



**JSC Interregional Distribution Grid  
Companies Holding**

**Consolidated Financial Statements  
for the years ended 31 December 2008 and 2007**

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## **Independent Auditors' Report**

To the Board of Directors of Joint Stock Company IDGC Holding

We have audited the accompanying consolidated financial statements of Joint Stock Company IDGC Holding and its subsidiaries (the "Group"), which comprise the consolidated balance sheets as at 31 December 2008 and 2007, and the consolidated income statements, consolidated statements of changes in equity and consolidated cash flow statements for the years then ended, and a summary of significant accounting policies and other explanatory notes.

### *Management's Responsibility for the Consolidated Financial Statements*

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

### *Auditors' Responsibility*

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

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

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

*Basis for Qualified Opinion*

We did not observe the counting of inventories stated at RUR 10,346,068 thousand as at 31 December 2007 because we were engaged as auditors of the Group only after that date. It was impracticable to satisfy ourselves as to those inventory quantities by other audit procedures. Accordingly, we were unable to determine whether any adjustments might be necessary to operating expenses, income tax expense and profit for the year ended 31 December 2008 and to inventories, operating expenses, income tax expense, profit for the year and retained earnings as at and for the year ended 31 December 2007.

*Qualified Opinion*

In our opinion, except for the effects of such adjustments, if any, that might have been determined to be necessary had it been practicable to obtain sufficient appropriate audit evidence as described in the Basis for Qualified Opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2008 and 2007, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.



ZAO KPMG

26 October 2009

**JSC IDGC Holding**  
*Consolidated Income Statement for the year ended 31 December 2008*  
*(in thousand of Russian roubles, unless otherwise stated)*

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Revenue and government subsidies	6	397,881,732	321,789,823
Operating expenses	7	(367,673,182)	(296,714,080)
Other operating income	8	2,281,407	1,552,292
<b>Results from operating activities</b>		<b>32,489,957</b>	<b>26,628,035</b>
Financial income	10	6,634,606	1,309,571
Financial expenses	10	(12,502,281)	(4,728,211)
Share of profit/(loss) of equity accounted investees (net of income tax)	14	20,519	(10,179)
<b>Profit before income tax</b>		<b>26,642,801</b>	<b>23,199,216</b>
Income tax expense	11	(6,880,491)	(9,246,282)
<b>Profit for the year</b>		<b>19,762,310</b>	<b>13,952,934</b>
Attributable to:			
Shareholders of the Company		11,040,869	7,591,657
Minority interest		8,721,441	6,361,277
<b>Earnings per share</b>	21		
Basic and diluted earnings per ordinary share		RUR 0.26	RUR 0.18
Basic and diluted earnings per preference share		RUR 0.26	RUR 0.18

These consolidated financial statements were approved by management on 26 October 2009 and were signed on its behalf by:

Deputy General Director, Economics and Finance  
A.V. Demidov



Chief Accountant  
G.I. Zhabbarova



**JSC IDGC Holding**  
*Consolidated Balance Sheet as at 31 December 2008*  
*(in thousand of Russian roubles, unless otherwise stated)*

	Notes	31 December 2008	31 December 2007
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	12	530,381,403	426,071,442
Intangible assets	13	3,882,771	3,121,215
Investments in equity accounted investees	14	631,335	610,816
Non-current accounts receivable	18	4,282,204	3,508,930
Other investments and financial assets	15	7,681,296	13,087,500
Deferred tax assets	16	4,233,367	4,556,339
<b>Total non-current assets</b>		<b>551,092,376</b>	<b>450,956,242</b>
<b>Current assets</b>			
Inventories	17	11,941,159	10,346,068
Other investments and financial assets	15	2,893,745	4,726,852
Income tax receivable		1,329,355	2,071,691
Trade and other receivables	18	75,858,067	53,291,766
Cash and cash equivalents	19	19,514,706	17,058,156
<b>Total current assets</b>		<b>111,537,032</b>	<b>87,494,533</b>
<b>Total assets</b>		<b>662,629,408</b>	<b>538,450,775</b>

**JSC IDGC Holding**  
*Consolidated Balance Sheet as at 31 December 2008*  
(in thousand of Russian roubles, unless otherwise stated)

	Notes	31 December 2008	31 December 2007
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>	20		
Share capital		43,116,903	43,116,903
Reserves		241,882	1,223,321
Retained earnings		148,239,509	137,242,858
<b>Total equity attributable to shareholders of the Company</b>		191,598,294	181,583,082
Minority interest		137,168,385	121,343,576
<b>Total equity</b>		<b>328,766,679</b>	<b>302,926,658</b>
<b>Non-current liabilities</b>			
Non-current debt	22	87,055,703	52,893,626
Non-current accounts payable	25	13,260,008	6,681,353
Employee benefits	23	7,621,034	7,125,271
Deferred tax liabilities	16	28,492,228	34,233,493
<b>Total non-current liabilities</b>		<b>136,428,973</b>	<b>100,933,743</b>
<b>Current liabilities</b>			
Current debt and current portion of non-current debt	22	55,473,672	35,745,548
Trade and other payables	25	138,821,811	94,497,314
Provisions	24	1,081,941	732,397
Income tax payable		2,056,332	3,615,115
<b>Total current liabilities</b>		197,433,756	134,590,374
<b>Total liabilities</b>		<b>333,862,729</b>	<b>235,524,117</b>
<b>Total equity and liabilities</b>		<b>662,629,408</b>	<b>538,450,775</b>

**JSC IDGC Holding**  
*Consolidated Statement of Cash Flows for the year ended 31 December 2008*  
*(in thousand of Russian roubles, unless otherwise stated)*

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
<b>Cash flows from operating activities</b>		
Profit for the year	19,762,310	13,952,934
<i>Adjustments for:</i>		
Depreciation and amortisation	33,884,624	26,868,464
Change in allowance for doubtful debts	4,927,500	3,098,195
Financial expense	12,502,281	4,728,211
Financial income	(6,634,606)	(1,309,571)
Surplus of assets	(993,045)	(244,154)
Gain on disposal of property, plant and equipment	(824,043)	(878,965)
Share of (profit)/loss of equity accounted investees	(20,519)	10,179
Change in provision for obsolescence	145,613	160,875
Income tax expense	6,880,491	9,246,282
<b>Operating profit before changes in working capital and provisions</b>	<b>69,630,606</b>	<b>55,632,450</b>
Change in inventories	(2,500,500)	(2,045,850)
Change in trade and other receivables	(26,245,700)	(9,759,500)
Change in financial assets related to employee benefit fund	(1,677,346)	(1,153,835)
Change in trade and other payables	51,173,575	36,038,832
Change in employee benefit liabilities	495,763	400,865
<b>Cash flows from operations before income taxes and interest paid</b>	<b>90,876,398</b>	<b>79,112,962</b>
Income taxes paid	(12,231,148)	(7,613,697)
Interest paid	(9,239,401)	(3,514,560)
<b>Cash flows from operating activities</b>	<b>69,405,849</b>	<b>67,984,705</b>

**JSC IDGC Holding**  
*Consolidated Statement of Cash Flows for the year ended 31 December 2008*  
*(in thousand of Russian roubles, unless otherwise stated)*

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
<b>INVESTING ACTIVITIES</b>		
Proceeds from disposal of property, plant and equipment	2,480,512	1,487,555
Proceeds from disposal of investments	10,018,397	209,501
(Issuance)/proceeds from loans to third parties	(300,677)	605,979
Interest received	932,059	823,733
Dividends received	23,992	45,188
Repayment of bank deposits	4,305,716	1,679,000
Acquisition of property, plant and equipment and intangible assets	(116,368,464)	(93,957,903)
Acquisition of other investments	(2,548,616)	(780,342)
Acquisition of subsidiaries, net of cash acquired	(794,071)	-
Placement of bank deposits	(2,419,000)	(3,754,800)
<b>Cash flows used in investing activities</b>	<b>(104,670,152)</b>	<b>(93,642,089)</b>
<b>FINANCING ACTIVITIES</b>		
Proceeds from shares issued to minority interest	-	500,000
Advance contributions for shares issued (repaid)/received	(10,018)	3,055,681
Proceeds from borrowings	133,600,660	121,894,165
Repayment of borrowings	(84,625,367)	(79,705,117)
Payment of financial lease liabilities	(10,724,331)	(7,570,829)
Dividends paid	(520,091)	(2,370,461)
<b>Cash flows from financing activities</b>	<b>37,720,853</b>	<b>35,803,439</b>
<b>Net increase in cash and cash equivalents</b>	<b>2,456,550</b>	<b>10,146,055</b>
Cash and cash equivalents at beginning of year	17,058,156	6,912,101
<b>Cash and cash equivalents at end of year (note 19)</b>	<b>19,514,706</b>	<b>17,058,156</b>

**JSC IDGC Holding**  
*Consolidated Statement of Changes in Equity for the year ended 31 December 2008*  
*(in thousand of Russian roubles, unless otherwise stated)*

	<b>Share capital</b>	<b>Available-for-sale investments revaluation reserve</b>	<b>Retained earnings</b>	<b>Total</b>	<b>Minority interest</b>	<b>Total equity</b>
<b>Balance at 1 January 2007</b>	<b>43,116,903</b>	<b>863,501</b>	<b>131,018,856</b>	<b>174,999,260</b>	<b>115,386,882</b>	<b>290,386,142</b>
Profit for the year	-	-	7,591,657	7,591,657	6,361,277	13,952,934
Revaluation of available-for-sale investments	-	359,820	-	359,820	-	359,820
Total recognised income and expense	-	359,820	7,591,657	7,951,477	6,361,277	14,312,754
Dividends to RAO UES of Russia	-	-	(1,367,655)	(1,367,655)	-	(1,367,655)
Dividends to minority interest shareholders	-	-	-	-	(904,583)	(904,583)
Shares issued	-	-	-	-	500,000	500,000
<b>Balance at 31 December 2007</b>	<b>43,116,903</b>	<b>1,223,321</b>	<b>137,242,858</b>	<b>181,583,082</b>	<b>121,343,576</b>	<b>302,926,658</b>
<b>Balance at 1 January 2008</b>	<b>43,116,903</b>	<b>1,223,321</b>	<b>137,242,858</b>	<b>181,583,082</b>	<b>121,343,576</b>	<b>302,926,658</b>
Profit for the year	-	-	11,040,869	11,040,869	8,721,441	19,762,310
Revaluation of available-for-sale investments	-	299,190	-	299,190	-	299,190
Disposal of available-for-sale investments	-	(1,280,629)	-	(1,280,629)	-	(1,280,629)
Total recognised income and expense	-	(981,439)	11,040,869	10,059,430	8,721,441	18,780,871
Transactions with shareholders	-	-	1,871,206	1,871,206	-	1,871,206
Effect of changes in minority interest	-	-	(1,617,940)	(1,617,940)	1,617,940	-
Acquisition of subsidiary	-	-	-	-	(134,774)	(134,774)
Dividends to RAO UES of Russia	-	-	(297,484)	(297,484)	-	(297,484)
Dividends to minority interest shareholders	-	-	-	-	(162,531)	(162,531)
Shares issued	-	-	-	-	5,782,733	5,782,733
<b>Balance at 31 December 2008</b>	<b>43,116,903</b>	<b>241,882</b>	<b>148,239,509</b>	<b>191,598,294</b>	<b>137,168,385</b>	<b>328,766,679</b>

## **1 Background**

### **(a) The Group and its operations**

Joint Stock Company Interregional Distribution Grid Company Holding (hereinafter referred to as “JSC IDGC Holding” or the “Company”) was established on 1 July 2008 in accordance with the resolution of the Extraordinary General Meeting of the Shareholders of the Unified Energy System of Russia (hereinafter referred to as “RAO UES”) dated 26 October 2007 by the means of spin-off from RAO UES.

The ordinary and preference shares of the Company are traded on the MICEX Stock Exchange and the Russian Commodities and Russian Trading System.

The Company’s registered office is located at 5A Akademika Chelomeya street, Moscow, Russia, 117630.

The JSC IDGC Holding Group (hereinafter referred to as “the Group”) comprises JSC IDGC Holding and its subsidiaries presented in Note 31.

The Group’s principal activity is electricity transmission and distribution and electricity sales. The Group also provides connection services as part of its core operations.

### **(b) Formation of the Group**

The Company was established in the course of the Russian electric utilities industry restructuring, discussed further below, to ensure the unified quality standards for electro-grid services and to provide the technological, economic and financial control over distribution grid complex, creating the conditions for high reliability and availability of the distribution grid infrastructure for the consumers in all the regions of the Russian Federation.

