Open Joint Stock Company Magnitogorsk Iron & Steel Works and Subsidiaries

Independent Auditors' Report

Consolidated Financial Statements

As of December 31, 2006, 2005 and 2004
and for the years ended
December 31, 2006, 2005 and 2004

OPEN JOINT STOCK COMPANY
MAGNITOGORSK IRON & STEEL WORKS AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of OJSC "Magnitogorsk Iron & Steel Works":

We have audited the accompanying consolidated balance sheet of OJSC "Magnitogorsk Iron & Steel Works" and its subsidiaries (the "Group") as of December 31, 2006 and the related consolidated statements of operations and comprehensive income, cash flows and changes in shareholders' equity for the year then ended. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of the Group for the years ended December 31, 2005 and 2004 were audited by another auditor, whose report, dated March 17, 2006, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit, such financial statements present fairly, in all material respects, the consolidated financial position of the Group as of December 31, 2006 and the consolidated results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche

March 15, 2007

CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2006, 2005 AND 2004
(Amounts in millions of U.S. dollars, except share amounts)

	Note	December 31, 2006	2005	2004
ASSETS				
Current assets:				
Cash and cash equivalents	3	338	1,138	1,884
Short-term bank deposits	4	228	-	209
Short-term investments	5	325	13	53
Accounts receivable from third parties, less allowance for doubtful accounts of USD 12 as of December 31, 2006, USD 20 as of December 31, 2005 and USD 23 as of December 31, 2004	6	834	569	734
Accounts receivable from related parties	24	17	3	23
Prepaid expenses		14	12	15
Inventories	7	688	568	455
Current deferred income tax assets	21	36	26	24
Total current assets		**2,480**	**2,329**	**3,397**
Property, plant and equipment, net	8	2,764	2,288	1,883
Investments in affiliates	9	123	104	7
Long-term investments	5	146	1	1
Long-term bank deposits	4	109	99	103
Long-term deferred income tax assets	21	10	2	3
Goodwill		2	2	1
Other intangible assets, net	10	43	26	16
Other long-term assets	11	12	3	5
TOTAL ASSETS		**5,689**	**4,854**	**5,416**

See notes to the consolidated financial statements.

OPEN JOINT STOCK COMPANY
MAGNITOGORSK IRON & STEEL WORKS AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (CONTINUED)
AS OF DECEMBER 31, 2006, 2005 AND 2004
(Amounts in millions of U.S. dollars, except share amounts)

		December 31,		
	Note	**2006**	**2005**	**2004**
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities:				
Bank overdrafts		2	-	-
Short-term borrowings and current portion of long-term debt	12	373	151	827
Current portion of long-term capital lease obligations	14	25	20	20
Accounts payable and accrued liabilities	15	545	460	403
Accounts payable to related parties	24	8	9	1
Current deferred income tax liabilities	21	11	26	11
Total current liabilities		**964**	**666**	**1,262**
Long-term debt, net of current portion	13	577	448	362
Long-term capital lease obligations, net of current portion	14	29	20	26
Employee benefit obligations	16	30	26	23
Long-term deferred income tax liabilities	21	50	5	3
Other long-term liabilities		-	1	1
Total liabilities		**1,650**	**1,166**	**1,677**
Commitments and contingencies	25,26	-	-	-
Minority interest		**12**	**11**	**11**
Shareholders' equity:				
Common stock (10,630,222 thousand shares with a par value of 1 Russian Ruble each, authorized and issued as of December 31, 2006 and 2005, and 7,972,666 thousand shares with a par value of 1 Russian Ruble each, authorized and issued as of December 31, 2004)	17	363	363	272
Preferred stock (2,657,556 thousand shares with a par value of 1 Russian Ruble each, authorized and issued as of December 31, 2004)	17	-	-	91
Treasury stock, at cost (common shares totaling 485,062 thousand shares, 472,832 thousand shares and 335,171 thousand shares as of December 31, 2006, 2005 and 2004, respectively, and preferred shares totaling 66,174 thousand shares as of December 31, 2004)	17	(85)	(64)	(30)
Additional paid-in capital		254	247	247
Accumulated other comprehensive income	5	18	-	-
Retained earnings		3,477	3,131	3,148
Total shareholders' equity		**4,027**	**3,677**	**3,728**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**5,689**	**4,854**	**5,416**

See notes to the consolidated financial statements.

The consolidated financial statements were approved and signed on March 15, 2007, by:

V. I. Shmakov	**A. S. Batrutdinov**
Vice-President Finance	Deputy Chief Accountant

OPEN JOINT STOCK COMPANY
MAGNITOGORSK IRON & STEEL WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004
(Amounts in millions of U.S. dollars, except earnings per share amounts)

	Note	Years ended December 31, 2006	2005	2004
Net revenue	19	6,424	5,380	4,829
Cost of products sold (exclusive of depreciation and amortization shown separately below)		(3,619)	(3,274)	(2,712)
Depreciation and amortization		(188)	(173)	(169)
Selling and distribution expenses		(415)	(237)	(128)
Administrative and other expenses		(285)	(262)	(213)
Social expenses				
Social asset construction costs		(18)	-	(1)
Social and maintenance expenses		(58)	(56)	(33)
Taxes other than income tax		(63)	(59)	(48)
Loss on disposal of property, plant and equipment		(52)	(15)	(28)
Other operating income, net	20	39	19	41
Income from operating activities		**1,765**	**1,323**	**1,538**
Equity in net (losses)/gains of affiliates		(8)	-	1
Interest income		69	97	69
Interest expense		(63)	(64)	(65)
Net foreign exchange gain/(loss)		132	(39)	78
Income before income tax and minority interest		**1,895**	**1,317**	**1,621**
Income tax expense	21	(468)	(372)	(389)
Income before minority interest		**1,427**	**945**	**1,232**
Minority interest		(1)	2	-
Net income		**1,426**	**947**	**1,232**
Other comprehensive income:				
Unrealized gain on securities classified as available for sale, net of income tax effect of USD 5	5	18	-	-
Comprehensive income		**1,444**	**947**	**1,232**
Basic and diluted earnings per common share (USD)	18	**0.140**	**0.095**	**0.125**

See notes to the consolidated financial statements.

OPEN JOINT STOCK COMPANY
MAGNITOGORSK IRON & STEEL WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004
(Amounts in millions of U.S. dollars)

	Years ended December 31,		
	2006	**2005**	**2004**
Operating activities:			
Net income	1,426	947	1,232
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	188	173	169
Loss on disposal of property, plant and equipment	52	15	28
Change in allowance for doubtful accounts receivable	(8)	(3)	5
Net gain on trading securities	(2)	(8)	(8)
Deferred income taxes	7	13	4
Equity in net losses/(gains) of affiliates	8	-	(1)
Minority interest	1	(2)	-
Changes in operating assets and liabilities:			
Increase in inventories	(120)	(112)	(147)
(Increase)/decrease in trade and other receivables	(262)	181	(389)
Increase in investments classified as trading securities	(308)	-	-
Increase in trade accounts payable, accrued liabilities and other current liabilities	132	44	110
(Decrease)/increase in income tax payable, net of prepaid income tax	(37)	7	7
Net cash provided by operating activities	**1,077**	**1,255**	**1,010**
Investing activities:			
Proceeds from sales of property, plant and equipment	25	16	3
Proceeds from disposal of subsidiary	7	-	-
Purchases of investments in affiliates	(5)	(44)	-
Acquisition of subsidiaries and minority interest in subsidiaries, net of cash acquired	-	(52)	(3)
Purchases of property, plant and equipment	(697)	(562)	(395)
Purchases of intangible assets	(28)	(18)	(12)
Net change in bank deposits	(228)	200	(312)
Loans provided to affiliates	(21)	-	-
Purchases of investment securities classified as available for sale	(122)	-	-
Net cash of other investments	(11)	48	6
Net cash used in investing activities	**(1,080)**	**(412)**	**(713)**
Financing activities:			
Proceeds from loans	1,724	1,319	1,357
Loan principal paid	(1,387)	(1,900)	(740)
Net increase/(decrease) in bank overdrafts	2	-	(47)
Acquisition of treasury shares	(24)	(34)	(39)
Proceeds from re-issuance of treasury shares	10	-	236
Principal payments on capital lease obligations	(27)	(25)	(10)
Dividends paid	(1,077)	(947)	(14)
Net cash (used in)/provided by financing activities	**(779)**	**(1,587)**	**743**
Effect of exchange rate changes on cash and cash equivalents	(18)	(2)	20
Net (decrease)/increase in cash and cash equivalents	**(800)**	**(746)**	**1,060**
Cash and cash equivalents at beginning of the year	**1,138**	**1,884**	**824**
Cash and cash equivalents at end of the year	**338**	**1,138**	**1,884**
Supplementary information:			
Interest paid	30	61	45
Income tax paid	498	352	448
Non-cash investing and financing activities:			
Machinery and equipment acquired under capital leases	33	24	37

See notes to the consolidated financial statements.

