**MOSENERGO GROUP**

**INTERIM CONSOLIDATED FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) FOR THE SIX MONTHS ENDED 30 JUNE 2007**

**(UNAUDITED)**

# Mosenergo Group
**Interim Consolidated Balance Sheet as at 30 June 2007**
(in millions of Russian Roubles)

| | Note | 30 June 2007 | 31 December 2006 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 5 | 115,457 | 59,679 |
| Investments in associates | 6 | 358 | 346 |
| Other non-current assets | | 279 | 215 |
| **Total non-current assets** | | **116,094** | **60,240** |
| **Current assets** | | | |
| Inventories | 7 | 4,369 | 4,346 |
| Trade and other receivables | 8 | 9,584 | 4,921 |
| Current income tax prepayments | | 1,239 | 56 |
| Short-term investments | 9 | 27,212 | - |
| Cash and cash equivalents | 10 | 23,271 | 5,729 |
| Other current assets | 11 | 612 | 666 |
| **Total current assets** | | **66,287** | **15,718** |
| **TOTAL ASSETS** | | **182,381** | **75,958** |
| **EQUITY AND LIABILITIES** | | | |
| **Equity** | | | |
| Share capital | 12 | 166,124 | 154,624 |
| Share premium | 12 | 49,213 | - |
| Accumulated loss | | (116,908) | (115,510) |
| Revaluation surplus | 12 | 37,534 | - |
| **Total equity** | | **135,963** | **39,114** |
| **Non-current liabilities** | | | |
| Deferred income tax liabilities | 13 | 17,932 | 6,291 |
| Non-current borrowings | 14 | 10,159 | 20,438 |
| Pension liabilities | 15 | 444 | - |
| **Total non-current liabilities** | | **28,535** | **26,729** |
| **Current liabilities** | | | |
| Current borrowings and current portion of non-current borrowings | 14 | 7,563 | 580 |
| Trade and other payables | 16 | 8,895 | 7,737 |
| Current income tax payable | | 578 | 723 |
| Other taxes payable | 17 | 847 | 1,075 |
| **Total current liabilities** | | **17,883** | **10,115** |
| **Total liabilities** | | **46,418** | **36,844** |
| **TOTAL EQUITY AND LIABILITIES** | | **182,381** | **75,958** |

Chairman of the Management Board — A.Y. Kopsov

Chief Accountant — T.P. Dronova

30 August 2007

(in millions of Russian Roubles, except for earning per ordinary share information)

| | Note | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|---|
| Revenues | 18 | 39,522 | 39,012 |
| Operating expenses | 19 | (39,528) | (39,273) |
| Other operating income | | 191 | 31 |
| **Operating profit/(loss)** | | **185** | **(230)** |
| Finance costs, net | 20 | (239) | (365) |
| Share of result of associates | 6 | 29 | 23 |
| **Loss before income tax** | | **(25)** | **(572)** |
| Income tax charge | 13 | (477) | (107) |
| **Loss for the period** | | **(502)** | **(679)** |
| Attributable to: | | | |
| Shareholders of OAO Mosenergo | | (502) | (679) |
| **Earnings per ordinary share for loss attributable to the shareholders of OAO Mosenergo – basic and diluted (in Russian Roubles)** | 21 | **(0.02)** | **(0.02)** |

Chairman of the Management Board A.Y. Kopsov

Chief Accountant T.P. Dronova

30 August 2007

(in millions of Russian Roubles)

| | Note | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| **Loss before income tax** | | **(26)** | **(572)** |
| Adjustments for: | | | |
| Depreciation of property, plant and equipment and impairment | 5 | 3,384 | 2,382 |
| Interest income | 20 | (305) | (3) |
| Interest expense | 20 | 555 | 444 |
| Foreign exchange gain | 20 | (11) | (76) |
| Charge for impairment of trade and other receivables | | 279 | 932 |
| Share of result of associates | 6 | (29) | (23) |
| Loss on disposal of property, plant and equipment | | 44 | 118 |
| Non-cash additions to property, plant and equipment | 5 | - | (522) |
| **Operating cash flows before working capital changes** | | **3,891** | **2,680** |
| Increase in inventories | | (23) | (378) |
| (Increase)/decrease in trade and other receivables | | (4,942) | 962 |
| Decrease in other current assets | | 54 | 531 |
| (Increase)/decrease in other non-current assets | | (64) | 18 |
| Increase/(decrease) in trade and other payables | | 205 | (195) |
| Decrease in taxes payable, other than income tax | | (176) | (1,115) |
| Increase in pension liabilities | | 444 | - |
| **Cash (used for)/generated from operations** | | **(611)** | **2,503** |
| Income tax paid in cash | | (2,069) | (549) |
| **Net cash (used for)/generated from operating activities** | | **(2,680)** | **1,954** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Purchase of short-term investments | | (26,907) | - |
| Purchase of property, plant and equipment and other non-current assets | | (9,430) | (3,238) |
| Proceeds from sale of property, plant and equipment | | 9 | 13 |
| Interest paid and capitalised | 5 | (396) | - |
| Dividends received | | 17 | - |
| **Net cash used in investing activities** | | **(36,707)** | **(3,225)** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Proceeds from non-current borrowings | | 1,213 | 6,800 |
| Proceeds from current borrowings | | 4,029 | 10,650 |
| Repayment of borrowings | | (8,524) | (15,691) |
| Issue of ordinary shares | 12 | 60,720 | - |
| Costs of issuing ordinary shares | 12 | (7) | - |
| Interest paid | | (494) | (320) |
| Dividends paid by the Group to the shareholders of OAO Mosenergo | | (8) | (6) |
| **Net cash generated from financing activities** | | **56,929** | **1,433** |
| **Increase in cash and cash equivalents** | | **17,542** | **162** |
| **Cash and cash equivalents at the beginning of the period** | 10 | **5,729** | **2,383** |
| **Cash and cash equivalents at the end of the period** | 10 | **23,271** | **2,545** |

Chairman of the Management Board — A.Y. Kopsov

Chief Accountant — T.P. Dronova

30 August 2007

(in millions of Russian Roubles)

| | Attributable to the shareholders of OAO Mosenergo | | | | |
|---|---|---|---|---|---|
| | **Share capital** | **Share premium** | **Accumulated loss** | **Revaluation surplus** | **Total** |
| **At 1 January 2006** | **154,624** | **-** | **(123,633)** | **-** | **30,991** |
| Loss for the period | - | - | (679) | - | (679) |
| **Total recognised loss for the period** | **-** | **-** | **(679)** | **-** | **(679)** |
| Dividends to the shareholders | - | - | (454) | - | (454) |
| **At 30 June 2006** | **154,624** | - | **(124,766)** | **-** | **29,858** |
| **At 1 January 2007** | **154,624** | **-** | **(115,510)** | **-** | **39,114** |
| Revaluation of property, plant and equipment (Note 5) | - | - | - | 37,534 | 37,534 |
| Loss for the period | - | - | (502) | - | (502) |
| **Total recognised income for the period** | **154,624** | **-** | **(116,012)** | **37,534** | **76,146** |
| Issue of ordinary shares (Note 12) | 11,500 | 49,213 | - | - | 60,713 |
| Dividends to the shareholders | - | - | (896) | - | (896) |
| **At 30 June 2007** | **166,124** | **49,213** | **(116,908)** | **37,534** | **135,963** |

Chairman of the Management Board A.Y. Kopsov

Chief Accountant T.P. Dronova

30 August 2007

# Note 1. The Group and its operations

OAO Mosenergo ("OAO Mosenergo" or the "Company") and its subsidiaries and associates (the "Group") is a regional utility generating electric power and heat and also providing heat distribution services to the city of Moscow and Moscow region. The Group's asset base includes 17 power stations. The overall operational capacity of OAO Mosenergo is approximately 10,627 megawatts ("MW") of installed generating capacity for electricity and 34,101 gigacalories ("Gkal") of installed generating capacity for heat.