The formation of the interregional distribution grid companies, which were formed as a result of the disaggregation of activities of AO-Energos during the reform, was completed in 2008.

On 1 July 2008 the reorganization of RAO UES was completed. As a result RAO UES ceased to exist as a legal entity and JSC IDGC Holding became one of its legal successors in accordance with the balance sheet on demerger. On that date RAO UES transferred to JSC IDGC Holding the shares of 11 interregional distribution grid companies (hereinafter referred to as “IDGCs”), 5 regional distribution companies and 7 regional retail electricity companies.

On 1 July 2008 as a result of RAO UES of Russia’s reorganisation the shares of the Company were split between the remaining shareholders of RAO UES proportionate to their existing ownership. The structure of the share capital of newly created Company, therefore, mirrored the structure of the share capital of RAO UES.

### **(c) Relations with state and current regulations**

The Group business is the natural monopoly which is under support of Russian government. The government of the Russian Federation directly affects the Group’s operations through the state tariffs.

In accordance with legislation the Group's tariffs are controlled by the Federal Service on Tariffs and the Regional Energy Commission.

As at 31 December 2008 the State owned 54.99% of the voting ordinary shares and 7.01 percent of the preference shares of the Company. The Government of the Russian Federation, through the Federal Agency for the Management of Federal Property, is the ultimate controlling party of the Company. The Group's customer base includes a number of state-controlled entities (Note 30).

## **2 Basis of preparation**

### **(a) Statement of compliance**

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

### **(b) Basis of measurement**

The consolidated financial statements are prepared on the historical cost basis except that derivative financial instruments and financial investments classified as available-for-sale are stated at fair value.

### **(c) First-time adoption of IFRS**

These Financial Statements are the Group's first consolidated financial statements prepared in accordance with IFRSs.

The accounting policies set out in Note 3 have been applied in preparing the consolidated financial statements as at and for the years ended 31 December 2008 and 31 December 2007, and in the preparation of an opening IFRS balance sheet as at 1 January 2007 (the Group's date of transition).

The formation of the Group was completed on 1 July 2008 (refer to Note 1 (b)). All the entities constituting the merged Group were under common control of RAO UES. These financial statements are prepared in accordance with the Group accounting policies in respect of business combinations involving entities under common control (refer to Note 3 (a)) as if the formation of the Group was completed as at 1 January 2007.

As the Group did not prepare consolidated financial statements under Russian Accounting Principles (RAP), no reconciliation to RAP on transition to IFRS is provided.

The Group elected to determine the deemed cost of property, plant and equipment as at 1 January 2007 using an independent appraisal at that date (refer to Note 12).

### **(d) Functional and presentation currency**

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

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

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

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

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is included in the following notes:

- Note 6 – Revenue;
- Note 17 – Inventories;
- Note 18 – Trade and other receivables;
- Note 23 – Employee benefits;
- Note 24 – Provisions.

**3 Significant accounting policies**

The significant accounting policies applied in the preparation of the consolidated financial statements are described in Note 3(a) to 3(s). These accounting policies have been consistently applied.

**(a) Basis of consolidation**

**(i) Subsidiaries**

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

**(ii) Acquisitions of entities under common control**

Business combinations arising from transfers of interests in entities that are under the control of the shareholder that controls the Group are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date that common control was established; for this purpose comparatives are restated. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the consolidated financial statements of the acquired entities. The components of equity are added to the same components within Group entity, except that any share capital of the acquired entities is recognized as part of retained earnings. Any cash or other contribution paid for the acquisition is recognized directly in equity.

**(iii) *Associates (equity accounted investees)***

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Associates are accounted for using the equity method. The consolidated financial statements include the Group's share of the income and expenses of equity accounted investees, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an associate, the carrying amount of that interest (including any non-current investments) is reduced to nil and the recognition of further losses is discontinued, except to the extent that the Group has an obligation or has made payments on behalf of the investee.

**(iv) *Transactions eliminated on consolidation***

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

**(b) *Foreign currency***

**(i) *Foreign currency transactions***

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

**(c) *Financial instruments***

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

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

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

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

Accounting for finance income and expenses is discussed in Note 3(o).

*Held-to-maturity investments*

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

*Available-for-sale financial assets*

The Group's investments in equity securities and certain debt securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see Note 3(i)(i)) which are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to the income statement.

*Other*

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses. Investments in equity securities that are not quoted on a stock exchange and where fair value cannot be estimated on a reasonable basis by other means are stated at cost less impairment losses.

**(ii) Derivative financial instruments**

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss.

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in the income statement when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are recognised immediately in the income statement.

**(d) Share capital**

Ordinary shares and non-redeemable preferred shares with the right to receive discretionary annual fixed dividends are both classified as equity.

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

**(i) Recognition and measurement**

Items of property, plant and equipment, except for land, are measured at cost less accumulated depreciation and impairment losses. The cost of property, plant and equipment as at 1 January 2007, the date of transition to IFRSs, was determined by reference to its fair value at that date.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment. Borrowing costs related to qualifying assets are recognised as part of the cost of such assets.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of an item of property, plant and equipment are recognised net in “other income” in the income statement.

**(ii) Subsequent costs**

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in the income statement as incurred.

**(iii) Depreciation**

Depreciation is recognised in the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

The estimated useful lives for the current and comparative periods are as follows:

- buildings 7-50 years
- transmission networks 5-40 years
- equipment for electricity transmission 5-40 years
- other 1-50 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

**(f) Intangible assets**

**(i) Goodwill**

Goodwill (negative goodwill) arises on the acquisition of subsidiaries, associates and joint ventures.

Goodwill represents the excess of the cost of the acquisition over the Group’s interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the difference between the cost of acquisition and the Group’s interest in the net fair value of identifiable assets is negative (negative goodwill), it is recognised immediately in the income statement.

*Acquisitions of minority interests*

Goodwill arising on the acquisition of a minority interest in a subsidiary represents the excess of the cost of the additional investment over the carrying amount of the net assets acquired at the date of exchange.

*Subsequent measurement*

Goodwill is measured at cost less accumulated impairment losses. In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment.

**(ii) Other intangible assets**

Other intangible assets that are acquired by the Group, which have finite useful lives, are measured at cost less accumulated amortisation and accumulated impairment losses.

**(iii) Subsequent expenditure**

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in the income statement as incurred.

**(iv) Amortisation**

Amortisation is recognised in the income statement on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use. The estimated useful lives for the current and comparative periods are as follows:

- licenses and certificates      1-10 years
- software                              1-15 years.

**(g) Leased assets**

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as financial leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised on the Group's balance sheet.

**(h) Inventories**

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is determined on the weighted average cost method, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

**(i) Impairment**

**(i) Financial assets**

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

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

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

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

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

**(ii) Non-financial assets**

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

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

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

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

**(j) Employee benefits**

**(i) Defined contribution plans**

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, including Russia's

State pension fund, are recognised in the income statement when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

**(ii) *Defined benefit post-employment plans***

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and any unrecognised past services are deducted. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations and that are denominated in the same currency in which the benefits are expected to be paid. The calculation is performed annually by a qualified actuary using the projected unit credit method.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised in the income statement on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in the income statement.

The Group recognises all actuarial gains and losses in the income statement for the reporting period under the 10% corridor of the post-employment benefit obligation.

**(iii) *Other non-current employee benefits***

The Group's net obligation in respect of non-current employee benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed using the projected unit credit method. Actuarial gains and losses on other non-current obligations are recognized immediately. Past service cost on other non-current obligations is recognized immediately.

**(iv) *Short-term benefits***

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

**(k) *Provisions***

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

**(l) Revenue**

**(i) Electricity transmission**

Revenue from electricity transmission is recognised in the income statement when the customer acceptance of the volume of electricity transmitted is received. The tariffs for energy transmission are approved by the government agencies of the constituents of the Russian Federation in the sphere of the state tariff regulation within the range of cap and/or floor tariffs approved by the Federal Tariffs Agency.

**(ii) Connection services**

Revenue from connection services represents a non-refundable fee for connecting the customer to the electricity grid network. The terms, conditions and amounts of these fees are negotiated separately and are independent from fees generated by electricity transmission services.

Revenue is recognized when electricity is activated and the customer is connected to the grid network, or, for contracts where connection services are performed in stages, revenue is recognized in the proportion to the stage of completion when act of acceptance is signed by the customer.

**(iii) Other services**

Revenue from installation, repair and maintenance services and other sales is recognized when the services are provided or when the significant risks and rewards of ownership of the goods have passed to the buyer.

**(m) Government subsidies**

Government subsidies that compensate the Group for low electricity tariffs are recognised in the income statement in the same periods in which the respective revenue is earned.

**(n) Other expenses**

**(i) Lease payments**

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

Minimum lease payments made under financial leases are apportioned between the financial expense and the reduction of the outstanding liability. The financial expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Contingent lease payments are accounted for by revising the minimum lease payments over the remaining term of the lease when the contingency no longer exists and the lease adjustment is known.

**(ii) Social expenditure**

To the extent that the Group's contributions to social programs benefit the community at large and are not restricted to the Group's employees, they are recognised in the income statement as incurred.

**(o) Financial income and expenses**

Financial income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, discount on financial instruments, changes in fair value of financial assets at fair value through profit or loss and foreign currency gains. Interest income is recognised as it accrues in the income statement, using the effective interest method. Dividend income is recognised in the income statement on the date that the Group's right to receive payment is established.

Financial expenses comprise interest expense on borrowings, financial leasing, foreign currency losses, discount on financial instruments and impairment losses recognised on financial assets other than trade receivables. All borrowing costs are recognised in the income statement using the effective interest method, except for borrowing costs related to qualifying assets which are recognised as part of the cost of such assets.

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

**(p) Income tax expense**

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

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

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

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

**(q) Earnings per share**

The Group presents basic earnings per share ("EPS") data for its ordinary and preference shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary and preference

shareholders of the Company by the weighted average number of ordinary and preference shares, respectively, outstanding during the period.

**(r) Guarantees**

The Group's policy is to provide financial guarantees only in respect of loans issued to the Group lessors. The Group considers these instruments as insurance contracts and accounts for them as such.

**(s) Segment reporting**

A segment is a distinguishable component of the Group that is engaged either in providing related products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Group's main business segment is transmission and distribution of electricity and connection services which are related activities, therefore they are reporting as one business segment. As a result segment information is presented in respect of the Group's geographical segments only.

Inter-segment pricing is determined on an arm's length basis.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly investments (other than investment property) and related revenue, loans and borrowings and related expenses, and income tax assets and liabilities.

Segment capital expenditure is the cost incurred during the period to acquire property, plant and equipment, and intangible assets other than goodwill.

**(t) New Standards and Interpretations not yet adopted**

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

- IFRS 8 *Operating Segments* introduces the "management approach" to segment reporting. IFRS 8 *Operating Segments*, which becomes mandatory for the Group's 2009 consolidated financial statements, will require the disclosure of segment information based on the internal reports regularly reviewed by the Group's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them. Currently the Group presents segment information in respect of its geographical segments (see Note 5).
- Revised IAS 1 *Presentation of Financial Statements (2007)* which becomes mandatory for the Group's 2009 consolidated financial statements is expected to have a significant impact on the presentation of the consolidated financial statements. The Standard introduces the concept of total comprehensive income and requires presentation of all owner changes in equity in the statement of changes in equity, separately from non-owner changes in equity.