OPEN JOINT STOCK COMPANY
MAGNITOGORSK IRON & STEEL WORKS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004
(Amounts in millions of U.S. dollars)

	Note	Common stock	Preferred stock	Common treasury stock	Preferred treasury stock	Additional paid-in capital	Accumulated other comprehensive income	Retained earnings	Total
Balance as of January 1, 2004		**272**	**91**	**(19)**	**-**	**39**	**-**	**1,930**	**2,313**
Acquisition of treasury shares		-	-	(12)	(27)	-	-	-	**(39)**
Re-issuance of treasury shares, net of income tax effect of USD 70		-	-	20	8	208	-	-	**236**
Dividends	17	-	-	-	-	-	-	(14)	**(14)**
Net income		-	-	-	-	-	-	1,232	**1,232**
Balance as of December 31, 2004		**272**	**91**	**(11)**	**(19)**	**247**	**-**	**3,148**	**3,728**
Acquisition of treasury shares		-	-	(13)	(21)	-	-	-	**(34)**
Share conversion	17	91	(91)	(40)	40	-	-	-	**-**
Dividends	17	-	-	-	-	-	-	(964)	**(964)**
Net income		-	-	-	-	-	-	947	**947**
Balance as of December 31, 2005		**363**	**-**	**(64)**	**-**	**247**	**-**	**3,131**	**3,677**
Acquisition of treasury shares		-	-	(24)	-	-	-	-	**(24)**
Re-issuance of treasury shares, net of income tax effect of USD 2		-	-	3	-	7	-	-	**10**
Revaluation of securities classified as available for sale, net of income tax effect of USD 5	5	-	-	-	-	-	18	-	**18**
Dividends	17	-	-	-	-	-	-	(1,080)	**(1,080)**
Net income		-	-	-	-	-	-	1,426	**1,426**
Balance as of December 31, 2006		**363**	**-**	**(85)**	**-**	**254**	**18**	**3,477**	**4,027**

See notes to the consolidated financial statements.

1. DESCRIPTION OF BUSINESS

The consolidated financial statements of Open Joint Stock Company Magnitogorsk Iron & Steel Works and its subsidiaries ("the Group") comprise the parent company Open Joint Stock Company Magnitogorsk Iron & Steel Works ("the Parent Company") and its 57 subsidiaries. The Parent Company is an open joint stock company as defined in the Civil Code of the Russian Federation. The head office of the Group is located at:

Ulitsa Kirova 93,
455002, Magnitogorsk,
The Russian Federation.

The Parent Company was established as a state owned enterprise in 1932. It was incorporated as an open joint stock company on October 17, 1992 as part of the Russian Federation privatization program. The principal activity of the Group is the production of ferrous metal products at the Parent Company's plant located in the city of Magnitogorsk in the Chelyabinsk region of the Russian Federation. The Group's products are sold in the Russian Federation and abroad. The Group's subsidiaries are mainly involved in the various sub-processes within the production cycle of ferrous metal products or in the distribution of those products.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND NEW ACCOUNTING PRONOUNCEMENTS

Basis of presentation

The accompanying consolidated financial statements have been prepared in conformity with the accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Group's Russian entities maintain their accounting records in Russian Rubles ("RUR") in accordance with the requirements of the Russian accounting and tax legislation.

The accompanying consolidated financial statements differ from financial statements prepared for statutory purposes in the Russian Federation in that they reflect certain adjustments, appropriate to present the consolidated financial position, results of operations and cash flows in accordance with U.S. GAAP.

Principles of consolidation

The consolidated financial statements include the financial statements of the Parent Company as well as entities where the Parent Company has operating and financial control through direct or indirect ownership of a majority voting interest. The consolidated financial statements also include accounts of variable interest entities where the Group is a primary beneficiary. All significant intercompany transactions, balances and unrealized gains/(losses) on transactions have been eliminated.

Entities acquired or disposed of during the year are included in the consolidated financial statements from the date of acquisition or to the date of disposal.

The effective ownerships indicated in the table below are also the nominal holdings, except for CJSC Ogneupor, a 100% subsidiary of OJSC MTSOZ.

Set forth below is a summary of the Group's primary subsidiaries:

Group entity	Registered in	Core business	Effective ownership, % As of December 31, 2006	2005	2004
OJSC Metizno-Kalibrovochniy Zavod "MMK-Metiz"	Russia	Production of hardware products	85.85[1]	88.16	88.16
OJSC Magnitogorskiy Kalibrovochniy Zavod	Russia	Production of hardware products	-[1]	79.72[2]	82.95
LLC IK RFC	Russia	Investing activities	100.00	100.00	100.00
CJSC Stroitelny Fond	Russia	Renting services	100.00	100.00	100.00
CJSC A-Kapital	Russia	Investing activities	100.00	100.00	100.00
CJSC Stroitelniy Komplex	Russia	Construction	100.00	100.00	100.00
CJSC Ogneupor	Russia	Production of refractory materials	98.89	98.89[3]	95.12
CJSC Mekhanoremontny Komplex	Russia	Maintenance of metallurgical equipment	100.00	100.00	100.00
CJSC Mechanoremont	Russia	Renting services	98.93	98.93	98.93
OJSC MTSOZ	Russia	Production of cement and refractory materials	98.89	98.89[4]	95.12
MMK Steel Trade AG	Switzerland	Trading activities	100.00	100.00	100.00
MMK Trading AG	Switzerland	Trading activities	99.60	99.60	99.60
MMK Finance S.A.	Luxemburg	Financing activities	96.77	96.77	96.77

[1] In May 2006, OJSC Metizno-Kalibrovochniy Zavod "MMK-Metiz" was merged with OJSC Magnitogorskiy Kalibrovochniy Zavod. As a result, the Group's effective ownership in OJSC Metizno-Kalibrovochniy Zavod "MMK-Metiz" decreased to 85.85%.
[2] In 2005, OJSC Magnitogorskiy Kalibrovochniy Zavod issued additional shares to its shareholders, under which the Group did not purchase its full entitlement. As a result, the Group's total effective ownership in this entity decreased to 79.72% and its minority interest increased by USD 2 million.
[3] CJSC Ogneupor is a 100% subsidiary of OJSC MTSOZ. Effective ownership changed due to the additional acquisition of OJSC MTSOZ shares in 2005 (refer to Note 22).
[4] Additional acquisition of shares in 2005 (refer to Note 22).

Consolidation of variable interest entities

In December 2003, the Financial Accounting Standards Board ("FASB") issued a revision to Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51", ("FIN 46R"). FIN 46R clarifies the application of Accounting Research Bulletin ("ARB") No. 51, "Consolidated Financial Statements", to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. FIN 46R requires the consolidation of these entities, known as variable interest entities ("VIEs"), by the primary beneficiary of the entity. The primary beneficiary is the entity, if any, that will absorb a majority of the VIE's expected losses, receive a majority of the VIE's expected residual returns, or both. Among other changes, the revisions of FIN 46R (a) clarified some requirements of the original FIN 46, which had been issued in January 2003, (b) eased some implementation problems, and (c) added new scope exceptions.

Following adoption of FIN 46R the Group re-evaluated its relationship with LLC MetAl, a related party of the Group, and determined that that entity was a VIE and that it was its primary beneficiary. Accordingly, the Group has consolidated LLC MetAl effective January 1, 2004. All intercompany balances have been eliminated in the consolidation and the results of that VIE have been included in the Group's consolidated financial statements.

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management of the Group to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period.

Examples of significant estimates include the allowance for doubtful accounts, the recoverability of intangible assets and other long-lived assets and valuation allowances on deferred tax assets. Actual results could differ from those estimates.

Concentration of business risk

The Group's principal business activities are within the Russian Federation. Laws and regulations affecting businesses operating in the Russian Federation are subject to rapid changes, which could impact the Group's assets and operations.

Reporting and functional currencies

The Group follows a translation policy in accordance with Statement on Financial Accounting Standards ("FAS") No. 52, "Foreign Currency Translation", ("FAS No. 52").

The national currency of the Russian Federation is the RUR, the local currency of the Group's primary operating subsidiaries. The Group has determined the functional currency of the Parent Company and each of its subsidiaries to be the U.S. dollar ("USD"). Management believes that USD is the appropriate functional currency for other subsidiaries of the Group.

Monetary assets and liabilities have been remeasured into USD at the rate prevailing at each balance sheet date. Non-monetary assets and liabilities have been remeasured into USD at historical rates. Revenues, expenses and cash flows have been remeasured into USD at rates which approximate actual rates at the date of the transaction. Remeasurement differences resulting from the use of these rates are included in the consolidated statement of operations and comprehensive income.

As of December 31, 2006, 2005 and 2004, exchange rates of 26.33, 28.78 and 27.75 RUR to USD, respectively, have been used for remeasurement purposes. The weighted average exchange rates for the years ended December 31, 2006, 2005 and 2004 were 27.32, 28.26 and 28.83 RUR to USD, respectively.

The RUR is not a readily convertible currency outside the territory of the Russian Federation. Accordingly, remeasurement of amounts recorded in RUR into USD should not be construed as a representation that the RUR amounts have been, could be, or will in the future be converted into USD at the exchange rate shown or at any other exchange rate.