OAO Mosenergo was registered in the Russian Federation on 6 April 1993 in accordance with State Property Management Committee Decree #169-R dated 26 March 1993. In accordance with the privatisation of the Russian electric utility industry, OAO Mosenergo was organised as a joint stock company.

In 2004 the general shareholders' meeting of OAO Mosenergo approved the entity's restructuring, which entailed the creation of 13 new companies. Before restructuring OAO Mosenergo operated as a vertically integrated utility with primary focus on generation of electricity and heat. Restructuring consisted in spin-off of the following lines of business:

- transmission and distribution of electricity and heat – monopolistic;
- retail sales of electricity, repair and construction – non-core activities;
- four power plants.

As result of the restructuring, in April 2005 each shareholder of OAO Mosenergo received ordinary shares of each of the 13 companies - shares in the companies were distributed among the shareholders of OAO Mosenergo pro rata to OAO Mosenergo shares held by them prior to spin-off.

As of 20 December 2006 the general shareholders' meeting of OAO Mosenergo approved an increase of share capital of OAO Mosenergo via additional issue of ordinary shares by closed subscription in favour of OAO Gazprom and its affiliates ("Gazprom Group"). After subscription for the new shares Gazprom Group became the majority shareholder of OAO Mosenergo .

OAO Mosenergo's registered office is located at 8, Raushskaya Naberezhnaya, Moscow, 115035, Russian Federation.

***Operating environment.*** Whilst there have been improvements in economic trends in the Russian Federation, the country continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside of the Russian Federation and relatively high inflation. The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and changes, which can occur frequently.

*Relations with the state and current regulation.* As at 30 June 2007 the Russian Federation owned (including both direct and indirect ownership) of over 50% in OAO Gazprom (the "Parent"), which in its turn owned (including both direct and indirect ownership) of over 52% in OAO Mosenergo. The Russian government is the ultimate controlling party of the Group.

The Group's customer base includes a large number of entities controlled by, or related to the state. Furthermore, the State controls a number of the Group's fuel and other suppliers.

The government of the Russian Federation directly affects the Group's operations through regulation by the Federal service on tariffs ("FST"), with respect to its wholesale energy purchases, and by the Moscow and Moscow Regional Energy Commissions ("REC's"), with respect to its retail electricity and heat sales. The operations of all generating facilities are coordinated by OAO System Operator – Central Despatch Unit of Unified Energy System ("SO-CDU") in order to meet system requirements in an efficient manner. SO-CDU is controlled by RAO UES of Russia.

Tariffs which the Group may charge for sales of electricity and heat are governed by regulations specific to the electricity and heat industry and by regulations applicable to natural monopolies. Historically, such tariffs have been based on a "cost-plus" system, meaning cost of service plus a margin, where costs are determined under the Regulations on Accounting and Reporting of the Russian Federation, a basis of accounting which significantly differs from International Financial Reporting Standards ("IFRS").

As described in Notes 2, 23 and 24, the government's economic, social and other policies could have material effects on the operations of the Group.

***Regulatory and sector restructuring.*** The Russian electric utilities industry in general and OAO Mosenergo in particular are presently undergoing a restructuring process designed to introduce competition into the electricity sector and to create an environment in which RAO UES Group and its successor companies (including OAO Mosenergo) can raise the capital required to maintain and expand current capacity.

A crucial step towards the target wholesale electricity (capacity) market model was the adoption of the new Wholesale Electric Power (capacity) Market ("NOREM") Rules of the Transitional Period approved by Resolution of the Government of the Russian Federation No. 529 dated August 31, 2006 which came into force on September 1, 2006. Under the new wholesale market model, the existing electricity and power purchase-and-sale relations in the regulated market sector are to be replaced by a regulated bilateral contract system. From 1 September 2006 regulated contracts covered all volumes of electricity and power produced and consumed.

From 2007 the volumes of electricity (power) traded in the wholesale market at regulated prices will substantially reduce. The pace of reduction will be set annually by the Russian Federation Government according to socio-economic development forecasts. In 2007 up to 95% of the forecasted production volumes will be traded at regulated prices. The period from 2006 to approximately 2013 is a transition period. After that it will become possible to launch a fully competitive wholesale market.

Operation on the New Wholesale Electric Power (capacity) Market did not have any material impact on these financial statements. Management believes that ultimately a stable regulatory regime and a competitive power market will be put in place such that the Group will be able to raise needed capital to sustain the business. However, there can be no assurance in this regard.

***Seasonality of business.*** Demand for both electricity and heat is influenced by both the season of the year and the relative severity of the weather. Revenues from heating are concentrated within the months of October to March. A similar, though less severe, concentration of electricity sales occurs within the same period. The seasonality of electricity and heat production has a corresponding impact on the usage of fuel and the purchase of power.

## Note 2. Financial condition

At 30 June 2007, the Group's current assets exceeded its current liabilities by 48,404 million Russian Roubles ("RR") (at 31 December 2006: RR 5,603 million).

As discussed above the Group is affected by government policy through the control of tariffs and other factors. The FST does not always permit tariff increases in excess of increases in the Group's costs and thus some tariffs are insufficient to cover all the costs of generation. Moreover, these tariffs consider costs only on a Russian statutory basis and, accordingly, exclude additional costs recognised under an IFRS basis of accounting. As a result, tariffs may not consistently allow for an adequate return on investment and currently do not provide sufficient funds for the full replacement of property, plant and equipment. However, the growing demand for electricity and capacity together with increasing free trading sector of the wholesale electricity market result in a revenue growth during the reporting period.

The Group's management has been taking the following actions in order to address the issues noted above and further improve the Group's financial position:

- introduction of improved financial budgeting procedures;
- negotiations with federal and regional governments and regulators for real increases in tariffs to support adequate long term investment into the Group's generation assets.

Management believes that ultimately a stable regulatory regime and a competitive power market will be put in place such that the Group will be able to raise needed capital to sustain the business. However, there can be no assurance in this regard.

## Note 3. Basis of preparation

*Statement of compliance.* These consolidated financial statements ("Financial Statements") have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Each enterprise of the Group individually maintains its own books of accounts and prepares its statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The accompanying Financial Statements are based on the statutory records and adjusted and reclassified for the purpose of fair presentation in accordance with IFRS.

***Reclassifications.*** Certain reclassifications have been made to prior year data to conform to the current year presentation. All these reclassifications made are not material.

***Functional and presentation currency.*** The national currency of the Russian Federation is the Russian rouble ("RR"), which is the functional currency of each of the Group's entities and the currency in which these financial statements are presented. All financial information presented in RR has been rounded to the nearest million.

***Accounting for the effects of hyperinflation.*** The Russian Federation has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 "Financial Reporting in Hyperinflationary Economies" ("IAS 29"). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. Hyperinflation in the Russian Federation ceased effective from 1 January 2003. Restatement procedures of IAS 29 are therefore only applied to assets acquired or revalued and liabilities incurred or assumed prior to that date. For these balances, prior to the adoption of revaluation as a basis for accounting for property, plant and equipment (Note 4) on 1 January 2006, the amounts expressed in the measuring unit current at 31 December 2002 were treated as the basis for the carrying amounts of these financial statements.

***New accounting developments.*** Certain new IFRSs became effective for the Group from 1 January 2007. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Group's operations and the nature of their impact on the Group's accounting policies.

