Polyus Gold

Consolidated financial statements
for the year ended 31 December 2008

POLYUS GOLD

CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

The following statement, which should be read in conjunction with the independent auditors' report set out on pages 2-3, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of Open Joint Stock Company "Polyus Gold" and its subsidiaries (the "Group").

Management is responsible for the preparation of consolidated financial statements that present fairly the financial position of the Group at 31 December 2008 and the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing consolidated financial statements, management is responsible for:

- selecting suitable accounting principles and applying them consistently;
- making judgments and estimates that are reasonable and prudent;
- stating whether IFRS have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- taking steps to safeguard the assets of the Group; and
- detecting and preventing fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2008 were approved on 17 April 2009 by:

Ivanov E.I.	**Ignatov O.V.**
General Director	Deputy General Director

Moscow, Russia
17 April 2009

ZAO Deloitte & Touche CIS
Business Center "Mokhovaya"
4/7 Vozdvizhenka St., Bldg. 2
Moscow, 125009
Russia

Tel: +7 (495) 787 0600
Fax: +7 (495) 787 0601
www.deloitte.ru

INDEPENDENT AUDITORS' REPORT

To shareholders of Open Joint Stock Company "Polyus Gold":

We have audited the accompanying consolidated financial statements of Open Joint Stock Company "Polyus Gold" and its subsidiaries (hereinafter refer to as the "Group"), which comprise the consolidated balance sheet as at 31 December 2008, and the consolidated statements of income, cash flows and changes in equity for the year 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 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 the financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

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

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

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

Opinion

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

Deloitte + Touche

Moscow, Russia
17 April 2009

POLYUS GOLD

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008
(in thousands of US Dollars)

	Notes	2008	2007
Gold sales		1,062,331	849,023
Other sales		24,987	18,096
Total revenue		**1,087,318**	**867,119**
Cost of gold sales	5	(558,118)	(449,216)
Cost of other sales		(25,061)	(25,866)
Gross profit		**504,139**	**392,037**
Selling, general and administrative expenses	6	(134,960)	(261,776)
Research and exploration expenses		(4,959)	(6,217)
Other expenses, net	7	(17,056)	(10,329)
Finance costs	8	(4,417)	(6,629)
(Loss)/income from investments	9	(217,591)	61,537
Foreign exchange (loss)/gain, net		(2,685)	8,484
Profit before income tax		**122,471**	**177,107**
Income tax	10	(62,110)	(85,299)
Profit for the year		**60,361**	**91,808**
Attributable to:			
Shareholders of the parent company		51,507	85,809
Minority interest		8,854	5,999
		60,361	**91,808**
Earnings per share			
Weighted average number of ordinary shares in issue during the year		178,138,065	175,739,670
Basic and diluted (US cents)		29	49

The accompanying notes are an integral part of these consolidated financial statements.

POLYUS GOLD

CONSOLIDATED BALANCE SHEET
AT 31 DECEMBER 2008
(in thousands of US Dollars)

	Notes	2008	2007
ASSETS			
Non-current assets			
Property, plant and equipment	11	1,772,319	1,783,432
Deferred stripping costs		163,988	82,061
Inventories	13	39,063	-
Investments in securities and other financial assets	12	4,095	2,147
Long-term portion of reimbursable value added tax	11	9,188	11,824
Other non-current assets		2,164	-
		1,990,817	**1,879,464**
Current assets			
Inventories	13	233,001	224,209
Reimbursable value added tax		104,872	108,926
Accounts receivable	14	15,513	13,477
Advances paid to suppliers	15	14,558	26,204
Investments in securities and other financial assets	12	285,236	1,270,918
Income tax prepaid		17,545	3,398
Other current assets	16	18,494	20,680
Cash and cash equivalents	17	398,826	226,174
		1,088,045	**1,893,986**
TOTAL ASSETS		**3,078,862**	**3,773,450**
EQUITY AND LIABILITIES			
Share capital and reserves			
Share capital	18	6,871	6,871
Additional paid-in capital		2,116,655	2,118,165
Treasury shares	18	(724,927)	(730,450)
Investments revaluation reserve		-	36,907
Translation reserve		(43,406)	425,727
Retained earnings		1,401,540	1,404,554
Equity attributable to shareholders of the parent company		**2,756,733**	**3,261,774**
Minority interest		37,808	47,187
		2,794,541	**3,308,961**
Non-current liabilities			
Deferred tax liabilities	19	148,244	200,609
Environmental obligations	20	34,379	81,341
		182,623	**281,950**
Current liabilities			
Consideration on acquisition of subsidiaries		-	22,197
Short-term borrowings	21	-	20,909
Trade payables	22	17,918	21,651
Other payables and accrued expenses	23	65,609	83,932
Income tax payable		1,344	12,663
Other taxes payable	24	16,827	21,187
		101,698	**182,539**
TOTAL LIABILITIES		**284,321**	**464,489**
TOTAL EQUITY AND LIABILITIES		**3,078,862**	**3,773,450**

The accompanying notes are an integral part of these consolidated financial statements.

POLYUS GOLD

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008
(in thousands of US Dollars)

	Notes	2008	2007
Operating activities			
Profit before income tax		**122,471**	**177,107**
Adjustments for:			
Amortisation and depreciation		86,927	82,066
Finance costs		4,417	6,629
Loss on disposal of property, plant and equipment		548	6,421
Impairment of property, plant and equipment		1,831	313
Change in provision for land restoration		(8,530)	482
Change in allowance for reimbursable value added tax		7,078	(3,641)
Loss/(income) from investments		217,591	(61,537)
Foreign exchange loss/(gain), net		2,685	(8,484)
Share option plan		-	132,548
Other		(3,983)	4,797
Operating profit before working capital changes		**431,035**	**336,701**
Increase in inventories		(101,665)	(42,015)
Increase in accounts receivable		(4,734)	(1,717)
Decrease in advances paid to suppliers		8,140	2,098
(Increase)/decrease in other current assets and reimbursable value added tax		(49,038)	1,067
(Decrease)/increase in trade payables		(3,500)	715
Increase in other payables and accrued expenses		5,884	14,117
Decrease in other taxes payable		(1,034)	(14,462)
Cash flows from operations		**285,088**	**296,504**
Interest paid		(2,434)	(1,671)
Income tax paid		(90,421)	(50,187)
Net cash generated from operating activities		**192,233**	**244,646**
Investing activities			
Increase of ownership in subsidiaries	4	(39,156)	-
Proceeds from disposal of subsidiary, net of cash disposed of		-	1,320
Repayment of consideration on acquisition of subsidiaries		(19,616)	(38,228)
Purchase of property, plant and equipment		(481,504)	(382,802)
Deferred stripping costs capitalised		(95,313)	(57,636)
Proceeds from sale of property, plant and equipment		5,747	17,952
Interest received		43,967	26,696
Purchase of promissory notes and other financial assets		(7,390)	(1,447,102)
Proceeds from sale of promissory notes and other financial assets		664,151	1,511,054
Net cash generated from/(used in) investing activities		**70,886**	**(368,746)**

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008 (CONTINUED)
(in thousands of US Dollars)

	Notes	2008	2007
Financing activities			
Proceeds from borrowings		-	7,109
Repayments of borrowings		(19,034)	(2,725)
Repayments of finance lease obligations		(1,622)	(3,434)
Proceeds from issuance of Company's shares from treasury shares	18	1,334	64,051
Dividends paid to shareholders of the Company	18	(22,258)	(21,722)
Dividends paid to minority shareholders of the Group's subsidiary		(2,008)	(942)
Net cash (used in)/generated from financing activities		**(43,588)**	**42,337**
Effect of translation to presentation currency		(46,879)	13,740
Net increase/(decrease) in cash and cash equivalents		**172,652**	**(68,023)**
Cash and cash equivalents at beginning of the year		**226,174**	**294,197**
Cash and cash equivalents at end of the year	17	**398,826**	**226,174**

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2008
(in thousands of US Dollars)

