# OGK-6 GROUP

## Consolidated Financial Statements
## prepared in accordance with
## International Financial Reporting Standards (IFRS)
## for the year ended
## 31 December 2008

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## Independent Auditors' Report

To the Board of Directors of Open Joint Stock Company "The Sixths Generating Company of the Wholesale Electric Power Market" (JSC "OGK-6")

### Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of JSC "OGK-6" (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at 31 December 2008, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flows statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

*Management's Responsibility for the Financial Statements*

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

*Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

ZAO KPMG, a company incorporated under the Laws of the Russian Federation and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative.

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

*Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2008, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO KPMG

ZAO KPMG

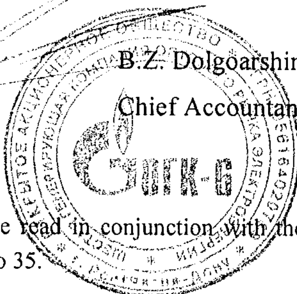
3 June 2009

| | Notes | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 5 | 53,751,322 | 31,567,910 |
| Other non-current assets | 6 | 1,253,464 | 604,720 |
| **Total non-current assets** | | **55,004,786** | **32,172,630** |
| **Current assets** | | | |
| Inventories | 7 | 4,585,801 | 3,255,204 |
| Short-term investments | 8 | 3,901,413 | 14,919,590 |
| Income tax receivable | | 413,818 | 400,798 |
| Other current assets | | 92,490 | 310,357 |
| Receivables and prepayments | 9 | 3,799,135 | 1,699,708 |
| Cash and cash equivalents | | 215,014 | 648,427 |
| **Total current assets** | | **13,007,671** | **21,234,084** |
| **TOTAL ASSETS** | | **68,012,457** | **53,406,714** |
| **EQUITY AND LIABILITIES** | | | |
| **Equity** | | | |
| Share capital-ordinary shares | 10 | 15,497,760 | 15,486,028 |
| Treasury shares | | - | (177) |
| Revaluation reserve | | 13,401,156 | - |
| Share premium | | 18,339,193 | 18,239,259 |
| Retained earnings | | 5,803,100 | 6,957,503 |
| **Total equity** | | **53,041,209** | **40,682,613** |
| **Non-current liabilities** | | | |
| Deferred income tax liabilities | 12 | 5,755,707 | 3,743,421 |
| Non-current debt | 11 | 2,923,677 | - |
| Employee benefits | 13 | 722,118 | 604,002 |
| Other non-current liabilities | | 34,972 | 278,304 |
| **Total non-current liabilities** | | **9,436,474** | **4,625,727** |
| **Current liabilities** | | | |
| Current debt and current portion of non-current debt | 11 | - | 5,000,000 |
| Accounts payable and accrued charges | 14 | 5,298,648 | 2,634,944 |
| Other taxes payable | | 236,126 | 463,430 |
| **Total current accounts payable** | | **5,543,774** | **8,098,374** |
| **Total liabilities** | | **14,971,248** | **12,724,101** |
| **TOTAL LIABILITIES AND EQUITY** | | **68,012,457** | **53,406,714** |

These consolidated financial statements were approved by management on 3 June 2009 and were signed on its behalf by:

A.A. Mityushov
General Director

B.Z. Dolgoarshinnikh
Chief Accountant





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 9 to 35.

| | Notes | 2008 '000 RUR | 2007 '000 RUR |
|---|---|---|---|
| Revenues | 15 | 42,275,050 | 35,333,819 |
| Operating expenses | 16 | (44,687,693) | (32,801,688) |
| Other (expenses)/income | | (155,796) | 369,058 |
| **Operating (loss)/profit** | | **(2,568,439)** | **2,901,189** |
| Finance income | 17 | 829,010 | 25,642 |
| Finance expenses | 17 | (357,907) | (606,935) |
| **(Loss)/profit before income tax** | | **(2,097,336)** | **2,319,896** |
| Income tax benefit/(expense) | 12 | 1,267,933 | (773,293) |
| **(Loss)/profit for the year** | | **(829,403)** | **1,546,603** |
| **(Loss)/earnings per ordinary share - basic and diluted (in Russian Roubles)** | 18 | (0.0257) | 0.0578 |



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 35.

| | Notes | 2008 '000 RUR | 2007 '000 RUR |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES:** | | | |
| **(Loss)/profit before income tax** | | **(2,097,336)** | **2,319,896** |
| Adjustments to reconcile profit before income tax to net cash provided by operations: | | | |
| Depreciation | 5 | 2,812,159 | 2,792,664 |
| Impairment loss of property, plant and equipment | 5 | 1,970,698 | - |
| Loss on disposal of property, plant and equipment | | 78,586 | - |
| Reversal of tax penalties | | - | (313,825) |
| Financial (income)/expenses | 17 | (471,103) | 571,171 |
| Other | | 246,136 | 61,692 |
| **Operating cash flows before working capital changes and income tax paid** | | **2,539,140** | **5,431,598** |
| Working capital changes: | | | |
| Change in accounts receivable and prepayments | | (1,945,930) | (618,855) |
| Change in inventories | | (1,387,080) | (335,722) |
| Change in other assets | | 217,868 | (101,496) |
| Change in other non-current assets | | (821,830) | (232,921) |
| Change in accounts payable and accruals | | 2,741,370 | 90,101 |
| Change in other non-current liabilities | | (101,606) | (3,749) |
| Change in taxes payable other than income tax | | (227,304) | (74,918) |
| **Cash provided by operating activities before interest and taxes** | | **1,014,628** | **4,154,038** |
| Interest paid | | (326,191) | (584,509) |
| Income tax paid | | (224,817) | (1,509,677) |
| **Net cash generated from operating activities** | | **463,620** | **2,059,852** |
| **CASH FLOWS FROM INVESTING ACTIVITIES:** | | | |
| Acquisition of property, plant and equipment | | (10,111,064) | (5,444,970) |
| Proceeds from/(acquisition of) short-term deposits | | 11,018,177 | (14,919,590) |
| Interests received | 17 | 829,010 | - |
| Proceeds from disposal of property, plant and equipment | | 11,949 | 61,784 |
| **Net cash from/(used in) investing activities** | | **1,748,072** | **(20,302,776)** |
| **CASH FLOWS FROM FINANCING ACTIVITIES:** | | | |
| Proceeds from borrowings | | 2,282,041 | 18,570,266 |
| Issue of share capital | | - | 20,894,377 |
| Repayment of borrowings | | (4,358,364) | (20,062,316) |
| Disposal/(acquisition) of treasury shares | | 177 | (177) |
| Dividends paid | | (568,959) | (654,057) |
| **Net cash (used in)/generated from financing activities** | | **(2,645,105)** | **18,748,043** |
| Change in cash and cash equivalents | | (433,413) | 505,169 |
| Cash and cash equivalents at the beginning of the year | | 648,427 | 143,258 |
| **Cash and cash equivalents at the end of the year** | | **215,014** | **648,427** |



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 9 to 35.