- IAS 39 (Amendment) – The Fair Value Option;
- IFRIC 4, Determining whether an Arrangement contains a Lease;
- IAS 39 (Amendment) – Cash Flows Hedge Accounting of Forecast Intragroup Transactions;
- IAS 39 (Amendment) – Financial Guarantee Contracts;
- IAS 21 (Amendment) – Net Investment in a Foreign Operation;
- IAS 19 (Amendment) – Employee Benefits;
- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds;

- IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment;
- IFRS 6, Exploration for and Evaluation of Mineral Resources.
- IFRS 7 Financial Instruments: Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures.
- IFRIC 7, Applying the Restatement Approach under IAS 29 (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007);
- IFRIC 8, Scope of IFRS 2 (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007).

The effect of adoption of the above new standards and interpretations on the Company's financial position at 30 June 2007 and 31 December 2006 and on the results of its operations for the six month ended 30 June 2007 and 30 June 2006 was not significant.

***Other new standards or interpretations.*** The Group has not early adopted the following other new standards or interpretations:

- IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009). The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information;
- IFRIC 7, Applying the Restatement Approach under IAS 29 (effective for periods beginning on or after 1 March 2006, that is from 1 January 2007);
- IFRIC 8, Scope of IFRS 2 (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007);
- IFRIC 9, Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006);
- IFRIC 11, IFRS 2—Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 13, Customer Loyalty Programmes (effective for annual periods beginning on or after 1 July 2008);
- IFRIC 14, IAS 19- Defined Benefit Assets and Minimum Funding Requirements (effective for annual periods beginning on or after 1 January 2008);
- IAS 23, Borrowing Cost (Amendment, applies to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009). The main change from the previous version is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale.

Unless otherwise described above, these new standards and interpretations are not expected to significantly affect the Company's financial statements.

***Going concern.*** The 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 Financial Statements do not include any adjustments should the Group be unable to continue as a going concern.

***Critical accounting estimates and assumptions.*** The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgments, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

*Useful lives of property, plant and equipment.* Fair value of property, plant and equipment has been determined by an independent appraiser based on the depreciated replacement cost method. Further, management assesses the remaining useful life of property, plant and equipment in accordance with the current technical conditions of assets and estimated period when these assets will bring economic benefit to the Group. Carrying value and depreciation of property, plant and equipment are affected by the estimates of replacement cost, depreciated replacement cost, residual value and remaining useful lives, and actual results could differ from these estimates.

*Provision for impairment of trade and other receivables.* Provision for impairment of trade and other receivables is based on the Group's assessment of whether the collectibility of specific customer accounts worsened compared to prior estimates. If there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates, the actual results could differ from these estimates.

*Provision for impairment of other assets.* At each balance sheet date the Group assesses whether there is any indication that the recoverable amount of the Group's assets has declined below the carrying value. The recoverable amount of property, plant and equipment is the higher of an asset's fair value less costs to sell and its value in use. When such a decline is identified, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recorded in the consolidated statement of income in the period in which the reduction is identified. If conditions change and management determines that the value of an asset other than goodwill has increased, the impairment provision will be fully or partially reversed.

*Tax contingencies.* Russian tax legislation is subject to varying interpretations and changes, which can occur frequently. Where the Group management believes it is probable that their interpretation of the relevant legislation and the Group's tax positions cannot be sustained, an appropriate amount is accrued for in these IFRS financial statements.

# Note 4. Summary of significant accounting policies

The following significant accounting policies have been applied in the preparation of the consolidated financial statements. These interim consolidated financial statements have been prepared by applying the accounting policies consistent with those of the annual financial statements for the year ended 31 December 2006, except for:

- the policies regarding the measurement of the property, plant and equipment, which was changed voluntarily (see disclosure in Note 5 "Property, plant and equipment"), and
- those policies which were changed to comply with the new or amended standards and interpretations that are in force for the year beginning 1 January 2007.

## (a) Principles 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. The minority interest has been disclosed as part of equity.

***(ii) Associates***

Associates are those enterprises in which the Group has significant influence, but not control, over the financial and operating policies. The consolidated IFRS financial statements include the Group's share of the total recognised gains and losses of associates on an equity accounted basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Group's share of losses exceeds the interest in the associate, that interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

***(iii) 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 gains arising from transactions with associates are eliminated to the extent of the Group's interest in the enterprise. Unrealised gains resulting from transactions with associates are eliminated against the investment in the associate. 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 RR 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 RR 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 RR 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 RR 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.

At 30 June 2007 the official rates of exchange, as determined by the Central Bank of the Russian Federation, were:

- RR 25.8162: US Dollar (US$) 1.00 (31 December 2006: RR 26.3311: US$ 1.00);
- RR 34.7150: Euro 1.00 (31 December 2006: RR 34.6965: Euro 1.00).

The RR is not freely convertible in most countries outside the Russian Federation.

### (c) Property, plant and equipment

Until 31 December 2006, property, plant and equipment are stated at depreciated cost. Deemed cost was initially determined by a third party valuation as at 31 December 1997 and restated for the impact of inflation until 31 December 2002.

The Group changed its accounting policy to revaluing its property, plant and equipment from 1 January 2007. Management believes that it would result in a more meaningful presentation of the Group's financial position and financial performance.

Property, plant and equipment are subject to revaluation on a regular basis. The frequency of revaluation depends upon the movements in the fair values of the assets being revalued. Increases in the carrying amount arising on revaluation of property, plant and equipment are credited to revaluation reserves in equity, unless the decrease of the reserve previously recognized in the income statements. Decreases that offset previous increases of the same asset are charged against revaluation reserves directly in equity; all other decreases are charged to the income statement.

Any accumulated depreciation at the date of revaluation is eliminated against the gross amount of the asset, and the net amount is restated to the revalued amount of the asset.

The Group charges deferred tax liabilities in respect of revaluation of property, plant and equipment directly to equity.

The cost of self constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads. Interest on borrowings to finance the construction of property, plant and equipment is capitalized during the period of time that is required to complete and prepare the asset for its intended use. 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.

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 if future economic benefits will arise from the expenditure. All other expenditure is recognised in the income statement as an expense as incurred.

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of the individual assets when it is available for use. Depreciation commences on the date of acquisition, or in respect of internally constructed assets, from the time the asset is completed and ready for use.

The estimated useful lives are as follows:

- Electricity and heat generation 17 to 50 years
- Electricity distribution 11 to 25 years
- Heating networks 14 to 20 years
- Other 15 years

Social assets are not capitalised as they are not expected to result in future economic benefits to the Group. Costs associated with fulfilling the Group's social responsibilities are expensed as incurred.

### (d) 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.

The cost of inventories is based on the weighted average cost principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition.

### (e) Trade receivables

Trade receivables are recorded inclusive of value added taxes. Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest rate method less provision for impairment. Such a provision for impairment of accounts receivable is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for the similar borrowers at the date of origination of the receivable.

### (f) Value added tax on purchases and sales

Value added taxes ("VAT") related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases which have not been settled at the balance sheet date (deferred VAT) is recognized in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, the impairment loss is recorded for the gross amount of the debtor's balance, including VAT. The related deferred VAT liability is maintained until the debtor is written off for tax purposes.

### (g) Cash and cash equivalents

Cash comprises cash in hand and cash deposited on demand at banks. Cash equivalents comprise short-term high liquid investments that are readily convertible into cash and have a maturity of three months or less from the date of acquisition and are subject to insignificant changes in value.

### (h) Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared (approved by shareholders) before or on the balance sheet date. Dividends are disclosed when they are declared after the balance sheet date, but before the financial statements are authorized for issue.

### (i) Borrowings

Debt is recognised initially at its fair value. Fair value is determined using the prevailing market rate of interest for a similar instrument, if significantly different from the transaction price. In subsequent periods, debt is stated at amortized cost using the effective interest method; any difference between the fair value of the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement as an interest expense over the period of the debt obligation.

### (j) Borrowing Costs

The Group applies the benchmark treatment of IAS 23 "Borrowing costs" and recognises all borrowing costs as an expense in the period in which they are incurred.

### (k) Pension and post-employment benefits

In the normal course of business the Group contributes to the Russian Federation state pension scheme on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred.