	Notes	Equity attributable to shareholders of the parent company								
		Share capital	Additional paid-in capital	Treasury shares	Investments revaluation reserve	Translation reserve	Retained earnings	Total	Minority interest	Total
Balance at 31 December 2006		**6,871**	**2,190,661**	**(995,557)**	**19,620**	**261,794**	**1,342,638**	**2,826,027**	**32,647**	**2,858,674**
Increase in fair value of available-for-sale investments	12	-	-	-	17,287	-	-	**17,287**	-	**17,287**
Translation of foreign operations		-	-	-	-	(44,412)	-	**(44,412)**	-	**(44,412)**
Effect of translation to presentation currency		-	-	-	-	211,977	-	**211,977**	3,088	**215,065**
Total income recognised directly in equity		**-**	**-**	**-**	**17,287**	**167,565**	**-**	**184,852**	**3,088**	**187,940**
Profit for the year		-	-	-	-	-	85,809	**85,809**	5,999	**91,808**
Total recognised income and expense for the year		**-**	**-**	**-**	**17,287**	**167,565**	**85,809**	**270,661**	**9,087**	**279,748**
Dividends to shareholders of the parent company	18	-	-	-	-	-	(21,722)	**(21,722)**	-	**(21,722)**
Dividends to minority shareholders in the Group's subsidiaries		-	-	-	-	-	-	**-**	(942)	**(942)**
Increase in minority interest due to increase in share capital of a subsidiary		-	-	-	-	-	(2,171)	**(2,171)**	2,171	**-**
Increase in minority interest due to disposal of preferred shares of a subsidiary		-	-	-	-	-	-	**-**	4,224	**4,224**
Issuance of shares from treasury shares under share option plan	18	-	(72,496)	265,107	-	(3,632)	-	**188,979**	-	**188,979**
Balance at 31 December 2007		**6,871**	**2,118,165**	**(730,450)**	**36,907**	**425,727**	**1,404,554**	**3,261,774**	**47,187**	**3,308,961**
Decrease in fair value of available-for-sale investments	12	-	-	-	(16,739)	-	-	**(16,739)**	8,190	**(8,549)**
Translation of foreign operations		-	-	-	-	214,920	-	**214,920**	-	**214,920**
Effect of translation to presentation currency		-	-	-	-	(683,746)	-	**(683,746)**	(7,528)	**(691,274)**
Total loss recognised directly in equity		**-**	**-**	**-**	**(16,739)**	**(468,826)**	**-**	**(485,565)**	**662**	**(484,903)**
Profit for the year		-	-	-	-	-	51,507	**51,507**	8,854	**60,361**
Realised gain on disposal of available-for-sale investments		-	-	-	(20,168)	-	-	**(20,168)**	(8,190)	**(28,358)**
Total recognised income and expense for the year		**-**	**-**	**-**	**(36,907)**	**(468,826)**	**51,507**	**(454,226)**	**1,326**	**(452,900)**
Dividends to shareholders of the parent company	18	-	-	-	-	-	(22,258)	**(22,258)**	-	**(22,258)**
Dividends to minority shareholders in the Group's subsidiaries		-	-	-	-	-	-	**-**	(2,008)	**(2,008)**
Decrease in minority interest due to increase in ownership in subsidiaries	4	-	-	-	-	-	(30,887)	**(30,887)**	(10,073)	**(40,960)**
Increase in minority interest due to change of shareholding structure of subsidiaries	4	-	-	-	-	-	(1,376)	**(1,376)**	1,376	**-**
Issuance of shares from treasury shares under share option plan	18	-	(1,510)	5,523	-	(307)	-	**3,706**	-	**3,706**
Balance at 31 December 2008		**6,871**	**2,116,655**	**(724,927)**	**-**	**(43,406)**	**1,401,540**	**2,756,733**	**37,808**	**2,794,541**

The accompanying notes are an integral part of these consolidated financial statements.

1. GENERAL

Organisation

Open Joint Stock Company "Polyus Gold" (the "Company" or "Polyus Gold") was incorporated in Moscow, Russian Federation, on 17 March 2006. The Company was formed as a result of a spin-off from OJSC "Mining and Metallurgical Company Norilsk Nickel" ("Norilsk Nickel"). The principal activities of the Company and its subsidiaries (the "Group") are the extraction, refining and sale of gold. Mining and processing facilities of the Group are located in the Krasnoyarsk and Irkutsk regions and the Sakha Republic of the Russian Federation. The Group also performs research, exploration and development works, primarily at the Natalka field located in the Magadan region and the Nezhdaninskoe field located in the Sakha Republic. Further details regarding the nature of the business and of the significant subsidiaries of the Group are presented in note 29.

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS"). IFRS include standards and interpretations approved by the International Accounting Standards Board ("IASB"), including International Accounting Standards ("IAS") and interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC").

Basis of presentation

The entities of the Group maintain their accounting records in accordance with the laws, accounting and reporting regulations of the jurisdictions, in which they are incorporated and registered. The accounting principles and financial reporting procedures in these jurisdictions may differ substantially from those generally accepted under IFRS. Accordingly, such financial statements have been adjusted to ensure that the consolidated financial statements are presented in accordance with IFRS.

The consolidated financial statements of the Group are prepared on the historical cost basis, except for mark-to-market valuation of certain financial instruments, in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

The consolidated financial statements for the year ended 31 December 2007 contained herein as comparative financial information represent amounts that were restated as reflected in the separate financial statements for the year ended 31 December 2007 that were issued on 3 February 2009.

Adoption of new and revised International Financial Reporting Standards

In the preparation of the consolidated financial statements, the Group has adopted all of the new and revised International Financial Reporting Standards that are relevant to its operations and effective for the annual reporting periods reported herein.

The following amendments issued by IASB and interpretations issued by IFRIC that were effective for the current period: Amendment to IAS 39 *Financial instruments: Recognition and Measurment* for reclassifications of financial assets; Amendment to IFRS 7 *Financial Instruments – Disclosures* for disclosures relating to reclassifications of financial assets; IFRIC 11 *IFRS 2 – Group and Treasury Share Transactions*; IFRIC 12 *Service Concession Arrangements*; IFRIC 13 *Customer Loyalty Programmes*; IFRIC 14 *IAS 19 – The Limit on a Benefit Asset, Minimum Funding Requirements and their Interaction*; IFRIC 16 *Hedges of a Net Investment in a Foreign Operation*. The adoption of these amendments and interpretations has not led to any changes in the Group's accounting policies or disclosures provided in the consolidated financial statements.

Standards and interpretations in issue but not yet adopted

At the date of approval of the Group's consolidated financial statements, the following new and revised standards and interpretations have been issued, but are not effective for 2008:

Standards and interpretations	**Effective for annual periods beginning on or after**
IAS 1 *Presentation of Financial Statements* (amendment)	1 January 2009
IAS 16 *Property, Plant and Equipment* (amendment)	1 January 2009
IAS 19 *Employee Benefits* (amendment)	1 January 2009
IAS 20 *Government Grants and Disclosure of Government Assistance* (amendment)	1 January 2009
IAS 23 *Borrowing Costs* (amendment)	1 January 2009
IAS 27 *Consolidated and Separate Financial Statements* (amendment)	1 July 2009
IAS 28 *Investments in Associates* (amendment due to revision of IFRS 3)	1 July 2009
IAS 29 *Financial Reporting in Hyperinflationary Economies* (amendment)	1 January 2009
IAS 31 *Interest in Joint Ventures* (amendment due to revision of IFRS 3)	1 July 2009
IAS 32 *Financial Instruments: Presentation* (amendment)	1 January 2009
IAS 36 *Impairment of Assets* (amendment)	1 January 2009
IAS 38 *Intangible Assets* (amendment)	1 January 2009
IAS 39 *Financial Instruments: Recognition and Measurement* (amendment)	1 January 2009
IAS 40 *Investment Property* (amendment)	1 January 2009
IAS 41 *Agriculture* (amendment)	1 January 2009
IFRS 1 *First-time Adoption of International Financial Reporting Standards* (amendment)	1 January 2009
IFRS 2 *Share-based Payment* (amendment)	1 January 2009
IFRS 3 *Business Combinations* (revised on applying the acquisition method)	1 July 2009
IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* (amendment)	1 July 2009
IFRS 8 *Operating Segments*	1 January 2009
IFRIC 15 *Agreements for the Construction of Real Estate*	1 January 2009
IFRIC 17 *Distributions of Non-cash Assets to Owners*	1 July 2009
IFRIC 18 *Transfers of Assets from Customers*	1 July 2009

Management anticipates that all of the above standards and interpretations will be adopted in the Group's consolidated financial statements for the respective periods. The impact of adoption of these standards and interpretations in the preparation of consolidated financial statements in the future periods is currently being assessed by the Group's management.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation

Subsidiaries

The consolidated financial statements of the Group include the financial statements of the Company and its subsidiaries, from the date that control effectively commenced until the date that control effectively ceased. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Minority interest in the net assets of consolidated subsidiaries is identified separately from the Group's equity therein. Minority interest includes interest at the date of the original business combination and minority's share of changes in net assets since the date of the combination. Losses applicable to minority interest in excess of the minority's interest in the subsidiary's net assets are allocated against the interest of the Group except to the extent that a minority has a binding obligation and is able to make an additional investment to cover the losses.

All intra-group balances, transactions and any unrealised profits or losses arising from intra-group transactions are eliminated on consolidation.

Accounting for acquisitions from third parties

Where an investment in a subsidiary is made, any excess of the purchase consideration over the fair value of the identifiable assets, liabilities and contingent liabilities at the date of acquisition is recognised as goodwill.

Goodwill is reviewed for impairment at least annually and if impairment has occurred, it is recognised in the income statement in the period during which the circumstances are identified and is not subsequently reversed. On disposal of a subsidiary or an associate the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Where an investment in a subsidiary is made, any excess of the Group's share in the fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost is recognised in the consolidated income statement immediately.

Functional and presentation currency

The individual financial statements of the Group entities operating in the Russian Federation are prepared in their functional currency, Russian Rouble ("RUR").

Functional currency of subsidiaries of the Group operating in Cyprus and the British Virgin Islands is United States of America Dollar ("USD").

The Group has chosen to present its consolidated financial statements in the USD, as management believes it is a more convenient presentation currency for international users of the consolidated financial statements of the Group. The translation of the financial statements of the Group entities from their functional currencies to the presentation currency is made as follows:

- all assets, liabilities, both monetary and non-monetary are translated at closing exchange rates at the dates of each balance sheet presented;
- all income and expenses in each income statement are translated at the average exchange rates for the years presented;
- resulting exchange differences are included in equity and presented as *Effect of translation to presentation currency* within *Translation reserve*;
- in the statement of cash flows, cash balances at beginning and end of each year presented are translated at exchange rates at the respective dates. All cash flows are translated at the average exchange rates for the years presented, except for significant transactions that are translated at rates on the date of transaction. Resulting exchange differences are presented as *Effect of translation to presentation currency*.