| '000 RUR | Ordinary share capital | Merger reserve | Revaluation reserve | Retained earnings | Share premium | Total equity |
|---|---|---|---|---|---|---|
| **As at 1 January 2007** | **26,731,061** | **(9,937,275)** | - | **2,282,917** | - | **19,076,703** |
| Profit for the year | - | - | - | 1,546,603 | - | 1,546,603 |
| **Total recognised income and expense** | - | - | - | - | - | **1,546,603** |
| Decrease in share capital | (13,900,152) | 9,937,275 | - | 3,845,485 | - | (117,392) |
| Issue of shares | 2,655,119 | - | - | - | 18,239,259 | 20,894,378 |
| Acquisition of treasury shares | - | - | - | (177) | - | (177) |
| Dividends | - | - | - | (717,502) | - | (717,502) |
| **As at 31 December 2007** | **15,486,028** | - | - | **6,957,326** | **18,239,259** | **40,682,613** |
| **As at 1 January 2008** | **15,486,028** | - | - | **6,957,326** | **18,239,259** | **40,682,613** |
| Loss for the year | - | - | - | (829,403) | - | (829,403) |
| Revaluation of property, plant and equipment | - | - | 13,401,156 | - | - | 13,401,156 |
| **Total recognised income and expense** | - | - | - | - | - | **12,571,753** |
| Dividends to shareholders | - | - | - | (325,000) | - | (325,000) |
| Disposal of treasury shares | | - | - | 177 | - | 177 |
| Acquisition under common control | 11,732 | - | - | - | 99,934 | 111,666 |
| **As at 31 December 2008** | **15,497,760** | - | **13,401,156** | **5,803,100** | **18,339,193** | **53,041,209** |



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 9 to 35.

# 1 Background

## (a) Business environment

The Russian Federation has 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 the Russian Federation involve risks that typically do not exist in other markets. In addition, the recent contraction in the capital and credit markets has further increased the level of economic uncertainty in the environment. The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

## (b) Organisation and operations

Open Joint Stock Company "The Sixths Generating Company of the Wholesale Electric Power Market" ("JSC "OGK-6", or "the Company") was established on 17 March 2005 within the framework of the Russian electricity sector restructuring in accordance with the Resolution of the Chairman of the Management Board of OJSC RAO Russian Open Joint Stock Company for Energy and Electrification Unified Energy System of Russia ("RAO UES") dated 16 March 2005.

JSC "OGK-6" and its following subsidiaries form the OGK-6 Group ("the Group"):

| | **As at 31 December 2008** | **As at 31 December 2007** |
|---|---|---|
| OJSC Agricultural entity Voskhod | 100% | 100% |
| OJSC OJSC Novomichurinskoe Vehicle Transportation Company | 100% | 100% |

During the year the Group operated 6 power plants: Kirishskaya GRES, Ryazanskaya GRES, Novochercasskaya GRES, Krasnoyarskaya GRES-2, Cherepovetskaya GRES, GRES-24.

The Group's principle activity is generation and sale of electricity and heat.

The registered office of JSC "OGK-6" is located at 49, Bolshaya Sadovaya st., 344007, Rostov-on-Don, Russia. The head office of JSC "OGK-6" is located at 21 Mytnaya st., 115162, Moscow, Russia.

## (c) Current regulation and industry restructuring

The Government of the Russian Federation directly affects the Group's operations through regulation by the Federal Tariff Service ("FTS"), with respect to its wholesale energy sales, and by the Regional Energy Commissions ("RECs") or by the Regional Tariff Services ("RTSs"), with respect to its heat sales. The operations of all generating facilities are coordinated by OJSC "System Operator – the Central Despatch Unit of Unified Energy System" ("SO-CDU") in order to meet system requirements in an efficient manner. SO-CDU is controlled by NP "Administrator of trade system".

In 2008 the Government ratified the decree on the launch of the capacity market in Russia, whose main goal is to ensure in short, middle and long terms the availability of the working generating facilities in the United energy systems of Russia so that it will be enough to cover all electric energy consumption in the system at any time with the relative reliability and quality parameters (including reserves). The draft decree on the capacity market stipulates the availability of two models: transition model – till 2011 and target model.

At present under the transition model the following mechanisms of capacity trade are applied:

1. At regulated prices:

- purchase/sale of capacity under regulated contracts, at prices set by Federal Tariff Service; volumes sold under regulated contracts shall decrease year by year according to liberalization schedule.

2. At free prices:

- purchase/sale of capacity through free bilateral contracts (this is possible only between counterparties of regulated contracts);

- purchase/sale of capacity as a result of the competitive capacity auction.

## 2 Financial condition

As discussed above, the Group is affected by policy of the Government of the Russian Federation through the control of tariffs and other factors. The regulated electricity tariffs are indexed mainly on fuel cost increases based on average national indicators set by FST/MERT, regardless of specific plant costs. Capacity Tariffs are driven by the inflation rate. Moreover, these tariffs consider costs only on a Russian statutory basis and, accordingly, exclude additional costs recognised under the 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.

## 3 Basis of preparation

### (a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs").

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.

### (b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that derivative financial instruments, investments at fair value through profit or loss, financial investments classified as available-for-sale and property, plant and equipment are measured at fair value.

### (c) Prior year reclassifications

Certain comparative figures for 2007 have been reclassified to conform to the 2008 financial statements presentation.

### (d) Functional and presentation currency

The national currency of the Russian Federation is the Russian Rouble ("RUR"), which is the Group's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in RUR has been rounded to the nearest thousand.

### (e) Use of judgments, estimates and assumptions

Management has made a number of judgments, 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 IFRSs. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

In particular, significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements include:

*Provision for impairment of accounts receivable*

Provision for impairment of accounts receivable 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.

*Revaluation of property, plant and equipment and other assets*

Fair value of property, plant and equipment has been determined by an independent appraiser based on the depreciated replacement cost method. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence. 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. See effect of these critical accounting estimates and assumptions in Note 5.

*Useful lives of property, plant and equipment*

The estimation of the useful lives of items of property, plant and equipment is a matter of management judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustments for future depreciation rates.

*Retirement benefit liabilities*

The Group uses an actuarial valuation method for measurement of the present value of post-employment benefit obligations and related current service cost. This involves the use of demographic assumptions about the future characteristics of the current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, disability and early retirement, etc.) as well as financial assumptions (discount rate, future salary and benefit levels, etc.).

*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 financial statements.

## 4 Significant accounting policies

The significant accounting policies applied in the preparation of the consolidated financial statements are described below. These accounting policies have been consistently applied.

### (a) Basis of consolidation

#### *(i) Subsidiaries*

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

#### *(ii) Transactions eliminated on consolidation*

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

#### *(iii) Transactions under common control*

Transfers of subsidiaries between parties under common control are accounted for using the predecessor basis of accounting method. Under this method the financial statements of the combined entity are presented

as if the businesses had been combined from the beginning of the earliest period presented. The assets and liabilities of the subsidiary transferred under common control are recognised at the predecessor entity's carrying amounts. Any difference between the carrying amount of net assets and the nominal value of share capital contributed is accounted for in these consolidated financial statements as an adjustment to equity.

**(b) Foreign currency transactions**

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising in translation are recognised in the income statement, except for differences arising on the translation of available-for-sale equity instruments.

**(c) Non-derivative financial instruments**

Non-derivative financial instruments comprise investments in equity, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

Cash and cash equivalents comprise cash balances and call deposits. Cash equivalents comprise short-term highly 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. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

*Held-to-maturity investments*

If the Group has the positive intent and ability to hold debt securities to maturity, then they are classified as held-to-maturity. Held-to-maturity investments are measured at amortised cost using the effective interest method, less any impairment losses.

*Available-for-sale financial assets*

The Group's investments in equity securities and certain debt securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses, and foreign exchange gains and losses on available-for-sale monetary items are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to the income statement.

*Financial assets at fair value through profit or loss*

An instrument is classified as at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Upon initial recognition attributable transaction costs are recognised in the income statement when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in the income statement.