OAO Mosenergo operates a number of defined benefit plans: lump-sum payments at retirement, old age life pension program and death benefits. Defined benefits plans, except old-age life pensions, are paid on a pay-as-you-go basis. For old-age life pensions payments OAO Mosenergo has contracted with a non-state pension fund. OAO Mosenergo settles its obligation in relation to former employees when they retire from OAO Mosenergo by purchasing annuity policies in the fund. All defined benefits plans are considered to be fully unfunded. When the pension obligation is settled via a non-state pension fund, the employer buys an annuity with the amount of contributions allocated to individual accounts held by the non-state pension fund and any additional contributions that may be required from the employer to meet the cost of the benefit promise.

Defined benefit plans determine the amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. The liability recognised in the balance sheet in respect of defined benefit pension plans operated by the Group is the present value of the defined benefit obligation at the balance sheet date, together with adjustments for unrecognised actuarial gains or losses and past service cost. The defined benefit obligations are calculated using the projected unit credit method. The present value of the defined benefit obligations are determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid associated with the operation of the plans, and that have terms to maturity approximating the terms of the related pension liabilities.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligations are charged or credited to the income statement over the employees' expected average remaining working lives.

### (l) Trade payables

Trade payables are stated inclusive of value added tax. Trade payables are accrued when counterparty performed its obligation under the contract and are carried at amortised cost using the effective interest method.

### (m) Income tax

The income tax expense represents the sum of the tax currently payable and deferred income tax. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted by the balance sheet date.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit or loss. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Deferred tax movements are recorded in the income statement except when they are related to the items directly charged to the shareholders' equity. In this case deferred taxes are recorded as part of the shareholders' equity.

Deferred tax is not provided for the undistributed earnings of subsidiaries, as the Group requires profits to be reinvested, and only insignificant dividends are expected to be declared from future profits of the subsidiaries. Neither these future profits nor the related taxes are recognized in these financial statements.

### (n) Revenues

Revenue is recognised on the delivery of electricity and heat, and on the dispatch of non-utility goods and services. Revenue amounts are presented exclusive of value added taxes.

### (o) Segment reporting

The Group operates predominantly in a single geographical area and industry, the generation of electric power and heat in the city of Moscow, Moscow region and the surrounding regions. It is not feasible to identify distinguishable business segments for electric power and heat production. The generation of electricity and heat are related activities and are subject to similar risks and returns, therefore they are reported as one business segment.

### (p) Earnings per share

The earnings per share is determined by dividing the profit/(loss) attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the reporting period.

### (q) Environmental liabilities

Liabilities for environmental remediation are recorded where there is a present obligation, the payment is probable and reliable estimates can be made.

### (r) Interest

Interest income and expense are recognised in the income statement for all interest bearing instruments on an accrual basis using effective interest method. Interest income includes nominal interest and accrued discount and premium. When loans become doubtful of collection, they are written down to their recoverable amounts (using the original effective rate) and interest income is thereafter recognised based on the same effective rate of interest.

### (s) Fair value disclosure

The fair value of accounts receivable for disclosure purposes is measured by discounting the value of expected cash flows at the market rate of interest for similar borrowers at the reporting date.

The fair value of financial liabilities and other financial instruments (except if publicly quoted) for disclosure purposes is measured by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments. The fair value of publicly quoted financial instruments for disclosure purposes are measured based on current market value at the close of business on the reporting date.

### (t) Embedded derivatives

The Group enters into purchase agreement for fuel within ordinary course of business. The contracts were entered into and continue to be held for the purpose of receipt or delivery of commodities in accordance with the Group's expected usage requirements and there are not within the scope of IAS 39 but need to be assessed at inception to determine if they contain embedded derivatives.

An embedded derivative is one or more implicit or explicit terms in a contract that affect the cash flows of the contract in a manner similar to a stand-alone derivative instrument. Any embedded derivative that meets the separation criterion should be separated from its host contracts and measured as if it was stand-alone derivative (fair value through profit or loss) if its economic characteristics are not closely related to those of the host contract.

(in millions of Russian Roubles)

# Note 5. Property, plant and equipment

| | Electricity and heat generation | Electricity distribution | Heating networks | Construction in progress | Other | Total |
|---|---|---|---|---|---|---|
| **Appraised value** | | | | | | |
| Opening balance as at 31 December 2006 | 62,768 | 3,861 | 4,421 | 12,339 | 28,160 | 111,549 |
| Elimination of accumulated depreciation | (26,613) | (987) | (2,517) | (20) | (21,733) | (51,870) |
| Revaluation | 36,124 | 2,461 | 10,237 | 2,248 | (1,683) | 49,387 |
| Additions | - | - | - | 9,787 | 23 | 9,810 |
| Transfers | 61 | 79 | 20 | (317) | 157 | - |
| Disposals | (29) | (1) | - | (6) | - | (36) |
| Closing balance as at 30 June 2007 | 72,311 | 5,413 | 12,161 | 24,031 | 4,924 | 118,840 |
| **Accumulated depreciation** | | | | | | |
| Opening balance as at 31 December 2006 | (26,613) | (987) | (2,517) | (20) | (21,733) | (51,870) |
| Elimination of accumulated depreciation | 26,613 | 987 | 2,517 | 20 | 21,733 | 51,870 |
| Charge for the period | (1,595) | (144) | (980) | - | (665) | (3,384) |
| Disposals | 1 | - | - | - | - | 1 |
| Closing balance as at 30 June 2007 | (1,594) | (144) | (980) | - | (665) | (3,383) |
| Net book value as at 31 December 2006 | 36,155 | 2,874 | 1,904 | 12,319 | 6,427 | 59,679 |
| Net book value as at 30 June 2007 | 70,717 | 5,269 | 11,181 | 24,031 | 4,259 | 115,457 |

| | Electricity and heat generation | Electricity distribution | Heating networks | Construction in progress | Other | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| Opening balance as at 31 December 2005 | 60,298 | 3,161 | 4,421 | 2,182 | 27,227 | 97,289 |
| Additions | 7 | - | - | 1,979 | 17 | 2,003 |
| Transfers | 35 | 30 | - | (116) | 51 | - |
| Disposals | (237) | (8) | - | - | (109) | (354) |
| Closing balance as at 30 June 2006 | 60,103 | 3,183 | 4,421 | 4,045 | 27,186 | 98,938 |

(in millions of Russian Roubles)

| | | | | | | |
|---|---|---|---|---|---|---|
| **Accumulated depreciation (including impairment)** | | | | | | |
| Opening balance as at 31 December 2005 | (33,613) | (1,427) | (2,693) | - | (21,401) | (59,134) |
| Charge for the period | (1,071) | (264) | (103) | - | (944) | (2,382) |
| Disposals | 101 | 5 | - | - | 102 | 208 |
| Closing balance as at 30 June 2006 | (34,583) | (1,686) | (2,796) | - | (22,243) | (61,308) |
| Net book value as at 31 December 2005 | 26,685 | 1,734 | 1,728 | 2,182 | 5,826 | 38,155 |
| Net book value as at 30 June 2006 | 25,520 | 1,497 | 1,625 | 4,045 | 4,943 | 37,630 |

Included in additions above is capitalized interest of RR 396 million and nil for the periods ended 30 June 2007 and 2006, respectively. Capitalization rate of 7.74% was used representing the weight average actual borrowing cost of the relevant borrowings for the year ended 31 December 2006.

Construction in progress includes advances to construction companies and suppliers of property, plant and equipment of RR 7,599 million (net of VAT) and RR 5,042 million (net of VAT) as of 30 June 2007 and 31 December 2006 respectively.

Other property, plant and equipment are comprised of motor vehicles, computer equipment, office fixtures and other assets not included in categories mentioned above.