Exchange rates quoted by the Central Bank of the Russian Federation were as follows (RUR to 1 USD):

	2008	2007
31 December	29.3804	24.5462
Average for the year	24.8553	25.5772

Foreign currencies

Transactions in currencies other than the entity's functional currencies (foreign currencies) are recorded at the exchange rates prevailing on the dates of the transactions. At each balance sheet date monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates prevailing at the balance sheet date. Non-monetary items carried at historical cost are translated at the exchange rate prevailing on the date of transaction. Non-monetary items carried at fair value are translated at the exchange rate prevailing on the date on which the most recent fair value was determined. Exchange differences arising from changes in exchange rates are recognised in the income statement.

Property, plant and equipment

Estimated ore reserves

Estimated proven and probable ore reserves reflect the economically recoverable quantities which can be legally recovered in the future from known mineral deposits. The majority of the Group's reserves are estimated in accordance with the JORC code or using the Russian Resource Reporting Code for alluvial gold reserves.

Mineral rights

Mineral rights are recorded as assets when acquired as part of a business combination and are then amortised within mining assets on a straight-line basis over the life of mines based on estimated proven and probable ore reserves.

Exploration and evaluation assets

Exploration and evaluation assets represent capitalised expenditures incurred by the Group in connection with the exploration for and evaluation of gold resources, such as:

- acquisition of rights to explore potentially mineralised areas;
- topographical, geological, geochemical and geophysical studies;
- exploratory drilling;
- trenching;
- sampling; and
- activities in relation to evaluating the technical feasibility and commercial viability of extracting a gold resource.

Exploration and evaluation expenditures are capitalised when it is expected that they will be recouped by future exploitation or sale, and when the exploration and evaluation activities have not reached a stage that permits a reasonable assessment of the existence of commercially recoverable gold reserves. When the technical feasibility and commercial viability of extracting a gold resource are demonstrable, capitalised exploration and evaluation assets are reclassified to mining assets.

Impairment of exploration and evaluation assets

Exploration and evaluation assets are assessed for impairment when facts and circumstances suggest that the carrying amount of an exploration and evaluation asset may exceed its recoverable amount. The following facts and circumstances, among other, indicate that exploration and evaluation assets must be tested for impairment:

- the term of exploration license in the specific area has expired during the reporting period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on further exploration for and evaluation of gold resources in the specific area is neither budgeted nor planned;
- exploration for and evaluation of gold resources in the specific area have not led to the discovery of commercially viable quantities of gold resources and the decision was made to discontinue such activities in the specific area;
- sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

For the purpose of assessing exploration and evaluation assets for impairment, such assets are allocated to cash-generating units, being exploration licence areas.

Any impairment loss is recognised as an expense in accordance with the policy on impairment of tangible assets set out below.

Mining assets

Mining assets are recorded at cost less accumulated amortisation. Mining assets include the cost of acquiring and developing mining properties, pre-production expenditure, mine infrastructure, mineral rights and mining and exploration licenses and the present value of future decommissioning costs.

Mining assets are amortised on a straight-line basis over the life of mines of 7 to 20 years, which is based on estimated proven and probable ore reserves. Amortisation is charged from the date on which a new mine reaches commercial production quantities and is included in the cost of production.

Non-mining assets

Non-mining assets are stated at cost less accumulated depreciation. Depreciation is provided on a straight-line basis over the economic useful lives of such assets at the following annual rates:

- buildings, structures, plant and equipment 2% to 10%;
- transport 9% to 25%;
- other assets 10% to 20%.

Capital construction-in-progress

Capital construction-in-progress comprises costs directly related to mine development, construction of buildings, infrastructure, processing plant, machinery and equipment. Amortisation or depreciation of these assets commences when the assets are placed into commercial production.

Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Assets subject to finance leases are capitalised as property, plant and equipment at the lower of fair value or present value of future minimum lease payments at the date of acquisition, with the related lease obligation recognised at the same value. Assets held under finance leases are depreciated over their estimated economic useful lives or over the term of the lease, if shorter. If there is reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is useful life of the asset.

Finance lease payments are allocated using the effective interest rate method, between the lease finance cost, which is included in interest paid, and the capital repayment, which reduces the related lease obligation to the lessor.

Impairment of tangible assets, other than exploration and evaluation assets

An impairment review of tangible assets is carried out when there is an indication that those assets have suffered an impairment loss. If any such indication exists, the carrying amount of the asset is compared to the estimated recoverable amount of the asset in order to determine the extent of the impairment loss (if any).Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell and value-in-use. If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. The impairment loss is recognised in the income statement immediately, unless the relevant asset is carried at revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the original carrying amount that would have been determined had no impairment loss been recognised in prior periods.

A reversal of an impairment loss is recognised in the income statement immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Deferred stripping costs

The Group accounts for stripping costs incurred using the average life-of-mine stripping ratio. The method assumes that stripping costs incurred during the production phase to remove waste ore are deferred and charged to operating costs on the basis of the average life-of-mine stripping ratio. The average stripping ratio is calculated as the number of cubic meters of waste material removed per ton of ore mined based on proven and probable reserves. The average life-of-mine ratio is revised annually or when circumstances change in the mine’s pit design or in the technical or economic parameters impacting the reserves. Changes to the life-of-mine ratio are accounted prospectively as changes in accounting estimates.

Stripping costs incurred in the period are deferred to the extent that the current period stripping ratio exceeds the expected life-of-mine ratio. Such deferred costs are then charged against profit and loss to the extent that, in subsequent periods, the current ratio falls short of the life-of-mine ratio.

The cost of excess stripping is capitalised as deferred stripping costs and forms part of the total investment in the relevant cash-generating unit, which is reviewed for impairment if events or a change in circumstances indicate that the carrying value may not be recoverable. Amortization of deferred stripping costs is included in cost of gold sales.

Deferred expenditures

Certain of the Group's surface (alluvial) mining operations are located in regions with the extreme weather conditions, and gold at these locations can only be mined during certain months of the year. Costs incurred in preparation for future seasons, usually during winter months, are deferred until summer of the following year. Such expenditures mainly include excavation costs and mine specific administration costs, and are recognised on the balance sheet within other current assets.

Inventories

Refined gold

Gold is measured at the lower of net production cost and net realisable value. The net cost of production per unit of gold is determined by dividing total production cost, by the saleable mine output of gold.

Production costs include consumables and spares, labour, tax on mining, utilities, outsourced mining services, refining costs, sundry costs, amortisation and depreciation of operating assets, adjustments for deferred stripping costs capitalised, change in provision for land restoration and change in gold-in-process and refined gold.

Gold-in-process and stockpiles

Costs that are incurred in or benefit the production process are accumulated as stockpiles and gold in process. Net realisable value tests are performed at least annually and represent the estimated future sales price of the product, based on prevailing spot metal prices, less estimated costs to complete production and bring the product to sale.

Gold-in-process is valued at the net unit cost of production based on the percentage of completion method.

Stockpiles are measured by estimating the number of tonnes added and removed from the stockpile, the number of contained gold ounces based on assay data, and the estimated recovery percentage based on the expected processing method. Stockpiles are verified by periodic surveys.

Stores and materials

Stores and materials consist of consumable stores and are valued at the weighted average cost less provision for obsolete and slow-moving items.

Financial assets

Financial assets are recognised on trade date where the purchase or sale of a financial asset is under a contract whose terms require delivery of the financial asset within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

The Group's financial assets are classified into the following categories:

- financial assets as at fair value through profit or loss ("FVTPL");
- held-to-maturity investments;
- available-for-sale ("AFS") financial assets; and
- loans and receivables.

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Financial assets at FVTPL

Financial assets are classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in the income statement. Together with any dividend or interest earned on the financial asset. Fair value is determined in the manner described in note 27.

Held-to-maturity investments

Promissory notes with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortised cost using the effective interest method less impairment, with revenue recognised on an effective yield basis.

Available-for-sale financial assets

Available-for-sale financial assets mainly include investments in listed and unlisted shares.

Listed shares held by the Group that are traded in an active market are stated at fair value. Fair value of AFS is determined as follows:

- the fair value of AFS financial assets with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- the fair value of other AFS financial assets are determined in accordance with generally accepted pricing model based on discounted cash flow analysis using prices from observable current market transactions.

Gains and losses arising from changes in fair value are recognised directly in equity in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in the consolidated income statement. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investment revaluation reserve is included in the consolidated income statement for the period.

Dividends on available-for-sale equity instruments are recognised in the consolidated income statement when the Group's right to receive the dividends is established.

The fair value of AFS monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the exchange rate at the balance sheet date. The change in fair value attributable to translation differences that result from a change in amortised cost of the asset is recognised in the income statement, and other changes are recognised in equity.

Loans and receivables

Loans and receivables with fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account.

When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in the income statement.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised. In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised directly in equity.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments other than those financial assets designated as at FVTPL.

Financial liabilities

Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs, and subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances, cash deposits and highly liquid investments with original maturities of three months or less, which are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

Employee benefit obligations

Remuneration to employees in respect of services rendered during a reporting period is recognised as an expense in that reporting period.

The Group contributes to the Pension Fund of the Russian Federation on behalf of all its employees. These contributions are recognised in the income statement when employees have rendered services entitling them to the contribution.

The Group does not maintain any separate retirement benefit plans.