*Other*

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses. Investments in equity securities that are not quoted on a stock exchange are principally valued using valuation techniques such as discounted cash flow analysis, option pricing models and comparisons to other transactions and instruments that are substantially the same. Where fair value cannot be estimated on a reasonable basis by other means, investments are stated at cost less impairment losses.

**(d) Share capital**

*Ordinary shares*

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

*Repurchase of share capital*

When share capital recognised as equity is repurchased, the amount of the consideration paid, which includes directly attributable costs, is net of any tax effects, and is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to / from retained earnings.

**(e) Dividends**

Dividends are recognized 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.

**(f) Inventories**

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the weighted average principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

**(g) Property, plant and equipment**

As at 31 December 2007 property, plant and equipment was stated at the carrying value determined in accordance with the IFRS as at the date of their transfer to the Group by the Predecessor, and adjusted taking into account further additions, disposals and depreciation charges.

Effective 1 January 2008, the Group changed its accounting policy to revaluing its property, plant and equipment at fair value from that date. Management believes that this resulted 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 the asset revaluation reserve in equity. However, the increase shall be recognised in the income statement to the extent that it reverses a revaluation decrease of the same asset previously recognised in the income statement. Decreases that offset previous increases of the same asset are charged against the revaluation reserve directly in equity; all other decreases are charged to the income statement. The Group does not transfer revaluation surplus directly to retained earnings when the asset is derecognized or as the asset is used by the entity.

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.

Renewals and improvements are capitalized and the carrying amounts of assets replaced are retired, if it is probable that the future economic benefits embodied within the newly installed parts will flow to the Group and its cost can be measured reliably. The costs of repair and maintenance are expensed as incurred.

Gains and losses arising from the retirement of property, plant and equipment are included in the income statement as incurred.

Depreciation of property, plant and equipment is calculated on a straight-line basis over the estimated useful life of the asset when it is available for use.

The estimated useful lives of assets by types of facility are as follows:

- Electricity and heat generation 22-54 years
- Electricity distribution 11-32 years
- Heating networks 10-30 years
- Other 7-37 years

Social assets are not capitalized 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.

**(h) Determination of fair values**

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

***(i) Property, plant and equipment***

The fair value of property, plant and equipment is based on market values, when possible. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of items of plant, equipment, fixtures and fittings is based on quoted market prices for similar items.

When no quoted market prices are available, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence. Information about significant assumptions used in determination of depreciation replacement cost is described in Note 5.

***(ii) Investments in equity and debt securities***

The fair value of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets is determined by reference to their quoted closing bid price at the reporting date. The fair value of held-to-maturity investments is determined for disclosure purposes only.

***(iii) Trade and other receivables***

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

***(iv) Non-derivative financial liabilities***

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

**(i) Impairment**

***(i) Financial assets***

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

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

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

All impairment losses are recognised in the income statement. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to the income statement.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in the income statement. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

*(ii) Non-financial assets*

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

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit").

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

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

### (j) Debt

Debt is recognised initially at its fair value net of transaction costs. If it is significantly different from the transaction price, fair value is determined using the prevailing market interest rate for a similar instrument. In subsequent periods, debt is stated at amortized cost using the effective rate method; any difference between the fair value at initial recognition (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.

### (k) Borrowing costs

Borrowing costs related to the acquisition or construction of qualifying assets are capitalized as part of that assets.

### (l) 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 in employee benefit expenses and payroll taxes in the income statement.

The Group operates defined benefit plans that cover the majority of the Group's employees. Benefit plans define 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 recognized in the balance sheet in respect of the defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognized actuarial gains or losses and unrecognized 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, and that have terms to maturity approximating the terms of the related pension liabilities.

Actuarial gains and losses arising from changes in actuarial assumptions and exceeding the higher of 10% of the defined benefit obligations and fair value of plan assets are charged or credited to the income statement over the average remaining service lives of employees starting from the next reporting period.

Past service costs are amortized over vesting period of 10.5 years.

**(m) Provisions**

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. 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 the risks specific to the liability.

**(n) Guarantees**

Where the Group enters into financial guarantee contracts to guarantee the indebtedness of other companies under common control, the Group considers these to be insurance arrangements, and accounts for them as such. In this respect, the Group treats the guarantee contract as a contingent liability until such time as it becomes probable that the Group will be required to make a payment under the guarantee.

**(o) Revenue recognition**

Revenue is recognized on the delivery of electricity, heat and on the dispatch of non-utility goods and services during the period. Revenue amounts are presented exclusive of value added tax. Revenue is based on the application of authorized tariffs for electricity sales as approved by the Regional Tariffs Authorities.

**(p) Finance income and expenses**

Finance income comprises dividend income, gains on the disposal of available-for-sale financial assets and foreign currency gains. Interest income is recognised as it accrues in the income statement, using the effective interest method. Dividend income is recognised in the income statement on the date that the Group's right to receive payment is established.

Finance expenses comprise interest expense on borrowings, foreign currency losses and impairment losses recognised on financial assets, other than trade receivables. Borrowing costs, except borrowing costs related to the acquisition or construction of qualifying assets as described in Note 4 (k), are recognised in the income statement using the effective interest method.

Foreign currency gains and losses are reported on a net basis.

**(q) Income tax expense**

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

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

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor

taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### (r) Earnings per share

The Group presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. The Group has no outstanding dilutive instruments.

### (s) Segment reporting

The Group operates predominantly in a single geographical area and industry, the generation of electric power and heat in Russian Federation. 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.

### (t) Seasonality of operations

Demand for 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. Furthermore, during the periods of lower production from April to September, there is an increase in the expenditures on repairs and maintenance. This seasonality does not impact the revenue or cost recognition policies of the Group.

### (u) New Standards and Interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2008, and have not been applied in preparing these consolidated financial statements. The Group plans to adopt these pronouncements when they become effective.

- IFRS 8 *Operating Segments*, which becomes mandatory for the Group's 2009 consolidated financial statements, introduces the "management approach" to segment reporting and requires the disclosure of segment information based on the internal reports regularly reviewed by the Group's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them. The Group is currently assessing what impact the standard will have on segment disclosures in the consolidated financial statements.

- Revised IAS 1 *Presentation of Financial Statements (2007)* which becomes mandatory for the Group's 2009 consolidated financial statements is expected to have a significant impact on the presentation of the consolidated financial statements. The Standard introduces the concept of total comprehensive income and requires presentation of all owner changes in equity in the statement of changes in equity, separately from non-owner changes in equity. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances.

- Revised IAS 23 *Borrowing Costs* removes the option to expense borrowing costs and requires that an entity capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. The revised IAS 23 will become mandatory for the Group's 2009 consolidated financial statements and will constitute a change in accounting policy for the Group. Future adoption of the revised IAS 23 will not have any impact on the consolidated financial statements as borrowing costs are capitalised in accordance with the Group's current accounting policy.

- Amended IAS 27 *Consolidated and Separate Financial Statements* (2008) requires accounting for changes in ownership interests by the Group in a subsidiary, while maintaining control, to be recognised as an equity transaction. When the Group loses control of a subsidiary, any interest retained in the former subsidiary will be measured at fair value with the gain or loss recognised in profit or loss. The amendments to IAS 27, which become mandatory for the Group's 2010 consolidated financial statements, are not expected to have a significant impact on the consolidated financial statements.