Comprehensive income

FAS No. 130, "Reporting Comprehensive Income", requires the reporting of comprehensive income in addition to net income. Accumulated other comprehensive income includes foreign currency translation adjustments, unrealized holding gains and losses on available-for-sale securities and on derivative financial instruments, as well as additional pension liabilities not yet recognized as net periodic pension cost.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances, call deposits and liquid promissory notes with original maturities of ninety days or less at the date of purchase.

Restricted cash

Restricted cash represents legally restricted collateral deposited with various banks as margin for irrevocable letters of credit.

Financial instruments

The Group's financial instruments include cash and cash equivalents, short-term and long-term investments, receivables, payables and debt. Except as described in Note 23, the estimated fair value of such financial instruments as of December 31, 2006, 2005 and 2004 approximates their carrying value as reflected in the consolidated balance sheet.

Investment securities

The Group's investment securities include debt and equity securities.

The Group classifies its debt securities in one of three categories: trading, available-for-sale or held-to-maturity; its equity securities as trading or available-for-sale. Trading securities are bought and held principally for the purpose of selling them in the short term. Held-to-maturity debt securities are those securities, for which the Group has the ability and intent to hold it until maturity. All securities not included in trading or held-to-maturity are classified as available-for-sale.

Trading and available-for-sale securities are recorded at fair value. Unrealized holding gains and losses on trading securities are included in earnings. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are reported as a separate component of other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. Held-to-maturity securities are recorded at amortized cost using the effective interest method, adjusted for the amortization or accretion of premiums or discounts.

A decline in the market value of any available-for-sale or held-to-maturity security below cost, that is deemed to be other than temporary, results in a reduction of the carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether impairment is other than temporary, the Group considers whether it has the ability and intent to hold the investment until the market price recovers and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, changes in value subsequent to year end and forecasted performance of the investee.

Investments in affiliates and joint ventures

Investments in majority owned affiliates and joint ventures, where control does not exist, and 20% to 50% owned affiliates in which the Group has the ability to exercise significant influence are accounted for under the equity method of accounting whereby the investment is carried at cost of acquisition, plus the Group's equity in net earnings or losses since acquisition, less dividends received.

Investments in affiliates and joint ventures, over which the Group does not have the ability to exercise significant influence and which have readily determinable fair value, are accounted for at fair value. To the extent that these investments do not have a readily determinable fair value, they are accounted for under the cost method.

The Group periodically reviews all of its investments in affiliates and joint ventures for which fair value is less than cost to determine if the decline in value is other than temporary. If the decline in value is judged to be other than temporary, the cost basis of the investment is written down to fair value. The amount of any write-down is included in the consolidated statement of operations and comprehensive income.

Trade and other receivables

Accounts receivable are stated at their net realizable value after deducting an allowance for doubtful accounts. The allowance for doubtful accounts is the Group's best estimate of the amount of probable credit losses in the Group's existing accounts receivable balances. The Group reviews its allowance for doubtful accounts monthly. Account balances are written off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

Value-added taxes

Value-added taxes ("VAT") related to sales are payable to the tax authorities upon issuance of invoices to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that are not reclaimable as of the balance sheet dates is recorded as VAT receivable in the consolidated financial statements.

Inventories

Inventories are stated at the lower of acquisition/manufacturing cost or market value. The cost of inventories is determined on the weighted average basis and includes all costs in bringing the inventory to its present location and condition.

The elements of costs include direct material, labour and allocable material and manufacturing overheads. Costs of production in process and finished goods include the purchase costs of raw materials and conversion costs such as direct labour and an allocation of fixed and variable production overheads. Raw materials are valued at purchase cost inclusive of freight and other shipping costs.

Market value is the estimated price at which inventories can be sold in the normal course of business after allowing for cost of completion and sale.

Property, plant and equipment

Owned assets

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses. Capitalized production costs for internally developed assets include materials, direct labor costs and allocable material and manufacturing overhead costs. When construction activities are performed over an extended period, interest costs incurred during construction are capitalized. Construction-in-progress and equipment held for installation are not depreciated until the constructed or installed asset is substantially ready for its intended use.

The costs of planned major maintenance activities are recorded as costs as incurred. Costs for activities that lead to the prolongation of useful life or to expanded future use capabilities of an asset are capitalized. Maintenance and repair costs are expensed as incurred.

Leased assets

Capital leases are recorded at the lower of the fair market value of the asset or the present value of future minimum lease payments, less accumulated depreciation and impairment losses. The discount rate used in determining present value of the minimum lease payments is the Group's incremental borrowing rate, unless (1) it is practicable to learn the implicit rate computed by the lessor and (2) the implicit rate is less than the Group's incremental borrowing rate. If both of those conditions are met, the interest rate implicit in the lease is used. Amounts due within one year are classified as short-term lease liabilities and the remaining balance as long-term lease liabilities.

Mineral licenses

Mineral licenses to develop mineral reserves and resources are stated at historical cost less accumulated amortization. Mineral licenses are presented as a separate component of property, plant and equipment in the consolidated balance sheet in accordance with Emerging Issues Task Force ("EITF") Issue No. 04-2, "Whether Mineral Rights are Tangible or Intangible Assets".

Depreciation

Depreciation is charged to the consolidated statement of operations and comprehensive income on a straight line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and substantially ready for use. Land is not depreciated.

The following useful lives are used as a basis for calculating depreciation:

Buildings	33-44 years
Machinery and equipment	17-32 years
Transportation equipment	8-22 years
Fixtures and fittings	8-14 years

Mineral rights are amortized using the straight-line basis over the license term assuming constant production during the period of license.

Goodwill and other intangible assets

Goodwill represents excess of the cost of business acquired over the fair value of identifiable net assets at the date of acquisition.

Goodwill and intangible assets acquired in business combinations that have an indefinite useful life are not amortized. Goodwill is reviewed annually for impairment or whenever it is determined that impairment indicators exist. The Group determines whether an impairment has occurred by assigning goodwill to the reporting unit identified in accordance with FAS No. 142, "Goodwill and Other Intangible Assets", and comparing the carrying amount of the reporting unit to the fair value of the reporting unit. If goodwill impairment has occurred, the Group recognizes a loss for the difference between the carrying amount and the implied fair value of goodwill.

Intangible assets, that primarily represent production licenses and various purchased software costs, with finite useful lives are amortized over their respective estimated useful lives to their estimated residual values and are reviewed periodically for impairment.

No impairment of goodwill and other intangible assets was recognized in the years ended December 31, 2006, 2005 and 2004.

Debt issuance costs

Debt issuance costs are amortized using the effective interest method over the terms of the related loans.

Impairment of long-lived assets

The Group periodically evaluates the recoverability of the carrying amount of its long-lived assets in accordance with FAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, the Group compares undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, the Group records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets. Management is not aware of any indicators of impairment occurred relating to the Group's investments in long-lived assets during the years ended December 31, 2006, 2005 and 2004.

Accrued and contingent liabilities

Liabilities for loss contingencies, arising from claims, assessments, litigation, fines, penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment can be reasonably estimated.

Borrowing costs

Borrowing costs are recognized as an expense in the period in which they are incurred. Borrowing costs for assets that require a period of time to get them ready for their intended use are capitalized and amortized over the related assets' estimated useful lives.

Employee benefits

Defined contribution plans

The Group's Russian subsidiaries are legally obliged to make defined contributions to the Russian Federation State Pension Fund (a defined contribution plan financed on a pay-as-you-go basis). The Group's contributions to the Russian Federation State Pension Fund relating to defined contribution plans are charged to income in the period to which they relate.

In the Russian Federation all state social contributions, including contributions to the Russian Federation State Pension Fund, are collected through a unified social tax ("UST") calculated by the application of a regressive rate from 26% to 2% of the annual gross remuneration of each employee (2004 – 35.6% to 2%). UST is allocated to three state social funds, including the Russian Federation State Pension Fund, where the rate of contributions to that fund vary from 20% to 2% (2004 – 28% to 2%), depending on the annual gross remuneration of each employee.

The Group's obligations for contributions to other defined contribution plans are recognized as expense as incurred.

Defined benefit plans

The Group accounts for the cost of defined benefit plans using the projected unit credit method. Under this method, the cost of providing pensions is charged to the consolidated statement of operations and comprehensive income, so as to attribute the total pension cost over the service lives of employees in accordance with the benefit formula of the plan. The Group's obligation in respect of defined retirement benefit plans is calculated separately for each defined benefit plan by discounting the amounts of future benefits that employees have already earned through their service in the current and prior periods. The discount rate applied represents the yield on government bonds that have maturity dates approximating the terms of the Group's obligations.

Revenue recognition

Revenue is recognized on an accrual basis when earned and realizable, which generally occurs when products are shipped and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, pervasive evidence of an arrangement exists and the sales price is fixed or determinable.

Revenue is recognized net of applicable provisions for discounts, allowances, associated value-added taxes and export duties.