- Amendments to IAS 32 Financial instruments: Presentation and IAS 1 Presentation of Financial Statements – *Puttable Financial Instruments and Obligations Arising on Liquidation* requires puttable instruments, and instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation, to be classified as equity if certain conditions are met. The amendments, which become mandatory for the Group's 2009 consolidated financial statements, with retrospective application required, are not expected to have any impact on the consolidated financial statements.
- Amendment to IAS 39 Financial Instruments: *Recognition and Measurement – Eligible Hedged Items* clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The amendment, which becomes mandatory for the Group's 2010 consolidated financial statements, with retrospective application required, is not expected to have any impact on the consolidated financial statements.
- Amendment to IFRS 2 *Share-based Payment – Vesting conditions and cancellations* clarify the definition of vesting conditions, introduce the concept of non-vesting conditions, require non-vesting conditions to be reflected in grant-date fair value and provide the accounting treatment for non-vesting conditions and cancellations. The amendments to IFRS 2 will become mandatory for the Group's 2009 consolidated financial statements, with retrospective application. The Group has not yet determined the potential effect of the amendment.
- Revised IFRS 3 *Business Combinations* (2008) and amended IAS 27 (2008) *Consolidated and Separate Financial Statements*, which come into effect on 1 July 2009 (i.e. become mandatory for the Group's 2010 consolidated financial statements). The revisions address, among others, accounting for step acquisitions, require acquisition-related costs to be recognised as expenses and remove exception for changes in contingent consideration to be accounted by adjusting goodwill. The revisions also address how non-controlling interests in subsidiaries should be measured upon acquisition and require to recognise the effects of transactions with non-controlling interest directly in equity. The Group has not yet analysed the likely impact of the new Standard on its financial position or performance.
- IFRIC 17 *Distributions of Non-cash Assets to Owners* addresses the accounting of non-cash dividend distributions to owners. The interpretation clarifies when and how the non-cash dividend should be recognised and how the differences between the dividend paid and the carrying amount of the net assets distributed should be recognised. IFRIC 17 becomes effective for annual periods beginning on or after 1 July 2009. The Group does not expect this amendment to have any impact on the consolidated financial statements.
- IFRIC 18 *Transfers of Assets from Customers* applies to the accounting for transfers of items of property, plant and equipment by entities that receive such transfers from their customers. The interpretation clarifies recognition and measurement of received items, how the resulting credit, as well as a transfer of cash from customers should be accounted for. IFRIC 18 is applied prospectively to transfers of assets from customers received on or after 1 July 2009. The Group has not yet analysed the likely impact of the new Standard on its financial position or performance.

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

## **4 Determination of fair values**

### **(a) Investments in equity and debt securities**

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

### **(b) Trade and other receivables**

The fair value of non-current trade and other receivables, is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. Management believes that the fair value of current trade and other receivables approximates their carrying amount.

### **(c) Derivatives**

The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds).

The fair value of interest rate and currency swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

### **(d) Non-derivative financial liabilities**

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. In respect of issued bonds the fair value is determined by reference to their quoted closing price at the reporting date. For financial leases the market rate of interest is determined by reference to similar lease agreements.

## **5 Segment reporting**

The Group has the following geographical segments:

- North-West region,
- Central region,
- Ural and Volga region,
- South region,
- Siberian region,
- Other regions.

The information for the year ended 31 December 2008 and 2007 is presented below:

	North-West		Centre		Ural and Volga		South		Siberia		Other regions		Consolidated	
	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007
Revenue from external customers	50,917,140	42,091,907	147,367,839	108,132,227	72,318,453	69,875,427	57,225,474	48,675,824	75,834,341	59,175,633	1,574,919	904,380	405,238,166	328,855,398
Inter-segment revenue	(73,584)	(37,397)	(882)	(579,166)	(44,767)	(608,501)	(7,000,769)	(5,802,148)	(20,212)	(38,019)	(216,220)	(344)	(7,356,434)	(7,065,575)
<b>Total segment revenue</b>	<u>50,843,556</u>	<u>42,054,510</u>	<u>147,366,957</u>	<u>107,553,061</u>	<u>72,273,686</u>	<u>69,266,926</u>	<u>50,224,705</u>	<u>42,873,676</u>	<u>75,814,129</u>	<u>59,137,614</u>	<u>1,358,699</u>	<u>904,036</u>	<u>397,881,732</u>	<u>321,789,823</u>
Segment result	<u>5,757,023</u>	<u>3,958,009</u>	<u>16,975,884</u>	<u>15,123,410</u>	<u>4,817,686</u>	<u>4,724,857</u>	<u>903,723</u>	<u>828,377</u>	<u>3,774,511</u>	<u>1,831,202</u>	<u>261,130</u>	<u>162,180</u>	<u>32,489,957</u>	<u>26,628,035</u>
<b>Unallocated expenses</b>														
Financial income													6,634,606	1,309,571
Financial expenses													(12,502,281)	(4,728,211)
Share of profit of equity accounted investees													20,519	(10,179)
Income tax expense													(6,880,491)	(9,246,282)
<b>Profit for the year</b>													<u>19,762,310</u>	<u>13,952,934</u>

	North-West		2008	Centre		Ural and Volga		South		Siberia		Other regions		Consolidated	
	2008	2007		2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	
Segment assets	56,150,265	35,563,448	435,645,575	366,402,597	46,884,328	36,294,502	34,406,617	18,098,347	81,996,345	72,715,754	2,681,576	4,208,972	657,764,706	533,283,620	
Investment in equity accounted investee													631,335	610,816	
Unallocated assets													4,233,367	4,556,339	
<b>Total assets</b>													<u>662,629,408</u>	<u>538,450,775</u>	
<b>Segment liabilities</b>	(26,903,629)	(20,163,841)	(86,935,271)	(57,514,237)	(10,871,561)	(8,798,290)	(21,259,750)	(12,254,362)	(15,282,725)	(12,195,645)	(1,588,192)	(1,725,074)	(162,841,128)	(112,651,449)	
Unallocated liabilities													(171,021,601)	(122,872,668)	
<b>Total liabilities</b>													<u>(333,862,729)</u>	<u>(235,524,117)</u>	
Depreciation/a mortisation	4,142,778	3,145,620	15,616,641	12,331,305	5,326,129	4,368,518	3,241,875	2,343,711	5,513,717	4,655,966	43,484	23,344	33,884,624	26,868,464	
Capital expenditure	21,491,889	15,665,534	72,744,836	66,304,244	16,017,034	13,423,349	13,385,753	8,448,960	16,027,156	12,855,415	92,064	31,216	139,758,732	116,728,718	

## 6 Revenue and government subsidies

### *Revenue*

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Electricity transmission	326,436,615	267,237,006
Connection services	34,403,117	21,654,668
Electricity sales	21,713,821	16,761,237
Repairs and maintenance services	3,555,254	4,809,978
Rental income	3,116,599	1,844,077
Other revenues	5,489,051	6,167,934
	<b>394,714,457</b>	<b>318,474,900</b>
Government subsidies	3,167,275	3,314,923
	<b>397,881,732</b>	<b>321,789,823</b>

Other revenue is comprised of communication services, transportation services, etc.

### *Government subsidies*

In accordance with government decrees some regions of the Russian Federation are subject to government subsidies. These government subsidies represent compensation for low electricity tariffs at which electricity is sold in these regions. During the period the Group received government subsidies in the amount of RUB 3,167,275 thousand (2007: RUB 3,314,923 thousand). The Group conduct its operating activity in the following subsidized regions: Republic of Dagestan, Karachayev - Cherkessian Republic and Kaliningrad region.

## 7 Operating expenses

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Electricity transmission	102,521,277	66,734,365
Purchased electricity for compensation of technological losses	66,183,687	67,715,529
Personnel costs (Note 9)	62,575,666	55,469,545
Depreciation and amortization	33,884,624	26,868,464
Purchased electricity for resale	17,264,021	12,665,112
Repairs, maintenance and installation services	17,222,574	19,381,027
Electricity metering services	11,632,049	7,387,197
Raw materials and supplies	11,581,212	8,724,727
Consulting, legal, audit services including professional training	6,470,668	3,457,586
Rent	5,261,573	2,560,384
Allowance for impairment of trade and other receivables	4,594,162	2,829,340
Transportation	2,868,297	1,878,244
Insurance	2,607,342	2,357,683
Technological connection services	2,440,849	1,142,797
Taxes other than income tax	2,321,397	2,091,989
Electricity and heat power for own needs	2,064,600	1,387,099
Security services	1,892,455	1,665,272
Telecommunication and information services	1,782,717	1,277,243
Social expenditures and charity expenses	1,100,439	800,293
Provision for legal claims	349,544	332,110
Allowance for impairment of prepayments	333,338	268,855
Taxes and penalties	214,061	115,252
Provision for obsolescence of inventories	145,613	160,875
Other expenses	10,361,017	9,443,092
	<b>367,673,182</b>	<b>296,714,080</b>

Other expenses are comprised of loss on disposal of inventories, management fees, agency services, bank commission, etc.

## 8 Other operating income

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Surplus of assets	993,045	244,154
Gain on disposal of property, plant and equipment	824,043	878,965
Fines and penalties	283,184	285,104
Other operating income	181,135	144,069
	<b>2,281,407</b>	<b>1,552,292</b>

Surplus of assets is represented by ownerless transfer facilities identified by the Group during the stock take. The Group used services of independent appraisers to determine the fair value of the identified assets recognized in the balance sheet.

## 9 Personnel costs

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Wages and salaries	47,288,290	41,587,497
Payroll taxes	12,475,886	11,003,487
Expense in respect of post-employment defined benefit plan	1,411,590	1,040,509
Expense in respect of long-term service benefits provided	103,487	152,496
Other	1,296,413	1,685,556
	<b>62,575,666</b>	<b>55,469,545</b>

The amount of contributions to defined contribution plan was RUR 603,832 thousand for the year ended 31 December 2008 (2007: RUR 565,583 thousand).

## 10 Financial income and expenses

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
<b><i>Financial income</i></b>		
Change in fair value of derivative instrument – interest/currency swap	1,887,531	-
Interest income on loans	771,326	253,337
Net gain on disposal of available-for-sale financial assets transferred from equity	2,691,724	59,764
Effect of discounting of financial instruments	628,333	391,736
Interest income on bank deposits	272,361	174,870
Interest income on promissory notes	215,244	258,666
Interest income on financial assets related to employee benefit fund	136,497	103,492
Dividend income on available-for-sale financial assets	31,590	67,706
	<b>6,634,606</b>	<b>1,309,571</b>
<b><i>Financial expenses</i></b>		
Interest expenses on financial liabilities measured at amortised cost	(5,917,685)	(2,553,195)
Financial leasing	(3,252,050)	(1,650,111)
Impairment loss on bank deposits	(1,201,687)	-
Impairment on available-for-sale financial assets	(1,046,609)	(109,518)
Net foreign exchange losses	(837,342)	(12,755)
Financial expense	(30,581)	(12,674)
Effect of discounting of financial instruments	(216,327)	(389,958)
	<b>(12,502,281)</b>	<b>(4,728,211)</b>

## 11 Income tax expense

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
<i>Current tax expense</i>		
Current year	(12,045,681)	(11,897,299)
Over provided in prior years	34,355	605,085
	<b>(12,011,326)</b>	<b>(11,292,214)</b>
<i>Deferred tax expense</i>		
Origination and reversal of temporary differences	422,647	2,045,932
Change in tax rate	4,708,188	-
	5,130,835	2,045,932
	<b>(6,880,491)</b>	<b>(9,246,282)</b>

The Group's applicable tax rate is the income tax rate of 24% for Russian companies (2007: 24%). With effect from 1 January 2009, the income tax rate for Russian companies has been reduced to 20%. This rate has been used in the calculation of deferred tax assets and liabilities.