- Amendments to IAS 32 *Financial instruments: Presentation* and IAS 1 *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation* requires puttable instruments, and instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation, to be classified as equity if certain conditions are met. The amendments, which become mandatory for the Group's 2009 consolidated financial statements, with retrospective application required, are not expected to have any impact on the consolidated financial statements.

- Amendment to IAS 39 *Financial Instruments*: Recognition and Measurement – Eligible Hedged Items clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The amendment, which becomes mandatory for the Group's 2010 consolidated financial statements, with retrospective application required, is not expected to have any impact on the consolidated financial statements.

- Amendment to IFRS 2 *Share-based Payment – Vesting conditions and cancellations* clarify the definition of vesting conditions, introduce the concept of non-vesting conditions, require non-vesting conditions to be reflected in grant-date fair value and provide the accounting treatment for non-vesting conditions and cancellations. The amendments to IFRS 2 will become mandatory for the Group's 2009 consolidated financial statements, with retrospective application. The Group has not yet determined the potential effect of the amendment.

- Revised IFRS 3 *Business Combinations* (2008) and amended IAS 27 (2008) *Consolidated and Separate Financial Statements*, which come into effect on 1 July 2009 (i.e. become mandatory for the Group's 2010 consolidated financial statements). The revisions address, among others, accounting for step acquisitions, require acquisition-related costs to be recognised as expenses and remove exception for changes in contingent consideration to be accounted by adjusting goodwill. The revisions also address how non-controlling interests in subsidiaries should be measured upon acquisition and require to recognise the effects of transactions with non-controlling interest directly in equity. The Group has not yet analysed the likely impact of the new Standard on its financial position or performance.

- IFRIC 17 *Distributions of Non-cash Assets to Owners* addresses the accounting of non-cash dividend distributions to owners. The interpretation clarifies when and how the non-cash dividend should be recognised and how the differences between the dividend paid and the carrying amount of the net assets distributed should be recognised. IFRIC 17 becomes effective for annual periods beginning on or after 1 July 2009.

- Various Improvements to IFRSs have been dealt with on a standard-by-standard basis. All amendments, which result in accounting changes for presentation, recognition or measurement purpose, will come into effect not earlier than 1 January 2009. The Group has not yet analysed the likely impact of the improvements on its financial position or performance.

# 5 Property, plant and equipment

## (a) Fair value or cost

| '000 RUR | Electricity and heat generation | Electricity transmission | Heating networks | Other | Construction in progress | Total |
|---|---|---|---|---|---|---|
| ***Cost / Revalued amount*** | | | | | | |
| Balance at 1 January 2007 | **36,301,128** | **2,317,267** | **192,263** | **9,247,807** | **840,249** | **48,898,714** |
| Additions | 639,492 | 12,414 | - | 158,807 | 4,703,522 | **5,514,235** |
| Transfers | 22,549 | 100,226 | - | 191,528 | (314,303) | **-** |
| Disposals | (15,905) | - | - | (10,554) | (1,687) | **(28,146)** |
| Balance at 31 December 2007 | **36,947,264** | **2,429,907** | **192,263** | **9,587,588** | **5,227,781** | **54,384,803** |
| Revaluation at 1 January 2008 | 29,229,762 | 257,885 | 375,749 | 9,000,070 | - | 38,863,466 |
| Net off - Accumulated depreciation at 1 January 2008 | (15,337,760) | (1,334,347) | (85,204) | (6,059,582) | - | (22,816,893) |
| Balance at 1 January 2008 after revaluation | 50,839,266 | 1,353,445 | 482,808 | 12,528,076 | 5,227,781 | 70,431,376 |
| Additions | - | - | 85,953 | 127,871 | 10,091,535 | 10,305,359 |
| Transfers | 398,731 | 105,671 | - | 704,746 | (1,209,148) | - |
| Disposals | (48,767) | (11,406) | (555) | (32,736) | (5,356) | (98,820) |
| Revaluation at 31 December 2008 | (17,948,341) | (257,885) | (189,905) | (3,715,890) | - | (22,112,021) |
| Net off - Accumulated depreciation at 31 December 2008 | (1,836,511) | (149,423) | (30,879) | (787,061) | - | (2,803,874) |
| Balance at 31 December 2008 | **31,404,378** | **1,040,402** | **347,422** | **8,825,006** | **14,104,812** | **55,722,020** |
| ***Depreciation and impairment losses*** | | | | | | |
| Balance at 1 January 2007 | **13,145,151** | **1,256,212** | **75,125** | **5,568,641** | - | **20,045,129** |
| Depreciation for the period | 2,206,230 | 78,135 | 10,079 | 498,220 | - | **2,792,664** |
| Disposals | (13,621) | - | | (7,279) | - | **(20,900)** |
| Balance at 31 December 2007 | **15,337,760** | **1,334,347** | **85,204** | **6,059,582** | - | **22,816,893** |
| Net off - Accumulated depreciation at 1 January 2008 | (15,337,760) | (1,334,347) | (85,204) | (6,059,582) | - | (22,816,893) |
| Balance at 1 January 2008 after revaluation | - | - | - | - | - | - |
| Depreciation for the period | 1,839,906 | 149,797 | 30,907 | 791,549 | - | 2,812,159 |
| Disposals | (3,395) | (374) | (28) | (4,488) | - | (8,285) |
| Net off - Accumulated depreciation at 31 December 2008 | (1,836,511) | (149,423) | (30,879) | (787,061) | - | (2,803,874) |
| Impairment loss | 128,589 | 201,804 | 77,828 | 338,356 | 1,224,121 | 1,970,698 |
| Balance at 31 December 2008 | **128,589** | **201,804** | **77,828** | **338,356** | **1,224,121** | **1,970,698** |
| ***Net book value*** | | | | | | |
| Balance at 1 January 2007 | **23,155,977** | **1,061,055** | **117,138** | **3,679,166** | **840,249** | **28,853,585** |
| Balance at 31 December 2007 | **21,609,504** | **1,095,560** | **107,059** | **3,528,006** | **5,227,781** | **31,567,910** |
| Balance at 1 January 2008 after revaluation | **50,839,266** | **1,353,445** | **482,808** | **12,528,076** | **5,227,781** | **70,431,376** |
| Balance at 31 December 2008 | **31,275,789** | **838,598** | **269,594** | **8,486,650** | **12,880,691** | **53,751,322** |

Construction in progress as at 31 December 2008 and 31 December 2007 includes prepayments for property, plant and equipment in amount of RUR 8,635,763 thousand and RUR 2,877,867 thousand respectively.

None of the property, plant or equipment was pledged as collateral according to loan agreements.

**(b) Revaluation**

Effective 1 January 2008, the Group changed its accounting policy to revaluing its property, plant and equipment from that date. Management believes that this resulted in a more meaningful presentation of the Group's financial position and financial performance.

*Revaluation as at 1 January 2008*

The Group's management commissioned CJSC "Rossiyskaya otsenka" to independently appraise property, plant and equipment as at 1 January 2008. The fair value was determined to be RUR 66,835,148 thousand.

The majority of the Company's property, plants and equipment is specialised in nature and is rarely sold on the open market other than as a part of continuing business. The market for similar property, plant and equipment is not active and does not provide a sufficient number of sales of comparable property, plant and equipment for using a market-based approach for determining fair value.