Income tax

Deferred income tax is accounted for under the liability method and reflects the tax effect of all significant temporary differences between the tax bases of assets and liabilities and their reported amounts in the consolidated financial statements. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in earnings in the period that includes the enactment date. Deferred income tax assets and liabilities arising in different tax jurisdictions are not offset.

In accordance with FAS No. 52 and FAS No. 109, "Accounting for Income Taxes", ("FAS No. 109"), deferred tax assets and liabilities are not recognized for temporary differences arising from the remeasurement of the local currency into the functional currency using historical exchange rates. Also in accordance with FAS No. 109, no deferred tax assets or liabilities are recognized for the effects of tax indexation of property, plant and equipment.

A valuation allowance is provided for deferred tax assets if it is more likely than not that the deferred tax assets will not be realized. In making this assessment, the Group's management considers all available evidence, including the scheduled reversal of deferred income tax liabilities, projected future taxable income and tax planning strategies.

Derivative financial instruments and hedging activities

Derivative instruments, consisting primarily of foreign currency forward and option contracts, are utilized by the Group to manage its exposure to fluctuations in foreign exchange rates. The Group does not enter into foreign currency hedging contracts related to its investment in affiliated companies.

The Group accounts for its derivative financial instruments following the provisions of FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended. All derivatives are recorded as either assets or liabilities in the consolidated balance sheets and measured at their respective fair values.

The accounting for changes in the fair value of derivative financial instruments depends on whether it has been designated and qualifies as an accounting hedge and further, on the type of hedging relationship. If a derivative is designated as a fair value hedge, the changes in the fair value of the derivative and the hedged item are recognized in earnings. If a derivative is designated as a cash flow hedge, changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the statement of operations and comprehensive income when the hedged item affects earnings. For a derivative not designated as a hedging instrument, the gain or loss is recognized in earnings in the period of change.

For the year ended December 31, 2006, no derivatives were designated as hedges and a net loss of USD 0.4 million relating to a change in the fair value of derivative instruments was included in net foreign exchange loss in the consolidated statement of operations and comprehensive income. For the years ended December 31, 2005 and 2004, the Group did not have any derivative financial instruments.

Distributions to shareholders

Distributable retained earnings of the Group are based on amounts recorded in the statutory accounts of individual entities and may significantly differ from amounts calculated on the basis of financial statements, prepared in accordance with U.S. GAAP.

Guarantees

A liability is recorded for the fair value of a guarantee issued by the Group when it represents a non-contingent obligation of the Group to stand ready to perform. Subsequent to initial measurement, the fair value assigned to the guarantee would be reduced and recognized in the consolidated statement of operations and comprehensive income as the Group is released from risk under the guarantee, as appropriate. All other guarantees are disclosed as a contingency in the consolidated financial statements.

Segment information

According to FAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", segment reporting follows the internal organizational and reporting structure of the Group. The Group operates in a single business segment, which is composed of the manufacturing of semi-finished and finished steel products. The revenues from the sale of these products constitute more than 95 percent of total revenues. All significant assets, production and management and administrative facilities are located in the city of Magnitogorsk, the Russian Federation.

New and recently adopted accounting pronouncements

In July 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes", ("FIN 48"), to clarify the accounting for uncertain tax positions stated in FAS No. 109. FIN 48 applies to all tax positions that are within the scope of FAS No. 109 and requires the two-step approach for recognizing and measuring tax benefits. FIN 48 establishes a "more-likely-than-not" recognition threshold that must be met before a tax benefit can be recognized in the financial statements. To meet this threshold, the enterprise must determine that upon examination by the taxing authority, the tax position is more likely to be sustained than not, based on the technical merits of the position. Once the recognition threshold has been met, enterprises are required to recognize the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with the taxing authority. In both steps, enterprises must presume that the taxing authority has full knowledge of all relevant information. FIN 48 also requires enterprises to make explicit disclosures at the end of each reporting period about uncertainties in their income tax positions, including a detailed rollforward of tax benefits taken that do not qualify for financial statement recognition. FIN 48 is effective for fiscal years beginning after December 15, 2006, and should be applied to all tax positions upon initial adoption. The cumulative effect of applying the provisions of FIN 48 should be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Group is currently assessing the impact of the adoption of FIN 48.

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements", ("FAS No. 157"). FAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. FAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, FAS No. 157 does not require any new fair value measurements. FAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. FAS No. 157 is required to be adopted by the Group on July 1, 2008. The Group is currently assessing the impact of the adoption of FAS No. 157.

In September 2006, the FASB issued FAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" – an amendment of FASB Statements No. 87, 88, 106, and 132(R)", ("FAS No. 158"). FAS No. 158 requires companies with publicly traded equity securities that sponsor a postretirement benefit plan to fully recognize, as an asset or liability, the overfunded or underfunded status of their benefit plan(s). The funded status is measured as the difference between the fair value of the plan's assets and its benefit obligation. FAS No. 158 also require companies to measure their plan assets and benefit obligations as of year-end balance sheet date. FAS No. 158 is effective for fiscal years ending after December 15, 2006; the provision to require measurement at the entity's year-end balance sheet date will be effective for fiscal years ending after December 15, 2008. If the Group had adopted the recognition provision of FAS No. 158 as of December 31, 2006, it would have been required to recognize a pre-tax liability for the underfunded status of the benefit plan in amount of USD 4.5 million.

Reclassifications

Certain reclassifications of prior years' amounts have been made to conform to the presentation adopted for the year ended December 31, 2006.

3. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise local and foreign currency bank balances, call deposits and highly-liquid bank promissory notes.

	December 31,		
	2006	2005	2004
Bank accounts, RUR	75	140	142
Bank accounts, USD	52	23	29
Bank accounts, EUR	6	4	5
Bank accounts, CHF	1	2	-
Bank deposits, RUR	148	898	1,619
Bank deposits, USD	8	41	61
Bank deposits, EUR	-	20	-
Bank promissory notes, RUR	44	3	4
Bank promissory notes, USD	-	4	-
Bank promissory notes, EUR	-	-	14
Cash equivalents, RUR	4	3	10
	338	**1,138**	**1,884**

As of December 31, 2006, 2005 and 2004, the weighted average interest rates on bank deposits with original maturities less than ninety days were 6.43%, 6.32% and 6.31%, respectively.

4. SHORT-TERM AND LONG-TERM BANK DEPOSITS

	December 31,		
	2006	2005	2004
Short-term bank deposits			
Bank deposits, RUR	228	-	209
Long-term bank deposits			
Bank deposits, RUR	109	99	103

As of December 31, 2006 and 2004, the weighted average interest rates on short-term bank deposits with original maturities exceeding ninety days were 10.08% and 6.21%, respectively.

As of December 31, 2006, 2005 and 2004, the long-term subordinated cash deposits were placed in a Russian bank and are not available to be withdrawn before December 15, 2009.

As of December 31, 2006, 2005 and 2004, the weighted average interest rate on long-term bank deposits was 6.50%.

5. SHORT-TERM AND LONG-TERM INVESTMENTS

	December 31,		
	2006	2005	2004
Short-term investments			
Trading promissory notes	212	-	-
Trading debt securities	78	9	16
Trading equity securities	30	3	2
Share in mutual investment fund	5	-	-
Promissory notes held to maturity	-	1	35
	325	**13**	**53**
Long-term investments			
Equity securities classified as available for sale	**146**	**1**	**1**

Trading debt securities and trading promissory notes are liquid publicly traded bonds and notes of Russian companies and banks. They are reflected at period-end market value based on last trade prices obtained from investment brokers.

Trading equity securities are liquid publicly traded shares of Russian companies. They are reflected at period-end market value based on last trade prices obtained from investment brokers.

Net gains on trading securities for the years ended December 31, 2006, 2005 and 2004 were USD 2 million, USD 8 million and USD 8 million, respectively. Those gains were included in other operating income in the consolidated statement of operations and comprehensive income (refer to Note 20).

Long-term equity securities classified as available for sale represent investments in equity securities of a foreign entity, where the Group has less than a 20% equity interest and no significant influence. As of December 31, 2006, unrealized holding gains on these securities were USD 18 million, net of the related income tax effect of USD 5 million, and reported as a separate component of other comprehensive income.