### Reconciliation of effective tax rate:

	<b>Year ended 31 December 2008</b>	<b>%</b>	<b>Year ended 31 December 2007</b>	<b>%</b>
Profit before income tax	26,642,801	100	23,199,216	100
Income tax at applicable tax rate	(6,394,272)	(24)	(5,567,812)	(24)
Effect of income taxed at (lower)/higher rates	11,264	-	(2,553)	-
Change in tax rate	4,708,188	18	-	-
Non-deductible expenses	(5,240,026)	(20)	(4,157,703)	(18)
Effect of derecognition of tax assets	-	-	(123,299)	(1)
Over provided in prior years	34,355	-	605,085	3
	<b>(6,880,491)</b>	<b>(26)</b>	<b>(9,246,282)</b>	<b>(40)</b>

## 12 Property, plant and equipment

	<b>Land and buildings</b>	<b>Transmis- sion networks</b>	<b>Equipment for electricity transmission</b>	<b>Construc- tion in progress</b>	<b>Other</b>	<b>Total</b>
<b><i>Cost / Deemed cost</i></b>						
Balance at 1 January 2007	52,082,145	194,420,310	39,846,872	28,852,907	23,223,428	338,425,662
Additions	735,168	9,297,992	9,524,793	92,872,243	4,298,522	116,728,718
Transfer	6,131,845	16,149,330	16,323,879	(48,137,136)	9,532,082	-
Disposals	(316,093)	(907,854)	(439,261)	(491,875)	(1,259,729)	(3,414,812)
Balance at 31 December 2007	<b>58,633,065</b>	<b>218,959,778</b>	<b>65,256,283</b>	<b>73,096,139</b>	<b>35,794,303</b>	<b>451,739,568</b>
Balance at 1 January 2008	58,633,065	218,959,778	65,256,283	73,096,139	35,794,303	451,739,568
Acquisitions through business combinations	35,035	386,088	151,968	128,468	46,480	748,039
Additions	2,932,534	6,448,056	8,361,352	118,080,137	3,936,653	139,758,732
Transfer	13,056,200	20,149,980	22,505,833	(69,100,119)	13,388,106	-
Disposals	(399,841)	(524,222)	(282,695)	(839,387)	(2,018,858)	(4,065,003)
Balance at 31 December 2008	<b>74,256,993</b>	<b>245,419,680</b>	<b>95,992,741</b>	<b>121,365,238</b>	<b>51,146,684</b>	<b>588,181,336</b>
<b><i>Depreciation</i></b>						
Balance at 1 January 2007	-	-	-	-	-	-
Depreciation charge	(2,534,558)	(14,488,778)	(4,803,468)	-	(4,577,899)	(26,404,703)
Disposals	17,938	94,517	164,590	-	459,532	736,577
Balance at 31 December 2007	<b>(2,516,620)</b>	<b>(14,394,261)</b>	<b>(4,638,878)</b>	<b>-</b>	<b>(4,118,367)</b>	<b>(25,668,126)</b>
Balance at 1 January 2008	(2,516,620)	(14,394,261)	(4,638,878)	-	(4,118,367)	(25,668,126)
Depreciation charge	(3,181,588)	(16,078,577)	(7,277,074)	-	(6,248,841)	(32,786,080)
Disposals	43,186	88,830	71,228	-	451,029	654,273
Balance at 31 December 2008	<b>(5,655,022)</b>	<b>(30,384,008)</b>	<b>(11,844,724)</b>	<b>-</b>	<b>(9,916,179)</b>	<b>(57,799,933)</b>
<b><i>Net book value</i></b>						
At 1 January 2007	<b>52,082,145</b>	<b>194,420,310</b>	<b>39,846,872</b>	<b>28,852,907</b>	<b>23,223,428</b>	<b>338,425,662</b>
At 31 December 2007	<b>56,116,445</b>	<b>204,565,517</b>	<b>60,617,405</b>	<b>73,096,139</b>	<b>31,675,936</b>	<b>426,071,442</b>
At 31 December 2008	<b>68,601,971</b>	<b>215,035,672</b>	<b>84,148,017</b>	<b>121,365,238</b>	<b>41,230,505</b>	<b>530,381,403</b>

As at 31 December 2008 construction in progress includes advance payments for property, plant and equipment of RUR 26,871,425 thousand (31 December 2007: RUR 18,442,182 thousand) which are stated net of impairment provision of RUR 225,566 thousand (31 December 2007: RUR 103,381 thousand).

The amount of capitalised interest for the year ended 31 December 2008 was RUR 4,150,166 thousand (2007: RUR 1,327,477 thousand).

***Determination of deemed cost***

The deemed cost of property, plant and equipment of the Group has been determined as the fair value of the assets based on the independent appraisal. The fair value and estimated remaining useful life as at 1 January 2007 was determined by the independent appraiser, comprised of the consortium of "Deloitte and Touch", "The institute for Enterprise Issues" and "AKF "Top-Audit" LLC". The appraisal was performed in accordance with International Standards on Appraisal.

As a result of the appraisal, the fair value of property, plant and equipment was determined to be RUR 338,425,662 thousand as at 1 January 2007. The net book value of property, plant and equipment in the financial statements, prepared in accordance with the Russian Accounting Principals was RUR 369,863,979 thousand as at 1 January 2007.

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

Consequently the fair value of property, plant and equipment was primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

The depreciated replacement cost was estimated based on internal sources and analysis of the Russian and international markets for similar property, plant and equipment. Various market data were collected from published information, catalogues, statistical data etc, and industry experts and suppliers of property, plant and equipment were contacted.

In addition to the determination of the depreciated replacement cost, cash flow testing was conducted in order to assess the reasonableness of those values, which resulted in the depreciated replacement cost values being decreased by RUR 569,811,228 thousand in arriving at the above value.

The following key assumptions were used in performing the cash flow testing:

- Cash flows were projected based on actual operating results and the business plan for the period till the year 2016.
- Based on Government regulations, the electricity transmission industry was expected to switch to the Regulatory Asset Base (RAB) regulation of tariffs, which is aimed at ensuring the fair return on the invested capital. The shift to RAB regulation as at 1 January 2007 was expected to occur in 2012 with the transition period 2010-2012. The RUR rate of return on the invested capital as determined by Government regulations was expected to be in the range of 5.5% to 6.5%.
- A discount rate was estimated in the range of 10.5% to 12.7% and was applied in determining the recoverable amount of property, plant and equipment. The discount rate was estimated on

the basis of the weighted average cost of capital, which was based on the cost of own capital (from 11.6% to 13.9%) and after-tax cost of borrowings of 6.84%.

The values assigned to the key assumptions represent management's assessment of future trends in the business and are based on both external and internal sources.

### ***Impairment testing***

Given the current challenging market conditions, the management performed an impairment test in respect of property, plant and equipment as at 31 December 2008. The Group property, plant and equipment are tested for impairment separately for each cash-generating unit. The following key assumptions were used in determining the recoverable amounts of property, plant and equipment:

- In 2008 the Government approved the methodology of RAB regulation through the issuance of resolution 231-э dated 26 June 2008 and approved the transition of eight subsidiaries of the Group to RAB regulated tariffs. As at the impairment testing date Management and industry experts expect the shift to RAB regulation of the remaining Group's subsidiaries to occur not later than 1 January 2011.
- Cash flows were projected based on the projections incorporating the Group's best estimates of production volumes, operating expenses and tariffs anticipated under the revised RAB regime. The projection period was set till the year 2016.
- Based on Government regulations, the return on capital invested before RAB regulation introduction period will gradually increase over the transition period and is expected to be 12% after the introduction of RAB. The return on the capital invested after the RAB regulation is introduced is expected to be 12%.
- A discount rate of 15.71% was applied in determining the recoverable amount. The discount rate was estimated based on the weighted average cost of capital, which was based on the cost of own capital of 17.36% and the after-tax cost of borrowings of 14.10%.

As a result of the analysis, no impairment loss has been recognised for the year ended 31 December 2008.

### ***Leased equipment and transport***

The Group leases production equipment and transport under a number of financial lease agreements. At the end of each of the leases the Group has the option to purchase the equipment. As at 31 December 2008 the net book value of leased property, plant and equipment was RUR 28,635,808 thousand (2007: RUR 19,373,893 thousand). The leased equipment secures lease obligations.

## 13 Intangible assets

	<b>Goodwill</b>	<b>Software</b>	<b>Certificates and licences</b>	<b>Total</b>
<b><i>Cost</i></b>				
Balance at 1 January 2007	-	986,669	419,752	1,406,421
Additions	-	631,987	1,628,561	2,260,548
Balance at 31 December 2007	-	1,618,656	2,048,313	3,666,969
Balance at 1 January 2008	-	1,618,656	2,048,313	3,666,969
Additions	143,042	1,453,440	263,618	1,860,100
Disposals	-	(40,195)	(6,336)	(46,531)
Balance at 31 December 2008	143,042	3,031,901	2,305,595	5,480,538
<b><i>Amortisation</i></b>				
Balance at 1 January 2007	-	(70,330)	(11,663)	(81,993)
Amortisation charge	-	(172,684)	(291,077)	(463,761)
Balance at 31 December 2007	-	(243,014)	(302,740)	(545,754)
Balance at 1 January 2008	-	(243,014)	(302,740)	(545,754)
Amortisation charge	-	(307,200)	(791,344)	(1,098,544)
Disposals	-	40,195	6,336	46,531
Balance at 31 December 2008	-	(510,019)	(1,087,748)	(1,597,767)
<b><i>Net book value</i></b>				
At 1 January 2007	-	<b>916,339</b>	<b>408,089</b>	<b>1,324,428</b>
At 31 December 2007	-	<b>1,375,642</b>	<b>1,745,573</b>	<b>3,121,215</b>
At 31 December 2008	<b>143,042</b>	<b>2,521,882</b>	<b>1,217,847</b>	<b>3,882,771</b>

## 14 Equity accounted investees

The Group has the following investments in equity accounted investees:

	<u>Country</u>	<u>Ownership/Voting</u>
JSC “Nurenergo”	Russian Federation	23%
JSC “Tuylaenergokplekt”	Russian Federation	50%
JSC “Kurganenergo”	Russian Federation	49%
JSC “G. M. Krgigianovsky Power Engineering Institute”	Russian Federation	31%

The following is summarised financial information, in aggregate, in respect of equity accounted investees:

	<u>31 December 2008</u>	<u>31 December 2007</u>
Total assets	5,375,610	3,644,181
Total liabilities	(11,330,847)	(8,374,403)
Revenue	5,241,645	3,523,113
Loss for the year	(161,063)	(1,353,207)

	<u>As at 1 January 2007</u>	<u>Share of profit/ (loss) for the year</u>	<u>As at 31 December 2007</u>	<u>Share of profit/ (loss) for the year</u>	<u>As at 31 December 2008</u>
JSC “Kurganenergo”	538,110	2,469	540,579	23,493	564,072
JSC “Tuylaenergokplekt”	60,560	(12,648)	47,912	(5,644)	42,268
JSC “G. M. Krgigianovsky Power Engineering Institute”	22,325	-	22,325	2,670	24,995
JSC “Nurenergo”	-	-	-	-	-
	<u>620,995</u>	<u>(10,179)</u>	<u>610,816</u>	<u>20,519</u>	<u>631,335</u>

## 15 Other investments and financial assets

	<b>31 December 2008</b>	<b>31 December 2007</b>
<b><i>Non-current</i></b>		
Available-for-sale investments	848,086	10,256,008
Promissory notes	2,624,372	-
Bank deposits	-	300,000
Financial assets related to employee benefit fund	4,208,838	2,531,492
	<b>7,681,296</b>	<b>13,087,500</b>
<b><i>Current</i></b>		
Fair value of the derivative instrument - interest/currency swap	1,891,854	4,323
Promissory notes	931,891	2,162,314
Bank deposits	70,000	2,560,215
	<b>2,893,745</b>	<b>4,726,852</b>

Available-for-sale investments are mainly represented by marketable securities stated at fair value.

As at 31 December 2007 available-for-sale investments included the 28% interest in JSC "Moscow Heat Distribution Company" with the carrying amount of RUR 6,565,352 thousand, which was received in the course of the reorganisation of RAO UES. During the year ended 31 December 2008 these shares were sold for the consideration of RUR 7,750,047 thousand.

The fair value of the derivative instrument was calculated by discounting future cash flows determined by reference to the conditions and payments schedule of the swap agreement using forward rates of similar instruments as at 31 December 2008. A change in the fair value of the swap contract for the year ended 31 December 2008 in the amount of RUR 1,887,531 thousand is included in financial income.

Promissory notes are mainly represented by bank promissory notes:

	<b>Effective interest rate</b>	<b>Year of maturity</b>	<b>31 December 2008</b>	<b>31 December 2007</b>
<b><i>Long term promissory notes</i></b>				
Bank promissory notes	8,3 %	2010	2,624,372	-
<b><i>Short-term promissory notes</i></b>				
Bank promissory notes	0%	2008	-	1,483,056
Bank promissory notes	13%	2009	400,000	-
Bank promissory notes	0-10%	2008	-	195,700
Bank promissory notes	12.5-14.5%	2009	238,767	-
Other short-term promissory notes		2008-2009	293,124	483,558
			<b>3,556,263</b>	<b>2,162,314</b>

***Financial assets related to employee benefit fund***

Financial assets related to employee benefit fund relate to the Group contributions accumulated in solidary and employees' individual pension accounts with the Non-State Pension Fund of Electric Power Industry (employee benefit fund). Subject to certain restrictions contributions to the employee benefit fund can be withdrawn at the discretion of the Group.

The Group's exposure related to credit risks and impairment losses related to other investments and financial assets is disclosed in Note 26.