Consequently the fair value of property, plant and equipment was primarily determined using depreciated replacement cost. The replacement cost of buildings, constructions and transmission equipment has been estimated based on technical characteristics, unit construction cost and construction estimates. The replacement cost of equipment was estimated based on data of aggregate replacement cost of heat-power station, current purchase contracts and price-list of producers and trading companies. The economic obsolescence was estimated based on cash flow projections for each cash-generating unit – Kirishskaya GRES, Novocherkasskaya GRES, Ryazanskaya GRES, Krasnoyarskaya GRES, Cherepovetskaya GRES, GRES-24.

The following key assumptions were used in performing the cash flow testing as at 1 January 2008:

- A discount rate of 12.97% was applied in determining the recoverable amount. The discount rate was estimated based on weighted average cost of capital, which was based on a possible range of debt leveraging of 56.82% at a market interest rate of 11.50%.
- Cash flows were projected based on actual operating results for 2008 and the twelve-year business plan.
- Cash flows were projected based on the anticipated average price which is based on Federal Tariff Service regulation and assumed to change in line with weighted average price of fuel. Fuel prices are projected based on official (Ministry of Economic Development and Trade) forecasts and trends.
- Dynamics of sales share attributable to non-regulated market are in line with Government resolutions' requirements: after 2011 electricity is anticipated to be sold on non-regulated market except of volumes of electricity intended for households, due to this 10% of electricity is assumed to continue to be sold at regulated prices.
- The anticipated annual production growth included in the cash flow projections was 0%.
- A terminal value was derived at the end of the 13-year interim period. A terminal rate of 12.97% was considered in estimating the terminal value of the plants.

As a result the Group's equity increased by RUR 31,090,773 thousand, comprising an increase in carrying value of property, plant and equipment of RUR 38,863,466 thousand (net of related deferred tax of RUR 7,772,693 thousand).

*Revaluation as at 31 December 2008*

Given the current economic downturn the management commissioned CJSC "Rossiyskaya otsenka" to conduct additional testing of economic obsolescence of property, plant and equipment based on cash flow projections as at 31 December 2008. The fair value was determined to be RUR 45,115,559 thousand.

The following key assumptions were used in performing the cash flow testing as at 31 December 2008:

- A discount rate of 16.51% was applied in determining the recoverable amount. The discount rate was estimated based on weighted average cost of capital, which was based on a possible range of debt leveraging of 62.65% at a market interest rate of 17.00%.
- Cash flows were projected based on actual operating results for 2008 and the twelve-year business plan.
- Cash flows were projected based on the anticipated average price which is based on Federal Tariff Service regulation and assumed to change in line with weighted average price of fuel. Fuel prices are projected based on official (Ministry of Economic Development and Trade) forecasts and trends.
- Dynamics of sales share attributable to non-regulated market are in line with Government resolutions' requirements: after 2011 electricity is anticipated to be sold on non-regulated market except of volumes of electricity intended for households, due to this 10% of electricity is assumed to continue to be sold at regulated prices.
- The anticipated annual production growth included in the cash flow projections was 0%.
- A terminal value was derived at the end of the 13-year interim period. A terminal rate of 16.51% was considered in estimating the terminal value of the plants.

As a result, the Group recognised a decrease of carrying amount of property, plant and equipment of RUR 24,082,719 thousand, which was charged against previously recognised valuation surplus in amount of RUR 17,689,617 thousand (net of related deferred tax of RUR 4,422,404 thousand) and to the income statement as impairment loss in amount of RUR 1,970,698 thousand.

Each revalued class of property, plant and equipment is stated at a revalued amount in these financial statements. The carrying amounts that would have been recognised had the assets been carried under the cost model are as follows:

| '000 RUR | Electricity and heat generation | Electricity transmission | Heating networks | Other | Construction in progress | Total |
|---|---|---|---|---|---|---|
| At 1 January 2008 | **21,609,504** | **1,095,560** | **107,059** | **3,528,006** | **5,227,781** | **31,567,910** |
| At 31 December 2008 | **20,385,189** | **1,088,298** | **192,789** | **3,937,260** | **13,642,544** | **39,246,080** |

*Useful lives*

As a part of the revaluation of property plant and equipment the Group management has reviewed the remaining useful lives of property, plant and equipment at 1 January 2008. As a result, the useful lives of certain elements of property, plant and equipment were extended, which had a positive impact on this year's depreciation charge. The useful lives are disclosed in Note 4(g).

## (c) Operating leases

The Group leases a number of land areas owned by local government under operating lease. Land lease payments are determined by lease agreements. Operating land lease rentals are payable as follows:

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Less than one year | 67,487 | 123,392 |
| Between one and five years | 189,393 | 472,026 |
| More than five years | 1,161,447 | 1,334,987 |
| **Total** | **1,418,327** | **1,930,405** |

Generally the leases run for an initial period of 5-49 years with an option to renew the lease after that date. Lease payments are reviewed regularly to reflect market rentals.

Operating lease rentals for other fixed assets are payable as follows:

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Less than one year | 111,013 | 98,805 |
| Between one and five years | 103,231 | 202,107 |
| More than five years | 220 | 8,207 |
| **Total** | **214,464** | **309,119** |

## 6 Other non-current assets

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| VAT recoverable | 639,295 | 369,269 |
| Other non-current assets | 400,830 | 8,141 |
| Trade accounts receivable | 387,269 | 368,787 |
| Investments | 89,164 | - |
| Allowance for impairment of trade accounts receivable | (263,094) | (141,477) |
| **Total** | **1,253,464** | **604,720** |

## 7 Inventories

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Fuel | 3,679,364 | 2,297,047 |
| Spare parts | 539,353 | 577,748 |
| Materials and supplies | 438,979 | 368,797 |
| Other inventories | 1,907 | 28,931 |
| Provision for slow-moving and obsolete inventory | (73,802) | (17,319) |
| **Total** | **4,585,801** | **3,255,204** |

None of the inventories held were pledged as collateral according to loan agreements.

## 8 Short-term investments

As at 31 December 2008 cash in the amount of RUR 3,901,413 thousand was deposited with JS "Gazenergoprombank" at the interest rates of 10% - 12.5%.

## 9 Accounts receivable and prepayments

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Advances to suppliers and prepayments | 1,716,858 | 732,345 |
| Trade receivables | 1,431,999 | 728,338 |
| Other receivables | 464,261 | 164,493 |
| VAT recoverable | 300,229 | 342,241 |
| Allowance for impairment of prepayments | (956) | (7,211) |
| Allowance for impairment of trade receivables | (44,220) | (180,881) |
| Allowance for impairment of other receivables | (69,036) | (79,617) |
| **Total** | **3,799,135** | **1,699,708** |

## 10 Equity

### (a) Share capital

| | 31 December 2008 | 31 December 2007 |
|---|---|---|
| **Number of shares issued and fully paid** | 32,287,001,231 | 32,262,558,936 |
| Par value (RUR) | 0,48 | 0,48 |
| **Total** | **15,497,760** | **15,486,028** |

As at 1 January 2007, the number of issued ordinary shares amounted to 26,731,061,492 with a par value of RUR 1.00 each.

On 10 April 2007 Shareholders of the Company resolved to decrease share capital of the Company from RUR 26,731,061,492 to RR 12,830,909,516 by decreasing the nominal value of the outstanding shares from RUR 1.00 to RR 0.48. The decrease of the share capital was performed in accordance with the requirements of the Federal Law "On Joint Stock Companies" which stipulates that net assets shall be equal or exceed charter capital.

On 29 June 2007 the General Shareholders' Meeting of the Company made the decision to increase the Company's share capital by placing additional shares.