6. ACCOUNTS RECEIVABLE FROM THIRD PARTIES

	December 31,		
	2006	2005	2004
Trade accounts receivable	422	247	470
Value-added tax receivable	191	201	184
Advances paid	137	45	59
Interest receivable	23	67	15
Prepaid income tax	19	-	-
Other receivables	54	29	29
	846	589	757
Allowance for doubtful accounts	(12)	(20)	(23)
	834	**569**	**734**

7. INVENTORIES

	December 31, 2006	2005	2004
Raw materials	360	292	306
Work-in-progress	124	112	118
Finished goods and goods for resale	204	164	31
	688	**568**	**455**

8. PROPERTY, PLANT AND EQUIPMENT, NET

	Gross carrying value	Accumulated depreciation	Net carrying value
Land and buildings	1,395	(714)	681
Mineral license	23	-	23
Machinery and equipment	3,551	(1,961)	1,590
Transportation equipment	173	(109)	64
Fixtures and fittings	107	(44)	63
Construction-in-progress	243	-	243
Advance payments for property, plant and equipment	100	-	100
Balance as of December 31, 2006	**5,592**	**(2,828)**	**2,764**
Land and buildings	1,276	(686)	590
Machinery and equipment	3,059	(1,875)	1,184
Transportation equipment	165	(105)	60
Fixtures and fittings	85	(31)	54
Construction-in-progress	367	-	367
Advance payments for property, plant and equipment	33	-	33
Balance as of December 31, 2005	**4,985**	**(2,697)**	**2,288**
Land and buildings	1,230	(662)	568
Machinery and equipment	2,828	(1,800)	1,028
Transportation equipment	152	(97)	55
Fixtures and fittings	60	(24)	36
Construction-in-progress	166	-	166
Advance payments for property, plant and equipment	30	-	30
Balance as of December 31, 2004	**4,466**	**(2,583)**	**1,883**

Depreciation expense for the years ended December 31, 2006, 2005 and 2004 amounted to USD 177 million, USD 165 million and USD 152 million, respectively.

The capitalized borrowing costs for the years ended December 31, 2006, 2005 and 2004 amounted to USD 8 million, USD 3 million and USD 1 million, respectively.

In December 2006, the Group acquired at a state auction an exploration and development license for the Prioskolskoe iron ore deposit located in the Kurskaya region, the Russian Federation, expiring in 2026. The carrying value of this license was USD 23 million as of December 31, 2006.

9. INVESTMENTS IN AFFILIATES

The Group's equity method investments in affiliates as of December 31, 2006, 2005 and 2004 comprised the following:

		Investment carrying value			Ownership and voting interest, %		
		December 31,					
Affiliate	**Registered in**	**2006**	**2005**	**2004**	**2006**	**2005**	**2004**
Carrying value of investments							
LLC M-Port	Russia	46	41	-	50%	50%	-
CJSC Kazankovskaya Mine	Russia	33	41	-	50%	50%	-
LLC MMK Trans	Russia	5	8	7	50%	50%	50%
Loans provided to affiliates							
CJSC Kazankovskaya Mine	Russia	39	14	-			
		123	**104**	**7**			

During the year ended December 31, 2005, the Group acquired a 37% stake in OJSC Vladivostok Trade Sea Port ("OJSC VTSP") for a cash consideration of USD 41 million. These shares were subsequently contributed to LLC M-Port, a jointly controlled entity established in that year. In the same year LLC M-Port acquired a further 20% stake in OJSC VTSP.

During the year ended December 31, 2006, LLC M-Port issued additional shares, 50% of which were acquired by the Group for a consideration of USD 5 million. As a result of the transaction the Group's share in the net assets of the affiliate increased by USD 5 million, while the Group's share in the affiliate remained the same.

As of December 31, 2006 and 2005, the Group's effective ownership in OJSC VTSP was 47%.

As of December 31, 2006 and 2005, the Group provided CJSC Kazankovskaya Mine with a total of USD 39 million and USD 14 million in unsecured loans, respectively, with maturity in December 2013. These loans bear interest of 10% per annum. As of December 31, 2006, outstanding amount of loans provided included accrued interest of USD 4 million.

During the year ended December 31, 2006, the Group received dividends of USD 3 million from LLC MMK Trans.

10. OTHER INTANGIBLE ASSETS, NET

	Gross carrying value	Accumulated amortization	Net carrying value
Licenses	33	(9)	24
Purchased software	24	(10)	14
Other intangibles	6	(1)	5
Balance as of December 31, 2006	**63**	**(20)**	**43**
Licenses	27	(14)	13
Purchased software	21	(9)	12
Other intangibles	1	-	1
Balance as of December 31, 2005	**49**	**(23)**	**26**

	Gross carrying value	Accumulated amortization	Net carrying value
Licenses	16	(12)	4
Purchased software	15	(3)	12
Other intangibles	-	-	-
Balance as of December 31, 2004	**31**	**(15)**	**16**

Amortization expense for licenses, purchased software and other intangibles for the years ended December 31, 2006, 2005 and 2004 amounted to USD 11 million, USD 8 million and USD 17 million, respectively.

The estimated amortization expense for each of the next five years and thereafter is as follows:

Year ended December 31,	
2007	11
2008	7
2009	4
2010	3
2011	2
Thereafter	16
	43

Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

11. OTHER LONG-TERM ASSETS

	December 31,		
	2006	2005	2004
Loans provided	6	-	-
Restricted cash	5	2	4
Loans to employees	1	1	1
	12	**3**	**5**

12. SHORT-TERM BORROWINGS AND CURRENT PORTION OF LONG-TERM DEBT

	Type of interest rate	Annual interest rate (actual as of December 31, 2006)	December 31, 2006	2005	2004
Short-term borrowings:					
Secured loans, USD	Floating	6%	226	82	-
Secured loans, RUR	Fixed	10%	6	10	150
Secured loans, RUR	Floating	-	-	-	4
Unsecured loans, RUR	Floating	8%	17	9	-
Unsecured loans, RUR	Fixed	12%	1	1	430
Unsecured loans, USD	Floating	-	-	-	40
			250	102	624

	Type of interest rate	Annual interest rate (actual as of December 31, 2006)	December 31, 2006	2005	2004
Current portion of long-term debt:					
Unsecured corporate bonds, USD	Fixed	9%	4	4	4
Unsecured bonds, EUR	Fixed	-	-	-	148
Unsecured corporate bonds, RUR	Fixed	-	-	-	28
Secured loans, RUR	Fixed	11%	1	4	2
Secured loans, USD	Floating	-	-	-	3
Unsecured loans, USD	Floating	6%	98	38	16
Unsecured loans, RUR	Floating	8%	10	-	-
Unsecured loans, RUR	Fixed	9%	7	3	2
Unsecured loans, USD	Fixed	5%	2	-	-
Unsecured loans, EUR	Fixed	6%	1		
			123	49	203
			373	**151**	**827**

The weighted average interest rate of the RUR-denominated short-term borrowings as of December 31, 2006, 2005 and 2004 was 9%, 10% and 7%, respectively. The weighted average interest rate of the USD-denominated short-term borrowings as of December 31, 2006, 2005 and 2004 was 6%, 5% and 4%, respectively.

As of December 31, 2006, 2005 and 2004, short-term borrowings were secured by the Group's property, plant and equipment with a net carrying amount of USD 1 million, USD 22 million and USD 196 million, respectively, and inventory of USD 9 million, USD 8 million and USD 6 million, respectively.

13. LONG-TERM DEBT, NET OF CURRENT PORTION

	Type of interest rate	Annual interest rate (actual as of December 31, 2006)	December 31, 2006	2005	2004
Unsecured corporate bonds, USD	Fixed	9%	299	297	296
Secured loans, RUR	Fixed	12%	1	1	3
Secured loans, USD	Floating	-	-	-	24
Unsecured loans, USD	Floating	6%	257	147	39
Unsecured loans, USD	Fixed	5%	10	1	-
Unsecured loans, RUR	Fixed	10%	5	1	-
Unsecured loans, EUR	Fixed	6%	3	1	-
Unsecured loans, RUR	Floating	7%	2	-	-
			577	**448**	**362**

Credit facilities

The most significant debt provided by bank financing included credit line facilities from certain Russian and foreign banks. As of December 31, 2006, 2005 and 2004, the total unused portions of all credit facilities were USD 246 million, USD 224 million and USD 92 million.

The information provided below refers to total long-term debt, including its current portion, identified in Note 12.

Corporate bonds

In October 2003, MMK Finance S.A., a wholly-owned subsidiary of the Group, issued on the Luxembourg Stock Exchange USD 300 million of 8% notes at an issue price of 98.99 percent, due in October 2008. The notes are fully, unconditionally and irrevocably guaranteed by the Parent Company. Interest payments on the notes are due semi-annually in equal installments on April 21 and October 21 of each year, commencing April 21, 2004. The notes are subject to certain restrictive covenants including, but not limited to, limitations on the incurrence of additional indebtedness, restrictions on mergers or consolidations, limitations on liens and dispositions of assets and limitations on transactions with affiliates. For the years ended December 31, 2006, 2005 and 2004, interest payments on these notes amounted to USD 24 million per annum.

Loans

In 2006, foreign banks provided USD-denominated loans, bearing interest at LIBOR+1.00% (6.35% as of December 31, 2006) per annum with maturity in June 2009. As of December 31, 2006, the outstanding balance was USD 144 million.

In 2005, foreign banks provided USD-denominated loans, bearing interest at LIBOR+0.25% (5.62% as of December 31, 2006), LIBOR+0.30% (5.67% as of December 31, 2006) and 4.05% per annum maturing serially from 2009 to 2011. The commitment fees are from 0.07% to 0.08% per annum on the undrawn facilities. As of December 31, 2006, the outstanding balance of these loans was USD 70 million.

In 2004, foreign banks provided USD-denominated loans, bearing interest at LIBOR+0.18% (5.56% as of December 31, 2006), LIBOR+0.25% (5.62% as of December 31, 2006) and LIBOR+1.20% (6.20% as of December 31, 2006) per annum maturing serially from 2010 to 2011. The commitment fees are from 0.08% to 0.10% per annum on the undrawn facilities. As of December 31, 2006, the outstanding balance of these loans was USD 103 million.

