

TGC-4 GROUP

**COMBINED AND CONSOLIDATED FINANCIAL STATEMENTS
PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)
FOR THE YEARS ENDED 31 DECEMBER 2006 AND 31 DECEMBER 2005**

INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of Open Joint-Stock Company Territorial Generation Company 4 (JSC "TGC-4"):

We have audited the accompanying combined and consolidated financial statements of JSC "TGC-4" and its subsidiaries (the "TGC-4 Group") which comprise the combined and consolidated balance sheet as at 31 December 2006 and 31 December 2005, the combined and consolidated statement of operations, combined and consolidated statement of changes in equity and combined and consolidated statement of cash flows for the two years then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the accompanying combined and consolidated financial statements present fairly, in all material respects, the financial position of the TGC-4 Group as at 31 December 2006 and 31 December 2005, and its financial performance and its cash flows for the two years then ended in accordance with International Financial Reporting Standards.

INDEPENDENT AUDITOR'S REPORT

Emphasis of Matter

Without qualifying our opinion, we draw your attention to Notes 1 and 7 to the accompanying combined and consolidated financial statements. The Government of the Russian Federation has an ultimate controlling interest in the Group and Governmental economic and social policies affect the Group's financial position, results of operations and cash flows.

Without qualifying our opinion, we draw attention to Note 3 of the accompanying combined and consolidated financial statements. These combined and consolidated financial statements include carved out revenues and expenses of predecessor legal entities that had other business activities, related to periods: from 1 to 11 January 2005 of electricity and heat generating divisions within OJSC Lipetskenergo, OJSC Tambovenergo and OJSC Ryazanenergo; from 1 to 31 January 2005 – of electricity and heat generating divisions within OJSC Kurskenergo and OJSC Smolenskenergo; from 1 January to 31 March 2005 – OJSC Tulenergo and OJSC Oryelenergo. Because of the various determinations used in carving out such revenues and expenses, as described in Note 3 and elsewhere in these combined and consolidated financial statements, those revenues and expenses related to the electricity and heat generation operations within predecessor legal entities may not be indicative of revenues expected to be earned and costs expected to be incurred on a prospective basis for the electricity and heat generation operations within the TGC-4 Group as a separate business and, as such, these combined and consolidated financial statements may not be indicative of future results of operations and trends.

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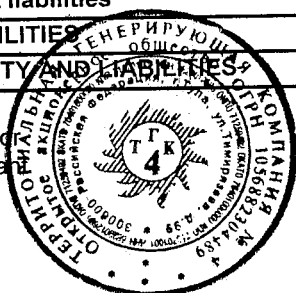
Moscow, Russian Federation
25 September 2007

TGC-4 GROUP

Combined and Consolidated Balance Sheet as at 31 December 2006 and 31 December 2005
(in thousands of Russian Roubles)

	Notes	31 December 2006	31 December 2005
ASSETS			
Non-current assets			
Property, plant and equipment	8	25,302,266	9,440,667
Intangible assets		6,421	8,474
Goodwill	5	642,794	-
Investments in associates	5	34,394	426,360
Deferred tax assets	20	581,506	446,127
Other non-current assets	9	571,673	209,484
Total non-current assets		27,139,054	10,531,112
Current assets			
Cash	10	116,841	207,314
Accounts receivable and prepayments	12	2,051,522	1,816,883
Inventories	11	1,980,630	898,460
Short-term investments		12,406	6,382
Other current assets		5,170	5,269
		4,166,569	2,934,308
Non-current assets held for sale	6	66,087	42,551
Total current assets		4,232,656	2,976,859
TOTAL ASSETS		31,371,710	13,507,971
EQUITY AND LIABILITIES			
Share capital			
Ordinary shares (nominal value)		13,212,020	10,000
Preference shares		752,729	-
Merger reserve		(1,807,993)	4,749,463
Share premium		959,867	-
Retained earnings		7,169,489	93,347
Equity attributable to shareholders of TGC-4		20,286,112	4,852,810
Minority interest		42,608	5,041,674
TOTAL EQUITY	13	20,328,720	9,894,484
Non-current liabilities			
Deferred tax liabilities	20	3,275,391	418,136
Non-current debt	15	3,089,297	133,809
Long-term tax payables		-	-
Other non-current liabilities		53,758	9,409
Pension liabilities	17	642,978	358,047
Total non-current liabilities		7,061,424	919,401
Current liabilities			
Current debt and current portion of non-current debt	16	2,386,129	961,145
Accounts payable and accruals	18	1,329,171	1,152,038
Current income tax liabilities	20	40,893	136,137
Other taxes payable	19	194,899	434,825
		3,951,092	2,684,145
Liabilities directly associated with non-current assets held for sale	6	30,474	9,941
Total current liabilities		3,981,566	2,694,086
TOTAL LIABILITIES		11,042,990	3,613,487
TOTAL EQUITY AND LIABILITIES		31,371,710	13,507,971

General Director
Chief Accountant



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G.A. Kochetkov
I.A. Lapitskaya
25 September 2007