During the period from 20 to 29 December 2007 the Company placed 5,531,497 thousand additional shares from which CJSC "Gazenergoprom-Invest", the affiliated company of OJSC "Gazprom", acquired 5,526,000 thousand shares.

The placement price of a share was approved by the Board of Directors of the Company in amount of RUR 3.80 for each additionally issued share that exceeded the nominal value by RUR 3.32. The resulted share premium amounted to RUR 18,239,259 thousand, including expenses on share issue in the amount of RUR 125,313 thousand.

As at 31 December 2007, the number of issued ordinary shares amounted to 32,262,558,936 with a par value of RUR 0.48 each.

In July 2008 the Group issued 24,442,295 ordinary shares. The shares were placed by conversion of shares of OJSC "OGK-6 Holding" to the shares of the Company in the spin-off process of OJSC "OGK-6 Holding" from RAO "UES of Russia".

This transaction under common control resulted in an increase in the share capital and in the share premium reserve of the Group by RUR 11,732 thousand and RUR 99,934 thousand, respectively.

As at 31 December 2008, the number of issued ordinary shares amounted to 32,287,001,231 with a par value of RUR 0.48 each.

### (b) Dividends

In accordance with Russian legislation the Company's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with Russian Accounting Principles. As at 31 December 2008 the Company had accumulated losses, including profit for the current year, of RUR 2,480,261 thousand (2007: RUR 2,967,218 thousand).

On 11 June 2008 the General Shareholders meeting of the Company approved interim dividends to the shareholders for the 1st quarter of 2008 in total amount of RUR 325,000 thousand.

## 11 Loans and borrowings

| | Currency | Interest rate | Amount '000 EUR | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|---|---|---|
| *Non-current liabilities* | | | | | |
| Bonded loan | RUR | 7,55% | | 2,874,136 | - |
| CJSC Unicreditbank | EUR | 8,63% | 1,195 | 49,541 | - |
| | | | | 2,923,677 | - |
| *Current liabilities* | | | | | |
| Bonded loan | RUR | 7,55% | | - | 5,000,000 |
| | | | | - | 5,000,000 |

On 26 April 2007 the Group completed a public offering of interest bearing non-convertible bonds, with a mandatory centralised custody. The number of issued bonds was 5,000,000 with a nominal value of RUR 1,000 per each bond, with maturity of 5 years with 3-year buy-back option.

As at 31 December 2007 the Group recognised the bonds as current liabilities because of possible early redemption due to anticipated reorganisation in the form of the merger with OJSC "OGK-6 Holding" in accordance with article 15 of the Federal Law on joint stock companies. During the year 2008 bonds of RUR 2,125,864 thousand were redempted.

As at 31 December 2008 bonds of RUR 2,874,136 thousand were not claimed for the early redemption and were reclassified to non-current liabilities.

On 24 April 2008 the Group fulfilled its obligations related to the payment of the second coupon yield on the bonds. Fixed interest rate coupon yield was 7,55% per annum. The amount of yield paid was RUR 296,461 thousand.

On 23 October 2008 the Group paid off third coupon yield on the bonds at the same rate in the amount of RUR 108,211 thousand.

## 12 Income tax

| | 2008<br>'000 RUR | 2007<br>'000 RUR |
|---|---|---|
| ***Current tax expense*** | | |
| Current year | 589,786 | 874,739 |
| Underprovided in prior years | - | 11,780 |
| Current tax charge | **589,786** | **886,519** |
| ***Deferred tax expense*** | | |
| Origination and reversal of temporary differences | (856,920) | (113,226) |
| Reimbursement of prior periods tax claims | (519,716) | - |
| Change in tax rate | (481,083) | - |
| **Total income tax (benefit) / charge** | **(1,267,933)** | **773,293** |

During 2008, the Group entities were subject to 24% income tax rate on taxable profits (2007: 24%). With effect from 1 January 2009 the income tax rate for Russian companies has been reduced to 20%. This rate has been used for the calculation of the deferred tax assets and liabilities.

In accordance with Russian tax legislation, tax losses in different Group companies may not be offset against taxable profits of other Group companies. Accordingly, tax may be accrued even where there is a net consolidated tax loss.

For the reporting purposes net profit before tax is reconciled with the tax charge as follows:

| | 2008<br>'000 RUR | % | 2007<br>'000 RUR | % |
|---|---|---|---|---|
| (Loss) / profit before tax | (2,097,336) | (100) | 2,319,896 | 100 |
| Theoretical tax (benefit) / charge at an average statutory tax rate of 24% | (503,361) | (24) | 556,775 | 24 |
| Underprovided in prior years | - | - | 11,780 | 1 |
| Reimbursement of prior periods tax claims | (519,716) | (25) | - | - |
| Change in tax rate | (481,083) | (22) | - | - |
| Non-deductible expenses | 236,227 | 11 | 204,738 | 8 |
| **Total income tax (benefit)/charge** | **(1,267,933)** | **(60)** | **773,293** | **33** |

| **'000 RUR** | **31 December 2007** | **Movement for the period recognized in the income statement** | **Movement for the period recognized directly in equity** | **31 December 2008** |
|---|---|---|---|---|
| Property, plant and equipment | (4,235,804) | 1,537,171 | (3,350,289) | (6,048,922) |
| Accounts receivable | 222,284 | (184,411) | - | 37,873 |
| Tax loss | 66,245 | (54,517) | - | 11,728 |
| Other | 203,854 | 39,760 | - | 243,614 |
| **Total** | **(3,743,421)** | **1,338,003** | **(3,350,289)** | **(5,755,707)** |

| | 31 December 2006 | Movement for the period recognized in the income Statement | Movement for the period recognized directly in equity | 31 December 2007 |
|---|---|---|---|---|
| Property, plant and equipment | (4,599,951) | 364,147 | - | (4,235,804) |
| Accounts receivable | 325,467 | (103,183) | - | 222,284 |
| Tax loss | 226,649 | (160,404) | - | 66,245 |
| Other | 191,188 | 12,666 | - | 203,854 |
| **Total** | **(3,856,647)** | **113,226** | - | **(3,743,421)** |

## 13 Employee benefits

The tables below provide information about the benefit obligations and actuarial assumptions used for the years ended 31 December 2008 and 2007.

| | 31 December 2008 | 31 December 2007 |
|---|---|---|
| | '000 RUR | '000 RUR |
| Present value of defined benefit obligations (unfunded) | 985,894 | 958,948 |
| Unrecognized net actuarial loss | (184,340) | (236,392) |
| Unrecognised past service cost | (79,436) | (118,554) |
| Net liability in the balance sheet | **722,118** | **604,002** |

Amounts recognized in the consolidated income statement:

| | 2008 | 2007 |
|---|---|---|
| | '000 RUR | '000 RUR |
| Current service cost | 36,633 | 37,582 |
| Interest cost | 64,195 | 51,538 |
| Net actuarial losses recognised in period | 30,638 | 4,727 |
| Amortisation of past service cost | 39,118 | 37,326 |
| Settlement gain | - | (111,572) |
| Immediate recognition of vested prior service cost | - | 155,904 |
| **Total** | **170,584** | **175,505** |

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

| | 31 December 2008 | 31 December 2007 |
|---|---|---|
| | '000 RUR | '000 RUR |
| Present value of defined benefit obligations at beginning of year | 958,948 | 811,012 |
| Service cost | 36,633 | 37,582 |
| Interest cost | 64,195 | 51,538 |
| Actuarial (gain)/loss | (21,414) | 121,285 |
| Past service cost | - | 179,758 |
| Benefits paid | (52,468) | (71,766) |
| Settlement gain | - | (170,461) |
| Present value of defined benefit obligations at end of year | **985,894** | **958,948** |

