TGC-2 GROUP
COMBINED AND CONSOLIDATED FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) FOR THE YEAR ENDED 31 DECEMBER 2006

PRICEWATERHOUSECOOPERS

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of Open Joint Stock Company "Territorial Generating Company # 2" (OJSC "TGC-2"):

We have audited the accompanying combined and consolidated financial statements of OJSC "TGC-2" and its subsidiaries (the "Group") which comprise the combined and consolidated balance sheet as at 31 December 2006, the combined and consolidated income statement, combined and consolidated statement of changes in equity and combined and consolidated statement of cash flows 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 combined and consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these combined and consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from 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 policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

PRICEWATERHOUSECOOPERS

INDEPENDENT AUDITOR'S REPORT

Opinion

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

Emphasis of Matter

Without qualifying our opinion, we draw your attention to Notes 1 and 8 to the accompanying combined and consolidated financial statements. The Government of the Russian Federation has an ultimate controlling interest in the Group and Governmental economic and social policies affect the Group financial position, results of operations and cash flows.

Without qualifying our opinion, we draw attention to Note 5 of the accompanying combined and consolidated financial statements. These combined and consolidated financial statements include carved - out of revenues and expenses of predecessor legal entities that had other business activities, related to the periods: from 1 to 10 January 2005 of electricity and heat generating divisions within OJSC Yarenergo and OJSC Tverenergo; from 1 January to 31 March 2005 - of electricity and heat generating divisions within OJSC Novgorodenergo; from 1 January to 30 September 2005 - of electricity and heat generating divisions within OJSC Vologdaenergo. Because of the various determinations used in carving – out such revenues and expenses, as described in Note 5 and elsewhere in these combined and consolidated financial statements, those revenues and expenses related to the electricity and heat generation operations within predecessor legal entities may not be indicative of revenues expected to be earned and costs expected to be incurred on a prospective basis for the electricity and heat generation operations within the TGC-2 Group as a separate business and, as such, these combined and consolidated financial statements may not be indicative of future results of operations and trends.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation

17 December 2007

TGC-2 Group
Combined and Consolidated Balance Sheet as at 31 December 2006

(in thousands of Russian Roubles)

	Notes	31 December 2006	31 December 2005
Non-current assets			
Property, plant and equipment	9	10,528,368	5,714,726
Deferred income tax assets	16	-	303,136
Other non-current assets	10	284,586	133,823
Total non-current assets		**10,812,954**	**6,151,685**
Current Assets			
Cash and cash equivalents	14	69,894	122,582
Accounts receivable and prepayments	13	1,168,912	1,334,864
Income tax prepayment		102,980	17,017
Inventories	11	1,079,097	759,568
Other current assets	12	278,032	100
Total current assets		**2,698,915**	**2,234,131**
TOTAL ASSETS		13,511,869	8,385,816
EQUITY AND LIABILITIES			
Share capital	15	7,117,127	10,000
Merger reserve	15	(1,872,193)	2,749,061
Retained earnings/(loss)		2,759,763	8,610
Equity attributable to parent company		**8,004,697**	**2,767,671**
Minority interest		-	3,041,116
Total equity		**8,004,697**	**5,808,787**
Non-current Liabilities			
Deferred income tax liabilities	16	923,663	220,567
Non-current borrowings	18	-	28,146
Pension liabilities	17	142,153	130,815
Other non-current liabilities		6,680	17,506
Total non-current liabilities		**1,072,496**	**397,034**
Current liabilities			
Current borrowings and current portion of non-current	18	3,369,652	1,051,532
Accounts payable and accrued liabilities	19	735,510	596,881
Income tax payable		6,330	71,045
Other taxes payable	20	323,184	460,537
Total current liabilities		**4,434,676**	**2,179,995**
Total liabilities		**5,507,172**	**2,577,029**
TOTAL EQUITY AND LIABILITIES		**13,511,869**	**8,385,816**

General Director A.A. Vagner

Chief Accountant Y.V. Ivanova

17 December 2007

TGC-2 Group
Combined and Consolidated Income Statement for the year ended 31 December 2006

(in thousands of Russian Roubles)

	Notes	Year ended 31 December 2006	Year ended 31 December 2005
Revenues			
Sales of electricity		3,781,522	3,648,951
Sales of heating		5,301,888	4,481,918
Other sales		627,015	387,404
Total revenues		**9,710,425**	**8,518,273**
Operating expenses	21	(10,292,468)	(8,443,832)
Other operating income		162,211	182,619
Release of impairment of property, plant and equipment	9	4,323,699	-
Operating profit		**3,903,867**	**257,060**
Finance income	22	10,656	781
Finance costs	22	(296,898)	(181,359)
Profit before income tax		**3,617,625**	**76,482**
Income tax charge	16	(57,107)	(133,243)
Deferred income tax	16	(1,006,232)	94,937
Profit for the year		**2,554,286**	**38,176**
Profit/(loss) attributable to:			
Parent company shareholders		2,927,402	19,246
Minority interest		(373,116)	18,930
Weighted average earnings per ordinary and preference share – basic and diluted (in RR)	24	0.008	0.027

General Director A.A. Vagner

Chief Accountant Y.V. Ivanova

17 December 2007

TGC-2 Group
Combined and Consolidated Cash Flow Statement for the year ended 31 December 2006

(in thousands of Russian Roubles)

	Notes	Year ended 31 December 2006	Year ended 31 December 2005
CASH FLOW FROM OPERATING ACTIVITIES:			
Profit before income tax		**3,617,625**	**76,482**
Adjustments to reconcile profit before income tax and net cash from operating activities:			
Depreciation of property, plant and equipment	9,21	471,253	600,874
Impairment loss reversed during the year	9	(4,323,699)	-
Provision for impairment of accounts receivable	13,21	301,032	290,279
Write off accounts receivable	21	8,628	1,802
Reversal of provision for obsolete inventories	11	(13,187)	959
Finance income	22	(10,656)	(781)
Finance costs	22	286,498	175,310
Loss on discounting of non-current accounts	21	284,617	-
Loss on discounting of loans issued to employees	21	9,606	3,578
Gain on disposal of subsidiaries	23	(66,554)	-
Charge of post-employment benefits obligations	17	10,400	4,464
Loss on disposal of property, plant and equipment		20,360	32,092
Gain on disposal of other assets		(1,339)	-
Operating cash flows before working capital changes and income tax paid		**594,584**	**1,185,059**
Working capital changes:			
Increase in accounts receivable		(651,707)	(382,974)
Increase in inventories		(306,342)	(171,318)
Increase in accounts payable and accrued liabilities		104,708	80,720
Increase in other non-current assets		(54,561)	-
Decrease in other non-current liabilities		(13,683)	(16,852)
(Decrease)/increase in taxes payable other than income tax		(137,353)	164,055
Income tax paid		(207,785)	(62,198)
Net cash generated by operating activities		**(672,139)**	**796,492**
CASH FLOW FROM INVESTING ACTIVITIES:			
Purchase of property, plant and equipment		(844,580)	(627,732)
Proceeds from sales of property, plant and equipment		3,244	-
Proceeds from disposals of subsidiaries	23	78,500	-
Issuing of loans to third parties		(450,000)	-
Proceeds from loans from third parties		173,400	-
Interest received		10,698	11
Net cash used for investing activities		**(1,028,738)**	**(627,721)**
CASH FLOW FROM FINANCING ACTIVITIES:			
Proceeds from borrowings		7,779,412	2,295,122
Repayment of borrowings		(5,489,438)	(2,351,492)
Interest paid		(282,341)	(140,471)
Dividends paid		(359,444)	-
Proceeds from shares issuance		-	10,000
Net cash generated by/(used for) financing activities		**1,648,189**	**(186,841)**
Decrease in cash and cash equivalents		**(52,688)**	**(18,070)**
Cash and cash equivalents at the beginning of the year	14	**122,582**	**140,652**
Cash and cash equivalents at the end of the year	14	**69,894**	**122,582**

General Director A.A. Vagner

Chief Accountant Y.V. Ivanova

17 December 2007

TGC-2 Group
Combined and Consolidated Statement Of Changes In Equity for the year ended 31 December 2006

(in thousands of Russian Roubles)

	Attributable to the parent's shareholders				Minority interest	Total Equity
	Share capital	Merger reserve	Retained earnings	Total		
At 1 January 2005	**-**	**2,749,061**	**-**	**2,749,061**	**3,033,176**	**5,782,237**
Issuance of shares (Note 15)	10,000	-	-	10,000	-	10,000
Profit for the year	-	-	19,246	19,246	18,930	38,176
Dividends (Note 15)	-	-	(10,636)	(10,636)	(10,990)	(21,626)
At 31 December 2005	**10,000**	**2,749,061**	**8,610**	**2,767,671**	**3,041,116**	**5,808,787**
At 1 January 2006	**10,000**	**2,749,061**	**8,610**	**2,767,671**	**3,041,116**	**5,808,787**
Profit for the year	-	-	2,927,402	2,927,402	(373,116)	2,554,286
Dividends (Note 15)	-	-	(176,249)	(176,249)	(182,127)	(358,376)
Issuance of shares (Note 15)	7,107,127	(4,621,254)	-	2,485,873	(2,485,873)	-
At 31 December 2006	**7,117,127**	**(1,872,193)**	**2,759,763**	**8,004,697**	**-**	**8,004,697**

General Director — A.A. Vagner

Chief Accountant — Y.V. Ivanova

17 December 2007

(in thousands of Russian Roubles, unless otherwise stated)

Note 1. The Group and its operations

Open Joint-Stock Company "Territorial Generating Company-2" ("TGC-2") was established on 19 April 2005 within the framework of Russian electricity sector restructuring in accordance with the Resolution of the Board of directors of OJSC RAO UES of Russia (minutes No. 188 of 25 February 2005) and Instruction of the Chairman of the Management Board of OJSC RAO UES of Russia (minutes No. 93 of 18 April 2005).The structure and principles of foundation of TGC-2 were adopted by the Board of Directors of OJSC RAO UES of Russia on 23 April 2004 (Resolution No. 168).