## 16 Deferred tax assets and liabilities

### (a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	31 December 2008	31 December 2007	31 December 2008	31 December 2007	31 December 2008	31 December 2007
Property, plant and equipment	2,607,205	2,710,862	(35,618,262)	(41,972,280)	(33,011,057)	(39,261,418)
Intangible assets	758	-	(30,516)	(30,994)	(29,758)	(30,994)
Investments	225,372	265,917	(793,101)	(463,718)	(567,729)	(197,801)
Inventories	487,114	461,501	-	-	487,114	461,501
Trade and other receivables and prepayments	3,922,600	4,190,405	(432,349)	(33,621)	3,490,251	4,156,784
Financial lease liability	3,855,957	3,337,834	(25,723)	(11,211)	3,830,234	3,326,623
Loans and borrowings	457,990	36,348	(152,673)	(41,716)	305,317	(5,368)
Provisions	158,611	116,974	(298,891)	(136,320)	(140,280)	(19,346)
Employee benefits	769,009	872,324	(317,640)	(216,401)	451,369	655,923
Trade and other payables	396,944	941,013	(140,867)	(462,338)	256,077	478,675
Tax loss carry-forwards	175,491	334,317	-	(3,411)	175,491	330,906
Other	568,813	459,534	(74,703)	(32,173)	494,110	427,361
Tax assets/(liabilities)	13,625,864	13,727,029	(37,884,725)	(43,404,183)	(24,258,861)	(29,677,154)
Set off of tax	(9,392,497)	(9,170,690)	9,392,497	9,170,690	-	-
Net tax assets/(liabilities)	<b>4,233,367</b>	<b>4,556,339</b>	<b>(28,492,228)</b>	<b>(34,233,493)</b>	<b>(24,258,861)</b>	<b>(29,677,154)</b>

**(b) Movement in temporary differences during the year**

	<b>Change in tax rate</b>						
	<b>1 January 2008</b>	<b>Recognised in income</b>	<b>Recognised in equity</b>	<b>Acquired/ disposed of</b>	<b>Recognised in income</b>	<b>Recognised in equity</b>	
Property, plant and equipment	(39,261,418)	60,337	-	(40,330)	6,230,354	-	(33,011,057)
Intangible assets	(30,994)	(4,715)	-	-	5,951	-	(29,758)
Investments	(197,801)	(730,665)	303,361	-	44,228	13,148	(567,729)
Inventories	461,501	188,333	-	(365)	(162,355)	-	487,114
Trade and other receivables and prepayments	4,156,784	(190,100)	-	(25)	(476,408)	-	3,490,251
Financial lease liability	3,326,623	1,272,935	-	-	(769,324)	-	3,830,234
Loans and borrowings	(5,368)	331,337	-	-	(20,652)	-	305,317
Provisions	(19,346)	(243,899)	-	-	122,965	-	(140,280)
Employee benefits	655,923	(128,087)	-	-	(76,467)	-	451,369
Trade and other payables	478,675	(175,129)	-	-	(47,469)	-	256,077
Other	427,361	162,609	-	11,673	(107,533)	-	494,110
Tax loss carry-forwards	330,906	(120,309)	-	(4)	(35,102)	-	175,491
	<b>(29,677,154)</b>	<b>422,647</b>	<b>303,361</b>	<b>(29,051)</b>	<b>4,708,188</b>	<b>13,148</b>	<b>(24,258,861)</b>

	<b>January 2007</b>	<b>Recognised in income</b>	<b>Recognised in equity</b>	<b>Acquired/ disposed of</b>	<b>31 December 2007</b>
Property, plant and equipment	(37,433,742)	(1,832,139)	4,463	-	(39,261,418)
Intangible assets	(13,966)	(17,028)	-	-	(30,994)
Investments	(113,824)	6,664	(90,641)	-	(197,801)
Inventories	329,648	131,853	-	-	461,501
Trade and other receivables and prepayments	2,585,422	1,571,362	-	-	4,156,784
Financial lease liability	576,610	2,750,013	-	-	3,326,623
Loans and borrowings	14,613	(19,981)	-	-	(5,368)
Provisions	266,965	(286,311)	-	-	(19,346)
Employee benefits	977,636	(321,713)	-	-	655,923
Trade and other payables	200,956	277,719	-	-	478,675
Other	546,915	(119,554)	-	-	427,361
Tax loss carry-forwards	425,859	(94,953)	-	-	330,906
	<b>(31,636,908)</b>	<b>2,045,932</b>	<b>(86,178)</b>	<b>-</b>	<b>(29,677,154)</b>

A temporary difference relating to investments in subsidiaries in the amount of RUR 45,529,055 thousand at 31 December 2008 (31 December 2007: RUR 30,391,685 thousand) has not been recognised as the Group is able to control the timing of reversal of the difference, and reversal is not expected in the foreseeable future.

## 17 Inventories

	<b>31 December 2008</b>	<b>31 December 2007</b>
Raw materials and consumables	11,174,820	9,644,091
Fuel	453,666	282,284
Finished goods and goods for resale	86,973	299,578
Other inventories	962,881	711,683
Provision for obsolescence of inventories	(737,181)	(591,568)
<b>Net book value</b>	<b>11,941,159</b>	<b>10,346,068</b>

At 31 December 2008 inventories with a carrying amount of RUR 821,314 thousand are pledged as collateral for bank loans (31 December 2007: RUR 332,135 thousand) (see Note 22).

## 18 Trade and other receivables

	<b>31 December 2008</b>	<b>31 December 2007</b>
<b>Non-current accounts receivable</b>		
Trade receivables	2,336,774	1,223,219
Trade receivables impairment allowance	(1,407,266)	(874,340)
Other receivables	905,601	1,894,958
Other receivables impairment allowance	(7,543)	(3,190)
Loans	91,497	120,163
<b>Total financial assets</b>	<b>1,919,063</b>	<b>2,360,810</b>
VAT recoverable	1,313,900	824,200
Advances given	1,049,241	323,920
	<b>4,282,204</b>	<b>3,508,930</b>
<b>Current accounts receivable</b>		
Trade receivables	39,103,589	25,410,462
Trade receivables impairment allowance	(9,859,631)	(9,176 516)
Other receivables	11,909,691	12,955,037
Other receivables impairment allowance	(2,602,032)	(2,491,361)
Receivables from equity accounted investees	1,824,679	1,824,602
Receivables from equity accounted investees impairment allowance	(332,447)	(71,160)
Loans	493,324	54,332
<b>Total financial assets</b>	<b>40,537,173</b>	<b>28,505,396</b>
Advances given	22,139,375	13,215,252
Advances given impairment allowance	(602,192)	(533,312)
VAT recoverable	3,139,131	4,244,376
VAT on advances from customers	8,348,292	4,597,858
Prepaid taxes, other than income tax	2,296,288	3,262,196
	<b>75,858,067</b>	<b>53,291,766</b>

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables (excluding advances for construction work in progress) are disclosed in Note 26.

## 19 Cash and cash equivalents

	<b>31 December 2008</b>	<b>31 December 2007</b>
Cash at bank and in hand	18,810,623	16,861,044
Cash equivalents	704,083	197,112
Cash and cash equivalents in the statement of cash flows and balance sheet	<u>19,514,706</u>	<u>17,058,156</u>

The Group's exposure to interest rate risk and sensitivity analysis for financial assets and liabilities are disclosed in Note 26.

## 20 Equity

### (a) Share capital

*Number of shares unless otherwise stated*

	<b>Ordinary shares</b>		<b>Preference shares</b>	
	<b>31 December 2008</b>	<b>31 December 2007</b>	<b>31 December 2008</b>	<b>31 December 2007</b>
Authorised shares	41,041,753,984	41,041,753,984	2,075,149,384	2,075,149,384
Par value	RUR 1	RUR 1	RUR 1	RUR 1
On issue at end of year, fully paid	<u>41,041,753,984</u>	<u>41,041,753,984</u>	<u>2,075,149,384</u>	<u>2,075,149,384</u>

### (b) Ordinary and preference shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at the Company shareholders' meetings

Holders of preference shares have no right of conversion or redemption, but are entitled to an annual dividend equal to 10% of net statutory profit divided by the number of preference shares. If the amount of dividends paid by the Company for each ordinary share in a given year exceeds the amount payable as a dividend on each preference share, dividend rate payable on the latter must be increased to the amount of dividends on ordinary shares.

If the dividend is not paid, preference shares carry the right to vote on all issues within the competence of general shareholders' meetings following the Annual Shareholders' Meeting at which a decision no to pay (or not to pay the full amount of) dividends on preference shares was taken. The right of preference shareholders to vote at general shareholders' meetings ceases from the date of the first full payment of dividends on such shares. However, the dividend is not cumulative. The preference shares also carry the right to vote in respect of issues that affect the interests of preference shareholders, including reorganisation and liquidation.

In the event of liquidation preference shareholders first receive any declared unpaid dividends and the par value of the preference shares. Thereafter all shareholders, ordinary and preference, participate equally in the distribution of the remaining assets.

**(c) Transactions with shareholders**

As part of the Group formation the former shareholder, RAO UES forgave the amount of RUR 1,871,206 thousand for the benefit of the Group which was recognised in the Statement of Changes in Equity.

**(d) Minority interest**

In 2008 JSC “Lenenergo”, the Group subsidiary, completed a closed placement of 234,167,535 ordinary shares announced in 2007. Total additional capital comprised RUR 5,782,733 thousand. Additional shares were subscribed to the City of St. Petersburg and some of the other existing minority shareholders that paid RUR 3,045,663 thousand in cash altogether. The remaining amount of RUR 2,737,070 thousand represented a fair value of fixed assets contributed by the city of St. Petersburg. The excess of the advance outstanding as at 31 December 2007 in the amount of 3,055,681 RUR thousand (Note 25) over cash contribution of RUR 3,045,663 thousand was repaid back to shareholders.

Total additional capital of RUR 5,782,733 thousand was recognized as minority interest in these consolidated financial statements. As a result of subscription of all additional shares to minority shareholders the Group’s ownership interest decreased from 59.34% to 45.71% and resulted in the change of minority interest of RUR 1,609,450 thousand as at 31 December 2008. For other changes in minority interest refer to Note 31.

In 2007 OJSC “Energocentr” issued 20 000 ordinary shares with par value of RUR 50,000 per share in amount of RUR 1,000,000 thousand. 50% of these shares were acquired by OJSC “MOESK”, the Group subsidiary, for RUR 500,000 thousand and the remaining 50% were acquired by minority shareholder - OJSC “Moskovskaya Oblastnaya Investicionnaya Trastovaya Kompaniya” for RUR 500,000 thousand.

**(e) Dividends**

In accordance with Russian legislation the Company’s distributable reserves are limited to the balance of retained earnings as recorded in the Company’s statutory financial statements prepared in accordance with Russian Accounting Principles. As at 31 December 2008 the Company had retained earnings, including the loss for the current year, of RUR 40,868,123 thousand. Net loss amounted to RUR 154,473,081 thousand.

The Company neither declared nor paid dividends for the year ended 31 December 2008.

## 21 Earnings per share

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Weighted average number of ordinary shares for the year ended 31 December (thousand of shares)	41,041,754	41,041,754
Weighted average number of preference shares for the year ended 31 December (thousand of shares)	2,075,149	2,075,149
<b>Total profit</b>	<b>11,040,869</b>	<b>7,591,657</b>
- attributable to holders of ordinary shares	10,509,490	7,226,282
- attributable to holders of preference shares	531,379	365,375
<b>Earnings per ordinary share (in RUR) – basic and diluted</b>	<b>0.26</b>	<b>0.18</b>
<b>Earnings per preference share (in RUR) – basic and diluted</b>	<b>0.26</b>	<b>0.18</b>

In accordance with the Group's accounting policy for business combinations under common control, weighted average number of shares used for the purpose of calculation of earnings per share has been determined as if the formation of the Group was completed at the beginning of the earliest period presented.

## 22 Non-current and current debt

This note provides information about the contractual terms of the Group's loans and borrowings and financial lease liabilities, which are measured at amortised cost.