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Net liability at beginning of year | 604,002 | 500,263 |
| Net expense recognised in the income statement | 170,584 | 175,505 |
| Benefits paid | (52,468) | (71,766) |
| Net liability at end of year | 722,118 | 604,002 |

Principal actuarial assumptions are as follows:

| | 31 December 2008 | 31 December 2007 |
|---|---|---|
| Discount rate | 9,0% | 6.75% |
| Pension increase (excl. annuities via non-state pension fund) | 7,0% | 6.0% |
| Inflation | 7,0% | 6.0% |
| Salary increase | 8,0% | 7.0% |

## 14 Accounts payable and accrued charges

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Trade payables | 3,524,803 | 1,964,993 |
| Advances received | 1,274,161 | 13,517 |
| Other payables | 321,176 | 258,857 |
| Payables to employees | 164,378 | 139,488 |
| Dividends payable | 14,130 | 258,089 |
| Total | **5,298,648** | **2,634,944** |

## 15 Revenues

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Electricity | 39,878,613 | 33,145,823 |
| Heating | 2,036,637 | 1,884,964 |
| Other | 359,800 | 303,032 |
| | **42,275,050** | **35,333,819** |

## 16 Operating expenses

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Fuel expenses | 24,271,556 | 17,898,648 |
| Purchased heat and electricity | 4,619,039 | 3,362,873 |
| Employee benefit expenses and payroll taxes | 3,601,541 | 2,854,555 |
| Depreciation charge | 2,812,159 | 2,792,664 |
| Impairment of property, plant and equipment | 1,970,698 | - |
| Repairs and maintenance | 1,834,597 | 1,252,532 |
| Other materials | 1,572,695 | 1,328,932 |
| Water usage expenses | 1,085,434 | 916,310 |
| Energy market infrastructure cost | 639,936 | 505,088 |
| Taxes | 437,181 | 413,639 |
| Rent and lease payments | 372,299 | 318,112 |
| Electricity transmission | 317,448 | 334,813 |
| Security and fire safety | 193,234 | 182,704 |
| Transport | 150,291 | 192,793 |
| Consulting, legal and information services | 132,537 | 101,864 |
| Insurance | 122,549 | 152,994 |
| Loss on disposal of property, plant and equipment | 78,576 | - |
| Charity expenditure | 70,473 | 75,699 |
| Impairment of inventories | 59,043 | 49,280 |
| (Reversal) / origination of allowance for accounts receivable | (31,880) | 56,829 |
| Other | 378,287 | 11,359 |
| **Total** | **44,687,693** | **32,801,688** |

Employee benefits expenses comprise the following:

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Salaries and wages, payroll taxes | 3,218,107 | 2,507,379 |
| Financial aid to employees and pensioners | 277,045 | 223,209 |
| Non-governmental pension fund expenses | 106,389 | 123,967 |
| | **3,601,541** | **2,854,555** |

## 17 Finance income/expenses

*Finance income*

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Interest income | 829,010 | 25,642 |
| **Total** | **829,010** | **25,642** |

*Finance expenses*

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Interest expense | (306,438) | (591,670) |
| Discounting of accounts receivable | (51,469) | (5,143) |
| Other | - | (10,122) |
| **Total** | **(357,907)** | **(606,935)** |

## 18 Earnings per share

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Weighted average number of ordinary shares issued (thousand) | 32,274,780 | 26,731,061 |
| (Loss)/profit for the year | (829,403) | 1,546,603 |
| **(Loss)/Earnings per ordinary share – basic and diluted (in RUR)** | **(0.0257)** | **0.0578** |

## 19 Commitments

### (a) Fuel commitments

The Group has signed a number of agreements for the fuel purchases. These agreements do not cover all the needs of the Group. The remaining part of the fuel required by the Group will be purchased on short-term agreements from a number of suppliers with immediate payment terms.

The quantity of supplies is determined annually on the basis of fuel stocks requirements.

The Group has entered into several long-term contracts for the supply of gas and coal that will be used in the ordinary course of the Group's activities. The pricing terms of these contracts are based on market prices.

At the end of 2008, the Group concluded the following fuel purchase contracts:

- Coal for the 2009-2011 of 5.7 million tons;
- Limited gas for 2009-2012 of 3.8 billion $m^3$;
- Additional gas for 2009-2010 of 1.4 billion $m^3$.

### (b) Capital commitments

Future capital expenditures for which contracts have been signed, amount to RUR 39,323,148 thousand and RUR 14,001,617 thousand on 31 December 2008 and 31 December 2007, respectively.

## 20 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.

### (b) Insurance

The Group holds limited insurance policies in relation to its assets, operations, public liability or other insurable risks. Hence, the Group is exposed to those risks for which it does not have insurance.

### (c) Legal proceedings

The Group was not a party to any legal proceedings which, upon final disposition, will have a material adverse effect on the financial position of the Group.

### (d) Taxation

The taxation system in the Russian Federation 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 the Russian Federation 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 tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

### (e) Environmental matters

Group entities and their predecessor entities have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement posture of the government authorities is continually being reconsidered. Group entities periodically evaluate their obligations under the environmental regulations.

Potential liabilities might arise as a result of changes in the legislation and regulations or civil litigation. The impact of these potential changes 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.

### (f) Guarantees

During the year the Group issued guarantees on behalf of OJSC "Mezhregionenergosbyt" to "Alteya Finance" LLC, "Sigma" LLC and OJSC "Joint stock bank "Rossiya" in the amount of RUR 2,725,000 thousand (2007: 0).

OJSC "Mezhregionenergosbyt" is a wholly owned subsidiary of the Group's parent company, OJSC "Gazprom" and has a strong credit history. Management believes that possibility of default in relation to the above-mentioned obligations is remote.

## 21 Related party transactions

Before 1 July 2008 RAO UES, the state-controlled entity, owned 77.45% of the Group. The remaining 22.55% of ordinary shares were placed among a large number of shareholders.

Effective 1 July 2008 OJSC "Gazprom" owns 60% of the Group's shares. The Russian Government is the ultimate controlling party of the Group.

Related parties include the ultimate beneficiaries, affiliates and entities under common ownership and control within the Group.

In the normal course of business the Group enters into transactions with related parties. Prices for natural gas, electricity and heat are based on tariffs set by FTS and RTS. Taxes are charged and paid under the Russian tax legislation. Other sales and purchase transactions are based on normal market prices.

### (a) Transactions with state-controlled entities

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Energy and heat sales | 21,356,997 | 12,185,191 |
| Other sales | 116,210 | 82,886 |
| Fuel purchases | 15,137,201 | 10,917,542 |
| Energy market infrastructure cost | 639,936 | 505,088 |
| Interest expense | 586,150 | 11,902 |

The outstanding balances with related parties were as follows:

| | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
|---|---|---|
| Short-term investments | 3,901,413 | 8,518,420 |
| Receivables and prepayments | 1,160,677 | 2,088,625 |
| Accounts payables and accrued charges | 84,716 | 492,341 |
| Dividends payable | - | 244,463 |
| Allowance for impairment of receivables and prepayments | (196,949) | (284,930) |

### (b) Transactions with management and close family members

Compensation is paid to members of the Management Board of the Company (hereinafter – the "Management Board") for their services in full time management positions and is made up of a contractual salary, non-cash benefits, and a performance bonus depending on the results for the period according to Russian statutory financial statements. The compensation is approved by the Board of Directors of the Company. Optional bonuses, which are approved by the Chairman of the Management Board according to his perception of the value of their contribution, are also payable to members of the Management Board.