In accordance with the above Resolution:

- On 19 April 2005 TGC-2 was established;
- On 13 April 2006 the OJSC RAO UES Board of Directors approved the share conversion ratios estimated by independent valuators for the regional generating companies (hereinafter – RGC's) being merged into and with TGC-2;
- On 28 February, 09, 13 and 27 March and 10 April 2006 TGC-2 and five of the RGC's held general shareholders' meetings at which the decisions were taken on reorganization of TGC-2 in the form of a merger with OJSC Yaroslavskaya Energy Company (Yaroslavskaya EC), OJSC Tverskaya Generating Company (Tverskaya GC), OJSC Novgorodskaya Generating Company (Novgorodskaya GC), OJSC Kostromskaya Generating Company (Kostromskaya GC), OJSC Vologodskaya HePP (Vologodskaya HePP).
- For share conversion purposes, the TGC-2 declared additional issuance and placement of 699,328,533,458 ordinary shares with the par value of 0.01 Russian Rouble and 11,384,171,043 preference shares with the par value of 0.01 RR for total amount of RR 7,107,127 thousand. As a result of the conversion the shareholders of RGC's became the shareholders of the united single company TGC-2, and the minority interest was removed at the TGC-2 level;
- On 1 July 2006 Yaroslavskaya GC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP had ceased operating as legal entities and their assets had merged into and with TGC-2;

During the merger, OJSC Kostromaenergoremont, OJSC Novgorodenergoservice and OJSC HePP Belyi Ruchei being the subsidiaries of Kostromskaya GC, Novgorodskaya GC and Vologodskaya HePP, respectively, became the subsidiaries of TGC-2:

Name	% owned	Location	Activities
OJSC Kostromaenergoremont	100%	Kostroma	Repair and construction
OJSC Novgorodenergoservice	100%	Novgorod	Repair and construction
OJSC HePP Belyi Ruchei	87.14%	Vologda	Generation of electricity and heat

OJSC Kostromaenergoremont was sold in November 2006 (see Note 23).

As at 31 December 2006 the 1st stage of the process of merger of assets of the RGC's into and with TGC-2 and forming of the united company TGC-2 (hereinafter - the "Group") has been completed.

The merger of assets of Arkhangelskaya Generating Company into and with TGC-2 in course of the 2nd and the last stage of forming the united company TGC-2 was completed in May 2007.

The TGC-2 Group as at 31 December 2006 for the purpose of preparation of the combined and consolidated accounts financial statements includes TGC-2 and five regional generating companies (Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP), whose assets were merged into and with TGC-2 as at 1 July 2006, and its subsidiaries, OJSC Novgorodenergoservice and OJSC HePP Belyi Ruchei.

OJSC Novgorodenergoservice was subsequently disposed of (see Note 28).

The combined and consolidated financial statements of the Group do not include the financial information of OJSC Arkhangelskaya Generating Company (Arkhangelskaya GC) whose assets are merged into and with TGC-2 in May 2007.

The Group principal activity is generation of electricity and heat in the Central and North Russia.

The Group owns 13 electric power stations, 8 boiler plants and 2 heating distribution companies. Total installed electric power capacity of the Group is 1,375.0 MW; total heating capacity – 8,384 Gkal/h.

Note 1. The Group and its operations (continued)

The Group is registered with the Inspectorate of the Russian Federal Tax Service for the Leninsky District, the city of Yaroslavl.

The Group's registered office is located at 42, prospekt Octyabrya, Yaroslavl, Russian Federation.

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

Relations with the state and current regulation. As at 31 December 2006 the Russian Open Joint Stock Company for Energy and Electrification Unified Energy System of Russia owns 49.18 % of voting ordinary shares of TGC-2. The Russian Government is the ultimate controlling party of the Group.

The Group customer base includes a large number of entities controlled by or related to the Government of the Russian Federation. Moreover, the state controls a number of the Group fuel and other suppliers (see Note 8).

The Government of the Russian Federation directly affects the Group operations through regulating by the Federal Service on Tariffs (FST), with respect to their wholesale energy sales, and through regulating by the regional services on tariffs (RST's), with respect to retail electricity and heating sales.

The operations of all generating facilities are coordinated by The System Operator – the Central Dispatch Unit of the Unified Electric System (SO-CDU), a subsidiary of OJSC RAO UES of Russia.

Tariffs which the Group may charge for sales of electricity are governed by regulations specific to the electricity industry and by regulations applicable to natural monopolies. Historically, such tariffs have been based on a "cost-plus" system, meaning cost of service plus a margin, where costs are determined under the Regulations on Accounting and Reporting of the Russian Federation ("RAR"), a basis of accounting which significantly differs from International Financial Reporting Standards ("IFRS"). In practice, tariff decisions were impacted significantly by social and political considerations, causing significant delays in tariff determinations and tariff increases that were lower than required to compensate for cost increases. As described in Note 2, the tariff structure in the Russian electric utilities industry is undergoing a liberalization process, which should lead to a competitive market-based tariff structure.

Also, as described in Notes 2, 25 and 26, the Russian government's economic, social and other policies could have material effect on the operations of the Group.

Regulatory issues and sector restructuring. The Russian electric utilities industry in general and the Group in particular are presently undergoing a reform process designed to introduce competition into the electricity sector and to create an environment in which energy companies can raise the capital required to maintain and expand current capacity.

- The regulatory framework governing the process of reforming the Russian Federation electric utilities industry and the functioning of the industry, both during the transition period and subsequent to the completion of reforms, is set forth in the following legislation: Federal Law No.35-FZ of 26 March 2003 "On Electric Utilities" and Federal Law No.36-FZ of 26 March 2003 "On the Specifics of the Functioning of Electric Utilities During the Transition Period" and the Introduction of Amendments to Certain Russian Federation Legislative Acts and the Invalidation of Certain Russian Federation Legislative Acts in Connection with the Adoption of the Law "On the Electric Utilities of the Russian Federation".
- As at 29 May 2003, the Board of Directors of OJSC RAO UES approved a "Concept of OJSC RAO UES strategy for the period from 2003 through 2008" (further – the "Concept of OJSC RAO UES Strategy").This document provides a detailed description of the major changes that are planned to take place in the OJSC RAO UES companies during the electric utilities reform program.

Note 1. The Group and its operations (continued)

- In October 2003, the Russian Federation Government issued Resolution No. 643 "On the Rules for the Wholesale Electricity (Power) Market during the Transition Period». According to the rules adopted, there were two sectors within the Federal Wholesale Electricity (Power) Market (FOREM): the regulated trading sector and free trading sector. Within the free trading sector, electricity suppliers were able to sell electricity generated with the use of facilities and equipment accounting for 15 percent of their working capacity. Since November 2003, the non-commercial partnership "Trade System Administrator of the Wholesale Electricity Market", in accordance with the rules for the wholesale electricity (power) market during the transition period, had been holding electricity bidding in the free trading sector. Starting from October 2005, a competitive balancing market was put in operation.
- A crucial step in developing a competitive wholesale electricity (capacity) market was the adoption of the new Wholesale Electric Power (capacity) Market (NOREM) Rules of the Transitional Period approved by Resolution of the Government of the Russian Federation No. 529 dated August 31, 2006 and which came into force on September 1, 2006. Under the new wholesale market framework, electricity and power purchase-and-sale transactions in the regulated market sector are to be governed by a regulated bilateral contract system. From 1 September 2006, regulated contracts covered all volumes of electricity and power produced and consumed.

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

This has lead the Group to reassess its financial condition and reassess the previously recorded impairment reserve on property, plant and equipment (see Note 9).

Note 2. Financial condition

At 31 December 2006 the Group current liabilities exceeded its current assets by RR 1,735,761 thousand (as at 31 December 2005: current assets exceeded current liabilities by RR 54,136 thousand).

As at 31 December 2006 the Group net assets were positive and amounted to RR 8,004,697 thousand (at 31 December 2005: RR 5,808,787 thousand).

As discussed in Note 1, the Group is significantly affected by government policy through control of tariffs and other factors. In recent years the Regional Energy Commissions have not always permitted tariff increases in line with inflation and thus some tariffs are insufficient to cover all the costs of generation. Moreover, these tariffs consider costs only on Russian statutory basis and, accordingly, exclude significant additional costs recognized under IFRS basis of accounting. As a result, tariffs often do not allow for an adequate return or provide sufficient funds for the full replacement of property, plant and equipment. However, during 2006 and to date in 2007 the growing demand for electricity and capacity together with increasing the free trading sector of the wholesale electricity market have resulted in a higher rate of revenue growth (see Sector restructuring in Note 1 and impairment reserve reversal in Note 9).

