "Ekibazstuzskaya Station GRES-2" OJSC, a power generation station located in Kazahstan, representing 50% interest in this company. The acquisition is paid for by set-off of Kazahstan debt to Russia for USD 10 million (EUR 7.3 million).

In July 2005 the Group acquired 4,170,116 shares of "Severo-Zapadnaya TEC", a thermal power plant located in Russia, representing 25% interest in this company plus one share. The purchase consideration paid was RUR 2,741,450 (EUR 72.5 million).

In July 2005 the Group acquired 1,400 shares of TGR Enerji Elektrik Toptan Ticaret A.S., an electricity trading company located in Turkey, representing 70% interest in this company. The purchase consideration paid was YTL 35,000 (EUR 515 thousand).

As at the date of the finalisation of these financial statements, the Group has not assessed the fair value of the assets acquired and liabilities assumed in the above transactions.