	<b>31 December 2008</b>	<b>31 December 2007</b>
<b><i>Non-current liabilities</i></b>		
Secured bank loans	(1,538,329)	(781,252)
Unsecured bank loans	(55,882,816)	(15,875,653)
Unsecured bond issued	(11,075,584)	(20,641,413)
Promissory notes	(4,761,327)	(4,693,987)
Loans from equity accounted investees	(3,553)	(44,425)
Loans from other related parties	(710,310)	(693,631)
Financial lease liabilities	(13,083,784)	(10,163,265)
	<b>(87,055,703)</b>	<b>(52,893,626)</b>
<b><i>Current liabilities</i></b>		
Current portion of loans and bonds	(12,957,497)	(7,121,467)
Secured bank loans	(1,688,820)	(3,999,503)
Unsecured bank loans	(24,866,303)	(16,778,456)

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	<b>31 December 2008</b>	<b>31 December 2007</b>
Promissory notes	(10,255,147)	(3,045,164)
Loans from equity accounted investees	(186,572)	(712,929)
Loans from other related parties	(27,685)	(2,576)
Current portion of financial lease liabilities	(5,491,648)	(4,085,453)
	<b>(55,473,672)</b>	<b>(35,745,548)</b>

### Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

	Cur- rency	Effective Interest rate	Year of maturity	31 December 2008		31 December 2007	
				Face value	Carrying amount	Face value	Carrying amount
<b>Secured bank loan</b>							
Secured bank loans	RUR	8.5 -17%	2009-2010	1,071,829	1,071,829	435,000	435,000
Secured bank loans	RUR	8-9%	2008-2009	2,019,820	2,019,820	2,173,826	2,173,826
Secured bank loans	RUR	13.5-17%	2008	-	-	619,900	619,900
Secured bank loans	RUR	11.5%	2008	-	-	450,000	450,000
Secured bank loans	RUR	11%	2008	-	-	324,796	324,796
Secured bank loans	RUR	8-17%	2008-2010	135,500	135,500	780,707	780,707
				<b>3,227,149</b>	<b>3,227,149</b>	<b>4,784,229</b>	<b>4,784,229</b>
<b>Unsecured bank facility</b>							
Unsecured bank facility	RUR	8-15.13%	2008-2011	27,079,510	27,079,510	7,053,494	7,053,494
Unsecured bank facility	RUR	7.85-17%	2008-2011	3,880,000	3,880,000	1,537,000	1,537,000
Unsecured bank facility	RUR	7.3 – 17%	2008-2014	16,887,238	16,887,238	4,157,239	4,157,239
Unsecured bank facility	RUR	Mosibor + 3.6 -7.3%	2008-2011	1,000,000	1,000,000	850,000	850,000
Unsecured bank facility	RUR	7.8- 12.5%	2009-2011	4,453,164	4,453,164	1,103,164	1,103,164
Unsecured bank facility	RUR	Mosprime + 4 - 5.25%	2009-2011	1,000,000	1,000,000	-	-
Unsecured bank facility	RUR	8.45 -12.5%	2008-2012	5,914,431	5,914,431	2,835,165	2,835,165
Unsecured bank facility	RUR	8.5 -17%	2009-2012	5,925,407	5,925,407	5,724,948	5,724,948
Unsecured bank facility	RUR	4.9-23.83%	2009-2012	710,000	710,000	-	-
Unsecured bank facility	RUR	Mosprime + 3 - 4.9%	2009-2012	1,110,000	1,110,000	700,000	700,000
Unsecured bank facility	RUR	11-12%	2009	450,000	450,000	-	-
Unsecured bank facility	RUR	9.8-24.3%	2008-2009	500,000	500,000	380,197	380,197
Unsecured bank facility	RUR	10.5-12%	2008-2013	2,115,305	2,115,305	926,651	926,651
Unsecured bank facility	RUR	9.04-9.58%	2010	8,558,564	8,558,564	-	-
Unsecured bank facility	USD	7%	2008	-	-	3,500,000	3,500,000
Unsecured bank facility	USD	Libor+1.25%	2010	4,900,000	5,834,784	4,900,000	4,847,536
Unsecured bank facility	RUR	11-12.5%	2009-2011	552,772	552,772	397,643	397,643
Unsecured bank facility	RUR	Mosprime + 7.2%	2008	500,000	500,000	-	-
Unsecured bank facility	RUR	7.7-17%	2008-2013	2,136,589	2,136,589	2,941,479	2,941,479
				<b>87,672,980</b>	<b>88,607,764</b>	<b>37,006,980</b>	<b>36,954,516</b>

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	Cur- rency	Effective Interest rate	Year of maturity	31 December 2008		31 December 2007	
				Face value	Carrying amount	Face value	Carrying amount
<b>Promissory notes</b>							
Promissory notes	RUR	9%	2009-2012	9,628,176	9,163,865	5,464,164	5,000,000
Promissory notes	RUR	10%	2010-2013	1,901,323	1,772,051	-	-
Promissory notes	RUR	10%	2009	705,487	705,487	-	-
Promissory notes	RUR	17%	2009	2,999,998	2,999,901	-	-
Promissory notes	RUR	0%	2009	286,372	286,372	286,372	286,372
Promissory notes	RUR	0%	2008	-	-	2,130,947	2,130,947
Promissory notes	RUR	0%	2010	-	-	258,153	230,035
Promissory notes	RUR	0-9%	2009-2012	88,798	88,798	91,797	91,797
				<b>15,610,154</b>	<b>15,016,474</b>	<b>8,231,433</b>	<b>7,739,151</b>
<b>Bonds</b>							
Unsecured bonds	RUR	9.03%	2010	3,000,000	3,000,000	3,000,000	3,000,000
Unsecured bonds	RUR	7.85%	2009-2010	60,177	60,177	3,000,000	3,000,000
Unsecured bonds	RUR	8.05%	2011	2,356,507	2,356,507	6,000,000	6,000,000
Unsecured bonds	RUR	8.54%	2012	3,000,000	2,979,406	3,000,000	2,970,663
Unsecured bonds	RUR	8.02%	2012	3,000,000	2,979,493	3,000,000	2,970,750
Unsecured bonds	RUR	8.15%	2012	1,000,000	1,000,000	1,000,000	1,000,000
Unsecured bonds	RUR	8.15%	2012	1,000,000	1,000,000	1,000,000	1,000,000
Unsecured bonds	RUR	8.4%	2008	-	-	600,000	600,000
Unsecured bonds	RUR	7.70%	2012	2,700,000	2,700,000	2,700,000	2,700,000
				<b>16,116,684</b>	<b>16,075,583</b>	<b>23,300,000</b>	<b>23,241,413</b>
<b>Loans from other related parties</b>							
	RUR	0- 9%	2008-2012	889,387	821,848	872,288	785,847
<b>Other debt</b>							
	RUR	0-12%	2008-2010	205,125	205,125	885,300	885,300
<b>Long-term financial lease liabilities</b>							
	RUR	9%	2008-2014	26,955,676	18,575,432	21,143,327	14,248,718
<b>Total debt</b>				<b>150,677,155</b>	<b>142,529,375</b>	<b>96,223,557</b>	<b>88,639,174</b>

At 31 December 2008 the bank loans in the amount of RUR 757,264 thousand (31 December 2007: RUR 265,600 thousand) are secured over inventories in the amount of RUR 821,314 thousand (31 December 2007: RUR 332,135 thousand) (see Note 17).

At 31 December 2007 the bank loans in the amount of RUR 324,796 thousand are secured over fixed assets in the amount of RUR 967,555 thousand. At 31 December 2008 no bank loans are secured over fixed assets.

At 31 December 2008 the bank loans in the amount of RUR 71,500 thousand (31 December 2007: RUR 1,476,838 thousand) are secured over promissory notes in the amount of RUR 166,363 thousand (31 December 2007: RUR 2,907,096 thousand).

At 31 December 2008 the bank loans in the amount of RUR 2,398,385 thousand (31 December 2007: RUR 2,716,995 thousand) are secured by cash flows on certain electric transmission contracts.

The wide range of the interest rates stems from changes in market conditions caused by the global economic crisis. The sharp interest rate growth has been observed since August 2008.

The effective interest rate is the market interest rate applicable to the loans at the date of origination for fixed rate loans and the current market rate for floating rate loans. The Group has not entered into any hedging arrangements in respect of interest rate exposures.

In February 2007 JSC “Lenenergo” registered the 2<sup>nd</sup> issue of RUR 3,000,000 thousand certified coupon bonds with a par value of RUR 1,000 each carrying 10 interest bearing coupons. Payments under the first coupon were due on 181<sup>th</sup> day from the date of bond placement, and other coupon payments are payable every 184<sup>th</sup> day. The interest rate under coupons is set at 8.54% p.a.

In April 2007 OJSC “Lenenergo” registered the 3<sup>rd</sup> issue of 3,000,000 certified coupons with par value of RUR 1,000 each carrying 10 interest-bearing coupons. Payments under the first coupon are due on the 181<sup>st</sup> day from the date of bond placement, and other coupon payments are effected every 184 days. The interest rate under coupons is set at 8.02% p.a.

In February 2007 JSC “Tumenenergo”, a subsidiary of the Group, registered the 2<sup>nd</sup> issue of bonds. The interest rate under coupons is set at 7.7% p.a. The bonds mature in 2012, in 1820 days from the date of placement. As at 31 December 2008 the outstanding 2<sup>nd</sup> issue of the bonds of 2,700,000 were classified as long-term debt (as at 31 December 2007: 2,700,000).

In May 2007 JSC “MOESK”, a subsidiary of the Group, registered 1<sup>st</sup> issue of RUR 3,000,000 thousand interest non-convertible bonds with a par value of RUR 1,000 each. Payments under the first, second and third coupons were due in 2007, and fourth coupon payment was due in 2008, fifth and sixth coupons are due in 2010. The interest rate under first, second and third coupons are set at 9.3% p.a., the interest rate under fourth coupon is set at 22% p.a, the interest rate under fifth and sixth coupons are set at 25% p.a. The bonds were planned to be matured in 2010, but were classified as current portion of long-term debt due to the possibility of early redemption. (As at 31 December 2007 as long-term debt: 3,000,000).

In September 2006 JSC “MOESK” registered 1<sup>st</sup> issue of RUR 6,000,000 thousand interest non-convertible bonds with a par value RUR 1,000 each. Payments under the first coupon were due on 182 days from the date of bond placement, and other coupon payments are payable every 182 days. The interest rate under coupons is set at 8.05% p.a. The bonds mature in 2011, in 1820 days from the date of placement. In 2008 part of the issue in the amount of RUR 3,643,493 thousand was prematurely redeemed.

In July 2007 JSC “Kubanenergo”, a subsidiary of the Group, registered 1<sup>st</sup> issue of RUR 3,000,000 thousand interest non-convertible bonds with a par value RUR 1,000 each. The interest rate under coupons is set at 7.85% p.a. The half of the bonds issued was planned to mature in 2009, in 546

days from the date of placement and the other part - in 2010, in 1092 days from the date of placement. In 2008 the issue was partly redeemed.

For more information about the Group exposure to interest rate and foreign currency risk, see Note 26.

Financial lease liabilities are payable as follows:

	2008		2007		Present value of minimum lease payments	Present value of minimum lease payments
	Future minimum lease payments	Interest	Future minimum lease payments	Interest		
Less than one year	9,150,048	(3,658,400)	5,491,648	7,064,199	(2,978,746)	4,085,453
Between one and five years	17,078,441	(4,541,003)	12,537,438	13,636,986	(3,766,011)	9,870,975
More than five years	727,187	(180,841)	546,346	442,142	(149,852)	292,290
	<b>26,955,676</b>	<b>(8,380,244)</b>	<b>18,575,432</b>	<b>21,143,327</b>	<b>(6,894,609)</b>	<b>14,248,718</b>

The financial lease liabilities are secured by the leased assets (see Note 12).

## 23 Employee benefits

The Group has defined benefit pension and other long-term defined benefit plans that cover most full-time and retired employees. Defined post-employment benefits consist of several unfunded plans providing for lump-sum payments upon retirement, financial support for current pensioners, death benefits, jubilee benefits.

(a) Amounts recognised in the balance sheet are as follows:

	31 December 2008	31 December 2008	31 December 2007	31 December 2007
	Post employment benefits	Other long-term benefits	Post employment benefits	Other long-term benefits
Total present value of obligations	9,671,202	502,963	8,285,122	472,921
Unrecognised actuarial loss/(gain)	427,982	-	(742,042)	-
Unrecognised past service cost	(2,981,113)	-	(890,730)	-
<b>Recognised liability for defined benefit obligations</b>	<b>7,118,071</b>	<b>502,963</b>	<b>6,652,350</b>	<b>472,921</b>

**(b)** Movements in the present value of the defined benefit obligations

	<b>2008</b>	<b>2008</b>	<b>2007</b>	<b>2007</b>
	<b>Post employment benefits</b>	<b>Other long- term benefits</b>	<b>Post employment benefits</b>	<b>Other long- term benefits</b>
Defined benefit obligations at 1 January	8,285,122	472,921	7,093,090	410,575
Benefits paid by the plan	(945,869)	(73,445)	(742,788)	(90,150)
Current service costs and interests	1,096,793	56,769	977,435	51,883
Actuarial (gains)/losses	(1,247,256)	28,955	746,038	99,407
Past service costs	2,701,914	18,411	358,036	1,411
Curtailments and Settlements	(219,502)	(648)	(146,689)	(205)
<b>Defined benefit obligations at 31 December</b>	<b>9,671,202</b>	<b>502,963</b>	<b>8,285,122</b>	<b>472,921</b>

**(c)** Expense recognised in the income statement:

	<b>2008</b>	<b>2008</b>	<b>2007</b>	<b>2007</b>
	<b>Post employment benefits</b>	<b>Other long- term benefits</b>	<b>Post employment benefits</b>	<b>Other long- term benefits</b>
Current service costs	555,406	25,835	513,199	24,931
Interests on obligation	541,387	30,934	464,236	26,952
Recognised actuarial gains and losses	(77,232)	28,955	(9,273)	99,407
Recognised past service costs	611,531	18,411	219,036	1,411
Curtailments and Settlements	(219,502)	(648)	(146,689)	(205)
<b>Total periodical pension cost</b>	<b>1,411,590</b>	<b>103,487</b>	<b>1,040,509</b>	<b>152,496</b>

The expense is recognised in the line "Personnel Cost" as part of operating expenses.