Despite the fact that the Group management has significantly improved the level of settlements of accounts receivable, the Group continues to experience difficulties in obtaining settlements of old accounts receivable. Currently, substantially all settlements of accounts receivable are made in cash. Despite the achieved successes, there still remains a significant level of uncollectible accounts receivable from earlier periods.

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

- introduction of improved financial analysis and budgeting procedures; a strong focus on timely cash collection of current debtor balances;
- discussions with strategic investors, and identification and assessment of projects requiring investment funds;
- negotiations with federal and regional governments and regulators for real increases in tariffs to support adequate long term investment into the Group generation assets.

Note 2. Financial condition (continued)

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

Note 3. Basis of preparation

Statement of compliance. These combined and consolidated financial statements (hereinafter – the Financial Statements) have been prepared in accordance with International Financial Reporting Standards (IFRS) including all previously adopted IFRS standards and interpretations prepared by the International Financial Reporting Interpretations Committee (formerly Standing Interpretations Committee).

Each company 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.

These are the first IFRS financial statements of the Group. The Group has, as permitted by IFRS, applied the date of transition 1 January 2005. The Group did not previously prepare Russian GAAP financial statements as a separate reporting entity and accordingly no meaningful reconciliations from Russian GAAP to IFRS can be provided.

Predecessor Accounting. In June 2006 OJSC RAO UES of Russia (hereinafter - the Parent)) transferred to the Group 49.18% of ordinary shares of the following companies: Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP.

Those companies were controlled by the Parent on the basis of a significant shareholding combined with other factors which allow the company to exercise control, namely: RAO UES had the majority in the Board of Directors, RAO UES was the dominant owner or RAO UES has major influence over the company operations through its ownership and operation of the Unified Energy System.

In these combined and consolidated financial statements, the Group accounted for this business combination amongst entities under common control using the predecessor values method. Accordingly, assets and liabilities of the transferred entities were accounted for at their carrying value, as determined by the Parent in its IFRS consolidated financial statements. Information in respect of the comparative period has been restated as if the business combination took place at the beginning of the earliest period presented.

Thus, starting from 1 January 2005 : Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP are aggregated into the Group financial statements as branches of TGC-2.

Functional and presentation currency. The national currency of the Russian Federation is the Russian Ruble ("RR"), which is the functional currency of the Group and the currency in which these combined and consolidated financial statements are presented. All financial information presented in RR has been rounded to the nearest thousand.

Accounting for the effects of hyperinflation. Prior to 1 January 2003 the adjustments and reclassifications made to the statutory records for the purpose of IFRS presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with International Accounting Standard 29 ("IAS") "Financial Reporting in Hyperinflationary Economies". IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy should be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicated that hyperinflation ceased, effective from 1 January 2003 the Group no longer applied the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current as of 31 December 2002 are treated as the basis for the carrying amounts in the consolidated financial statements for subsequent periods.

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

(in thousands of Russian Roubles, unless otherwise stated)

Note 4. Summary of significant accounting policies

Principles of consolidation. The combined and consolidated financial statements comprise the financial statements of TGC-2 and the financial statements of those entities whose operations are controlled by TGC-2. Control is presumed to exist when TGC-2 owns, directly or indirectly through subsidiaries, over 50.00 percent of the voting shares.

The financial statements of subsidiaries are included in the combined and consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. The minority interest has been disclosed as part of equity.

Intercompany transactions and balances as well as unrealized gains and losses on transactions between Group companies are eliminated.

Transfers of subsidiaries from parties under common control. Contributions to share capital of shares in subsidiaries from parties under common control are accounted for using the predecessor values 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. Any difference between the carrying amount of net assets and the nominal value of share capital and other considerations contributed is accounted for in the combined and consolidated financial statements as an adjustment to equity.

Foreign currency transactions. Monetary assets and liabilities, which are held by the Group entities and denominated in foreign currencies at the balance sheet date, are translated into RR at the exchange rates prevailing at that date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement. At 31 December 2006, the official rate of exchange, as determined by the Central Bank of the Russian Federation, was RR 26.33: USD 1.00 (31 December 2005: RR 28,78: USD 1.00) and RR 34.70 : Euro 1.00 (31 December 2005: RR 34.19: Euro 1.00).

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.

Property, plant and equipment. As of the beginning of 2005 property plant and equipment were recognized at the carrying value determined in accordance with the IFRS at the date of their transfer to the Group by the Predecessor,

Property, plant and equipment are stated at cost less accumulated depreciation. Assets under construction are stated at historical cost. The Group starts depreciating these assets after they are put into operation.

At each balance sheet date, management assesses whether there is any indication of impairment of the Group property, plant and equipment. If any such indication exists, the Group management estimates the recoverable amount which is determined as the higher of an asset's net realizable value and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognized as an expense (impairment loss) in the income statement. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Significant renewals and improvements are capitalized and the assets replaced are retired immediately. The cost 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 .

Depreciation on 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. For the property, plant and equipment which were subject to the third party valuation as of 31 December 1997, the depreciation rate applied is based on the estimated remaining useful lives as of the valuation date. The useful lives of property, plant and equipment annually revised.

The useful lives, in years, of assets by type of facility are as follows:

Type of facility	Acquired prior to 31 December 1997	Acquired subsequent to 31 December 1997
Electricity and heat generation	12-50	20-50
Electricity distribution	6-26	25-30
Heating grids	6-13	20-25
Other	8	10

Note 4. Summary of significant accounting policies (continued)

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 social responsibilities are are expensed as incurred.

Operating lease. Where the Group is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the period of the lease.

The lease payments receivable under operating lease contracts (less allowances provided by the lessor) are recognized in the income statement on a straight-line basis over the lease term.

Finance lease. Where the Group is a lessee in a lease which transferred substantially all the risks and rewards incidental to ownership to the Group, the assets leased are capitalised in property, plant and equipment at the commencement of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding.The corresponding rental obligations, net of future finance charges, are included in debts. The interest cost is charged to the income statement over the lease period using the effective interest method. The assets acquired under finance lease are depreciated over their useful life or the shorter lease term if the Group is not reasonably certain that it will obtain ownership by the end of the lease term.

Cash and cash equivalents. Cash comprises cash in hand and cash deposited on demand at banks. 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.

Inventories. Inventories are recorded at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses. Cost of inventory is determined on the weighted average basis. Provision is made for potential losses on obsolete or slow-moving inventories, taking into account their expected use and future realizable value.

Value added tax on purchases and sales. Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) transfer of ownership for the goods to customers. Input VAT is generally recoverable against output VAT on the cash basis. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is disclosed separately as a current asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Accounts receivables and prepayments. Accounts receivable are recorded inclusive of value added taxes. Trade and other receivables are adjusted for an allowance made for impairment of these receivables. Such an allowance for doubtful debtors is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the allowance is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the original effective rate of interest.

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

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

Note 4. Summary of significant accounting policies (continued)

Accounts payable and accrued liabilities. Trade and other payables are accrued when the counterparty performed its obligations under the contract and are carried at amortised cost, using the effective interest method. Accounts payable are stated inclusive of value added tax.

Borrowings. Borrowings are recognised initially at their fair value. Fair value is determined using the prevailing market rates of interest for similar instruments, if significantly different from the interest rates under the loan received. In subsequent periods, borrowings are stated at amortised cost using the effective interest method; any difference between the amount at intitial recognition and the redemption amount is recognised in the income statement as an interest expense over the period of the debt obligation. All borrowing costs, including those incurred in realtion to the construction of property, plant and equipment, are recognised as an expense in the period in which they are incurred.

Minority interest. Minority interest represents the minority shareholders' proportionate share of the equity and results of operations of the Group subsidiaries. This has been calculated based upon the minority interests' ownership percentage of these subsidiaries. In purchases of minority interest, difference between the carrying amount of a minority interest and the amount paid to acquire it is recorded as loss directly in equity.

Provisions. Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Pension benefits and other social obligations. 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. Additional pension payments and other post-employment benefits to the employees are included within salaries, employee benefit expenses and payroll taxes in the income statement.

Some of the Group companies operate defined benefit plans with respect to the majority of the Group 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 recognised in the balance sheet in respect of the defined benefit pension plans is the present value of defined benefit obligations at the balance sheet date less the fair value of plan assets, including adjustments related to unrecognised actuarial gains and losses.The defined benefit obligations are calculated using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality government bonds denominated in the same currency as pension benefits, with terms to maturity approximating the terms of the related pension liability.

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

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

Financial guarantees. Financial guarantees are contracts that requires the Group to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantees are initially recognised at their fair value. This amount is amortised on a straight line basis over the life of the guarantee. At each balance sheet date, the guarantees are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the obligation at the balance sheet date.