Income tax

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

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets arising from deductible temporary differences associated with such investments are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax are recognised as an expense or income in the income statement, except when they relate to items credited or debited directly to equity, in which case the tax is also recognised directly in equity, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is taken into account in calculating goodwill or determining the excess of the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over cost.

Revenue recognition

Gold sales revenue

Revenue from the sale of refined gold is recognised when the risks and rewards of ownership are transferred to the buyer. Gold sales revenue represents the invoiced value of gold shipped to customers, net of value-added tax. Revenues from sale of by-products are netted off against production costs.

Other revenue

Other revenue consists of sales of electricity, transportation, handling and warehousing services, and other. Revenue from sale of goods is recognised when significant risks and rewards of ownership are transferred to the buyer in accordance with the shipping terms specified in the sales agreements. Revenue from service contracts are recognised when the services are rendered.

Operating leases

The lease of assets under which all the risks and benefits of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are recognised in the income statement in the period in which they are due in accordance with lease terms.

Dividends

Dividends and related taxation thereon are recognised as a liability in the period in which they have been declared and become legally payable.

Retained earnings legally distributable by the Company are based on the amounts available for distribution in accordance with the applicable legislation and as reflected in the statutory financial statements of the individual entities of the Group. These amounts may differ significantly from the amounts calculated on the basis of IFRS.

Segment information

The Group predominantly operates in a single business segment, being mining and refining of gold. The Group's production facilities are based in the Russian Federation. Therefore, business activities are subject to the same risks and returns, and are addressed in the consolidated financial statements as one reportable segment.

Environmental obligations

Environmental obligations include decommissioning and land restoration costs.

Future decommissioning costs, discounted to net present value, are capitalised and corresponding decommissioning obligations raised as soon as the constructive obligation to incur such costs arises and the future decommissioning cost can be reliably estimated. Decommissioning assets are amortised on a straight-line basis over the life of mine. The unwinding of the decommissioning obligation is included in the income statement as finance costs. Decommissioning obligations are periodically reviewed in light of current laws and regulations, and adjustments made as necessary with correspondence to property, plant and equipment.

Provision for land restoration, representing the cost of restoring land that arises when environmental disturbance is caused by the development or ongoing production of a mining property, is estimated at the net present value of the expenditures expected to settle the obligation. Change in provision and unwinding of discount on land restoration are recognised to the consolidated income statement and included in cost of production.

Ongoing restoration costs are expensed when incurred.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Preparation of the consolidated financial statements in accordance with IFRS requires the Group's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The determination of estimates requires judgments which are based on historical experience, current and expected economic conditions, and all other available information. Actual results could differ from those estimates.

The most significant areas requiring the use of management estimates and assumptions relate to recent volatility in global and Russian financial markets; useful economic lives of property, plant and equipment; deferred stripping costs; recognition of exploration and evaluation assets; impairment of tangible assets; calculation of allowances; environmental obligations, renewal of a license and income taxes.

Recent volatility in global and Russian financial markets

In recent months a number of major economies around the world have experienced volatile capital and credit markets. A number of major global financial institutions have either been placed into bankruptcy, taken over by other financial institutions and/or supported by government funding. As a consequence of the recent market turmoil in capital and credit markets both globally and in Russia, notwithstanding any potential economic stabilisation measures that may be put into place by the Russian Government, there exists as at the date these consolidated financial statements are authorised for issue economic uncertainties surrounding the continual availability, and cost of credit both for the Group and its counterparties, the potential for economic uncertainties to continue in the foreseeable future and, as a consequence, the potential that certain assets may be not be recovered at their carrying amount in the ordinary course of business. In addition, in development of certain of the Group's critical estimates and areas of critical judgement, management uses projected cash flows. These projected cash flows are dependent on various assumptions including historical experience and growth rates. As a result of the volatility in the global and Russian financial markets, management's estimates may change and result in a significant impact on the Group.

Useful economic lives of property, plant and equipment

The Group's mining assets, classified within property, plant and equipment, are amortised using the straight-line method over life of mine based on proven and probable ore reserves. When determining life of mine, assumptions that were valid at the time of estimation, may change when new information becomes available.

The factors that could affect estimation of life of mine include the following:

- change of estimates of proven and probable ore reserves;
- the grade of mineral reserves varying significantly from time to time;
- differences between actual commodity prices and commodity price assumptions used in the estimation of ore reserves;
- unforeseen operational issues at mine sites; and
- changes in capital, operating mining, processing and reclamation costs, discount rates and foreign exchange rates possibly adversely affecting the economic viability of ore reserves.

Any of these changes could affect prospective amortisation of mining assets and their carrying value.

Non-mining property, plant and equipment are depreciated on a straight-line basis over their useful economic lives. Management periodically reviews the appropriateness of assets' useful economic lives. The review is based on the current condition of the assets and the estimated period during which they will continue to bring economic benefit to the Group.

Deferred stripping costs

The Group defers stripping costs incurred during the production stage of its open-pit operations, on the basis of the average life-of-mine stripping ratio.

The factors that could affect capitalisation and expensing of deferred stripping costs include the following:

- change of estimates of proven and probable ore reserves;
- changes in mining plans in the light of additional knowledge and change in mine's pit design, technical or economic parameters; and
- changes in estimated ratio of the number of cubic meters of waste material removed per ton of ore mined.

Exploration and evaluation assets

Management's judgment is involved in the determination of whether the expenditures which are capitalised as exploration and evaluation assets will be recouped by future exploitation or sale. Determining this, management estimates the possibility of finding recoverable ore reserves related to a particular area of interest. However these estimates are subject to significant uncertainties. The Group is involved in exploration and evaluation activities, and some of its licensed properties contain gold reserves under the definition of ore reserves under internationally recognised reserve reporting methodology. A number of licensed properties have no resource delineation. Many of the factors, assumptions and variables involved in estimating resources are beyond the Group's control and may prove to be incorrect over time. Subsequent changes in gold resources estimates could impact the carrying value of exploration and evaluation assets.

Impairment of tangible assets

The Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets are impaired. In making the assessment for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash-generating unit. Management necessarily applies its judgment in allocating assets that do not generate independent cash flows to appropriate cash-generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. Subsequent changes to the cash-generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets.

Allowances

The Group creates allowances for doubtful debts to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful debts, management bases its estimates on the current overall economic conditions, the aging of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms. Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful debts recorded in the consolidated financial statements.

Environmental obligations

The Group's mining and exploration activities are subject to various environmental laws and regulations. The Group estimates environmental obligations based on the management's understanding of the current legal requirements in the various jurisdictions, terms of the license agreements and internally generated engineering estimates. Provision is made, based on net present values, for decommissioning and land restoration costs as soon as the obligation arises. Actual costs incurred in future periods could differ materially from the amounts provided. Additionally, future changes to environmental laws and regulations, life of mine estimates and discount rates could affect the carrying amount of this provision.

Renewal of a license

The Group's geological research license for Kyutchus field expires on 31 October 2009. If the license is not renewed the Group will have to write off costs of USD 18,563 thousand incurred in connection with this project as at 31 December 2008. The consolidated financial statements are prepared based on management's expectation that either the term of this license will be extended, or the Group will obtain an exploration and production license for the same area.

Income taxes

The Group is subject to income taxes in numerous jurisdictions. Significant judgment is required in determining the worldwide provision for income taxes due to the complexity of legislation. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

Deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. The estimation of that probability includes judgments based on the expected performance. Various factors are considered to assess the probability of the future utilisation of deferred tax assets, including past operating results, operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected.

(in thousands of US Dollars)

4. INCREASE OF OWNERSHIP IN SUBSIDIARIES

OJSC "Matrosov Mine"

On 7 September 2007, the Group acquired 100% of additional shares issued by OJSC "Matrosov Mine" for a cash consideration of USD 72,085 thousand (at 7 September 2007 exchange rate), bringing its ownership in the company from 93.3% to 94.8%. This transaction resulted in an increase of minority interest by USD 2,171 thousand.

During 2008, the Group has acquired the remaining shares of Matrosov mine from minority shareholders for cash consideration of USD 38,909 thousand, bringing its ownership to 100%. This transaction resulted in a decrease of minority interest by USD 9,292 thousand.

OJSC "Aldanzoloto GRK"

During 2008, the Group has acquired the remaining shares of OJSC "Aldanzoloto GRK" from minority shareholders for cash consideration of USD 247 thousand, bringing its ownership to 100%. This transaction resulted in a decrease of minority interest by USD 781 thousand.

CJSC "ZDK Lenzoloto"

During 2008, the Group acquired 100% of additional shares issued by CJSC "ZDK Lenzoloto" for a cash consideration of USD 24,728 thousand, bringing its ownership in the company from 64.1% to 66.2%. This transaction resulted in an increase of minority interest by USD 1,376 thousand.