The Group changed its accounting policy to revaluing its property, plant and equipment, excluding construction in progress, from 1 January 2007. The Group contracted independent appraisers to estimate fair value of the Group's property, plant and equipment at 1 January 2007. New fair value as at 1 January 2007 amounted to RR 104,547 million. This change was accounted for prospectively in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors", therefore comparatives were not restated.

Fair values were determined primarily based on the depreciated replacement cost method. The replacement cost of buildings, constructions and transfer devices has been estimated based on technical characteristics, unit construction cost and construction estimates. The replacement cost of equipment was estimated based on data of aggregative replacement cost of heat-power station, current purchase contracts and price-list of producers and trading companies. The economic obsolescence was estimated based on profitability test results for each cash-generating unit. The discount rate used was 11.28%, the forecast period - 19 years, long-term growth – 3%.

As a result of the revaluation, the Group’s equity increased by RR 37,534 million, comprising in increase in carrying value of property, plant and equipment of RR 49,387 million, net of related deferred tax of RR 11,853 million.

For each revalued class of property, plant and equipment stated at revalued amount in these financial statements, the carrying amount that would have been recognized had the assets been carried under the cost model is following:

| | Electricity and heat generation | Electricity distribution | Heating networks | Construction in progress | Other | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| Net book value as at 30 June 2007 | 35,334 | 2,842 | 1,552 | 21,784 | 5,580 | 67,092 |

(in millions of Russian Roubles)

### (a) Impairment provision for property, plant and equipment

The carrying value of property, plant and equipment at 31 December 2005 is stated net of an impairment loss of RR 11,250 million. As at 31 December 2006, the Group assessed whether there is any indication that an impairment loss recognised in prior periods for property, plant and equipment may no longer exist.

Management concluded that at the reporting date there were indications for reversing previously recognised impairment losses based on significant changes with a favorable effect on the Group that have occurred or are expected to occur in the near future in the market and economic environment in which the Group operates.

Key positive developments include:

1. higher expected growth of demand for electricity and heat in the region in which the Group operates, which is based on recent trends;
2. higher certainty about the free trading sector for electricity, which has been enacted by the government of the Russian Federation as of August 2006 (Note 1);

These developments have resulted in a change to the assumptions that were used to determine the value in use of the assets and a reversal of the previously recognised impairment loss in the amount of RR 10,532 million at 31 December 2006. A respective gain together with a corresponding deferred tax expense of RR 2,528 million were recognised in the income statement for the year ended 31 December 2006.

Management believes that there were no indications of impairment of the Group's principal operating assets at 30 June 2007, as prices for gas, tariffs for electric energy and heat (in regulated sector), approved for 2007 by corresponding regulating bodies, have grown by 15.0 %, 15.0 % and 16.5 % respectively in comparison with the year ended 31 December 2006.

### (b) Non cash transactions

Non cash transactions during the year were as follows:

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Property, plant and equipment additions | - | 522 |

Non-cash property, plant and equipment additions for the period ended 30 June 2006 – as a part of a general city restructuring plan, elements of the Group's property, plant and equipment were removed and replaced during the year. The cost of removing existing property, plant and equipment is met by the local government and its subcontractors, with the replacement property, plant and equipment being transferred to the Group on its completion.

### (c) Operating lease

The Group leases a number of land areas owned by local governments under operating lease. Land lease payments are determined by lease agreements.

Operating lease rentals are payable as follows:

| | 30 June 2007 |
|---|---|
| Less than one year | 280 |
| Between one and five years | 1,401 |
| More than five years | 12,192 |
| | **13,873** |

(in millions of Russian Roubles)

The land areas leased by the Group are the territories on which the Group's electric power stations, heating stations and other assets are located. The leases typically run for an initial period of 5 to 45 years with an option to renew the lease after that date. Leased payments are reviewed regularly to reflect market rentals.

## Note 6. Investments in associates

The Group has the following investments in associates:

| | Country | Ownership/ Voting |
|---|---|---|
| OOO KB Transinvestbank | Russia | 24.61% |

The table below summarise the movements in the carrying amount of the Group's investments in associates:

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Carrying amount at 1 January | 346 | 328 |
| Share of result of associates | 29 | 42 |
| Dividends received from associates | (17) | (24) |
| Carrying amount at the end of reporting period | **358** | **346** |

At 30 June 2007 and 31 December 2006 summarized financial information of associates, including total assets, liabilities, revenues and profit were as follows:

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Assets | 3,499 | 3,829 |
| Liabilities | (2,045) | (2,423) |
| Total equity | **1,454** | **1,406** |

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Revenues | 386 | 491 |
| Expenses | (267) | (306) |
| Net profit | **119** | **185** |

## Note 7. Inventories

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Fuel production stocks | 2,519 | 2,998 |
| Materials and supplies | 1,816 | 1,322 |
| Other inventories | 34 | 26 |
| | **4,369** | **4,346** |

(in millions of Russian Roubles)

Materials and supplies are shown net of a provision for obsolete inventory and an adjustment for slow-moving inventory of RR 16 million as at 30 June 2007 and RR 17 million as at 31 December 2006.

## Note 8. Trade and other receivables

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Advances to suppliers and prepayments | 783 | 500 |
| Trade receivables (Net of provision for impairment of receivables of RR 1,398 million as at 30 June 2007 and RR 1,161 million as at 31 December 2006) | 5,698 | 2,066 |
| Value Added Tax recoverable | 1,821 | 1,492 |
| Tax prepayments (other than current income tax prepayments) | 360 | 76 |
| Receivables from associate | 1 | - |
| Other receivables (Net of provision for impairment of receivables of RR 298 million as at 30 June 2007 and RR 255 million as at 31 December 2006) | 921 | 787 |
| | **9,584** | **4,921** |

Management has determined the allowance for doubtful debtors based on specific customer identification, customer payment trends, subsequent receipts and settlements and analyses of expected future cash flows. The management of the Group believes that the Group will be able to realize the net receivable amount through direct collections and other non-cash settlements, and because of their short term nature, therefore the recorded value approximates their fair value.

## Note 9. Short-term investments

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Promissory notes | 22,212 | - |
| Bank deposit | 5,000 | - |
| | **27,212** | **-** |

In May 2007 the Company purchased a number of promissory notes of AB Gazprombank (ZAO) maturing in 2008. Interest rates for promissory notes are within 4.75 – 6.7% per annum.

During the period ended 30 June 2007 OAO Mosenergo placed on short-term deposit in AK Srednerusskii bank SB RF for RR 5,000 million.

(in millions of Russian Roubles)

## Note 10. Cash and cash equivalents

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Cash at bank and in hand | 23,262 | 5,720 |
| Foreign currency bank accounts | 9 | 9 |
| | **23,271** | **5,729** |

Cash and cash equivalents balances do not include balances on special accounts in OAO ABN AMRO bank and OAO KB Citibank in the aggregate amounts of RR 89 million and RR 143 million as at 30 June 2007 and 31 December 2006 respectively. Such balances are allotted for the purpose of repayment of principal amount of a debt and interest on EBRD and IFC loans. Such balances are classified within other current assets.

## Note 11. Other current assets

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Assets constructed under financing from Moscow Government (Note 16) | 523 | 523 |
| Other current assets | 89 | 143 |
| | **612** | **666** |

## Note 12. Equity

### (a) Share capital

| | Number of ordinary shares | Registered share capital | Unregistered share capital | Total |
|---|---|---|---|---|
| Opening balance as at 31 December 2006 | 28,249,359,700 | 154,624 | - | 154,624 |
| Issue of ordinary shares | 11,500,000,000 | - | 11,500 | 11,500 |
| Closing balance as at 30 June 2007 | **39,749,359,700** | **154,624** | **11,500** | **166,124** |

The total authorised number of ordinary shares is 39,749,359,700 shares with a par value of RR 1.00 per share. All issued ordinary shares are fully paid.