In 2003, foreign banks provided USD-denominated loans, bearing interest at LIBOR+0.30% (5.67% as of December 31, 2006), LIBOR+0.45% (5.82% as of December 31, 2006) and LIBOR+0.75% (6.12% as of December 31, 2006) per annum maturing serially from 2008 to 2011. The commitment fees are from 0.10% to 0.20% per annum on the undrawn facilities. As of December 31, 2006, the outstanding balance of these loans was USD 48 million.

In 2002, foreign bank provided a USD-denominated loan, bearing interest at LIBOR+0.80% (5.91% as of December 31, 2006) per annum with maturity in June 2007. The commitment fee is 0.50% per annum on the undrawn facility. As of December 31, 2006, the outstanding balance of this loan was USD 3 million.

The bank loans are subject to certain restrictive covenants, including, but not limited to:

- The ratio of consolidated debt / consolidated EBITDA should not exceed 3.5:1; and
- The ratio of consolidated EBITDA / consolidated debt service should not be less than 3:1.

As of December 31, 2006, 2005 and 2004, loans were secured by the Group's property, plant and equipment with a net carrying amount of USD 2 million, USD 5 million and USD 45 million, respectively, and inventory of USD 2 million as of December 31, 2006.

Debt repayment schedule

Year ended December 31,	
2007 (presented as current portion of long-term debt, Note 12)	123
2008	421
2009	88
2010	47
2011 and thereafter	21
	700

14. CAPITAL LEASE OBLIGATIONS

The following table presents future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 2006:

Year ended December 31,	
2007	31
2008	18
2009	10
2010	4
2011	2
Thereafter	-
Total minimum lease payments (undiscounted)	**65**
Less amount representing interest	(11)
Present value of net minimum lease payments	**54**
Less current portion of long-term capital lease obligations	(25)
Long-term capital lease obligations	**29**

As of December 31, 2006, 2005 and 2004, leased assets with a net carrying amount of USD 72 million, USD 57 million and USD 54 million, respectively, were included in property, plant and equipment as follows:

	Gross carrying value	Accumulated depreciation	Net carrying value
Machinery and equipment	76	(12)	64
Construction-in-progress	8	-	8
Balance as of December 31, 2006	**84**	**(12)**	**72**
Machinery and equipment	59	(9)	50
Construction-in-progress	7	-	7
Balance as of December 31, 2005	**66**	**(9)**	**57**
Machinery and equipment	49	(6)	43
Construction-in-progress	11	-	11
Balance as of December 31, 2004	**60**	**(6)**	**54**

15. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December, 31		
	2006	2005	2004
Trade accounts payable	225	161	166
Advances from customers	191	151	106
Dividends payable	20	14	-
Income tax payable	-	18	11
Other taxes payable	37	54	44
Other current liabilities	72	62	76
	545	**460**	**403**

16. EMPLOYEE BENEFITS

Defined contribution plans

Payments of unified social tax, which includes contributions to the Russian Federation State Pension Fund, amounted to USD 59 million, USD 51 million and USD 38 million for the years ended December 31, 2006, 2005 and 2004, respectively.

In addition, the Group makes monthly contributions to a non-government pension fund Sotsialnaya Zashchita Starosti where its employees have individual accumulation agreements with the fund. The Group has the ability to exercise significant influence over the financial and operating policy decisions of the fund through positions that certain directors of the Group have on the board of directors of the fund. The monthly contribution made by the Group is equal to the employee's contribution, unless the employee is a male aged between 55 and 60, or a female aged between 50 and 55, in which case the contribution will be 1.5 times the employee's contribution. For the years ended December 31, 2006, 2005 and 2004, the maximum monthly contributions by the Group for each employee were RUR 6,000 (USD 221), RUR 5,000 (USD 176) and RUR 4,000 (USD 144), respectively. The Group's total contributions to the fund amounted to USD 5.5 million, USD 2.9 million and USD 2.7 million for the years ended December 31, 2006, 2005 and 2004, respectively.

Defined benefit plan

The Group has a defined benefit plan in favour of employees who retired prior to April 1, 2001. Effective April 1, 2001, no employees retired after that date were allowed to participate in the plan. Pensions from this defined benefit plan are administered by the independent charity fund BOF Metallurg.

Those employees receive lifetime pension payments varying from RUR 250 (USD 9.19) to RUR 450 (USD 16.55) per month depending on the employee's actual years of services and qualifications.

For the years ended December 31, 2006, 2005 and 2004, the Group made monthly payments to the fund of RUR 389 (USD 14.30), RUR 327 (USD 11.56) and RUR 276 (USD 9.58), respectively, per retiree, which were then distributed by the fund to the retirees.

As of December 31, 2006, 2005 and 2004, principal actuarial assumptions used in determining the projected benefit obligations and net periodic pension expense were as follows:

	December 31,		
	2006	2005	2004
Discount rate	9.0%	9.1%	10.6%
Future pension benefit increases	8.4%	8.5%	8.7%
Average life expectancy of members from date of retirement	10.4	10.3	10.6

The change in the projected benefit obligations is presented in the following table:

	2006	2005	2004
Projected benefit obligations at beginning of the year	26	23	22
Interest cost	2	3	3
Actuarial losses/(gains)	3	4	(1)
Benefit payments during the year	(3)	(3)	(3)
Foreign exchange losses/(gains)	2	(1)	2
Unfunded status of the plan at end of the year	**30**	**26**	**23**

The fund does not hold any assets set aside for the benefit of retirees under this plan.

The accumulated benefit obligations as of December 31, 2006, 2005 and 2004 were as follows:

	December 31,		
	2006	**2005**	**2004**
Accumulated benefit obligations	**30**	**26**	**23**

The components of the net periodic benefit costs for the years ended December 31, 2006, 2005 and 2004 were as follows:

	2006	2005	2004
Interest cost	2	3	3
Actuarial losses/(gains)	3	4	(1)
Foreign exchange losses/(gains)	2	(1)	2
	7	**6**	**4**

Net periodic benefit costs were recognized as part of administrative expenses in the consolidated statement of operations and comprehensive income.

The future benefit payments to retirees under the defined benefit plan are expected to be as follows:

Year ended December 31,	
2007	3
2008	3
2009	3
2010	2
2011	2
2012-2016	8
Thereafter	9
	30

17. SHAREHOLDERS' EQUITY

Common stock

As of December 31, 2006 and 2005, the Parent Company had 10,630,222 thousand authorized, issued and outstanding common shares with a par value of RUR 1 each. As of December 31, 2004, the Parent Company had 7,972,666 thousand authorized, issued and outstanding common shares with a par value of RUR 1 each.

Preferred stock

As of December 31, 2004, the Parent Company had 2,657,556 thousand authorized, issued and outstanding preferred shares with a par value of RUR 1 each.

In 2005, the Parent Company converted all its preferred shares to 2,657,556 common shares with a par value of RUR 1 each.

Treasury stock

As of December 31, 2006, 2005 and 2004, the Group held in treasury 485,062 thousand, 472,832 thousand and 335,171 thousand, respectively, issued common shares of the Parent Company.

In addition, as of December 31, 2004, the Group held in treasury 66,174 thousand issued preferred shares of the Parent Company.

All treasury stock is recorded at cost.

Shareholders' voting rights

The shareholders of fully paid common stock are entitled to one vote per share at the annual general shareholders' meeting of the Parent Company.

Dividends

Year ending December 31, 2006

On November 28, 2006, the Parent Company declared an additional interim dividend of RUR 0.910 (USD 0.035) per common share in respect of the nine months ended September 30, 2006 representing a total dividend of USD 366 million. Of this total, USD 16 million was attributable to Group entities.

On August 29, 2006, the Parent Company declared an additional interim dividend of RUR 0.815 (USD 0.030) per common share in respect of the six months ended June 30, 2006 representing a total dividend of USD 324 million. Of this total, USD 14 million was attributable to Group entities.

On May 26, 2006, the Parent Company declared an interim dividend of RUR 0.593 (USD 0.022) per common share in respect of the three months ended March 31, 2006 representing a total dividend of USD 233 million. Of this total, USD 10 million was attributable to Group entities.

Year ending December 31, 2005

On April 21, 2006, the Parent Company declared a final dividend of RUR 0.532 (USD 0.019) per common share in respect of the year ended December 31, 2005 representing a total dividend of USD 206 million. Of this total, USD 9 million was attributable to Group entities.

On November 29, 2005, the Parent Company declared an additional interim dividend of RUR 0.667 (USD 0.023) per common share in respect of the nine months ended September 30, 2005 representing a total dividend of USD 249 million. Of this total, USD 11 million was attributable to Group entities.

On August 30, 2005, the Parent Company declared interim dividends of RUR 0.655 (USD 0.023) per common share representing a total dividend of USD 182 million and of RUR 0.655 (USD 0.023) per preferred share representing a total dividend of USD 61 million in respect of the six months ended June 30, 2005. Of these totals, USD 8 million and USD 2 million, respectively, were attributable to Group entities.