5. COST OF GOLD SALES

	2008	**2007**
Cash operating costs	587,332	442,224
Consumables and spares	239,522	200,601
Labour	207,403	144,008
Tax on mining	72,588	51,138
Utilities	26,646	23,340
Outsourced mining services	15,105	8,826
Refining costs	5,383	3,569
Sundry costs	20,685	10,742
Amortisation and depreciation of operating assets	98,999	87,196
Deferred stripping costs capitalised	(112,804)	(68,065)
(Decrease)/increase in provision for land restoration	(8,530)	482
Increase in gold-in-process and refined gold	(6,879)	(12,621)
Total	**558,118**	**449,216**

(in thousands of US Dollars)

6. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	2008	2007
Salaries	73,742	76,291
Taxes other than mining and income taxes	18,318	20,724
Professional services	13,321	8,288
Depreciation	3,782	3,969
Share option plan	-	132,548
Other	25,797	19,956
Total	**134,960**	**261,776**

7. OTHER EXPENSES, NET

	2008	2007
Donations	7,135	3,868
Change in allowance for reimbursable value added tax	7,078	(3,641)
Impairment of property, plant and equipment	1,831	313
Loss on disposal of property, plant and equipment	548	6,421
Other	464	3,368
Total	**17,056**	**10,329**

8. FINANCE COSTS

	2008	2007
Unwinding of discount on decommissioning obligations (refer to note 20)	4,329	3,975
Interest on borrowings	88	2,654
Total	**4,417**	**6,629**

9. (LOSS)/INCOME FROM INVESTMENTS

	2008	2007
(Loss)/income from financial assets at fair value through profit and loss		
(Loss)/income from investments in listed companies held for trading	(178,377)	9,898
Loss from available-for-sale investments		
Gain on disposal of available-for-sale investments	13,770	-
Impairment of available-for-sale investments	(100,090)	-
Income from held-to-maturity investments		
Interest income on promissory notes	5,493	6,813
Income from loans given		
Interest income on bank deposits	31,646	30,836
Interest income on loans under repurchase agreements	9,967	13,844
Other	-	146
Total	**(217,591)**	**61,537**

(in thousands of US Dollars)

10. INCOME TAX

	2008	2007
Current tax expense	85,003	77,017
Deferred tax (benefit)/expense	(22,893)	8,282
Total	**62,110**	**85,299**

The corporate income tax rates in the countries where the Group has a taxable presence vary from 0% to 24%.

A reconciliation of statutory income tax at the rate effective in the Russian Federation, location of the Group's production entities, to the amount of actual income tax expense recorded in the income statement is as follows:

	2008	2007
Profit before income tax	**122,471**	**177,107**
Income tax at statutory rate of 24%	29,393	42,506
Effect of different tax rates of subsidiaries operating in other jurisdictions	21,089	27,839
(Benefit arising from a previously unrecognised taxable losses of subsidiaries)/taxable losses of subsidiaries not carried forward	(8,929)	10,866
Effect of change in statutory income tax rate	(29,649)	-
Deferred tax asset not recognised on loss from investments	42,810	-
Tax effect of non-deductible expenses and other permanent differences	7,396	4,088
Income tax at effective rate of 51% (2007: 48%)	**62,110**	**85,299**

At 31 December 2008, as a result of the change in income tax rate in the Russian Federation from 24% to 20% that was substantially enacted on 26 November 2008 and that will be effective from 1 January 2009, deferred tax liabilities for all Group's subsidiaries registered on the territory of the Russian Federation have been remeasured by using 20% income statutory tax rate.

(in thousands of US Dollars)

11. PROPERTY, PLANT AND EQUIPMENT

	Exploration and evaluation assets	Mining assets	Non-mining assets	Capital construction-in-progress	Total
Cost					
Balance at 31 December 2006	**133,930**	**1,281,171**	**50,755**	**168,258**	**1,634,114**
Additions	151,457	144,342	7,920	101,865	**405,584**
Transfers	-	88,622	-	(88,622)	**-**
Disposals	-	(30,749)	(896)	(552)	**(32,197)**
Disposed of on disposal of subsidiary	(239)	(765)	(984)	(1)	**(1,989)**
Effect of translation to presentation currency	16,090	101,622	3,944	12,768	**134,424**
Balance at 31 December 2007	**301,238**	**1,584,243**	**60,739**	**193,716**	**2,139,936**
Additions	138,366	104,876	13,734	248,748	**505,724**
Transfers	(181,811)	261,400	-	(79,589)	**-**
Change in decommissioning liabilities	-	(35,491)	-	-	**(35,491)**
Disposals	-	(10,078)	(1,335)	(658)	**(12,071)**
Effect of translation to presentation currency	(42,873)	(310,450)	(11,903)	(57,826)	**(423,052)**
Balance at 31 December 2008	**214,920**	**1,594,500**	**61,235**	**304,391**	**2,175,046**
Accumulated amortisation, depreciation and impairment					
Balance at 31 December 2006	**(119)**	**(219,232)**	**(13,405)**	**(5,753)**	**(238,509)**
Charge for the year	-	(99,244)	(5,991)	-	**(105,235)**
Disposals	-	7,124	234	-	**7,358**
Impairment loss	-	(295)	(18)	-	**(313)**
Disposed of on disposal of subsidiary	122	760	713	1	**1,596**
Effect of translation to presentation currency	(3)	(19,791)	(1,188)	(419)	**(21,401)**
Balance at 31 December 2007	**-**	**(330,678)**	**(19,655)**	**(6,171)**	**(356,504)**
Charge for the year	-	(121,689)	(6,692)	-	**(128,381)**
Disposals	-	4,995	781	-	**5,776**
Impairment loss	-	(1,831)	-	-	**(1,831)**
Effect of translation to presentation currency	-	73,052	4,145	1,016	**78,213**
Balance at 31 December 2008	**-**	**(376,151)**	**(21,421)**	**(5,155)**	**(402,727)**
Net book value					
31 December 2007	**301,238**	**1,253,565**	**41,084**	**187,545**	**1,783,432**
31 December 2008	**214,920**	**1,218,349**	**39,814**	**299,236**	**1,772,319**

(in thousands of US Dollars)

Mining assets at 31 December 2008 included mineral rights of USD 433,112 thousand (31 December 2007: USD 534,451 thousand).

Amortisation and depreciation capitalised during the year ended 31 December 2008 amounted to USD 41,454 thousand (2007: USD 23,169 thousand).

The balance of property, plant and equipment at 31 December 2008 was recorded net of value added tax ("VAT") incurred on acquisition of exploration and evaluation and mining assets of USD 9,188 thousand (31 December 2007: USD 11,824 thousand). This VAT is reimbursable when the respective assets are put into operation. Management of the Group believes that VAT amounts are recoverable in full.

In 2008, the Group reclassified capitalised exploration and evaluation assets related to Natalka, Verninskoe, Blagodatnoe and Titimukhta deposits to mining assets in the amount of USD 181,811 thousand as the works reached a stage that permitted a reasonable assessment the technical feasibility and commercial viability of extracting a gold resource.

Impairment loss recognised in respect of property, plant and equipment for the year ended 31 December 2008 in the amount of USD 1,831 thousand (2007: USD 313 thousand) was attributable to the greater than anticipated wear and tear and certain production assets.

12. INVESTMENTS IN SECURITIES AND OTHER FINANCIAL ASSETS

	2008	2007
Non-current		
Loans advanced	3,772	1,731
Other	323	416
Total non-current	**4,095**	**2,147**
Current		
Available-for-sale equity investments	208,680	400,483
Equity investments in listed companies held for trading	40,628	187,628
Promissory notes receivable	35,928	110,865
Bank deposits	-	280,648
Loans under repurchase agreements	-	201,719
Investment deposit in Rosbank	-	89,575
Total current	**285,236**	**1,270,918**

Financial assets at fair value through profit or loss, carried at fair value

Equity investments in listed companies held for trading were acquired by Managing Company Rosbank (the "Bank"), a related party, on behalf of the Group under Assets management agreements.

Available-for-sale investments, carried at fair value

At 31 December 2008 and 2007, available-for-sale equity investments mainly represented investment in shares of Rosfund, SPC (Cayman Islands) acquired in July 2006. The principal amounts invested by the Group to Rosfund, SPC shares as of 31 December 2008 was USD 308,770 thousand (31 December 2007: USD 360,000 thousand).

(in thousands of US Dollars)

In 2008, the Group sold 14.2% of shares of Rosfund, SPC for USD 35,000 thousand. As a result of this transaction the Group recognised loss in the amount of USD 16,230 thousand in the consolidated income statement.

As a result of recent volatility in global and Russian financial markets, and the uncertainty surrounding long-term recovery, the decline in the fair value of investment in shares of Rosfund, SPC below its cost in 2008 in the amount of USD 100,090 thousand was assessed as not recoverable and was recognised in the consolidated income statement. Fair value of AFS investment in Rosfund, SPC was determined based on quoted market prices of securities, included in the portfolio as at 31 December 2008. Increase in the fair value of this investment in 2007 in the amount of USD 17,287 thousand was recognised directly in equity and reversed in 2008.

In July 2008 a subsidiary of the Group sold 350,000 ordinary shares of OJSC "Vysochaishy" for cash consideration for USD 30,000 thousand. As a result, the Group has recognised realised gain in the consolidated income statement for the same amount.

Investments, carried at amortised cost

Promissory notes at 6.0% per annum are repayable on demand.

Loans and receivables, carried at amortised cost

At 31 Decemeber 2007 bank deposits at 5.75-8.60% per annum were denominated in RUR and matured in November 2008. Bank deposits were fully repaid in 2008.

At 31 December 2007 loans under repurchase agreements, acquired by Managing Company Rosbank, a related party, on behalf of the Group under Assets management agreements, had effective interest rates at 9.88%. These loans were fully repaid in 2008.

At 31 December 2007 investment deposit in Rosbank primarily represented promissory notes purchased and held by the Bank on behalf of the Group. The principal amount of this deposit of USD 83,362 thousand was guaranteed by the Bank. The deposit was fully repaid in 2008.