The carrying amount of share capital has been adjusted to take into account the effects of hyperinflation that existed in Russian Federation until the end of 2002.

As of 20 December 2006 the shareholders' meeting of OAO Mosenergo approved increase of share capital of OAO Mosenergo via additional issue of 11,500,000,000 of ordinary shares with nominal value equal to RR 1.00 per share by closed subscription in favour of OAO Gazprom and its affiliates. Offering price was approved at RR 5.28 per share (determined based on quoted price of OAO Mosenergo shares during the period of 19 June 2006 – 19 December 2006). The Report on additional issue of securities was registered by the Federal Securities Commission of Russian Federation on 5 July 2007. Shares were paid during March-May 2007.

(in millions of Russian Roubles)

### (b) Share premium

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Share premium in excess of par value | 49,220 | - |
| Costs of issuing shares | (7) | - |
| | **49,213** | **-** |

Total amount of cash proceeds from the issuance of 11,500,000,000 of ordinary shares at price of RR 5.28 per each share was RR 60,720 million. Share premium received in excess of par value was RR 49,220 million.

Total costs of issuing shares accounted for as a deduction from equity amounted to RR 7 million in the period.

### (c) Revaluation surplus

Revaluation surplus represents the result of the revaluation of property, plant and equipment performed as at 1 January 2007 (Note 5).

### (d) Dividends

The Company's annual statutory accounts form the basis for the annual profit distribution and other appropriations. The specific Russian legislation identifies the basis of distribution as the net profit. However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and, accordingly, management believes at present it would not be appropriate to disclose an amount for the distributable reserves in these financial statements.

A decision in respect of the payment of dividends following OAO Mosenergo's 2005 results was taken on 26 May 2006. The amount of declared (accrued) dividends on the issuer's shares was RR 0.01607 per share, total amount of dividends is RR 454 million.

In May 2007 the Company declared dividends for the year ended 31 December 2006 of RR 0.02116389 per share for the total of RR 600 million. These dividends were recognized as a liability and deducted from equity at 30 June 2007.

In July 2007 the Company declared dividends for the three months ended 31 March 2007 of RR 0.0104408508 per share for the total of RR 296 million. These dividends were recognized as a liability and deducted from equity at 30 June 2007.

## Note 13. Income tax

### (a) Income tax expense

The Group's applicable tax rate is the corporate income tax rate of 24% (2006: 24%).

| *Income tax benefit/(charge)* | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Current income tax charge | (689) | (682) |
| Deferred income tax benefit | 212 | 575 |
| | **(477)** | **(107)** |

(in millions of Russian Roubles)

As of 30 June 2007 and 31 December 2006 the Federal Tax Authority declared its decision concerning tax inspection for 2002 and 2003 years. In accordance with this decision OAO Mosenergo was exposed to additional income tax amounting to RR 576 million, which has been accrued for in these consolidated financial statements.

Profit before tax for the financial reporting purposes is reconciled to the income tax as follows:

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Profit/(loss) before tax | **(25)** | (572) |
| Theoretical tax (charge)/benefit at the statutory tax rate of 24% | 6 | 137 |
| Non-deductible/non-taxable items | (483) | (307) |
| Other effects | - | 63 |
| | **(477)** | **(107)** |

**(b) Deferred income tax**

***(i) Recognised deferred tax assets and liabilities***

Difference between IFRS and Russian statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes. Deferred income tax assets and liabilities are measured at 24%, the rate applicable when the asset or liability will reverse.

***(ii) Movements for the periods***

| | 31 December 2006 | Movement for the period recognized in the income statement | Movement for the period recognized in the statement of changs in equity | 30 June 2007 |
|---|---|---|---|---|
| Property, plant and equipment | (6,768) | 254 | (11,853) | (18,367) |
| Trade and other receivables | 173 | 111 | - | 284 |
| Other | 304 | (153) | - | 151 |
| | **(6,291)** | **212** | **(11,853)** | **(17,932)** |

| | 31 December 2005 | Movement for the period recognized in the income statement | 30 June 2006 |
|---|---|---|---|
| Property, plant and equipment | (4,425) | 559 | (3,866) |
| Trade and other receivables | 62 | (3) | 59 |
| Other | 370 | 19 | 389 |
| | **(3,993)** | **575** | **(3,418)** |

(in millions of Russian Roubles)

# Note 14. Borrowings

| | Currency | Effective Interest rate | 30 June 2007 | 31 December 2006 |
|---|---|---|---|---|
| ***Non-current borrowings*** | | | | |
| *Secured bank loans* | | | | |
| EBRD | RR | MosPrime+4%, MosPrime+2.75% | - | 7,200 |
| EBRD | USD | LIBOR+3.5% | - | 178 |
| IFC | USD | LIBOR+3.5% | - | 118 |
| *Unsecured bank loans* | | | | |
| Vneshtorgbank | RR | 8,50% | - | 2,787 |
| *Unsecured bonds* | | | | |
| Unsecured bond issue #1 | RR | 7,54% | 5,000 | 5,000 |
| Unsecured bond issue #2 | RR | 7,65% | 5,000 | 5,000 |
| *Other LT borrowings* | RR | | 159 | 155 |
| Total | | | **10,159** | **20,438** |
| ***Current borrowings and current portion of non-current borrowings*** | | | | |
| *Secured bank loans* | | | | |
| EBRD | RR | MosPrime+4%, MosPrime+2.75% | 7,200 | - |
| EBRD | USD | LIBOR+3.5% | 218 | 89 |
| IFC | USD | LIBOR+3.5% | 145 | 59 |
| EBRD | USD | LIBOR+4% | - | 432 |
| Total | | | **7,563** | **580** |
| | | | **17,722** | **21,018** |

The effective interest rate is the market interest rate applicable to the loan at the date of origination for fixed rate loan and the current market rate for floating rate loans.

Borrowings include fixed rate loans with a carrying value of RR 10,159 million and RR 12,942 million and fair value of RR 10,166 million and RR 12,949 million as of 30 June 2007 and 31 December 2006, respectively. All other borrowings generally have variable interest rates linked to LIBOR or MosPrime, and the carrying amounts approximates fair value.

The Group has not entered into any hedging arrangements in respect of its foreign currency obligation or interest rate exposure.

### (a) EBRD and IFC loans

These loans were obtained in April 1998 to finance capital expenditure. Loans from EBRD and IFC were received under non-revolving line of credit agreements (loan amount not to exceed USD 50 million in total). The full amount available under the agreements had been provided to the Group by 31 March 2001. The Group is required to make 18 principal payments on a semi-annual basis, beginning 15 January 2001. Interest is payable at the same time as the principal.

In August 2002 OAO Mosenergo obtained a loan from EBRD under a non-revolving line of credit for the amount of USD 70 million. OAO Mosenergo is required to make 10 principal payments semi-annually, beginning 28 May 2003. Interest is payable at the same time as the principal.

(in millions of Russian Roubles)

On 23 December 2005 the Group concluded the agreement with EBRD to open a credit line in the total amount of RR 7,200 million for more than 10 years. The credit line consisted of two credit lines in amounts of RR 2,900 million and RR 4,300 million respectively. The loan was obtained for the purchase of acquiring additional equipment for the Group. The loan interest on loans is determined on Mosprime plus basis.

The payment of interest on the loan is carried out on a quarterly basis, and the principal amount is to be repaid by 40 and 18 equal installments for the first and second credit lines respectively starting after 31 December 2007.

Net book value of fixed assets pledged as security for loans was RR 2,105 million and RR 679 million as of 30 June 2007 and 31 December 2006.

### (b) Unsecured bonds

On 2 March 2006 the placement of OAO Mosenergo's 5,000,000 unconvertible fixed interest rate bearing bonds took place through underwriter Gazprombank on the trading floor of Moscow Interbank Currency Exchange. The total amount of placement equaled RR 5 billion. The face value of each bond is RR 1,000 and term of maturity of ten years. Interest of 7.65% will be paid to the bond holders semiannually.