Earnings per share. Preference shares are considered to be participating shares as their dividend may not be less than that given with respect to ordinary shares. The earnings per share is determined by dividing the net income attributable to ordinary and preference shareholders by the weighted average number of ordinary and preference shares outstanding during the reporting period, excluding the average number of treasury shares held by the Group. Preference shares participate in losses.

Segment reporting. The Group operates in a single geographical area and industry – generation of electricity and heat in the territory of the Russian Federation. The generation of electricity and heat are related activities and are subject to similar risks; therefore they are reported as one business segment.

(in thousands of Russian Roubles, unless otherwise stated)

Note 4. Summary of significant accounting policies (continued)

Seasonality. 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.

Note 5. Critical accounting estimates and assumptions

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

Impairment provision for accounts receivable. The impairment provision for accounts receivable is based on the Group assessment of wether 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.

Impairment of non-financial assets. At each balance sheet date the Group assesses whether there is any indication that the carrying amount of the Group assets exceeds their recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. When such indication of impairment is identified, the carrying amount is reduced to the recoverable amount. The amount of the impairment is recorded in the income statement in the period when the impairment is actually identified. If conditions change and management determines that the assets' value has increased, the impairment provision will be fully or partially reversed. Accounting for impairment includes provisions against property, plant and equipment and inventory obsolescence, calculated based on assumptions made by the Group (see Note 9).

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 tax positions cannot be sustained, an appropriate amount is accrued in these IFRS financial statements (see Note 26).

Useful lives of property, plant and equipment. The estimation of the useful lives of an item 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.

Carve-out methodologies. These consolidated and combined financial statements include carved out financial statement data of Yaroslavskaya Energeticheskaya Company, Tverskaya Generating Company, Vologodskaya HePP and Novgorodskaya Generating Company for the period and from the predecessor legal entities as outlined in the table below.

Branch	Predecessor legal entity	Period requiring carve-out accounting
Yaroslavskaya EC	Yarenergo	10 days ended 10 January 2005
Tverskaya GC	Tverenero	10 days ended 10 January 2005
Vologodskaya HePP	Vologdaenergo	9 months ended 30 September 2005
Novgorodskaya GC	Novgorodenergo	3 months ended 31 March 2005

In carving out this financial statement data, the following determinations were made:

- electricity and heat sales were based on actual electricity and heat power production volume multiplied by actual tariffs approved by RSTs for the power stations (Yaroslavskaya EC, Tverskaya EC, Vologodskaya HePP and Novgorodskaya GC) after their spin-off from the predecessor legal entities for the year 2005;

Note 5. Critical accounting estimates and assumptions (continued)

- operating expenses were determined on an actual basis;
- depreciation of property, plant and equipment was calculated on IFRS predecessor values;
- general and administrative overheads were not allocated but were specifically determined on an actual basis;
- current income tax was determined using the effective income tax rate of the predecessor entities;
- deferred income tax was determined from movements in deferred tax assets/liabilities between 1 January 2005 and the date of set up of the power stations as stand-alone legal entities;
- property, plant and equipment were based on IFRS predecessor values and rolled back to 1 January 2005 taking into account additions and disposals before their spin-off;
- accounts payable, taxes payable, accounts receivable (except for trade receivables), inventories were determined on an actual basis;
- trade receivables are calculated based on balances transferred to the Group from the predecessor legal entities.

Note 6. Adoption of new or revised Standards and Interpretations

Certain new IFRSs became effective for the Group from 1 January 2006. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Group operations and the nature of their impact on the Group accounting policies.

- IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006). IFRIC 4 requires that determining whether an arrangement contains a lease be based on the substance of the arrangement. It requires an assessment of whether (a) fulfillment of the arrangement is dependent on the use of a specific asset or assets (the asset); and (b) the arrangement conveys a right to use the asset. The Group reassessed its arrangements and concluded that no adjustments are required as a result of adoption of IFRIC 4.

- IAS 39 (Amended) – The Fair Value Option (effective from 1 January 2006). IAS 39 (as revised in 2003) permitted entities to designate irrevocably on initial recognition practically any financial instrument as one to be measured at fair value with gains and losses recognized in profit or loss ('fair value through profit or loss'). The amendment changes the definition of financial instruments 'at fair value through profit or loss' and restricts the ability to designate financial instruments as part of this category. The Group may now designate financial instruments as part of this category only if (a) such classification eliminates or significantly reduces an accounting mismatch that would otherwise arise from measuring assets or liabilities or recognizing the gains and losses on them on different bases; or (b) a Group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information on that basis is regularly provided to and reviewed by the Group's Board of Directors; or (c) a contract contains one or more embedded derivatives unless: (i) the embedded derivative(s) does not significantly modify the cash flows that otherwise would be required by the contract; or (ii) it is clear with little or no analysis when the embedded derivative is first considered that separation of the embedded derivative(s) is prohibited. The Group applies the amendment retrospectively in accordance with the transitional provisions of the Fair Value Option amendment to IAS 39. The amendment did not have an impact on these financial statements.

- IAS 39 (Amended) - Cash Flow Hedge Accounting of Forecast IntraCompany Transactions (effective from 1 January 2006). The amendment allows the foreign currency risk of a highly probable forecast intraCompany transaction to qualify as a hedged item in the consolidated financial statements provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and the foreign currency risk will affect consolidated profit or loss. The Group does not apply hedge accounting and therefore the amendment did not have an impact on these financial statements.

- IAS 39 (Amended) – Financial Guarantee Contracts (effective from 1 January 2006). As a result of this amendment, the Group measures issued financial guarantees initially at their fair value, which is normally evidenced by the amount of fees received. This amount is then amortized on a straight line basis over the life of the guarantee. At each balance sheet date, the guarantees are measured at the higher of (i) the unamortized balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the balance sheet date. This amendment did not have a significant impact on these financial statements.

Note 6. Adoption of new or revised Standards and Interpretations (continued)

- IAS 21 (Amended) – Net Investment in a Foreign Operation (effective from 1 January 2006). This amendment requires foreign exchange gains and losses on monetary items that form part of net investment in a foreign operation (e.g. quasi-equity intercompany loans) to be reported in consolidated equity even if the loans are not in the functional currency of either the lender or the borrower. Previously, such exchange differences were required to be recognized in consolidated profit or loss. It also extended the definition of 'net investment in a foreign operation' to include loans between sister companies. This amendment did not have a significant impact on these financial statements.

- IAS 19 (Amended) - Employee Benefits (effective from 1 January 2006). The amendment introduced an additional option to recognize actuarial gains and losses arising in post-employment defined benefit plans in full directly in retained earnings in equity. It also requires new disclosures about defined benefit plans and clarifies accounting for a contractual agreement between a multi-employer plan and participating employers. This amendment did not have a significant impact on these financial statements.

- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006). Subject to certain exceptions, this interpretation prohibits offsetting a liability for decommissioning costs with an asset representing an interest in a decommissioning or similar fund and clarifies measurement of the reimbursement asset. This interpretation did not have a significant impact on these financial statements.

- IFRIC 6, Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment (effective for periods beginning on or after 1 December 2006, that is from 1 January 2006). The Interpretation states that a liability shared among market participants in proportion to their respective market share, in particular the liability for the decommissioning of historical waste electrical and electronic equipment in the European Union, should not be recognized until the measurement period because participation in the market during the measurement period is the obligating event in accordance with IAS 37. This interpretation did not have a significant impact on these financial statements.

- IFRS 6, Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006). IFRS 6 allows an entity to continue using the accounting policies for exploration and evaluation assets applied immediately before adopting the IFRS, subject to certain impairment test requirements. This standard did not have a significant impact on these financial statements.

Note 7. New accounting pronouncements

These new standards and interpretations are not yet in force and were not applied by the Group in these financial statements:

- IFRS 7, "Financial instruments: Disclosures", effective for annual periods beginning on or after 1 January 2007. The standard will require increased disclosure in respect of the Group financial instruments.

- Amendment to IAS 1 'Presentation of Financial Statements – Capital Disclosures', effective for annual periods beginning on or after 1 January 2007. The standard will require increased disclosure in respect of the Group capital.

- Amendment to IAS 23 "Borrowing Cost", effective for annual periods beginning on or after 1 January 2009. The amendment disallows the choice of recognizing borrowing costs that relate to qualifying assets as an expense of the reporting period and their capitalization in the cost of the qualifying asset. Starting from 1 January 2009 capitalization of expenses is the only method allowed.

- IFRIC 7, Applying the Restatement Approach under IAS 29 "Financial Reporting in Hyperinflationary Economies" (effective for periods beginning on or after 1 March 2006, that is from 1 January 2007). The Interpretation clarifies application of IAS 29 in the reporting period in which hyperinflation is first identified. It states that IAS 29 should initially be applied as if the economy has always been hyperinflationary. It further clarifies calculation of deferred income taxes in the opening balance sheet restated for hyperinflation in accordance with IAS 29.

- IFRIC 8, Scope of IFRS 2, effective for periods beginning on or after 1 March 2006, that is from 1 January 2007. The interpretation states that IFRS 2 also applies to transactions in which the entity receives unidentifiable goods or services and that such items should be measured as the difference between the fair value of the share-based payment and the fair value of any identifiable goods or services received (or to be received).