Year ending December 31, 2004

On April 22, 2005, the Parent Company declared a final dividend of RUR 1.34 (USD 0.048) per common share representing a total dividend of USD 385 million and of RUR 1.34 (USD 0.048) per preferred share representing a total dividend of USD 128 million in respect of the year ended December 31, 2004. Of these totals, USD 16 million and USD 4 million, respectively, were attributable to Group entities.

Year ending December 31, 2003

On May 28, 2004, the Parent Company declared a final dividend of RUR 0.027 (USD 0.001) per common share representing a total dividend of USD 7 million and RUR 0.081 (USD 0.003) per preferred share representing a total dividend of USD 7 million in respect of the year ended December 31, 2003.

18. EARNINGS PER COMMON SHARE

Basic net income per common share is calculated by adjusting net income for the dividend requirements of preferred stock and is based on the weighted average number of common shares outstanding during the year. Diluted net income per common share assumes the exercise of stock options, the vesting of restricted stock and the conversion of preferred stock, provided in each case the effect is dilutive.

The calculation of basic and diluted earnings per common share for the years ended December 31, 2006, 2005 and 2004 was as follows:

	2006	2005	2004
Net income applicable to common stock	1,426	781	903
Weighted average number of common shares outstanding (in thousands):			
Basic	10,160,990	8,250,930	7,198,738
Diluted	10,160,990	8,250,930	7,198,738
Earnings per common share (USD):			
Basic	0.140	0.095	0.125
Diluted	0.140	0.095	0.125

There were no dilutive securities issued as of December 31, 2006, 2005 and 2004.

19. NET REVENUE

By product	2006	2005	2004
Rolled steel	3,752	3,165	2,853
Assorted rolled products	604	341	365
Galvanized steel	377	338	322
Hardware products	283	117	121
Tin plated steel	254	295	217
Band	251	274	251
Galvanized steel with polymeric coating	168	148	50
Formed section	127	112	73
Coking production	113	102	66
Slabs	107	140	258
Tubes	49	39	45
Wire, sling, bracing	30	71	80
Others	309	238	128
	6,424	**5,380**	**4,829**

By customer destination	2006	2005	2004
The Russian Federation and CIS	62%	61%	55%
Turkey	8%	6%	5%
Iran	5%	4%	2%
Italy	5%	3%	6%
USA	3%	1%	3%
India	2%	4%	3%
China	1%	8%	6%
Taiwan	-	1%	4%
Others (countries each representing less than 2% of total net revenue)	14%	12%	16%
	100%	**100%**	**100%**

20. OTHER OPERATING INCOME, NET

	2006	2005	2004
Net gain on sales of other assets	24	1	18
Change in allowance for doubtful accounts receivable	8	3	(5)
Net gain on trading securities	2	8	8
Other operating gain, net	5	7	20
	39	**19**	**41**

21. INCOME TAXES

The Group's provision for income taxes attributable to different tax jurisdictions for the years ended December 31, 2006, 2005 and 2004 was:

	2006	2005	2004
Current provision for income tax:			
The Russian Federation	460	358	384
Switzerland	1	1	1
Deferred income tax expense:			
The Russian Federation	7	13	4
Total income tax expense	**468**	**372**	**389**

The provision for income taxes is different from that which would be obtained by applying the Russian Federation statutory income tax rate of 24% to net income before income tax and minority interest. The items causing this difference are as follows:

	2006	2005	2004
Statutory rate applied to income before income tax and minority interest	455	316	389
Adjustments due to:			
Expenses not deductible for tax purposes	12	51	1
Effect of dividends paid within the Group entities	4	4	-
Currency exchange and translation differences	(3)	1	(1)
Income tax expense	**468**	**372**	**389**

Deferred income tax assets and liabilities were comprised of differences arising between the tax and accounting bases of the following assets and liabilities:

	December 31,		
	2006	2005	2004
Inventories	18	5	1
Loans	15	4	7
Accounts payable	12	15	10
Accounts receivable	1	2	5
Investments	-	2	3
Tax loss carry forward	-	-	1
Gross deferred income tax assets	46	28	27
Property, plant and equipment	(41)	(5)	(2)
Inventories	(10)	(16)	(9)
Investments	(8)	(2)	(1)
Accounts receivable	(2)	(7)	(2)
Loans	-	(1)	-
Gross deferred income tax liabilities	(61)	(31)	(14)
Net deferred income tax (liabilities)/assets	**(15)**	**(3)**	**13**

Deferred income tax balances were classified in the consolidated balance sheet as follows:

	December 31,		
	2006	**2005**	**2004**
Current deferred income tax assets	36	26	24
Current deferred income tax liabilities	(11)	(26)	(11)
Long-term deferred income tax assets	10	2	3
Long-term deferred income tax liabilities	(50)	(5)	(3)
Net deferred income tax (liabilities)/assets	**(15)**	**(3)**	**13**

For the years ended December 31, 2006, 2005 and 2004, statutory retained earnings of the Group's foreign subsidiaries amounted to USD 21 million, USD 22 million and USD 22 million, respectively, on which deferred income tax of USD 1 million has not been recognised because remittance of the earnings has been indefinitely postponed through reinvestment and, as a result, such amounts are considered to be permanently invested.

In accordance with FAS No. 52 and FAS No. 109 deferred tax assets and liabilities were not recognized for temporary differences arising from the remeasurement of the local currency into the functional currency using historical exchange rates. Also in accordance with FAS No. 109 no deferred tax assets or liabilities were recognized for the effect of tax indexation of property, plant and equipment.

Based upon the level of historical taxable income and projections for the future taxable income over the periods in which the deferred income tax assets are deductible, management of the Group believes it is more likely than not that Group will realize the benefits of the deductible differences. Accordingly, no valuation allowances have been provided against deferred tax assets as of December 31, 2006, 2005 and 2004.

22. ACQUISITIONS

OJSC Shelkovsky Zavod Spetzmontazhizdelie

In July, October and December 2005, the Group acquired stakes of 77.98%, 15.03% and 2.84%, respectively, in OJSC Shelkovsky Zavod Spetzmontazhizdelie which is a producer of metal ware products for a total cash consideration of USD 8 million.

This acquisition was accounted for using the purchase method. The purchase price allocation for the acquisition was as follows:

Current assets	1
Non-current assets	12
Deferred income tax	(3)
Current liabilities	(2)
Goodwill	-
Purchase price	**8**

LLC MetAl

In 2004, LLC MetAl was considered by the Group's management to be a variable interest entity of the Group and was accordingly consolidated for the year ended December 31, 2004.

In 2005, the Group acquired a 100% stake in LLC MetAl for a cash consideration of USD 44 million.

OJSC MTSOZ

In 2004, in addition to the Group's existing shareholding of 77.93% the Group acquired a further 17.19% stake in OJSC MTSOZ for a cash consideration of USD 0.38 million, increasing the Group's effective ownership interest in OJSC MTSOZ to 95.12%. Accordingly, the Group's effective ownership interest in ZAO Ogneupor, a wholly-owned subsidiary of OJSC MTSOZ, increased to 95.12%. These transactions resulted in recognition of goodwill in the amount of USD 0.1 million.

In September 2005, in addition to the Group's existing shareholding of 95.12% the Group acquired a further 3.77% stake in OJSC MTSOZ for a cash consideration of USD 6 million, increasing the Group's effective ownership interest in OJSC MTSOZ to 98.89%. Accordingly, the Group's effective ownership interest in ZAO Ogneupor, a wholly-owned subsidiary of OJSC MTSOZ, increased to 98.89%. The allocation of purchase price decreased the value of property, plant and equipment by USD 2 million.

LLC Magfer

In 2005, in addition to the Group's existing shareholding of 50.50% the Group acquired a further 49.50% stake in LLC Magfer for a cash consideration of USD 0.6 million, increasing the Group's effective ownership interest to 100%.

CJSC Mekhanoremont

In 2004, in addition to the Group's existing shareholding of 66.31% the Group acquired a further 32.62% stake in CJSC Mekhanoremont for a cash consideration of USD 2.4 million, increasing the Group's effective ownership interest to 98.93%. The allocation of purchase price decreased the value of property, plant and equipment by USD 9 million.

23. FAIR VALUE OF FINANCIAL INSTRUMENTS AND CREDIT RISK

Fair value of financial instruments

The estimated fair value of certain financial instruments have been determined using available market information or other valuation methodologies that require considerable judgment in interpreting market data and developing estimates. Accordingly, the estimates applied are not necessarily indicative of the amounts that the Group could realize in a current market exchange. The use of different assumptions and/or estimation methodologies may have a material impact on the estimated fair values.

As of December 31, 2006, the estimated fair value of financial instruments, consisting of cash and cash equivalents, accounts receivable and accounts payable, approximates their carrying value due to the short-term nature of these instruments. As of December 31, 2006, USD 300 million of corporate bonds due in 2008 have a fair value of 102.50% or USD 308 million. The fair value of other fixed-rate debt including capital lease obligations and floating-rate debt approximates its carrying value.