Key management received the following remuneration during the years ended 31 December 2008 and 2007:

| | Year ended 31 December 2008 '000 RUR | Year ended 31 December 2007 '000 RUR |
|---|---|---|
| Termination costs | 132,273 | - |
| Salaries and bonuses | 125,620 | 132,897 |
| Payroll taxes | 4,114 | 2,656 |
| Other | 13,762 | - |
| **Total** | **275,769** | **135,553** |

## 22 Financial instruments and financial risk factors

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk.

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

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

The Group established a number of controls over compliance with Group's risk management policies and procedures. On a quarterly basis, the Group's Audit Committee reviews managements actions and estimates the adequacy of the measures taken in relation to the risks faced by the Group. The Group's Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures as well as day-to-day activities and reports to the Audit Committee on a monthly basis.

The Group's activities expose it to a variety of financial risks, including the effects of changes in foreign currency exchange rates, changes in interest rates, and the collectibility of receivables. The Group does not have a risk policy to hedge its financial exposures.

### (a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

#### Exposure to credit risk

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

| | | Carrying amount | |
|---|---|---|---|
| | Note | 31 December 2008 '000 RUR | 31 December 2007 '000 RUR |
| **Available-for-sale financial assets** | | | |
| Investments | 6 | 89,164 | - |
| **Loans and receivables** | | | |
| Long-term accounts receivable | 6 | 124,175 | 227,310 |
| Short-term investments | 8 | 3,901,413 | 14,919,590 |
| Trade and other accounts receivable | 9 | 1,783,004 | 632,333 |
| Cash and cash equivalents | | 215,014 | 648,427 |
| **Total** | | **6,112,770** | **16,427,660** |

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

**Impairment losses**

The aging of trade receivables at the reporting date was:

| | 31 December 2008 | | 31 December 2007 | |
|---|---|---|---|---|
| | Gross '000 RUR | Impairment '000 RUR | Gross '000 RUR | Impairment '000 RUR |
| Not past due | 896,592 | - | 415,486 | - |
| Past due 3-6 months | 555,455 | - | 113,668 | - |
| More than 6 months | 59,907 | - | 245,613 | - |
| More than 1 year | 307,314 | (307,314) | 322,358 | (322,358) |
| | **1,819,268** | **(307,314)** | **1,097,125** | **(322,358)** |

The Group's management believes that Group entities will be able to realize the net receivable amount through direct collections and other non-cash settlements, and that therefore the recorded values approximate their fair values. The individually impaired receivables mainly relate to energocompanies which are in difficult economic situation. The aging of these receivables is over 1 year old.

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

| | 2008 '000 RUR | 2007 '000 RUR |
|---|---|---|
| **1 January** | **322,358** | **339 024** |
| Increase during the period | 159,083 | 225 793 |
| Decrease due to recognized impairment loss | (1,968) | (56 902) |
| Decrease due to reversal | (172,159) | (185,557) |
| **31 December** | **307,314** | **322,358** |

**(b) Liquidity risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements. Values presented in the table reflect non-discounted cash flows.

| '000 RUR | Carrying amount | Contractual cash flows | 0-6 mths | 6-12 mths | 1-2 years | 2-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2008** | | | | | | | |
| Non-derivative financial liabilities: | | | | | | | |
| Bonded loan | 2,874,136 | 3,631,545 | 108,201 | 108,201 | 432,806 | 2,982,337 | - |
| Bank loan | 49,541 | 70,906 | - | 4,273 | 4,273 | 62,360 | - |
| Accounts payable | 4,024,487 | 4,024,487 | 3,963,965 | 33,415 | 26,601 | 3 | 503 |
| **As at 31 December 2007** | | | | | | | |
| Non-derivative financial liabilities: | | | | | | | |
| Bonded loan | 5,000,000 | 6,694,136 | 94,126 | 94,127 | 376,506 | 6,129,377 | - |
| Accounts payable | 2,621,427 | 2,621,427 | 2,557,225 | 4,579 | 47,800 | 10,500 | 1,323 |

### (c) Market risk

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

Power and heat produced by the Group is sold on the internal market of Russian Federation with prices fixed in the currency of Russian Federation. Hence, the Group is not subject to the foreign currency exchange risk. The financial condition of the Company, its liquidity, financing sources and the results of activities do not considerably depend on currency rates as the Group activities are planned to be performed in such a way that its assets and liabilities are denominated in the national currency.

Although the Group may from time to time conclude contracts in foreign currency for implementation of investment program or other purposes, the Group's management considers the currency risk on financial performance and operations in case of unfavourable changes of foreign currency rates as minimal due to insignificance of underlying amounts. The Group sees market risk principally in the risk of a change in interest rates.

### (d) 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 raising new loans or 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.

The Group's income and operating cash flows are largely independent of changes in market interest rates. The Group is exposed to interest rate risk only through market value fluctuations of interest-bearing assets, loans and borrowings. The interest rates on most long- and short-term interest-bearing assets, loans and borrowings are fixed.

Since the power industry is regarded as a capital-intensive one, reinforcement of the Group's market standing would require significant capital endowments. The Group is planning to raise additional debt capital in accordance to its planned financial policy. The increase of market interest rates would increase the cost of borrowed funds attracted by the Group for financing of its investment program and operations. But at the same time, the growth of market interest rates would decrease the real cost of capital of existing fixed-rate loans.

**Fair values versus carrying amounts**

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows:

| | 31 December 2008 | | 31 December 2007 | |
|---|---|---|---|---|
| | Carrying amount '000 RUR | Fair value '000 RUR | Carrying amount '000 RUR | Fair value '000 RUR |
| Investments | 89,164 | 89,164 | - | - |
| Cash and cash equivalents | 215,014 | 215,014 | 648,427 | 648,427 |
| Bank deposits | 3,901,413 | 3,901,413 | 14,919,590 | 14,919,590 |
| Trade and other receivables | 1,783,004 | 1,783,004 | 632,333 | 632,333 |
| Long term trade receivables | 124,175 | 124,175 | 227,310 | 227,310 |
| **Total assets** | **6,112,770** | **6,112,770** | **16,427,660** | **16,427,660** |
| **Non-derivative financial liabilities** | | | | |
| Accounts payable and accrued charges | 4,024,487 | 4,024,487 | 2,621,427 | 2,621,427 |
| Bonded loan | 2,874,136 | 2,578,788 | 5,000,000 | 5,000,000 |
| Bank loan | 49,541 | 49,541 | - | - |
| **Total liabilities** | **6,948,164** | **6,652,816** | **7,621,427** | **7,621,427** |

Management believes that the fair value of its financial assets and liabilities approximates their carrying amounts.

## 23 Capital risk management

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

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents. Total capital is calculated as equity, as shown in the consolidated balance sheet, plus net debt. The gearing ratios at 31 December 2008 and at 31 December 2007 were as follows:

| | 31 December 2008 | 31 December 2007 |
|---|---|---|
| | '000 RUR | '000 RUR |
| Total borrowings | 2,923,677 | 5,000,000 |
| Less: cash and cash equivalents (Note 10) | (215,014) | (648,428) |
| Net debt | 2,708,663 | 4,351,572 |
| Total equity | 53,041,209 | 40,682,613 |
| **Total capital** | **55,749,872** | **45,034,185** |
| Gearing ratio | 4,9% | 10% |