Movements in the net liability in the balance sheet are as follows:

	<b>2008</b>	<b>2008</b>	<b>2007</b>	<b>2007</b>
	<b>Post employment benefits</b>	<b>Other long- term benefits</b>	<b>Post employment benefits</b>	<b>Other long- term benefits</b>
Recognised liability in balance sheet for defined benefit obligations as at 1 January	6,652,350	472,921	6,354,629	410,575
Total periodical pension cost	1,411,590	103,487	1,040,509	152,496
Benefits paid by the plan	(945,869)	(73,445)	(742,788)	(90,150)
Recognised liability in balance sheet for defined benefit obligations as at 31 December	<b>7,118,071</b>	<b>502,963</b>	<b>6,652,350</b>	<b>472,921</b>

**(d)** Actuarial assumptions

Principal actuarial assumptions at the balance sheet date (expressed as weighted averages):

	<b>2008</b>	<b>2007</b>
Discount rate at 31 December	9.00%	7.00%
Future salary increases	7.00%	7.00%
Inflation rate	6.00%	6.00%
Average future working life (yrs)	11	11
Mortality table	Russian 2002	Russian 2002

**24 Provisions**

	<b>2008</b>	<b>2007</b>
Balance at 1 January	732,397	400,287
Provisions raised during the year	758,174	471,748
Provisions used during the year	(408,630)	(139,638)
Balance at 31 December	<b>1,081,941</b>	<b>732,397</b>

Provisions relate to the legal proceedings and unsettled claims against the Group.

## 25 Trade and other payables

	<b>31 December 2008</b>	<b>31 December 2007</b>
<b>Non-current accounts payable</b>		
Trade payables	510,061	232,373
Other payables and accrued expenses	2,324,797	1,331,077
<b>Total financial liabilities</b>	<b>2,834,858</b>	<b>1,563,450</b>
Advances from customers	10,425,150	5,117,903
	<b>13,260,008</b>	<b>6,681,353</b>
<b>Current accounts payable</b>		
Trade payables	49,467,656	32,441,474
Interest accrued on loans and borrowings	1,509,084	680,634
Other payables and accrued expenses	3,195,495	5,986,384
Payables to employees	4,901,961	5,757,814
Dividends payable	177,190	338,654
<b>Total financial liabilities</b>	<b>59,251,386</b>	<b>45,204,960</b>
Advances from customers	76,466,484	41,845,115
Advance contributions for future share issue (Note 20)	-	3,055,681
	<b>135,717,870</b>	<b>90,105,756</b>
	<b>31 December 2008</b>	<b>31 December 2007</b>
<b>Taxes payable</b>		
Value added tax	780,844	964,028
Property tax	426,139	288,094
Unified social tax	664,836	769,628
Other taxes payable	1,232,122	2,369,808
	<b>3,103,941</b>	<b>4,391,558</b>
	<b>138,821,811</b>	<b>94,497,314</b>

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in Note 26.

## **26 Financial risk management**

### **(a) Overview**

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

- credit risk
- liquidity risk
- market risk.

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

The Group's principal objective when managing capital risk is to sustain its creditworthiness and a normal level of capital adequacy for doing business as a going concern, in order to ensure returns for shareholders and benefits to other stakeholders and to maintain an optimal capital structure to reduce the cost of borrowed capital.

The Group's risk management policies deal with identifying and analyzing the risks faced by the Group, setting appropriate risk limits and controls, and monitoring risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its internal policies, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders or issue new shares.

The Group's Audit Committee oversees how management monitors compliance with the Group's internal control procedures.

### **(b) Credit risk**

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

#### **(i) Trade and other receivables**

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. The demographics of the Group's customer base, including the default risk of the industry and country, in which customers operate, has less of an influence on credit risk.

To manage the credit risk, the Group attempts, to the extent possible, to demand prepayments from customers. As a rule, prepayment for connection services is stipulated by contract and depends on the amount of capacity to be connected.

The Group does not require collateral in respect of trade and other receivables.

The Group establishes an allowance for impairment that represents its estimate of anticipated losses in respect of trade and other receivables that relate to individually significant exposures.

### Exposure to credit risk

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

	<b>Carrying amount</b>	
	<b>31 December 2008</b>	<b>31 December 2007</b>
Available-for-sale financial assets	848,086	10,256,008
Promissory notes	3,556,263	2,162,314
Loans and receivables	42,456,236	30,866,206
Bank deposits, cash and cash equivalents	19,584,706	19,918,371
Derivative instrument - interest/currency swap	1,891,854	4,323
Financial assets related to employee benefit fund	4,208,838	2,531,492
	<b>72,545,983</b>	<b>65,738,714</b>

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	<b>Carrying amount</b>	
	<b>31 December 2008</b>	<b>31 December 2007</b>
North-West region	4,387,043	2,286,882
Central region	9,470,507	5,561,348
Ural and Volga region	5,422,803	3,531,629
South region	5,666,831	2,725,047
Siberian region	5,147,549	2,391,653
Other regions	78,733	86,266
	<b>30,173,466</b>	<b>16,582,825</b>

The Group's ten most significant customers accounts for RUR 8,614,815 thousand of the trade receivables carrying amount at 31 December 2008 (2007: RUR 3,333,401 thousand).

### Impairment losses

The aging of receivables at the reporting date was:

	<b>Gross</b>	<b>Impairment</b>	<b>Gross</b>	<b>Impairment</b>
	<b>31 December 2008</b>	<b>31 December 2008</b>	<b>31 December 2007</b>	<b>31 December 2007</b>
Not past due	34,914,311	(2,947,987)	25,466,917	(679,566)
Past due less than 3 months	2,881,615	(1,083,026)	921,787	(176,383)
Past due more than 3 months and less than 6 months	2,205,730	(530,634)	59,720	(19,206)
Past due more than 6 months and less than 1 year	5,466,751	(1,824,898)	2,158,766	(241,535)
Past due more than 1 year	10,611,927	(7,822,374)	14,701,088	(11,499,877)
	<b>56,080,334</b>	<b>(14,208,919)</b>	<b>43,308,278</b>	<b>(12,616,567)</b>

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

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Balance at 1 January	(12,616,567)	(11,263,514)
Increase during the period	(5,880,005)	(3,644,479)
Decrease due to recognised impairment loss	3,001,810	1,476,287
Decrease due to reversal	1,285,843	815,139
Balance at 31 December	<b>(14,208,919)</b>	<b>(12,616,567)</b>

The movement in the allowance for impairment in respect of available for sale investments during the year was as follows:

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Balance at 1 January	109,518	-
Increase during the period	1,046,609	109,518
Balance at 31 December	<b>1,156,127</b>	<b>109,518</b>

An impairment loss in respect of available for sale investments was recognised owing to significant decline in their fair value.

During the year the management accrued an allowance for impairment of bank deposits and cash equivalent in the amount of RUR 1,201,687 thousand in relation to the deposits held by JSC "MOESK", the Group subsidiary, in Moskovskiy Zalogoviy bank due to insolvency procedures initiated against the bank during the year.

The allowance accounts in respect of trade receivables, available for sale investments and bank deposits are used to record impairment losses, unless the Group is satisfied that no recovery of the amount owing is possible; at that point the amount considered irrecoverable and written off against the financial asset directly. At 31 December 2008 the Group does not have any collective impairment on its trade receivables, available for sale investments and bank deposits (2007: nil).

**(c) Liquidity risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due.

The Group monitors the risk of cash shortfalls by means of current liquidity planning. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. This approach is used to analyze payment dates associated with financial assets, and also to forecast cash flows from operating activities.

The contractual maturities of financial liabilities presented excluding estimated interest payments and the impact of netting agreements:

**31 December 2008**

	<b>Carrying amount</b>	<b>Contractual cash flows</b>	<b>0-1 years</b>	<b>1-2 years</b>	<b>2-3 years</b>	<b>3-4 years</b>	<b>4-5 years</b>	<b>Over 5 years</b>
<b>Non-derivative financial liabilities</b>								
Loans	92,861,885	91,994,642	34,445,791	32,545,619	18,069,647	2,236,703	696,882	4,000,000
Bond issued	16,075,584	16,116,685	3,000,000	60,178	5,056,507	8,000,000	-	-
Promissory notes	15,016,474	15,610,153	9,827,636	2,266,803	1,872,065	1,534,424	109,225	-
Financial Leasing	18,575,432	18,575,432	5,491,648	5,401,810	3,664,262	2,395,063	1,076,303	546,346
Trade and other payables	62,086,244	62,354,033	59,251,386	2,546,727	106,377	71,931	26,470	351,142
	<b>204,615,619</b>	<b>204,650,945</b>	<b>112,016,461</b>	<b>42,821,137</b>	<b>28,768,858</b>	<b>14,238,121</b>	<b>1,908,880</b>	<b>4,897,488</b>

**31 December 2007**

	<b>Carrying amount</b>	<b>Contractual cash flows</b>	<b>0-1 years</b>	<b>1-2 years</b>	<b>2-3 years</b>	<b>3-4 years</b>	<b>4-5 years</b>	<b>Over 5 years</b>
<b>Non-derivative financial liabilities</b>								
Loans	43,409,892	43,548,797	24,296,285	5,684,327	8,911,905	2,592,204	2,064,076	-
Bond issued	23,241,413	23,300,000	3,600,000	3,000,000	-	8,700,000	8,000,000	-
Promissory notes	7,739,151	8,231,433	3,038,408	1,905,396	1,350,769	1,048,580	888,280	-
Financial Leasing	14,248,718	14,248,718	4,085,453	3,882,286	3,328,580	1,912,523	747,586	292,290
Trade and other payables	46,768,410	46,860,304	45,204,960	1,113,188	133,608	30,967	22,367	355,214
	<b>135,407,584</b>	<b>136,189,252</b>	<b>80,225,106</b>	<b>15,585,197</b>	<b>13,724,862</b>	<b>14,284,274</b>	<b>11,722,309</b>	<b>647,504</b>

**(d) Market risk**

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

**(i) Currency risk**

Currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates.

The majority of the Group's revenues and expenditures are denominated in RUR, accordingly operating profits are insignificantly impacted by changes in exchange rates.

**Exposure to currency risk**

The Group's exposure to foreign currency risk was as follows based on notional amounts:

	<b>USD-denominated</b>	<b>USD-denominated</b>
	<b>31 December 2008</b>	<b>31 December 2007</b>
Bank loans	5,834,784	8,347,536
Derivative financial instruments - interest/currency swap	(1,891,854)	(4,323)
Net exposure	<b>3,942,930</b>	<b>8,343,213</b>

The following exchange rates applied during the year:

<b>RUR</b>	<b>Average rate</b>		<b>Reporting date spot rate</b>	
	<b>2008</b>	<b>2007</b>	<b>31 December 2008</b>	<b>31 December 2007</b>
USD 1	24.855	25.577	29.3804	24.5462

**Sensitivity analysis**

A 10% weakening of the RUR against the USD at 31 December would have decreased equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2007.

	<b>Equity</b>	<b>Profit or loss</b>
	<b>RUR</b>	<b>RUR</b>
<b>2008</b>		
USD	-	(299,663)
<b>2007</b>		
USD	-	(634,805)

A 10% strengthening of the RUR against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

**(ii) Interest rate risk**

The Group obtains borrowing both with fixed and with floating rate and is subject to the risk of interest rate changes.

Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

**Profile**

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	<b>Carrying amount</b>	
	<b>31 December 2008</b>	<b>31 December 2007</b>
<b>Fixed rate instruments</b>		
Financial assets	4,004,690	3,536,474
Financial liabilities	(132,608,092)	(79,042,593)
<b>Variable rate instruments</b>		
Financial assets	1,891,854	4,323
Financial liabilities	(9,444,784)	(6,397,536)

**Fair value sensitivity analysis for fixed rate instruments**

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss, and the Group does not designate interest/currency swaps as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

### Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the reporting date would have decreased equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates remain constant. The analysis is performed on the same basis for 2007.