(in thousands of Russian Roubles, unless otherwise stated)

Note 7. New accounting pronouncements (continued)

- IFRIC 9, "Reassessment of Embedded Derivatives", effective for annual periods beginning on or after 1 June 2006. The Interpretation clarifies that an entity should assess whether an embedded derivative should be accounted for separately from the host contract when the entity first becomes party to the contact. The entity reconsiders whether an embedded derivative should be accounted for separately from the host contract if the contract is subsequently changed considerably.
- IFRIC 10, "Interim financial reporting and impairment", effective for annual periods beginning on or after 1 November 2006. The interpretation states that in subsequent interim and annual periods the entity cannot recover impairment losses for goodwill or investments recorded in the previous periods.
- IFRIC 11, IFRS 2 - Group and Treasury Share Transactions, effective for annual periods beginning on or after 1 March 2007.The interpretation explains the way of applying IFRS 2 "Equity Compensation Benefits" to equity compensation benefit arrangements which include the entity's own equity instruments or equity instruments of another entity within the Group (for example, the Parent's equity instruments).
- IFRIC 12, Service Concession Arrangements, effective for annual periods beginning on or after 1 January 2008.
- IFRS 8, Operating Segments, effective for annual periods beginning on or after 1 January 2009. The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organization for the purpose of issuing any class of financial instruments in a public market. IFRS 8 requires an entity to report financial and other information about its operating segments and specifies how an entity should report such information. The Group is currently assessing what impact the new IFRS will have on disclosures in its financial statements.
- IFRIC 13, Customer Loyalty Programmes, effective for annual periods beginning on or after 1 July 2008.
- IFRIC 14, IAS 19 - The limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, effective for annual periods beginning on or after 1 January 2008.

As follows from the analysis of new standards and interpretations performed by the Group, unless otherwise described above, these new standards and interpretations are not expected to significantly affect the Group financial statements.

Note 8. Related parties

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

Related parties include shareholders, directors, subsidiaries and enterprises controlled by the state.

OJSC RAO UES is the main shareholder of TGC-2 and has a control over the Group's activity.

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions in 2006 and in 2005 or had significant balances outstanding at 31 December 2006 and at 31 December 2005 are detailed below.

Parent company

Balances with OJSC RAO UES were as follows:

	31 December 2006	31 December 2005
Dividends payable	-	10,241
Borrowings (see note 18)	28,130	215,045

Transactions with OJSC RAO UES were as follows:

	31 December 2006	31 December 2005
Interest expense	94,225	67,647

(in thousands of Russian Roubles, unless otherwise stated)

Note 8. Related parties (continued)

Transactions with OJSC RAO UES subsidiaries and associates

Transactions with the Parent's subsidiaries and associates were as follows:

	Year ended 31 December 2006	Year ended 31 December 2005
Sales of electricity and heat	3,275,227	4,139,900
Other income	1,550	33,785

	Year ended 31 December 2006	Year ended 31 December 2005
Loss on discounting of non-current accounts receivable	232,863	-
Electricity purchases	196,569	130,882
Electricity dispatching services	59,851	-
Repairs and maintenance services	27,325	142,535
Rent expenses	9,784	6,056

Balances with the Parent's subsidiaries and associates at the end of the period were as follows:

	Currency	31 December 2006	31 December 2005
Accounts receivable	RR	530,435	517,292
Accounts payable	RR	64,345	22,493
Loan receivable (due April 2008)	RR	276,600	-

The loan receivable represents the loan agreement with OJSC Arkhangelsk generation company (RR 450,000 thousand). The company made the loan in the form of Sherbank securities. The terms of the loan stated that the loan should be repaid either by the Sherbank securities or by cash. Interest of 11% is payable on the loan. On 31.12.06 the loan was repaid in cash (RR 173,400 thousand).

State controlled entities

In the normal course of business the Group enters into transactions with other entities under Government control. The prices for natural gas, electricity and heat are based on tariffs established by FTS and RST. Bank loans are obtained under market rates. Taxes are charged and paid under the Russian tax legislation.

The Group had the following significant transactions with state-controlled entities:

	Year ended 31 December 2006	Year ended 31 December 2005
Fuel purchases	(4,605,282)	(3,827,359)
Sales of electricity and heat	864,363	841,787
Interest expense	(90,815)	(63,786)

The Group had the following significant balances with state-controlled entities:

	Currency	31 December 2006	31 December 2005
Cash		7,219	21,537
Current accounts receivable and prepayments	RR	-	75,397
Borrowings	RR	2,575,306	546,500
Accounts payable and accrued liabilities	RR	16,496	87,348

Note 8. Related parties (continued)

Tax balances are disclosed in the balance sheet and Notes 13 and 20. Tax transactions are disclosed in Group combined and consolidated income statement and Note 21.

Transactions with Board of Directors and key management personnel

Compensation is paid to the TGC-2 Management Board for performing their functions and comprised their contractual salaries and performance bonuses depending on results for the year according to Russian statutory financial statements. The compensation is approved by the Board of Directors. Deiscretionary bonuses are also payable to members of the Management Board, which are approved by the Chairman of the Management Board According to his perception of the value of their contribution.

Fees, compensation or allowances to the members of Board of Directors for their services in that capacity and for attending Board meetings are paid depending on results for the year.

Total remuneration paid in the form of salary and bonuses paid to the members of the Board of Directors, Management Board and key management personnel is RR 8,635 thousand for the year ended 31 December 2006 and RR 3,902 thousand as at 31 December 2005.

The Group has no other compensation programs.

(in thousands of Russian Roubles, unless otherwise stated)

Note 9. Property, plant and equipment

	Electricity and heat generation	Electricity distribution	Heat networks	Construction in progress	Other	Total
Cost						
Opening balance as at 1 January 2006	**11,794,439**	**895,871**	**4,162,497**	**1,279,130**	**2,597,071**	**20,729,008**
Additions	13,961	126	140	927,241	67,228	**1,008,696**
Transfers	135,219	45,664	83,561	(596,550)	332,106	-
Disposals	(13,635)	(96)	-	(12,888)	(14,374)	**(40,993)**
Closing balance as at 31 December 2006	**11,929,984**	**941,565**	**4,246,198**	**1,596,933**	**2,982,031**	**21,696,711**
Accumulated depreciation (including impairment)						
Opening balance as at 1 January 2006	**(8,552,564)**	**(673,261)**	**(3,569,795)**	**-**	**(2,218,663)**	**(15,014,283)**
Charge for the period	(273,189)	(18,223)	(108,317)	-	(71,524)	**(471,253)**
Disposals	(3,782)	(29)	-	-	(2,695)	**(6,506)**
Release of impairment loss	3,633,705	219,162	374,677	-	96,155	**4,323,699**
Closing balance as at 31 December 2006	**(5,195,830)**	**(472,351)**	**(3,303,435)**	**-**	**(2,196,727)**	**(11,168,343)**
Net book value as at 1 January 2006	**3,241,875**	**222,610**	**592,702**	**1,279,130**	**378,408**	**5,714,725**
Net book value as at 31 December 2006	**6,734,154**	**469,214**	**942,763**	**1,596,933**	**785,304**	**10,528,368**

	Electricity and heat generation	Electricity distribution	Heat networks	Construction in progress	Other	Total
Cost						
Opening balance as at 1 January 2005	**11,687,003**	**867,639**	**4,077,959**	**982,388**	**2,524,931**	**20,139,920**
Additions	6,768	195	1,238	573,842	31,510	**613,553**
Transfers	102,461	28,041	83,316	(261,629)	47,811	-
Disposals	(1,793)	(4)	(16)	(15,471)	(7,181)	**(24,465)**
Closing balance as at 31 December 2005	**11,794,439**	**895,871**	**4,162,497**	**1,279,130**	**2,597,071**	**20,729,008**
Accumulated depreciation (including impairment)						
Opening balance as at 1 January 2005	**(8,293,065)**	**(656,099)**	**(3,466,852)**	**-**	**(2.003,945)**	**(14,419,961)**
Charge for the period	(260,994)	(17,162)	(102,944)	-	(219,774)	**(600,874)**
Disposals	1,495	-	1	-	5,056	**6,552**
Closing balance as at 31 December 2005	**(8,552,564)**	**(673,261)**	**(3,569,795)**	**-**	**(2,218,663)**	**(15,014,283)**
Net book value as at 1 January 2005	**3,393,938**	**211,540**	**611,107**	**982,388**	**520,986**	**5,719,959**
Net book value as at 31 December 2005	**3,241,875**	**222,610**	**592,702**	**1,279,130**	**378,408**	**5,714,725**

(in thousands of Russian Roubles, unless otherwise stated)

Note 9. Property, plant and equipment (continued)

Construction in progress represents the carrying amount of property, plant and equipment that has not yet been put into operation.

Depreciation is charged once an asset is available for use.

Property, plant and equipment balances as at 31 December 2006 included RR 3,643,611 thousand of assets which were fully amortized (at 31 December 2005: RR 1,891,431 thousand).

Other property, plant and equipment include motor vehicles, computers, office furniture and other equipment.