The bonds may become subject for early redemption only upon the decision of the issuer to grant such option to the bond holders. The main purpose of bond issues is to refinance short-term bank loans.

On 19 September 2006 OAO Mosenergo registered the second issue of 5,000,000 fixed interest rate bearing bonds with the face value of RR 1,000 and term of maturity of five years. The total amount of placement equaled RR 5 billion. Interest of 7.54% will be paid to the bond holders semiannually.

### (c) Borrowings maturity

As of 30 June 2007 OAO Mosenergo did not comply with debt service coverage requirement as stated in loan agreements with the EBRD and IFC. This breache gives the EBRD and IFC the right to demand immediate repayment of the loans. Therefore, in accordance with IAS 32, these loans were reclassified to current debt at the balance sheet date.

As of 30 June 2007 the maturity portfolio of long-term borrowings is presented below:

| | 30 June 2007 |
|---|---|
| Between one and two years | - |
| Between two and five years | 5,159 |
| After five years | 5,000 |
| | **10,159** |

(in millions of Russian Roubles)

# Note 15. Pension liabilities

The tables below provide information about the benefit obligations, plan assets and actuarial assumptions used for the period ended 30 June 2007. Amounts recognised in the consolidated balance sheet:

| | 30 June 2007 |
|---|---|
| Present value of defined benefit obligations (DBO) | 2,150 |
| Unrecognised actuarial gain | 125 |
| Unrecognised past service cost | (1,831) |
| | **444** |

Benefit expenses recognised in the consolidated income statement:

| | Six months ended 30 June 2007 |
|---|---|
| Current service cost | 67 |
| Interest cost | 74 |
| Amortisation of past service cost | 210 |
| Benefit plan amendment - immediate recognition of vested prior service cost | 213 |
| | **564** |

Changes in the present value of the Group's defined benefit obligation are as follows:

| | 30 June 2007 |
|---|---|
| Present value of defined benefit obligations (DBO) at 1 January 2007 | - |
| Current service cost | 67 |
| Interest cost | 74 |
| Actuarial gain | (125) |
| Past service cost | 2,019 |
| Benefits paid | (120) |
| Benefit plan amendment | 235 |
| **Present value of defined benefit obligations (DBO) at the end of period** | **2,150** |

Principal actuarial assumptions are as follows:

| | 30 June 2007 |
|---|---|
| Nominal discount rate | 6.8% |
| Wage growth rate | 7.0% |
| Inflation rate | 5.0% |

(in millions of Russian Roubles)

There were no changes in actuarial assumptions during the reporting period. Thus actuarial gains and losses arising during this period correspond to experience adjustments in full.

| | 30 June 2007 |
|---|---|
| Present value of defined benefit obligations (DBO) | (2,150) |
| Surplus in plan | (2,150) |
| Losses arising from experience adjustments on plan liabilities | (125) |

Expected payments under the schemes in the period starting 1 July 2007 till 31 December 2007 are RR 112 million.

## Note 16. Trade and other payables

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Trade payables | 3,144 | 2,581 |
| Account payable for acquisition of property, plant and equipment | 1,971 | 1,987 |
| Advances received | 1,167 | 1,028 |
| Accrued liabilities and other payables | 1,201 | 1,617 |
| Dividends payable | 889 | 1 |
| Financing from Moscow Government | 523 | 523 |
| | **8,895** | **7,737** |

Financing from the Moscow government relates to the funds received by the Group, on a return basis, as a contribution by the Moscow government towards the construction of distribution and heating network assets. Repayment terms stipulated that certain assets (as provided by further agreements), upon their completion, will be transferred to the Moscow government in the settlement of the above liability.

## Note 17. Other taxes payable

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Property tax | 279 | 174 |
| VAT payable | 271 | 527 |
| Payroll taxes payable | 169 | 203 |
| Other taxes payable | 128 | 171 |
| | **847** | **1,075** |

(in millions of Russian Roubles)

# Note 18. Revenues

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Electricity | 17,953 | 16,181 |
| Heating | 19,216 | 19,878 |
| Other | 2,353 | 2,953 |
| | **39,522** | **39,012** |

# Note 19. Operating expenses

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Fuel expenses | 19,006 | 18,178 |
| Subscription fees/Electricity and heat distribution expenses | 7,636 | 7,176 |
| Depreciation of property, plant and equipment and impairment (Note 5) | 3,384 | 2,382 |
| Wages and payroll taxes | 3,296 | 3,732 |
| Taxes other than income and payroll taxes | 1,353 | 147 |
| Repairs and maintenance | 1,102 | 1,010 |
| Other materials | 353 | 789 |
| Charge for impairment of trade and other receivables | 279 | 932 |
| Insurance cost | 235 | 36 |
| Benefit plan amendment – past service cost recognized immediately (Note 15) | 213 | - |
| Water usage expenses | 185 | 56 |
| Non-governmental pension fund expenses | 156 | - |
| Loss on disposal of property, plant and equipment | 44 | 118 |
| Social expenditures | 21 | 74 |
| Other | 2,265 | 4,643 |
| | **39,528** | **39,273** |

# Note 20. Finance costs, net

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Interest expense | 555 | 444 |
| Interest income | (305) | (3) |
| Foreign exchange gain | (11) | (76) |
| | **239** | **365** |

# Note 21. Earnings per share

The calculation of earnings per share is the net profit for the year period divided by the weighted average number of ordinary shares outstanding during the period, calculated as shown below. OAO Mosenergo does not have dilutive potential ordinary shares.

| *In thousands of shares* | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Weighted average number of ordinary shares issued (thousands) | 28,824,360 | 28,249,360 |
| Loss attributable to the shareholders of OAO Mosenergo for the period | (502) | (679) |
| **Earnings per ordinary share for loss attributable to the shareholders of OAO Mosenergo – basic and diluted (in Russian Roubles)** | **(0.02)** | **(0.02)** |

# Note 22. Financial Risk Management

### (a) Credit risk

Financial assets which potentially subject Group entities to concentrations of credit risk consist principally of trade receivables including promissory notes. Credit risks related to trade receivables are systematically monitored and are considered when the allowance for doubtful debtors is made. The carrying amount of trade receivables, net of the allowance for doubtful debtors, represents the maximum amount exposed to credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group other than to the extent to which provision for impairment of receivables has already been made.

Cash is placed in financial institutions, which are considered at time of deposit to have minimal risk of default.

### (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). The largest part of interest rate in long-term borrowings are fixed, which expose the Group to fair value interest rate risk.

Currently the Group does not operate a formal management program focusing on the unpredictability of financial markets or seeking to minimise potential adverse effects on the financial performance of the Group. However, at the time of taking new borrowings 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 operates within the Russian Federation. The majority of the Group's purchases are denominated in RR. The major concentration of foreign exchange risk is in relation to foreign currency denominated purchase commitments (Note 23) and foreign currency denominated debt (Note 14). Management does not hedge the Group's exposure to foreign currency risk.

### (d) Fair values

The fair value of borrowings is discussed in Note 14. Management believes that the fair value of other financial assets and financial liabilities is not significantly different from their carrying amounts.

Exposure to credit, interest rate and currency risk arises in the normal course of the Group's business. The Group does not have a risk policy to hedge its financial exposures.

## Note 23. Commitments

### (a) Fuel commitments

The Group has a number of outstanding fuel contracts. Gas supplies are mostly received from OOO Mosregiongas, a subsidiary of OAO Gazprom. The gas is supplied under annual agreement, which is effective till 31 December 2007. The quantity of gas to be supplied is determined based on the budgeted production requirements. The purchase price of the contract is fixed at the level determined by Government (FST).