13. INVENTORIES

	2008	**2007**
Inventories expected to be recovered after twelve months		
Stockpiles	39,063	-
Total	**39,063**	**-**
Inventories expected to be recovered in the next twelve months		
Gold-in-process at net production cost	49,052	54,961
Refined gold at net production cost	1,849	1,283
Total metal inventories	**50,901**	**56,244**
Stores and materials at cost	185,313	170,373
Less: Allowance for obsolescence	(3,213)	(2,408)
Total	**233,001**	**224,209**

(in thousands of US Dollars)

In July 2008 a subsidiary of the Group acquired a license for exploration and gold extraction from stockpiles. Total consideration paid for the license amounted to USD 50,000 thousand. These stockpiles were recognised in the consolidated financial statements as non-current inventories.

14. ACCOUNTS RECEIVABLE

	2008	**2007**
Accounts receivable from third parties	19,593	21,699
Accounts receivable from related parties (refer to note 25)	15	135
	19,608	**21,834**
Less: Allowance for doubtful debts	(4,095)	(8,357)
Total	**15,513**	**13,477**

The Group sells gold produced to three customers on advance payment terms. At 31 December 2008 and 2007 the Group did not have any outstanding amounts receivable in respect of gold sales.

Accounts receivable balance included amounts receivable from the customers of non-mining subsidiaries of the Group in respect of sale of other goods, electricity and other services.

In 2008 the average credit period for the customers of non-mining subsidiaries was 78 days (2007: 30 days). The Group has fully provided for all receivables over 365 days because historical experience is such that receivables that are past due beyond 365 days are generally not recoverable.

The procedure of accepting a new customer includes check by security department for a business reputation, licenses and certifications. At 31 December 2008, the Group's largest customers individually exceeding 5% of the total balance represented 24% (31 December 2007: 55%) of the outstanding balance of accounts receivable.

At 31 December 2008 included in the Group's accounts receivable were balances of USD 3,185 thousand (31 December 2007: USD 4,956 thousand) which were past due but which were not impaired. The Group does not hold any collateral over these amounts. The average age of these receivables was 166 days (31 December 2007: 177 days).

Aging of past due but not impaired receivables:

	2008	**2007**
Less than 90 days	1,054	1,726
91-180 days	720	1,021
181-365 days	1,411	2,209
Total	**3,185**	**4,956**

(in thousands of US Dollars)

Movement in the allowance for doubtful debts:

	2008	2007
Balance at beginning of the year	**8,357**	**7,366**
Receivable balances written off	(3,229)	-
Recognised in income statement	1,008	2,790
Amounts recovered during the year	(1,390)	(2,331)
Effect of translation to presentation currency	(651)	532
Balance at end of the year	**4,095**	**8,357**

15. ADVANCES PAID TO SUPPLIERS

	2008	2007
Advances paid to third parties	14,533	26,088
Advances paid to related parties (refer to note 25)	25	116
Total	**14,558**	**26,204**

At 31 December 2008, advances paid to third parties were presented net of impairment loss of USD 2,085 thousand (31 December 2007: USD 2,459 thousand).

16. OTHER CURRENT ASSETS

	2008	2007
Deferred expenditures	14,938	13,751
Other prepaid taxes	3,556	6,929
Total	**18,494**	**20,680**

Deferred expenditures relate to the preparation for the seasonal alluvial mining activities mostly comprised of excavation costs, general production and specific administration costs.

17. CASH AND CASH EQUIVALENTS

		2008	2007
Bank deposits		278,449	163,005
Current bank accounts	– RUR	25,645	40,113
	– foreign currencies	81,409	690
Other cash and cash equivalents		13,323	22,366
Total		**398,826**	**226,174**

Bank deposits are denominated in RUR, USD and EURO and bear interest of 1.25-17.00% per annum with original maturity within three months.

(in thousands of US Dollars)

18. SHARE CAPITAL

At 31 December 2008 and 2007, authorised, issued and fully paid share capital of the Company comprised of 190,627,747 ordinary shares at par value of RUR 1.

In November 2006 the Company bought 17,146,780 ordinary shares from shareholders for a total consideration of USD 995,557 thousand. Treasury shares which are held by a subsidiary of the Group have been recorded at cost and presented as a separate component in equity.

The immediate shareholders of the Company at 31 December 2008 and 2007 were as follows:

	31 December 2008		31 December 2007	
Shareholders	**Number of shares**	**% held**	**Number of shares**	**% held**
CJSC "ING Bank Evrazia" (nominal)	67,863,260	38.1%	59,982,175	33.7%
NP "National Deposit Centre" (nominal)	56,725,589	31.8%	16,541,447	9.3%
CJSC "Depositary and Clearing Company" (nominal)	16,483,146	9.3%	14,183,547	8.0%
Bristaco Holdings Co. Limited	10,986,194	6.2%	24,866,670	14.0%
OJSC "Rosbank" (nominal)	10,744,173	6.0%	14,795,364	8.3%
Lovenco Holdings Co. Limited	-	-	24,866,670	14.0%
CJSC "KM Invest"	-	-	14,100,053	7.9%
Other	15,348,984	8.6%	8,720,106	4.8%
	178,151,346	**100.0%**	**178,056,032**	**100.0%**

At 29 June 2007 the Company declared dividends of RUR 3.23, or USD 0.13 (at 29 June 2007 exchange rate) per share for the year ended 31 December 2006. Dividends in the amount of USD 21,722 thousand (net of USD 2,147 thousand attributable to treasury shares) were paid to shareholders at 31 August 2007.

At 26 June 2008 the Company declared dividends of RUR 2.95, or USD 0.13 (at 26 June 2008 exchange rate) per share for the year ended 31 December 2007. Dividends in the amount of USD 22,258 thousand (net of USD 1,559 thousand attributable to treasury shares) were paid to shareholders at 31 August 2008.

Share Option Plan

The Group granted 4,765,693 options to management in June 2007 at an exercise price of USD 14 per share. Share options granted under the share option plan are exercisable during three years from the date of grant.

The total fair value of the options granted was USD 132,548 thousand, which was recognised at the date of grant as the options were fully vested. The total fair value was recorded as an expense in selling, general and administrative expenses in the consolidated income statement. Fair value of the options was determined based on an internally developed model which included assumptions that the Group considered appropriate in estimating the fair value of the share-based payment awards.

In July 2007, management exercised 4,575,065 options for a total cash consideration of USD 64,051 thousand. Treasury shares of the Company were issued to management upon exercise of the options resulting in a decrease in treasury shares of USD 265,107 thousand and decrease in additional paid-in-capital of USD 72,496 thousand.

(in thousands of US Dollars)

In February 2008, management exercised 95,314 options for a total cash consideration of USD 1,334 thousand. Treasury shares of the Company were issued to management upon exercise of the options resulting in a decrease in treasury shares of USD 5,523 thousand and decrease in additional paid-in-capital of USD 1,510 thousand. The remaining unsettled options were cancelled in 2008. At 31 December 2008 there were nil shares outstanding under the share option plan (31 December 2007: 190,628 shares).

19. DEFERRED TAX LIABILITIES

The movement in the Group's deferred taxation position was as follows:

	2008	**2007**
Net liability at beginning of the year	**200,609**	**178,860**
Recognised in the income statement	6,756	8,282
Revaluation of available-for-sale investments	7,200	-
Effect of change in statutory income tax rate	(29,649)	-
Recycled from equity on disposal of investments classified as available-for-sale	(7,200)	-
Effect of translation to presentation currency	(29,472)	13,467
Net liability at end of the year	**148,244**	**200,609**

Deferred taxation is attributable to the temporary differences that exist between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. The tax effects of temporary differences that give rise to deferred taxation are presented below:

	2008	**2007**
Property, plant and equipment	132,083	192,537
Deferred stripping costs	32,798	19,695
Investments valuation	-	(377)
Inventory valuation	4,542	4,930
Accrued operating expenses	(20,889)	(13,942)
Valuation of receivables	(290)	(2,234)
Total	**148,244**	**200,609**

The Group did not recognise a deferred tax liability for taxable temporary differences associated with investments in subsidiaries of USD 135,279 thousand (2007: USD 111,591 thousand), because management believes that it is able to control the timing of reversal of such differences and has no intention to reverse them in the foreseeable future.

(in thousands of US Dollars)

20. ENVIRONMENTAL OBLIGATIONS

Decommissioning obligations

	2008	2007
Balance at beginning of the year	**63,656**	**55,480**
New obligations raised	2,784	-
Change in estimate	(38,275)	-
Unwinding of discount on decommissioning obligations (refer to note 8)	4,329	3,975
Effect of translation to presentation currency	(5,674)	4,201
Balance at end of the year	**26,820**	**63,656**

Provision for land restoration

	2008	2007
Balance at beginning of the year	**17,685**	**16,033**
New obligations raised	290	-
Change in estimate	(10,030)	-
Charge to the income statement	1,210	482
Effect of translation to presentation currency	(1,596)	1,170
Balance at end of the year	**7,559**	**17,685**
Total environmental obligations	**34,379**	**81,341**

The principle assumptions used for the estimation of environmental obligations were as follows:

	2008	2007
Discount rates	15.0%	5.7-7.0%
Expected mine closure dates	2010-2050	2010-2050

Present value of cost to be incurred for settlement of environmental obligations was as follows:

	2008	2007
Due from second to fifth year	1,013	1,626
Due from sixth to tenth year	1,216	2,008
Due from eleventh to fifteenth year	29,261	68,226
Due from sixteenth to twentieth year	2,601	1,975
Due thereafter	288	7,506
Total	**34,379**	**81,341**

(in thousands of US Dollars)

21. SHORT-TERM BORROWINGS

	2008	2007
USD-denominated borrowings	-	11,900
RUR-denominated borrowings	-	7,408
Obligations under finance lease	-	1,601
Total	**-**	**20,909**

At 31 December 2007, USD-denominated short-term borrowings included loans from Flemicort Consulting Inc. at the effective interest rate of 8% per annum maturing in January 2008.