	Profit or loss		Equity	
	100 bp increase	100 bp decrease	100 bp increase	100 bp decrease
<b>2008</b>				
Variable rate instruments	(71,780)	71,780	-	-
Interest/currency swap	14,738	(14,738)	-	-
Cash flow sensitivity (net)	<b>(57,042)</b>	<b>57,042</b>	-	-
<b>2007</b>				
Variable rate instruments	(48,621)	48,621	-	-
Interest/currency swap	33	(33)	-	-
Cash flow sensitivity (net)	<b>(48,588)</b>	<b>48,588</b>	-	-

### (e) Fair values versus carrying amounts

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

	Note	Carrying amount	Fair value	Carrying amount	Fair value
		31 December 2008	31 December 2008	31 December 2007	31 December 2007
Derivative instrument – interest/currency swap	15	1,891,854	1,891,854	4,323	4,323
Loans and receivables	18	42,456,236	41,979,862	30,866,206	30,529,742
Available-for-sale financial assets	15	848,086	848,086	10,256,008	10,256,008
Promissory notes	15	3,556,263	3,415,909	2,162,314	2,162,314
Bank deposits, cash and cash equivalents	15, 19	19,584,706	19,584,706	19,918,371	19,918,371
Financial assets related to employee benefit fund	15	4,208,838	4,208,838	2,531,492	2,531,492
Non-current and current debt	22	142,529,375	134,279,261	88,639,174	86,076,891
Trade and other payables	25	62,086,244	60,957,739	46,768,410	46,485,508
		<b>277,161,602</b>	<b>267,166,255</b>	<b>201,146,298</b>	<b>197,964,649</b>

The basis for determining fair values is disclosed in Note 4.

The interest rates used to discount estimated cash flows, where applicable, were as follows:

	<u>31 December 2008</u>	<u>31 December 2007</u>
Loans and receivables	15.7%	11.46%
Promissory notes	12%	-
Non-current and current debt	17.4%	11.5%
Trade and other payables	17.4%	11.5%

**(f) Capital management**

Management's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. Management monitors the return on capital, which the Group defines as net profit after tax divided by total shareholders' equity.

Management seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

There were no changes in the Group's approach to capital management during the year.

The Company and its subsidiaries are subject to external capital requirements that require that their net assets as determined in accordance with Russian Accounting Principles must exceed their charter capital at all times.

**27 Operating leases**

Non-cancellable operating lease rentals are payable as follows:

	<u>Year ended</u> <u>31 December 2008</u>	<u>Year ended</u> <u>31 December 2007</u>
Less than one year	3,048,791	1,471,605
Between one and five years	2,575,790	1,840,967
More than five years	13,844,140	9,274,752
	<u><b>19,468,721</b></u>	<u><b>12,587,324</b></u>

The land plots leased by the Group are the territories on which power lines, equipment for electricity transformation and other assets are located. Lease payments are reviewed regularly to reflect market rentals. Contracts for land lease are concluded for 49 years, other contracts are concluded for one year with prolongation.

During the year RUR 3,729,796 thousand was recognised in the income statement in respect of operating leases (in 2007: RUR 1,277,037 thousand).

## **28 Commitments**

As at 31 December 2008 the Group has outstanding commitments under the contracts for the purchase and construction of property, plant and equipment for RUR 118,509,441 thousand (as at 31 December 2007: RUR 64,878,030 thousand).

## **29 Contingencies**

### **(a) Insurance**

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

### **(b) Taxation contingencies**

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

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

In April 2008 the tax authorities performed a tax field audit of the Group covering the period from 1 January 2005 to 31 December 2006. As a result the tax authorities additionally accrued RUR 1,349,999 thousand of taxes, RUR 161,361 thousand of penalties and RUR 300,061 thousand of late payment interests. The Group did not agree with the decision and filed a complaint to the Arbitration court.

The Group has accrued RUR 1,236,989 thousand of the above-mentioned additional taxes in these financial statements. The Group believes that the tax authority had no legal grounds to charge RUR 113,010 thousand of additional taxes, RUR 161,361 thousand of penalties and RUR 300,061 thousand of late payment interests. Thus, as at 31 December 2008 and 2007 the Group did not accrue provision for contingent liability related to the income tax and other taxes of RUR 113,010 thousand, late payment interests of RUR 300,061 thousand and penalties of RUR 161,361 thousand.

**(c) Legal proceedings**

The Group is a 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, which, upon final disposition, will have a material adverse effect on the financial position of the Group.

One of the Group's customers is proceeding with litigation against the Group for breach of tariff policies in the period from May till December 2006 and is seeking the reimbursement of RUR 1,066,429 thousand. In the opinion of management, after taking appropriate legal advice, this case will be resolved in the Group's favour. As a result, no provision has been recognized in these consolidated financial statements.

**(d) Environmental matters**

The Group and its predecessors have operated in the electric transmission industry in the Russian Federation for many years. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement posture of Government authorities is continually being reconsidered. Company management periodically evaluates its 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. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

**(e) Guarantees**

The Group provided the following financial guarantees for loans granted by the following banks to the Group's lessors.

	<b>Amount on contract</b>	<b>Amount on contract</b>
	<b>31 December 2008</b>	<b>31 December 2007</b>
OJSC "Rosbank"	1,050,000	-
Belgorodskoe OSB №8582	767,127	652,755
OJSC VTB Severo-zapad	351,590	-
CJSC "Gazenergoprombank"	90,519	133,768
Voronezhskiy branch of OJSC "Alpha Bank"	68,840	87,223
	<b>2,328,076</b>	<b>873,746</b>

## 30 Related party transactions

### (a) Control relationships

The Russian Federation held the majority of the voting rights of RAO UES before 30 June 2008 and of the Company after 1 July 2008 (see Note 1(a)).

### (b) Transactions with RAO UES and its subsidiaries

During the year ended 31 December 2007 and for the first half of 2008 the Group had the following significant transactions with RAO UES and its subsidiaries:

#### *Revenue and expenses*

	Revenue		Expenses	
	Transaction value	Transaction value	Transaction value	Transaction value
	2008	2007	2008	2007
<b>RAO UES of Russia's subsidiaries:</b>				
Electricity transmission	67,014,126	168,673,220	30,519,103	68,016,470
Electricity (capacity) sales/purchase	232,855	412,614	12,040,474	30,014,651
Technological connection services	-	-	1,220,425	1,142,797
Other	1,003,606	12,540,260	6,418,032	6,652,756
	<b>68,250,587</b>	<b>181,626,094</b>	<b>50,198,034</b>	<b>105,826,674</b>

Balances with RAO UES and its subsidiaries were as follows:

	Outstanding balance	Outstanding balance
	31 December 2008	31 December 2007
Accounts receivable	-	12,989,766
Accounts payable	-	7,880,253
Advances received	-	165,720
Advances paid	-	2,208,696
Loans and borrowings	-	2,733,723
	-	<b>25,978,158</b>

**(c) Transactions with other state-controlled entities**

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

**Revenue and expenses**

	Revenue		Expenses	
	Transaction value	Transaction value	Transaction value	Transaction value
	2008	2007	2008	2007
<b>State-controlled entities:</b>				
Electricity transmission	53,419,572	18,950,516	49,394,340	8,854,541
Electricity (capacity) sales/purchase	7,375,949	6,404,702	12,131,238	1,651,170
Technological connection services	3,717,753	1,393,685	1,220,425	-
Other	5,662,295	1,528,346	10,201,178	5,369,682
	<b>70,175,569</b>	<b>28,277,249</b>	<b>72,947,181</b>	<b>15,875,393</b>

Balances with state-controlled entities were as follows:

	Outstanding balance	Outstanding balance
	31 December 2008	31 December 2007
Accounts receivable	14,220,435	7,669,460
Accounts payable	8,824,911	3,222,559
Advances received	13,916,139	9,061,506
Advances paid	7,987,649	4,035,131
Loans and borrowings	39,525,022	24,839,055
	<b>84,474,156</b>	<b>48,827,711</b>

**(d) Transactions with associates**

The Group had the following significant balances with associates:

	Outstanding balance	Outstanding balance
	31 December 2008	31 December 2007
Accounts receivable	1,492,232	1,753,442
	<b>1,492,232</b>	<b>1,753,442</b>

**(e) Management remuneration**

There are no transactions or balances with key management and close family members except their remuneration in the form of salary and bonuses.

Key management received the following remuneration during the year, which is included in personnel costs:

	<b>Year ended 31 December 2008</b>	<b>Year ended 31 December 2007</b>
Salaries and bonuses	1,570,504	1,919,826

**(f) Pricing policies**

Related party revenue for electricity transmission is based on the tariffs determined by the government. Other related party transactions are based on normal market prices.

In accordance with the Company Charter documents, the following transactions are subject to the approval of the Board of Directors, if the amount of the transaction is below 2% of the total assets of the Company as determined in accordance with RAP, and are subject to the approval at the Shareholders' meeting if the amount of the transaction exceeds 2% of the total assets of the Company as determined in accordance with RAP:

- Transactions involving the entities where the shareholders of the Company have ownership interest of 20% or more;
- Transactions involving the entities where the management of the Company also act in management capacity.

## 31 Significant subsidiaries

		<b>2008</b>	<b>2007</b>
	<b>Country of incorporation</b>	<b>Ownership/voting, %</b>	<b>Ownership/voting, %</b>
JSC "Tyumenenergo"	Russian Federation	100	100
JSC "IDGC of Volga"	Russian Federation	67.63	67.63
JSC "IDGC of North Caucasus"	Russian Federation	58.25	57.72
JSC "IDGC of North-West"	Russian Federation	55.38	55.38
JSC "IDGC of Siberia"	Russian Federation	52.88	52.88
JSC "IDGC of South"	Russian Federation	51.66	51.66
JSC "IDGC of Urals"	Russian Federation	51.52	51.52
JSC "MOESK"	Russian Federation	50.9	50.9
JSC "Lenenergo"	Russian Federation	45.71 / 50.31	59.34 / 67.34
JSC "IDGC of Center and Volga region"	Russian Federation	50.4	50.4
JSC "IDGC of Centre"	Russian Federation	50.23	50.23
JSC "Yantarenergo"	Russian Federation	100	100
JSC "Tomsk Distribution Company"	Russian Federation	52.03 / 59.88	52.03 / 59.88
JSC "Chechenenergo"	Russian Federation	51	51
JSC "Company of Energy and Electrification of Kuban"	Russian Federation	49*	49*
JSC "Karachaevo-Cherkesskenergo"	Russian Federation	100	100
JSC "Kalmenergosbyt"	Russian Federation	100	100
JSC "Tyvaenergosbyt"	Russian Federation	100	100
JSC "Kabbalkenergo"	Russian Federation	65.27 / 68.42	65.27 / 68.42
JSC "Dagestan Power Sales Company"	Russian Federation	51	51
JSC "Sevkavkazenergo"	Russian Federation	49*	49*
JSC "Ingushenergo"	Russian Federation	49*	49*
JSC "Reaserch Institute of Energy and Economics "	Russian Federation	100	100
VNIPI Energoprom	Russian Federation	100	100
JSC "SPECIAL DESIGN BUREAU heat and power equipment VTI"	Russian Federation	100	100
JSC "Aviaenergo"	Russian Federation	100	100
JSC "Center for the settlement of accounts receivable and payable Unified Energy Systems"	Russian Federation	100	100

		<b>2008</b>	<b>2007</b>
	<b>Country of incorporation</b>	<b>Ownership/voting, %</b>	<b>Ownership/voting, %</b>
Nedvizhimost VNIPIEnergoprom	Russian Federation	100	100
JSC "UES of NIC"	Russian Federation	100	100
JSC "NIC North - West"	Russian Federation	100	100
JSC "NIC Volga"	Russian Federation	100	100
JSC "NIC of the South"	Russian Federation	100	100
JSC "NIC Urals"	Russian Federation	100	100
JSC "NIC Siberia"	Russian Federation	100	100
"Grozenargo"	Russian Federation	49*	49*

\* The Group exercises control over these entities through stemming from majority representation on the Board of Directors.

## **32 Events subsequent to the balance sheet date**

On 25 May 2009 JSC "MOESK", the Group subsidiary, entered into a credit facility agreement with OJSC Alfa Bank. According to this agreement the Group received a loan in the amount of RUR 8.7 billion at the interest rate of 18.7%. The loan is to be repaid on 25 May 2011.