### (b) Social commitments

The Group contributes to the maintenance and upkeep of the local infrastructure and the welfare of its employees, including contributions toward the construction, development and maintenance of housing, hospitals, recreation and other social needs in the geographical areas in which it operates.

### (c) Capital commitments

Future capital expenditure for which contracts have been signed amounted to RR 19,309 million at 30 June 2007 (RR 21,921 million as of 31 December 2006). RR 4,895 million of capital commitments as of 30 June 2007 are denominated in foreign currencies, mainly Euro and Swiss francs.

## Note 24. Contingencies

### (a) Tax and currency legislation

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

No disclosure has been made in respect of the possible financial effect of potential claims or disputes on these matters, as this might seriously prejudice the position of the Group.

As at 30 June 2007 management believes that its interpretation of the relevant legislation is appropriate and the Group's tax and currency positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued for in these financial statements.

### (b) Legal proceedings

The Group is a party to certain legal proceedings arising in the ordinary course of business. In general those legal proceedings relate to unreasonable application of tariffs. In the opinion of management, there are no current legal proceedings or other claims outstanding that, upon final disposition, will have a material adverse effect on the financial position of the Group.

As of the date of issuing these consolidated financial statements management believes that it has adequately provided for all significant potential losses that may result from any such claims being asserted and contested.

### (c) Compliance with covenants

The Group is subject to certain covenants related primarily to its borrowings. Non-compliance with such covenants may result in negative consequences for the Group including growth in the cost of borrowings and declaration of default.

### (d) Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately.

Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

### (e) Guarantees

The Group issued guarantees for mortgage loans of employees of RR 288 million as of 30 June 2007 (RR 212 million as of 31 December 2006).

## Note 25. Related parties

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

The nature of the related party relationships for these related parties with whom the Group entered into significant transactions or had significant balances outstanding for the periods ended 30 June 2007 and 2006 and as of 30 June 2007 and 31 December 2006 are detailed below.

### (a) Parent company and its subsidiaries

Gazprom Group owns of over 52% in OAO Mosenergo and has effective control over the Group's operations.

The Government of the Russian Federation is the ultimate controlling party of OAO Gazprom and has controlling interest (including both direct and indirect ownership) of over 50% in OAO Gazprom.

(in millions of Russian Roubles)

For the periods ended 30 June 2007 and 2006 and as of 30 June 2007 and 31 December 2006, respectively, the Group had the following significant transactions and balances with Gazprom Group:

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Revenue - other | 87 | 94 |
| Fuel expenses | (16,578) | (15,051) |
| Interest expense | (1) | (176) |
| Proceeds from current borrowings | 1,170 | 8,650 |
| Repayment of borrowings | 1,170 | 12,015 |

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Cash and cash equivalents | 1,093 | 2,347 |
| Other current assets | 22,212 | - |
| Trade receivables | 74 | - |
| Trade payables | 28 | 501 |
| Advances to suppliers and prepayments | - | 110 |

During the periods ended 30 June 2007 OAO Mosenergo placed and withdrew cash on short-term deposit in AB Gazpormbank (ZAO) for RR 6,300 million and RR 7,200 million, respectively.

### (c) Transactions with associates (OOO KB Transinvestbank)

Included within short-term account receivable and prepayments are account receivable from associated undertaking (OOO KB Transinvestbank) in the amount RR 1 million and RR nil as of 30 June 2007 and 31 December 2006, respectively.

During the periods ended 30 June 2007 and 2006 the Group provided rent services to OOO KB Transinvestbank for RR 2 million and RR 2 million, respectively.

During the periods ended 30 June 2007 and 2006 the Group received bank services from OOO KB Transinvestbank for RR 51 million and RR 72 million respectively.

Included in cash and cash equivalents of the Group are cash accounts with OOO KB Transinvestbank of RR 380 million and RR 587 million as of 30 June 2007 and 31 December 2006, respectively.

### (d) Transactions with key management

Key management personnel (the members of the Board of Directors and Management Committee of OAO Mosenergo) are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

The remuneration for serving on the Board of Directors is subject to approval by the General Meeting of Shareholders, compensation of key management personnel (other then remuneration for serving as members of Board of Directors) is determined by the terms of the employment contracts.

(in millions of Russian Roubles)

Total remuneration accrued and paid to the members of the Board of Directors for the periods ended 30 June 2007 and 2006 was as follows:

| | Six months ended 30 June 2007 | | Six months ended 30 June 2006 | |
|---|---|---|---|---|
| | **Expense** | **Accrued liability** | **Expense** | **Accrued liability** |
| Short-term compensation, including salary and bonuses | 75 | 3 | 7 | 4 |
| Remuneration for serving on the Board of Directors and Management Committee | 10 | 5 | 7 | 4 |

Short-term compensation include personal income tax and are net of unified social tax.

At 30 June 2007 and at 31 December 2006 there were 13 members of the Board of Directors and 13 members of the Management Committee.

### (f) Other state-controlled entities, besides OAO Gazprom and its subsidiaries

Information provided below excludes transactions and balances with OAO Gazprom and its subsidiaries that are disclosed in Note 25 (a) above.

In the normal course of business the Group enters into transactions with other entities under Government control.

Bank loans are provided on the basis of market rates. Taxes are accrued and settled in accordance with Russian tax legislation. Tax balances are disclosed in Note 17. Tax transactions are disclosed in the income statement.

For the periods ended 30 June 2007 and 2006 and as of 30 June 2007 and 31 December 2006, respectively, the Group had the following significant transactions and balances with Government and parties under control of the Government:

| | Six months ended 30 June 2007 | Six months ended 30 June 2006 |
|---|---|---|
| Revenue - electricity | 10,269 | 13,161 |
| Revenue - heat | 13,108 | 13,928 |
| Revenue - other | 1,242 | 694 |
| Operating expenses, including: | (9,530) | (8,952) |
| *Fuel expenses* | *(1,290)* | *(999)* |
| *Water usage expenses* | *(155)* | *(109)* |
| *Subscribtion fee/Electricity and heat distribution expenses* | *(7,636)* | *(7,453)* |
| *Other expense* | *(449)* | *(391)* |
| Interest expense | (159) | (11) |
| Proceeds from non-current borrowings | 2,859 | 2,000 |
| Proceeds from current borrowings | 1,213 | - |
| Repayment of borrowings | 6,859 | 2,000 |

(in millions of Russian Roubles)

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Cash and cash equivalents | 4,862 | 2 404 |
| Trade receivables (Net of provision for impairment of receivables of RR 1,133 million as at 30 June 2007 and RR 843 million as at 31 December 2006) | 4,008 | 1,316 |
| Other receivables (Net of provision for impairment of receivables of RR 298 as at 30 June 2007 and RR 255 as at 31 December 2006) | 56 | 285 |
| Advances to suppliers and prepayments | 2,278 | 2,213 |
| Trade payables | 1,983 | 1,078 |
| Accrued liabilities and other payables | 99 | 279 |
| Advances received | 638 | 32 |
| Non-current borrowings | - | 2 787 |

## Note 26. Events subsequent to the balance sheet date

### (a) Investments in OOO KB Transinvestbank

In July 2007 the Group acquired additional shares of OOO KB Transinvestbank representing 47.83% of its share capital. As at the date of sign-off of these financial statements, the total Group's share in OOO KB Transinvestbank's capital was 72.44%.

### (b) Kyoto protocol

In May 2007 the Resolution on Practical Implementation of the Kyoto Protocol Mechanisms in Russia was signed by the Chairman of the Russian Federation Government. The Group will now be able to go ahead with projects designed to improve energy efficiency and cut $CO_2$ emissions. According to RAO UES experts, these projects may generate over Euro 31.5 million in funds for OAO Mosenergo, which will be used to help modernize the existing and build new generation capacity using the most advanced power equipment.