At 31 December 2007, RUR-denominated short-term borrowings included loans from Rosbank Management Company, a related party, at the effective interest rate of 7% per annum, secured by investments in listed companies held for trading maturing in January 2008.

22. TRADE PAYABLES

	2008	2007
Trade payables to third parties	17,918	17,753
Trade payables to related parties (refer to note 25)	-	3,898
Total	**17,918**	**21,651**

In 2008 the average credit period for payables was 16 days (2007: 18 days). There was no interest charged on the outstanding payables balance during the credit period. The Group has financial risk management policies in place, which include budgeting and analysis of cash flows and payments schedules to ensure that all amounts payable are settled within the credit period.

The table below summarises the maturity profile of the Group’s trade payables at 31 December 2008 and 2007 based on contractual undiscounted payments:

	2008	2007
Due within three months	16,232	18,919
Due from three to six months	1,113	2,563
Due from six months to twelve months	573	169
Total	**17,918**	**21,651**

(in thousands of US Dollars)

23. OTHER PAYABLES AND ACCRUED EXPENSES

	2008	2007
Other payables, including:		
Wages and salaries payable	37,159	28,069
Other accounts payable	9,908	31,037
Interest payable	-	2,987
Total other payables	**47,067**	**62,093**
Accruals, including:		
Accrued annual leave	18,542	16,482
Unsettled liabilities under share option plan	-	5,357
Total accruals	**18,542**	**21,839**
Total	**65,609**	**83,932**

The table below summarises the maturity profile of the Group's other payables as at 31 December 2008 and 2007 based on contractual undiscounted payments:

	2008	2007
Due within three months	45,850	58,281
Due from three to six months	1,217	3,812
Total	**47,067**	**62,093**

24. OTHER TAXES PAYABLE

	2008	2007
Social taxes	7,063	4,321
Tax on mining	3,781	3,682
Property tax	2,259	3,213
Value added tax	1,417	7,420
Other taxes	2,307	2,551
Total	**16,827**	**21,187**

Contribution to Pension Fund of the Russian Federation for the year ended 31 December 2008 amounted to USD 29,502 thousand (2007: USD 25,816 thousand).

(in thousands of US Dollars)

25. RELATED PARTIES

Related parties include shareholders, entities under common ownership and control with the Group and members of key management personnel. The Company and its subsidiaries, in the ordinary course of business, enter into various sale, purchase and service transactions with related parties. During 2008 and 2007 related party transactions included only transactions with entities under common control. The terms of these transactions would not necessarily be on similar terms had the Group entered into the transactions with third parties.

As a result of change of shareholders of OJSC “MMC Norilsk Nickel”, this company and its subsidiaries are no longer considered related parties for the Group from 24 April 2008. As a result of change of shareholders of Rosbank, this company and its subsidiaries are no longer considered related parties for the Group from 13 February 2008.

During the years ended 31 December 2008 and 2007, Group entered into the following transactions with related parties:

	2008	**2007**
Gold sales	57,753	540,755
Purchase of goods and services	15,392	202,744
Income from investments	567	3,750
Sale of property, plant and equipment	-	16,287
Cash and cash equivalents	-	86,414
Investments in securities and other financial assets	-	201,404
Accounts receivable	15	135
Advances paid to suppliers	25	116
Trade payables	-	3,898
Other payables	6	2,590

The amounts outstanding are unsecured and expected to be settled in cash. No expense has been recognised in the reporting period for bad or doubtful debts in respect of the amounts owed by related parties. All trade payable and receivable balances are expected to be settled on a gross basis.

The Group has Assets management agreements with Managing Company Rosbank, a related party, which acts on behalf of the Group. The principal amounts invested by the Group under these agreements at 31 December 2008 amounted to USD 159,971 thousand (31 December 2007: USD 311,657 thousand) were not guaranteed by the Bank.

Compensation of key management personnel

	2008	**2007**
Short-term employee benefits	8,792	28,377
Share-based payment	-	132,548
Total	**8,792**	**160,925**

(in thousands of US Dollars)

26. CONTINGENCIES

Capital commitments

The Group's budgeted capital expenditures commitments for the year ended 31 December 2009 amounted to USD 270,128 thousand, including USD 97,892 thousand of contractual capital commitments.

Operating leases: Group as a lessee

The land in the Russian Federation on which the Group's production facilities are located is owned by the state. The Group leases land through operating lease agreements, which expire in various years through 2057.

Future minimum lease payments due under non-cancellable operating lease agreements at 31 December 2008 were as follows:

Due within one year	4,339
From one to five years	6,767
Thereafter	14,519
Total	**25,625**

Litigation

The Group has a number of insignificant claims and litigation relating to sales and purchases of goods and services from suppliers. Management believes that none of these claims, individually or in aggregate, will have a material adverse impact on the Group.

Compliance with licenses

The business of the Group depends on the continuing validity of its licenses, particularly subsoil licenses for the Group's exploration and mining operations, the issuance of new licences and the Group's compliance with the terms of its licenses. Russian regulatory authorities exercise considerable discretion in the timing of licenses issuances and renewals and the monitoring of a licensee's compliance with the terms of a license. Requirements imposed by these authorities, including requirements to comply with numerous industrial standards, recruit qualified personnel and subcontractors, maintain necessary equipment and quality control systems, monitor the operations of the Group, maintain appropriate filings and, upon request, submit appropriate information to the licensing authorities, may be costly and time-consuming and may result in delays in the commencement or continuation of exploration or production operations. Accordingly, licenses that may be needed for the operations of the Group may be invalidated or may not be issued or renewed, or if issued or renewed, may not be issued or renewed in a timely fashion.

The legal and regulatory basis for the licensing requirements is subject to frequent change, which increases the risk that the Group may be found in non-compliance. In the event that the licensing authorities discover a material violation by the Group, the Group may be required to suspend its operations or incur substantial costs in eliminating or remediating the violation, which could have a material adverse effect on the Group's business and financial condition.

Insurance

The insurance industry is not yet well developed in the Russian Federation and many forms of insurance protection common in more economically developed countries are not yet available on comparable terms. The Group does not have full insurance coverage for its mining, processing and transportation facilities, for business interruption, or for third party liabilities in respect of property or environmental damage arising from accidents on the Group's property or relating to the Group's operations, other than limited coverage required by law. The Group, as a participant in exploration and mining activities may become subject to liability for risks that can not be insured against, or against which it may elect not to be insured because of high premium costs. Losses from uninsured risks may cause the Group to incur costs that could have a material adverse effect on the Group's business and financial condition.

Taxation contingencies in the Russian Federation

The taxation system in the Russian Federation is characterised by numerous taxes, frequent changes and inconsistent enforcement at federal, regional and local levels. The government of the Russian Federation has commenced a revision of the Russian tax system and passed certain laws implementing tax reform. The new laws reduce the number of taxes and overall tax burden on businesses and simplify tax legislation. However, these new tax laws continue to rely heavily on the interpretation of local tax officials and fail to address many existing problems. Many issues associated with practical implication of new legislation are unclear and complicate the Group's tax planning and related business decisions.

In terms of Russian tax legislation, authorities have a period of up to three years to re-open tax declarations for further inspection. Changes in the tax system that may be applied retrospectively by authorities could affect the Group's previously submitted and assessed tax declarations.

With regards to matters where practice concerning payment of taxes is unclear, management estimated the tax exposure at 31 December 2008 of approximately USD 436 thousand (31 December 2007: USD 347 thousand). This amount had not been accrued at 31 December 2008 as management does not believe the payment to be probable.

Environmental matters

The Group is subject to extensive federal, local environmental controls and regulations in the regions in which it operates. The Group's operations involve the discharge of materials and contaminants into the environment, disturbance of land that could potentially impact on flora and fauna, and give rise to other environmental concerns.

The Group's management believes that its mining and production technologies are in compliance with the existing environmental legislation of the Russian Federation. However, environmental laws and regulations continue to evolve. The Group is unable to predict the timing or extent to which those laws and regulations may change. Such change, if it occurs, may require that the Group modernise technology to meet more stringent standards.

The Group is obliged in terms of various laws, mining licenses and 'use of mineral rights' agreements to decommission mine facilities on cessation of its mining operations and to restore and rehabilitate the environment. Management of the Group regularly reassesses environmental obligations for its operations. Estimations are based on management's understanding of the current legal requirements and the terms of the license agreements. Should the requirements of applicable environmental legislation change or be clarified, the Group may incur additional environmental obligations.

(in thousands of US Dollars)

Russian Federation risk

As an emerging market, the Russian Federation does not possess a fully developed business and regulatory infrastructure including stable banking and judicial systems, which would generally exist in a more mature market economy. The economy of the Russian Federation is characterised by a currency that is not freely convertible outside the country, currency controls, low liquidity levels for debt and equity markets and continuing inflation. As a result operations in the Russian Federation involve risks that are not typically associated with those in more developed markets.