Credit risk

Credit risk represents the accounting loss that would be recognized at the reporting date if counterparties failed completely to perform as contracted and from movements in interest rates and foreign exchange rates. The Group does not anticipate non-performance by counterparties. The Group generally does not require collateral or other security to support financial instruments with credit risk.

Financial instruments that potentially subject the Group to significant credit risk primarily consist of cash and cash equivalents, bank deposits and accounts receivable.

The Group has bank accounts, held in OJSC Credit Ural Bank ("OJSC CUB"), a related party of the Group. In addition the Group classifies promissory notes, purchased from OJSC CUB, as cash equivalents. Also the Group holds significant amounts of cash in bank deposits in Russian banks.

To reduce risk the Group performs credit risk exposure evaluations for all banks in which the Group holds bank deposits on a monthly basis.

The Group sells its products to a number of customers globally. The Group grants credit to its customers based on an evaluation of each customer's financial position, in certain cases, without requiring guarantees or letters of credit, and thereafter monitors the exposure of potential losses from granting credit. To reduce risk the Group routinely assesses the financial strength of its customers and as a consequence, believes that its accounts receivable credit risk exposure is limited.

The maximum credit risk exposure is represented by the carrying amount of each financial asset and the contractual amounts of the financial guarantees and disclosed in Note 26.

24. RELATED PARTY TRANSACTIONS

Related parties include shareholders, key management personnel, affiliates and entities under common ownership, and entities over which the Group has the ability to exercise a significant influence.

Cash held at a related party bank is disclosed in Note 23. Issuance of guarantees in favor of related parties and receipt of guarantees from related parties transactions are disclosed in Note 26.

The following companies are considered to be related parties to the Group:

CJSC Profit

CJSC Profit, a company affiliated with the Group's controlling shareholders, purchases scrap metals from third parties and Group entities, reprocesses it and sells reprocessed scrap metals to the Group.

OJSC CUB

The Group holds certain deposits and current accounts in OJSC CUB, a commercial bank affiliated with the Group's controlling shareholders and the Group's management. During the reporting period the Group received financing from OJSC CUB in the form of loans for the Group's operating activities.

LLC MMK Trans

LLC MMK Trans, the Group's affiliate, provides transportation and forwarding services to the Group. In 2004, the Group provided loans to LLC MMK Trans.

OJSC SKM

OJSC SKM, an insurance company affiliated with the Group's controlling shareholders and the Group's management, provides insurance services to the Group.

CJSC Kazankovskaya Mine

CJSC Kazankovskaya Mine, the Group's affiliate, holds a license to explore and mine coal deposits located in Kemerovo region, the Russian Federation. In 2006 and 2005, the Group provided loans to CJSC Kazankovskaya Mine.

CJSC SKM-Invest

CJSC SKM-Invest, a leasing company affiliated with the Group's management, provides assets under capital lease to the Group.

Transactions	December 31, 2006	2005	2004
Revenue			
CJSC Profit	125	78	40
LLC MMK Trans	1	1	13
Other	-	-	25
Total	126	79	78
Purchases			
CJSC Profit	771	337	245
LLC MMK Trans	24	27	31
Total	795	364	276
Loans provided			
OJSC Kazankovskaya Mine	20	14	-
OJSC SKM	2	-	-
CJSC Profit	-	26	-
LLC MMK Trans	-	-	2
Other	-	1	-
Total	22	41	2
Loans repaid			
OJSC SKM	2	-	-
CJSC Profit	-	26	-
LLC MMK Trans	-	-	2
Other	1	-	-
Total	3	26	2
Bank charges			
OJSC CUB	12	11	11
Loans and overdrafts obtained			
OJSC CUB	36	24	21
Loans and overdrafts repaid			
OJSC CUB	40	20	27
Insurance payments			
OJSC SKM	37	30	31
Lease payments			
CJSC SKM-Invest	15	8	3
Other	-	-	12
Total	15	8	15

Balances	December 31, 2006	2005	2004
Cash and cash equivalents			
OJSC CUB	151	44	85
Loans and overdraft facilities			
OJSC CUB	6	9	5
Loans provided			
OJSC Kazankovskaya Mine	39	14	-
Other	-	1	-
Total	39	15	-
Accounts receivable			
CJSC Profit	13	-	21
LLC MMK Trans	4	3	2
Total	17	3	23
Accounts payable			
CJSC Profit	5	6	1
LLC MMK Trans	2	2	-
OJSC SKM	-	1	-
Total	7	9	1
Insurance payable			
OJSC SKM	1	-	-
Lease payable			
CJSC SKM-Invest	25	18	19

25. COMMITMENTS

In the course of carrying out its operations and other activities the Group enters into various agreements, which would require the Group to invest in or provide financing to specific projects or undertakings. In the opinion of the Group's management, these commitments are entered into under standard terms, which are representative of each project's feasibility and should not result in unreasonable losses for the Group.

As of December 31, 2006, the Group had executed non-binding purchase agreements in the amount of approximately USD 2,834 million to subsequently acquire property, plant and equipment, and coking coal, zinc and aluminum, which are valid until 2011 – 2012.

In the past the Group has transferred social assets to local municipal authorities, however, Group's management expects that the Group will continue to partly fund those social operations in the foreseeable future. These costs are recognized in the consolidated statement of operations and comprehensive income as incurred.

Operating leases

The land in the Russian Federation on which the Group's production facilities are located is owned by the State. The Group pays land tax based on the total area and the location of the land occupied. The amounts of land tax for the years ended December 31, 2006, 2005 and 2004 were approximately USD 23 million, USD 22 million and USD 22 million, respectively.

The Group leases land through operating lease agreements, which expire in various years through 2054. Future minimum lease payments due under non-cancelable operating lease agreements as of December 31, 2006 were as follows:

Due in one year	2
Due in the second year	1
Due thereafter	5
	8

26. CONTINGENCIES

Issued guarantees

As of December 31, 2006, the Group has provided financial guarantees for loans obtained by certain related and third party suppliers of the Group. The amounts related to the Group's financial guarantees were as follows:

Non-current	
Related parties	200
Third parties	37
	237
Current	
Related parties	1
Third parties	7
	8
Total	**245**

The Group’s estimated maximum exposure to credit risk in the event of non-performance by other parties to these financial guarantees is represented by the contractual amounts disclosed above. The Group’s management believes that the likelihood of material payments being required under these agreements is remote.

As of December 31, 2006, the Group did not have any contractual commitments to extend financial guarantees, credit or other assistance.

Litigation

As of December 31, 2006, the Group was subject to various lawsuits, claims and proceedings related to matters incidental to its business. In the opinion of the Group’s management as of December 31, 2006 there were no material unresolved adverse claims or other matters.

Russian business environment

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

Tax contingencies

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

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for all 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 financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

Environmental liabilities

The Group is obligated to undertake certain environmental remediation activities to ensure site restoration of a large iron ore quarry in the Magnitogorsk region, the Russian Federation. In accordance with permission granted by the Magnitogorsk Regional Ecological Committee, the Group utilizes production waste to fill the iron ore quarry where this waste does not exceed a prescribed toxicity level. Amounts of waste which exceed this toxicity level are not significant and are treated by licensed specialists. The future cost associated with the restoration of the iron ore quarry are not expected to be significant. These costs and other environmental compliance costs associated with air and water pollution are included in the normal operating expenses of the Group as they are incurred.

Environmental regulations are currently under consideration in the Russian Federation and the Group is continuously evaluating its obligations relating to new and changing legislation. The likelihood and amount of liabilities relating to environmental obligations under proposed or any future legislation cannot be reasonably estimated at present and could become material.

Under existing legislation, management believes that there are no significant unrecorded liabilities or contingencies, which could have a significant adverse effect on the operating results or financial position of the Group.

27. DISPOSAL OF SUBSIDIARY

On March 10, 2006, the Group disposed of its entire operations of CJSC Shakhtouchastok Uregolskiy, a subsidiary of the Group, to OJSC Coal Company Yuzhniy Kuzbass for a cash consideration of USD 7 million. Net assets of CJSC Shakhtouchastok Uregolskiy comprised property, plant and equipment with a net carrying amount of USD 7 million.

28. SUBSEQUENT EVENTS

On January 18, 2007, the Parent Company registered an additional issuance of common stock of 1,450 million shares with a par value of RUR 1.

On January 31, 2007, the Group acquired a 51% stake in LLC Bakalskoe Rudoupravlenie for a cash consideration of USD 15 million.

On February 27, 2007, the Board of Directors of the Parent Company recommended a final dividend of RUR 0.891 (USD 0.034) per common share in respect of the year ended December 31, 2006 representing a total dividend of USD 362 million. Of this total, USD 16 million was attributable to Group entities. The final dividend is subject to approval by the shareholders at the Parent Company's annual general shareholders' meeting.

In the beginning of 2007, the Group entered into long-term purchase agreements in the amount of approximately USD 8,621 million to subsequently acquire coking coal, zinc, aluminum and iron ore until 2012 – 2017.