Impairment

Management considered recent favorable changes in operation of the Russian electricity market (see also Note 1, section "Regulatory issues and sector restructuring") and reassessed recoverable amount of the Group's property, plant and equipment as at 31 December 2006 to its value in use. As a result, management believes that provision for impairment of property, plant and equipment recorded by the Group as at 1 January 2005 and 31 December 2005 in respect of electricity and heat generating assets using the predecessor accounting basis of the Group should be fully reversed as at 31 December 2006. The amount of reversal is estimated by management as RR 4,323,699 thousand.

Management applied the following significant assumptions when estimating value in use of the property, plant and equipment as at 31 December 2006 and determining the levels of impairment provisions as at 31 December 2006:

- annual increase in electricity tariffs is estimated by the management as 15%-27% p.a. in 2008-2011 and 5% p.a. in 2012 and onwards;
- annual increase in heat tariffs is estimated by the management as 17%-18% p.a. in 2008-2011, 5% p.a. in 2012 and onwards;
- annual growth of gas prices is estimated by the management as 23%-26% p.a. in 2008-2011; 4% p.a. in 2012 and onwards;
- annual growth of coal prices is estimated by the management as 5%-10% p.a. in 2008-2011; 3% p.a. in 2012 and onwards;
- growth of mazut prices set for the Group were on average 5-6% in 2008-2011 and 5% p.a. in 2012 and onwards;
- growth of peat prices set for the Group were on average 5-7% in 2008-2011 and 4% p.a. in 2012 and onwards;
- the assumption was made that production volumes of electricity and heat will remain at the current level for the whole impairment test period (investment programme is not included);
- increase of major cost (except of fuel) will not exceed the inflation rate;
- weighted average cost of capital of 14% was applied for discounting future operating cash flows generated by the Group for all cash generating units;
- the Group's restructuring did not change the manner of recovery of the assets – the regulator allocated previously single tariffs for electricity and heat set for a vertically integrated power
- companies among newly created generating businesses.

Leased property, plant and equipment

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

Operating lease rentals under non-cancelable leases are payable as follows:

	31 December 2006	31 December 2005
not later than one year	107,360	76,486
later than one year and not later than five years	316,606	244,687
later than five years	2,217,504	1,556,216
Total	**2,641,470**	**1,877,389**

(in thousands of Russian Roubles, unless otherwise stated)

Note 9. Property, plant and equipment (continued)

The land areas leased by the Group are the territories on which the Group' electric power stations, heating stations and other assets are located. Some contracts for land lease are concluded for 49 years, other contracts are concluded for one year with prolongation. Lease payments are reviewed regularly to reflect market rentals.

Finance lease. As at 31 December assets under finance lease which are included in the "Other" category within property, plant and equipment were as follows:

	31 December 2006	31 December 2005
Cost of finance leased assets	149,624	149,624
Accumulated depreciation	(35,045)	(20,083)
Net book value	**114,579**	**129,541**

The maturity table and information about minimum lease payments of finance lease liability as follows:

	31 December 2006	31 December 2005
not later than one year	2,978	13,705
later than one year and not later than five years	4,733	7,341
later than five years	430	800
Lease payments	**8,141**	**21,846**

Assets under the financial lease agreements were received from LLC «RosBusinesLeasing», LLC «Verhnevolzhskaya Lease Company».

Note 10. Other non-current assets

	Currency	Effective interest rate,%	31 December 2006	31 December 2005
Non-current trade and receivables (due 2007-2029)	RR	12	150,989	-
Non-current input VAT (to be recovered more than one year after reporting date)	RR	-	74,898	89,696
Other	RR	-	39,517	36,338
Loans issued to employees	RR	12	19,182	7,789
Other non-current assets		-	**284,586**	**133,823**

Non-current trade receivable as at 31 December 2006 includes RR 150,989 thousand receivable from OJSC Tver Utilities.

On 12 September 2006 TGC-2 and OJSC Tver Utilities signed the schedule of payments, under which the accounts receivable equal RR 437,286 thousand will be repaid over the period 22 years.

Loss on discount of restructured receivable amounted RR 284,617 thousand has been included in operating expenses (see Note 21).

Note 11. Inventories

	31 December 2006	31 December 2005
Fuel	669,646	420,832
Spare parts	181,959	180,688
Other inventories	227,492	158,048
Total inventories	**1,079,097**	**759,568**

Other inventories are presented net of provision for obsolescence of RR nil thousand at 31 December 2006 and RR 13,187 thousand at 31 December 2005.

(in thousands of Russian Roubles, unless otherwise stated)

As at 31 December 2006 and 31 December 2005, the inventory balance included RR 388,823 thousand and RR 130,524 thousand, respectively, of inventory pledged as collateral under loan agreements.

Note 12. Other current assets

	Currency	Effective interest rate, %	31 December 2006	31 December 2005
Loan receivable from related party (due to April, 2008) (see Note 8)	RR	11	276,600	-
Other current assets	RR	-	1,432	100
Other current assets			**278,032**	**100**

Note 13. Accounts receivable and advances issued

	Currency	31 December 2006	31 December 2005
Trade receivables (net of allowance for doubtful debtors of RR 1,215,214 thousand as at 31 December 2006 and RR 915,460 thousand as at 31 December 2005)	RR	726,673	846,639
Advances to suppliers (net of allowance for doubtful debtors of RR 0 thousand as at 31 December 2006 and RR 1,462 thousand as at 31 December 2005)	RR	211,012	169,091
Value added tax recoverable	RR	107,436	174,681
Other receivables (net of allowance for doubtful debtors of RR 106,305 thousand as at 31 December 2006 and RR 103,565 thousand as at 31 December 2005)	RR	108,679	139,877
Prepayments to the budget (other than income tax)	RR	15,112	4,576
Total		**1,168,912**	**1,334,864**

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

Certain trade receivables and other accounts receivable have been restructured and are due to be realized more than one year from the balance sheet date (see Note 10).

Note 14. Cash and cash equivalents

	31 December 2006	31 December 2005
Cash in bank and in hand	69,393	122,582
Cash equivalents	501	-
Total	**69,894**	**122,582**

All cash and cash equivalents are denominated in Russian Roubles.

Cash equivalents represent bank notes with original maturities of three month or less.

Note 15. Equity

Basis of presentation of movements in equity. The Group was formed by the combination of a number of businesses under common control. Because of the consequent use of the predecessor basis (see Note 3), the principal component of the net equity recognized for the Group is based on the historic carrying value of the net assets of the businesses contributed as recorded in the IFRS financial records of the predecessor enterprises, rather than the fair values of those net assets. As the Group was formed as a result of share issue completed after 01 January 2005, the equity statement reflects additions to share capital in the amount equal to the statutory nominal value of the shares issued which is based on the fair value of the net assets of the businesses contributed. In accordance with the predecessor basis of accounting, the effect of such addition to equity is offset by a corresponding increase in the merger reserve and reduction in minority interest.

(in thousands of Russian Roubles, unless otherwise stated)

Note 15. Equity (continued)

Share capital

	31 December 2006	31 December 2005
Number of ordinary and preference shares authorized, issued and fully paid	711,712,704,501	1,000,000,000
Par value (in RR)	0.01	0.01
Total share capital (in thousand RR)	**7,117,127**	**10,000**

As at 19 April 2005, the date that the Group was established, the number of issued ordinary shares amounted to 1,000,000,000 with a par value of RR 0.01 each.

Contributions to the Group's share capital in amount of RR 10,000 thousand were paid in cash in the year 2005.

As of 29 June 2006 the Group increased it's share capital by RR 7,107,127 thousand by conversion of ordinary and preference shares of OJSC Vologodskaya HePP, OJSC Kostromskaya GC, OJSC Novgorodskaya GC, OJSC Tverskaya GC and OJSC Yaroslavskaya EC into the ordinary shares of TGC-2.

As a result, OJSC RAO UES shareholdings (49.18% of OJSC Vologodskaya HePP, OJSC Kostromskaya GC, OJSC Novgorodskaya GC, OJSC Tverskaya GC and OJSC Yaroslavskaya EC) and minorities' shareholdings (50.82%) were exchanged for the shares of TGC-2.

As at 31 December 2006 number of issued ordinary shares amounted to 700,328,533,458 with a par value of RR 0.01 each and number of preference shares amounted to 11,384,171,043 a par value of RR 0.01 each.

Ordinary shares and preference shares. Preference shares have no right of conversion or redemption. In total the preference dividend may not be less than the ordinary dividend and is not cumulative. Preference shares carry no voting rights except when dividends on preference shares have not been declared fully at the Annual Shareholders' meeting. At liquidation, preference shareholders are first paid any declared unpaid dividends and then the nominal value of the shares ("liquidation value"). Following this, preference shareholders then participate equally in the distribution of remaining assets with ordinary shareholders.

Merger reserve. Merger reserve of RR 2,749,061 thousand as at the opening date represents the difference between IFRS carrying value of the contributed net assets merged into the Group, totaling RR 5,808,787 thousand, and the minority interest of RR 3,041,116 thousand. The merger reserve was subsequently adjusted by the share capital issued by TGC-2 to reflect the transfer of businesses owned by the entities under common control.

Dividends. In accordance with Russian legislation, the Group distributes profits as dividends on the basis of financial statements prepared in accordance with Russian Accounting Rules. The statutory accounting reports are the basis for the annual profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit. However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and, accordingly, management believes at present it would not be appropriate to disclose an amount for the distributable reserves in these financial statements.