Stability and success of Russian economy depends on the effectiveness of the government economic policies and the continued development of the legal and political systems.

27. RISK MANAGEMENT ACTIVITIES

Capital risk management

The Group manages its capital to ensure that entities of the Group will be able to continue as a going concern while maximising the return to the shareholders through the optimisation of the debt and equity balance. The capital structure of the Group consists of short-term borrowings (disclosed in note 21), cash and cash equivalents (disclosed in note 17) and equity attributable to shareholders of the parent company, comprising issued capital, reserves and retained earnings. As at 31 December 2008 and 2007 cash and cash equivalents balance exceeded borrowings of the Group. Management of the Group believes that currently there are no risks associated with the capital structure.

Major categories of financial instruments

The Group's principal financial liabilities comprise borrowings and trade and other payables. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various financial assets such as accounts receivable and loans advanced, cash and cash equivalents, and promissory notes and other investments.

	2008	**2007**
Financial assets		
Financial assets at fair value through profit or loss, carried at fair value		
Equity investments in listed companies held for trading	40,628	187,628
Held-to-maturity financial assets, carried at amortised cost		
Promissory notes receivable	35,928	110,865
Loans and receivables, including cash and cash equivalents		
Cash and cash equivalents	398,826	226,174
Accounts receivable	15,513	13,477
Loans advanced	3,772	1,731
Bank deposits	-	280,648
Loans under repurchase agreement	-	201,719
Investment deposit in Rosbank	-	89,575
Available-for-sale financial assets, carried at fair value		
Available-for-sale equity investments	208,680	400,483
Total financial assets	**703,347**	**1,512,300**

(in thousands of US Dollars)

	2008	2007
Financial liabilities		
Trade payables	17,918	21,651
Other payables	47,067	62,093
Consideration on acquisition of subsidiaries	-	22,197
Short-term borrowings	-	20,909
Total financial liabilities	**64,985**	**126,850**

The main risks arising from the Group's financial instruments are commodity price, equity investments price, foreign currency, credit and liquidity risks. Due to the fact that the amount of borrowings is not significant, management believes that the Group is not exposed to interest rate risk.

Commodity price risk

Commodity price risk is the risk that the Group's current or future earnings will be adversely impacted by changes in the market price of gold. A decline in gold prices could result in a decrease in profit and cash flows. Management of the Group regularly monitors gold price, market forecasts and believes that current trend of price increase will continue in the future.

The Group does not enter into any hedging contracts or use other financial instruments to mitigate the commodity price risk.

Equity investments price risk

The Group is exposed to equity investments price risk. Presented below is the sensitivity analysis illustrating the Group's exposure to equity investments price risks at the reporting date. Management of the Group has decided to use the range of market prices of 10% higher/lower for the sensitivity analysis as the effect of such variation is considered to be significant and appropriate in the current market situation.

If market prices for equity investments had been 10% higher/lower:

- profit before tax for the year ended 31 December 2008 would increase/decrease by USD 4,063 thousand (2007: USD 18,763 thousand) as a result of changes in fair value of securities held-for-trading ; and
- investment revaluation reserve within equity balance would increase/decrease by USD 20,868 thousand (2007: USD 40,048 thousand) as a result of changes in fair value of securities available-for-sale.

The Group normally places the investments under Assets management agreements with asset management companies who, in turn, utilize a variety of risk management activities in relation to the investments.

Foreign currency risk

Currency risk is the risk that the financial results of the Group will be adversely affected by changes in exchange rates to which the Group is exposed. The Group undertakes certain transactions denominated in foreign currencies. The majority of the Group's revenues are denominated in USD, whereas the majority of the Group's expenditures are denominated in RUR, accordingly, operating profits are adversely impacted by appreciation of RUR against USD. In assessing this risk management takes into consideration changes in gold price. In 2007 favourable changes in market price of gold mitigated the adverse effect of appreciation of RUR against USD.

(in thousands of US Dollars)

The carrying amounts of monetary assets and liabilities denominated in foreign currencies other than functional currencies of the individual Group entities at 31 December 2008 and 2007 were as follows:

	Assets		**Liabilities**	
	2008	**2007**	**2008**	**2007**
USD	499,415	35,764	1,108	81,234
EURO	40,312	-	3,542	-
Total	**539,727**	**35,764**	**4,650**	**81,234**

Currency risk is monitored on a monthly basis by performing sensitivity analysis in order to verify that the potential loss is at an acceptable level.

The table below details the Group's sensitivity to changes of exchange rates of the RUR to USD and EURO by 10% which is the sensitivity rate used by the Group for internal reporting purposes. The analysis was applied to monetary items at the balance sheet dates denominated in respective currencies.

	2008	**2007**
Profit or loss (RUR to USD)	49,831	(4,547)
Profit or loss (RUR to EURO)	3,677	-

Credit risk

Credit risk is the risk that a customer may default or not meet its obligations to the Group on a timely basis, leading to financial losses to the Group. Credit risk arises from cash and cash equivalents, deposits with banks, loans advanced, promissory notes and trade and other receivables.

Prior to dealing with new counterparty, management assesses the credit worthiness and liquidity of potential customer. Information available from the major rating agencies is used in evaluating the creditworthiness of foreign banks. The eligible counterparty should have rating above A level. For Russian banks the credit limits are established using financials analysis and the overall market experience. Bank should be solvent, liquid and have efficient system of risk management.

Although the Group sells all the gold produced to three customers, the Group is not economically dependant on these customers because of the high level of liquidity in the gold commodity market. Buyers of gold are required to make advance payments, therefore credit risk related to trade receivables is minimal. At 31 December 2008 and 2007, the Group did not have any outstanding trade receivables for gold sales.

Other receivables include amounts receivable from the customers of non-mining subsidiaries of the Group in respect of sale of other goods, electricity and other services. The procedures of accepting a new customer include check by a security department and responsible on-site management for a business reputation, licenses and certification, credit worthiness and liquidity.

The Group has a concentration of cash and cash equivalents with a related party commercial bank, that at 31 December 2008 represented nil per cent (31 December 2007: 38 %) of total cash and cash equivalents.

Management of the Group believes that there is no other significant concentration of credit risk.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due. The Group's liquidity position is carefully monitored and managed. The Group manages liquidity risk by maintaining detailed budgeting, cash forecasting process and matching the maturity profiles of financial assets and liabilities to help ensure that it has adequate cash available to meet its payment obligations.

The maturity profile of the Group's financial liabilities at 31 December 2008 and 2007 based on contractual payments is presented in notes 22 and 23.

Fair value of financial instruments

The fair value of financial assets and liabilities is determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- the fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing model based on discounted cash flow analysis using prices from observable current market transactions.

Management believes that the carrying values of financial assets (refer to notes 12, 14 and 17) and financial liabilities (refer to notes 21, 22 and 23) recorded at amortised cost in the consolidated financial statements approximate their fair values due to their short-term nature.

28. EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

Agreement with Kinross Gold

At 26 January 2009, the Group signed an agreement with Kinross Gold Corporation on intention and possible set-up of a new company for joint-development of Nezhdaninskoye deposit. The final decision will be made based on the results of feasibility studies that are expected to be performed within 18 months. The shares of the Group and Kinross Gold Corporation in the new company in case of positive decision would be 51% and 49%, respectively.

(in thousands of US Dollars)

29. INVESTMENTS IN SIGNIFICANT SUBSIDIARIES

Subsidiaries	Country of incorporation	Nature of business	Effective % held[1] 2008	2007
CJSC "Gold Mining Company Polyus"	Russian Federation	Mining	100.0	100.0
OJSC "Aldanzoloto GRK"	Russian Federation	Mining	100.0	99.4
OJSC "Lenzoloto"	Russian Federation	Market agent	64.1	64.1
LLC "Lenskaya Zolotorudnaya Company"	Russian Federation	Market agent	100.0	100.0
CJSC "ZDK Lenzoloto"	Russian Federation	Mining	66.2	64.1
CJSC "Lensib"	Russian Federation	Mining	40.4	39.1
CJSC "Svetliy"	Russian Federation	Mining	55.6	53.8
CJSC "Marakan"	Russian Federation	Mining	55.6	53.8
CJSC "Dalnaya Taiga"	Russian Federation	Mining	54.3	52.6
CJSC "Sevzoto"	Russian Federation	Mining	43.0	41.7
CJSC "GRK Sukhoy Log"	Russian Federation	Mining	100.0	100.0
OJSC "Matrosov Mine"	Russian Federation	Mining (development stage)	100.0	94.8
CJSC "Tonoda"	Russian Federation	Mining (exploration stage)	100.0	100.0
OJSC "Pervenets"	Russian Federation	Mining (development stage)	100.0	100.0
OJSC "South-Verkhoyansk Mining Company"	Russian Federation	Mining (exploration stage)	100.0	100.0
OJSC "Polyus Geologorazvedka" [2]	Russian Federation	Geological research	100.0	100.0
Polyus Exploration Ltd. [2]	British Virgin Islands	Geological research	100.0	100.0
Jenington International Inc.	British Virgin Islands	Market agent	100.0	100.0
Polyus Investments Ltd.	Cyprus	Market agent	100.0	100.0

[1] Effective % held by the Company, including holdings by other subsidiaries of the Group
[2] Established by the Group in 2007