(in thousands of Russian Roubles, unless otherwise stated)

Note 15. Equity (continued)

The following dividends were declared by the Group, recognised as a liability and deducted from equity for the reporting periods:

	Year ended 31 December 2006		Year ended 31 December 2005	
	Declared dividends, in thousand of RR	Dividends per share, RR	Declared dividends, in thousand of RR	Dividends per share, RR
OJSC Yaroslavskaya EC in respect of the nine month ended 30 September 2005	-	-	21,626	0.99885
OJSC Yaroslavskaya EC in respect of the year ended 31 December 2005	76,620	3.538605	-	-
OJSC Kostromskaya GC in respect of the year ended 31 December 2005	60,000	0.110025	-	-
OJSC Novgorodskaya GC in respect of the year ended 31 December 2005	16,222	0.076311	-	-
OJSC Tverskaya GC in respect of the year ended 31 December 2005	25,540	0.05534	-	-
OJSC Yaroslavskaya EC in respect of three months ended 31 March 2006	90,241	4.1680015	-	-
OJSC Kostromskaya GC in respect of three months ended 31 March 2006	23,241	0.042629	-	-
OJSC Novgorodskaya GC in respect of three months ended 31 March 2006	11,100	0.052216	-	-
OJSC Tverskaya GC in respect of three months ended 31 March 2006	33,703	0.073027	-	-
OJSC Vologodskaya HePP in respect of three months ended 31 March 2006	21,709	1.0675684	-	-
Total dividends	**358,376**	-	**21,626**	-

Note 16. Income tax

Income tax charge

	Year ended 31 December 2006	Year ended 31 December 2005
Current income tax charge	(57,107)	(133,243)
Deferred income tax charge/ (benefit)	(1,006,232)	94,937
Income tax charge	**(1,063,339)**	**(38,306)**

In 2006 and 2005 the Group companies were subject to a 24% income tax rate on taxable profits.

Reconciliation between the expected and the actual tax charge is provided below:

	Year ended 31 December 2006	Year ended 31 December 2005
Profit before tax	**3,617,625**	**76,482**
Theoretical tax charge at the statutory tax rate of 24%	**(868,230)**	**(18,356)**
Tax effect of items which are not deductible or assessable for taxation purpose	**(195,109)**	**(19,950)**
Total income tax charge	**(1,063,339)**	**(38,306)**

Deferred tax assets and liabilities

Differences between IFRS and Russian statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes

(in thousands of Russian Roubles, unless otherwise stated)

Note 16. Income tax (continued)

and their tax bases. Deferred tax assets and liabilities are measured at the rate of 24% which is expected to be applied to the period when the assets are realized and liabilities are settled.

In the context of the Group's current structure, tax losses and current tax assets of different consolidated entities may not be offset against current tax liabilities and taxable profits of other consolidated entities and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

As at 31 December 2006, deferred tax assets and liabilities were offset within TGC-2 as a single entity, resulting in a net liability of RR 923,663 thousand.

	31 December 2006	Movement for the year recognized in Income Statement	31 December 2005
Trade receivables and prepayments	281,824	36,464	245,360
Accounts payable and accrued liabilities	25,684	10,598	15,086
Pension liabilities	34,117	2,721	31,396
Other	-	(11,294)	11,294
Deferred tax assets	**341,625**	**38,489**	**303,136**
Property, plant and equipment	(1,252,474)	(1,043,387)	(209,087)
Other	(12,814)	(1,334)	(11,480)
Deferred tax liabilities	**(1,265,288)**	**(1,044,721)**	**(220,567)**
Net deferred tax liabilities	**(923,663)**	**(1,006,232)**	**(82,569)**

Property, plant and equipment movement includes a deferred tax expense of RR 1,342,892 thousand in relation to the reversal of a previously recognised impairment loss.

	31 December 2005	Movement for the year recognized in Income Statement	31 December 2004
Trade receivables and prepayments	245,360	69,196	176,164
Accounts payable and accrued liabilities	15,086	13,798	1,288
Pension liabilities	31,396	3,383	28,013
Other	11,294	5,204	6,090
Deferred tax assets	**303,136**	**91,581**	**211,555**
Property, plant and equipment	(209,087)	2,046	(211,133)
Future period income	(11,480)	1,310	(12,790)
Deferred tax liabilities	**(220,567)**	**3,356**	**(223,923)**
Net deferred tax assets/(liabilities)	**82,569**	**94,937**	**(12,368)**

The Group has not recorded a deferred tax liability in respect of taxable temporary differences associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

Note 17. Pension liabilities

The Group operates defined benefit and defined contribution pension plans. In respect of some of these plans the Group has contract with a pension fund "Non-state pension fund of electrical energy industry" ("NPFE"), which is a separate legal entity; the other plans are operated by the Group without engaging pension funds. Defined contribution plans are considered immaterial for disclosure.

The defined benefit pension plan through NPFE provides for monthly pension benefit paid upon retirement. Annual contributions are made by the Group to the solidarity account in the non-state pension fund. Amount of the contribution is defined by TGC-2 budget and is considered to be enough at least to finance running pension benefits. No part of this contribution is recognised as a plan asset to the extend that

(in thousands of Russian Roubles, unless otherwise stated)

Note 17. Pension liabilities (continued)

TGC-2 can recall the contribution and the plan is considered as unfunded thereat. Pension benefits are paid from the solidarity account on 'pay-as-you-go' basis.

Additionally to the NPFE pension plan, the Group provides financial support, of a defined benefit nature, to its old-age pensioners, who have completed certain service for the Group, and other post-employment benefit such as lump-sum payments upon retirement, lump-sum material aid, etc.

The non-statutory pension plan providing monthly pensions had approximately 7,900 active participants as at 31 December 2006 and 1,700 pensioners receiving financial support from the employer.

The tables below provide information about the benefit obligations, plan assets and actuarial estimations used for the years ended 31 December 2006 and 31 December 2005.

Amounts recognized in the balance sheet:

	31 December 2006	31 December 2005
Defined benefit obligations	222,019	148,570
Unrecognised net actuarial losses	(35,815)	(17,755)
Unrecognised past service cost	(44,051)	-
Net liability on balance sheet	**142,153**	**130,815**

Amounts recognized in the income statement:

	Year ended 31 December 2006	Year ended 31 December 2005
Current service cost	8,305	7,678
Interest cost	10,400	9,630
Net actuarial loss recognized in year	192	-
Total	**18,897**	**17,308**

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

	31 December 2006	31 December 2005
Benefit obligations		
Benefit obligations as at the beginning of the period	148,570	116,722
Current service cost	8,305	7,678
Interest cost	10,400	9,630
Past service cost	44,051	-
Benefits paid	(7,559)	(3, 215)
Actuarial losses	18,252	17,755
Benefit obligations as at the end of the period	**222,019**	**148,570**

Principal actuarial estimations are as follows:

	31 December 2006	31 December 2005
Discount rate for benefits at accumulation phase	6.75%	7.0%
Future Salary increase	7.0%	7.0%
Future inflation rate	5.0%	5.0%

Note 18. Borrowings

Non-current borrowings

Creditor	Currency	Effective interest rate,%	31 December 2006	31 December 2005
OJSC RAO UES	RR	34	-	28,146
Total non-current borrowings			-	28,146

(in thousands of Russian Roubles, unless otherwise stated)

Note 18. Borrowings (continued)

Current borrowings

Creditor	Currency	Effective interest rate,%	31 December 2006	31 December 2005
OJSC Vneshtorgbank*	RR	8.75	1,716,381	139,000
OJSC Alfa-Bank	RR	8.70-10.20	699,319	165,198
OJSC TransCreditBank	RR	9.50-10.20	458,101	304,393
OJSC Sberbank *	RR	8.75-11.00	447,733	144,668
OJSC RAO UES	RR	34.0	28,130	186,899
OJSC Sberbank	RR	12.0	19,988	-
OJSC NB Trust*	RR	11.00-13.50	-	111,374
Total current borrowings			**3,369,652**	**1,051,532**

* - inventory pledged as collateral under loan agreements (see Note 11).

Note 19. Accounts payable and accrued liabilities

	Currency	31 December 2006	31 December 2005
Trade payables	RR	268,757	223,706
Payables to employees	RR	141,558	128,205
Advances from the buyers	RR	138,382	87,993
Payables to the capital construction contractors	RR	128,955	58,968
Accrued liabilities and other payables	RR	37,300	76,383
Dividends	RR	20,558	21,626
Total		**735,510**	**596,881**

Note 20. Taxes other than income tax

	31 December 2006	31 December 2005
Value added tax	210,350	382,767
Property tax	43,290	30,544
Unified social tax	36,885	21,461
Water tax	14,916	6,858
Other taxes	17,743	18,907
Total	**323,184**	**460,537**

As of 31 December 2006 included in the payable for value added tax is RR 151 532 thousand of deferred VAT which only becomes payable to the authorities when the underlying receivables balance is either recovered or written off (as at 31 December 2005: RR 299,525 thousand).

(in thousands of Russian Roubles, unless otherwise stated)

Note 21. Operating expenses

	Year ended 31 December 2006	Year ended 31 December 2005
Fuel	5,194,165	4,292,526
Payroll	1,317,656	1,063,980
Other materials	492,937	397,148
Repair & maintenance costs	404,118	570,754
Depreciation	471,253	600,874
Purchased power	309,765	175,735
Provision for doubtful debts	301,032	290,279
Effect on discounting of non-current accounts receivable	284,617	-
Taxes other than income tax	266,503	214,887
Gas transportation expenses	178,573	221,791
Rent expenses	111,485	89,393
Transportation services	107,987	25,129
Costs of heat & electricity's transfer	63,132	75,418
Electricity dispatching services	59,851	-
Insurance expenses	43,100	24,029
Water usage expenses	40,932	32,464
Consulting services	35,467	41,609
Security services	31,925	40,252
Expenses for reforming	25,375	2,835
Non refundable VAT	22,523	-
Effect on discounting of loans issued to employees	9,606	3,578
Write off accounts receivable	8,628	1,802
Other expenses	511,838	279,349
Total operating expenses	**10,292,468**	**8,443,832**

Note 22. Finance income and costs

Finance income

	Year ended 31 December 2006	Year ended 31 December 2005
Interest income	10,656	781
Total finance income	**10,656**	**781**

Finance costs

	Year ended 31 December 2006	Year ended 31 December 2005
Interest expense	283,641	153,639
Interest cost for pension obligation (see Note 17)	10,400	9,630
Interest expense (leasing)	2,857	18,090
Total finance costs	**296,898**	**181,359**

Note 23. Disposal of subsidiaries

In November 2006 the Group has sold 100% share of its non-core subsidiary OJSC "Kostromaenergoremont" for RR 78,500 thousand. Gain on the disposal was RR 66,554 thousand and has been included in "Other operating income".

(in thousands of Russian Roubles, unless otherwise stated)

Note 23. Disposal of subsidiaries (continued)

Net assets of OJSC "Kostromaenergoremont" at the date of sale were the following:

	OJSC "Kostromaenergoremont" net assets
Current assets	51,404
Property, plant and equipment	7,658
Current liabilities	(46,986)
Non-current liabilities	(130)
Net assets	**11,946**
% of ownership	100%
The Group's share in net assets disposed of	(11,946)
Consideration received	78,500
Gain on disposal of subsidiaries	**66,554**

Note 24. Earnings per share

	Year ended 31 December 2006	Year ended 31 December 2005
Weighted average number of ordinary shares issued (thousands)	355,454,188	701,370
Weighted average number of preference shares issued (thousands)	5,770,059	-
Weighted average number of ordinary and preference shares outstanding (thousands)	361,224,247	701,370
Profit attributable to the shareholders of TGC-2	2,927,402	19,246
Weighted average earnings per ordinary and preference share – basic and diluted (in RR)	0.008	0.027

Note 25. Commitments

Sales commitments. The Group entities sell electricity (capacity) on the two wholesale market sectors: free trading sector and regulated trading sector. The tariffs for the electricity sold/purchased in the regulated trading sector (including the sector of deviations) are set by the Federal Service on Tariffs.

The Group has entered into a number of annual electricity sales agreements with CJSC "Center for Financial Settlements", retail companies and large industrial customers.

Fuel purchase commitments. The Group has a number of annual contracts to purchase natural gas and coal. The quantity of natural gas to be supplied is annually allocated by OJSC RAO UES in coordination with OJSC GAZPROM given the capacity of utilization of alternative fuel and the required fuel reserve fixed by OJSC RAO UES. The purchase price of gas is fixed by the Federal Service of Tariffs.

Note 26. Contingencies

Political environment. The operations and earnings of the Group entities 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.

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

Legal proceedings. The Group entities are party to certain legal proceedings arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding and not provided for which, upon final disposition, will have a material adverse effect on the financial position of the Group.

(in thousands of Russian Roubles, unless otherwise stated)

Note 26. Contingencies (continued)

Guarantees. The Group has entered in number of agreements under which the Group is guarantor to third parties in case of default of principal debtor. The amount of guarantees given as at 31 December 2006 is 1,400 million (31 December 2005 – RR 52.5 million):

	31 December 2006	31 December 2005
OJSC Vologdaenergo	-	52,500
OJSC Arkhangelsk generating company	1,400,000	-
Total guarantees	**1,400,000**	**52,500**

Guarantees were issued for the period of 1-2 years. All guaranties are denominated in Russian Roubles.

The fair value of these guarantees have been estimated and have been included within accounts payable and accrued liabilities.

Provisions for impairment of inventories and accounts receivable. Movements in provision for impairment of accounts receivables,and inventories are as follows:

	Total obsolescence inventory provision (Note 11)	Provision for impairment of receivables (Notes 13, 21)
Balance as at 1 January 2005	**12,229**	**730,208**
Write-down of inventories to net realisable value / Charge of impairment of accounts receivable	958	290,279
Bad debts write - off which was not initially provided	-	-
Balance as at 31 December 2005	**13,187**	**1,020,487**
Charge of impairment of accounts receivable		303,535
Reversal of write-down of inventories to net realisable value / Reversal of impairment of accounts receivable / Accrual of provision for liabilities and charges	(13,187)	(2,503)
Balance as at 31 December 2006	**-**	**1,321,519**

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

Due to the fact, that the tax and other legislation do not fully cover all the aspects of the Group restructuring, there might be respective legal and tax risks.

As at 31 December 2006, management believes that its interpretation of the relevant legislation is appropriate and the Group tax, currency and customs positions will be sustained. Accordingly, at 31 December 2006 no provision for potential tax liabilities had been recorded (31 December 2005: no provision).

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

Potential liabilities might arise as a result of changes in legislation and regulation or civil litigation. The impact of these potential changes cannot be estimated, but could be material. Currently, management believes that there are no significant liabilities related to environmental matters.

(in thousands of Russian Roubles, unless otherwise stated)

Note 27. Financial instruments and financial risk factors

Financial risk factors. The Group activities expose it to a variety of financial risks, including the effects of changes in interest rates and the collectability of receivables. The Group does not hedge its financial exposures.

Credit risk. Financial assets, which potentially subject the Group to concentrations of credit risk, consist principally of trade receivables. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision for impairment of receivables already recorded.

Cash has been deposited in financial institutions with no more than minimal exposure to default.

Interest rate risk. The Group operating profits and cash flows from operating activity are largely not dependent on the changes in market interest rates. The majority of interest rates on current and non-current borrowings are fixed, these are disclosed in Note 18.

Fair values. Management believes that the fair values of its financial assets and liabilities approximates their carrying amount.

Note 28. Subsequent events

Revaluation of property, plant and equipment

In 2006 the Group engaged CJSC Ernst&Young as an independent appraiser for revaluation of the Group fixed assets as at 1 January 2007. Results of the fixed assets revaluation will be reflected in the financial statements for the year ended 31 December 2007.

Group restructuring

The shareholders' extraordinary meeting of the Group (Minutes of the meeting of OJSC RAO UES Management Board No1436pr/4 dated 13.04.2006) approved that the merger of the Group with OJSC Arkhangelskaya GC to be finalized in May 2007. The merger was completed on 11 May 2007.

Dividends

11 May 2007 the general meeting of the shareholders of TGC-2 declared annual dividends for the year 2006 in the total amount of RR 406 thousand.

Disposal of subsidiary

In August 2006 the Board of Directors of the Group approved the sale of non-core subsidiary OJSC "Novgorodenergoservice". In April 2007 the Group sold 100% of shares in OJSC "Novgorodenergoservice" for RR 34,733 thousand. Net assets of OJSC "Novgorodenergoservice" as at 31 December 2006 were the following:

	OJSC "Novgorodenergoservice" net assets
Current assets	7,687
Property, plant and equipment	33,425
Other non-current assets	887
Current liabilities	(1,588)
Non-current liabilities	(348)
Net assets	**40,063**

Issue of promissory notes

On 02 June 2007 the Group issued promissory notes for total amount of RR 1,500,000 thousand, with maturity date till 29 December 2007 and interest rate 8.5%.

Reorganization of the Group and additional share issue

Extraordinary General Shareholders Meeting, held on 5 December 2007, made decision of reorganization of the Group by merging with OJSC TGC-2 Holding, which was separated from OJSC RAO UES of Russia at the final stage of energy sector reform. Shareholders also ratified agreement of merging and converting OJSC TGC-2 Holding's shares into the Group's shares.

Shareholders also made decision to increase the Group's authorized capital amount for converting purposes: the Group can place 2,705,952,526 shares with par value of RR 0.01 per share and a total value of RR 27,060 thousand.

Note 28. Subsequent events (continued)

OJSC TGC-2 Holding's shares are declared as converted into Group's ordinary shares on the date of entry being made in the Unified State Register of Legal Entities about the termination of OJSC TGC-2 Holding activity. Then TGC-2 Holding's shares subject to conversion will be cancelled.

Also, Extraordinary General Shareholders Meeting authorized additional share issue in the amount of 440,550,372,763 ordinary shares with the face value of RR 0.01 per share and a total value of RR 4,405,504 thousand. Placement will be conducted through public offering. Additional issue is intended to be carried out for the Group's investment program realization purposes.