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

TGC-4 GROUP

Combined and Consolidated Statement of Operations for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

	Note	Year ended 31 December 2006	Year ended 31 December 2005
Revenue	21	18,971,940	16,314,515
Cost of sales	22	(17,933,090)	(15,588,907)
Gross profit		1,038,850	725,608
Other operating income		103,364	226,714
Income from impairment reversal	8	10,520,508	-
Operating profit		11,662,722	952,322
Finance income		8,447	-
Finance costs	23	(429,896)	(87,796)
Share of result of associates		45,750	16,979
Profit/(loss) before income tax		11,287,023	881,505
Income tax expense	20	(2,880,469)	(370,174)
Profit/(loss) for the year from continuing operations		8,406,554	511,331
<i>Discontinued operations:</i>			
Profit/(loss) for the year from discontinued operations	6	10,057	(2,614)
Profit/(loss) for the year		8,416,611	508,717
Attributable to:			
The Group shareholders		8,416,611	249,272
Minority interest		-	259,445
Earnings / (loss) per ordinary share for loss attributable to the Group shareholders – basic and diluted (in Russian Roubles per share)			
	14	0.021	0.040

General Director

Chief Accountant



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G.A. Kochetkov

I.A. Lapitskaya

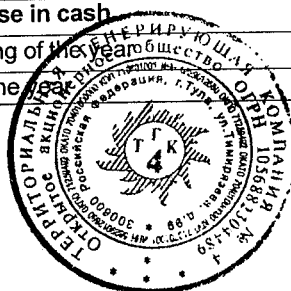
25 September 2007

TGC-4 GROUP
Combined and Consolidated Statement of Cash Flows for the years ended 31 December 2006 and
31 December 2005
(in thousands of Russian Roubles)

	Note	Year ended 31 December 2006	Year ended 31 December 2005
CASH FLOW FROM OPERATING ACTIVITIES:			
Profit before tax		11,287,023	881,505
Profit/(loss) for the year from discontinued operations		10,057	(2,614)
Adjustments for other non-cash items:			
Depreciation	8, 22	771,092	1,213,241
Reversal of impairment of property, plant and equipment	8	(10,520,508)	-
Loss on disposal of subsidiary		7,783	405,069
Share of profits of associate		(45,750)	(16,979)
Accounts payable written off		(4,991)	(18,673)
Interest expense	23	374,792	102,982
Interest income		(8,447)	-
Effect of discounting	23	18,961	(52,904)
Profit/Loss on disposal of property, plant and equipment	8	35,139	(14,889)
Pension interest expense	17	36,143	37,718
Pension operating expenses/accruals	17	83,240	(53,501)
Carve out influence		-	(466,760)
Other non-cash items		4,154	(160,488)
Operating cash flows before working capital changes and income tax paid		2,048,688	1,853,707
Working capital changes:			
(Increase) / decrease in accounts receivable and prepayments		222,029	(614,558)
(Increase) / decrease in non-current assets		(376,945)	48,278
(Increase) / decrease in inventories		(945,222)	68,549
(Increase) / decrease in other current assets		(10,451)	327
Increase / (decrease) in accounts payable and accruals		188,223	8,907
Increase / (decrease) taxes payable other than profits tax		(268,259)	478,324
Increase / (decrease) other long-term payables		44,349	7,082
Income tax paid		(521,390)	(234,760)
Interest received		8,447	-
Interest paid		(301,384)	(100,940)
Net cash generated from operating activities		88,085	1,514,916
CASH FLOW FROM INVESTING ACTIVITIES:			
Purchase of property, plant and equipment and other non-current assets		(2,451,171)	(1,669,885)
Proceeds from sale of property, plant and equipment and other non-current assets		28,827	28,759
Acquisition of subsidiary, net of cash acquired		163,923	-
Disposal of subsidiaries, net of cash disposed		151,907	-
Proceeds from ST financial investments sales		51,444	99,145
Purchase of ST financial investments		(57,468)	(105,527)
Net cash used in investing activities		(2,112,538)	(1,647,508)
CASH FLOW FROM FINANCING ACTIVITIES:			
Proceeds from borrowing		17,500,019	5,707,153
Repayment of debts		(15,157,221)	(5,260,251)
Repayment of financial lease		(256,513)	-
Dividend paid		(152,305)	(191,279)
Proceeds from share issuance		-	4,999
Net cash generated from financing activities		1,933,980	260,622
(Decrease) / increase in cash		(90,473)	128,030
Cash at the beginning of the year	10	207,314	79,284
Cash at the end of the year	10	116,841	207,314

General Director

Chief Accountant



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G.A. Kochetkov

I.A. Lapitskaya

25 September 20

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

TGC-4 GROUP

Combined and Consolidated Statement of Changes in Equity for the years ended 31 December 2006 and 31 December 2005
(in thousands of Russian Roubles)

Attributable to the shareholders of TGC-4

	Ordinary share capital	Preference share capital	Unpaid share capital	Merger reserve	Share premium	Retained Earnings	Total	Minority interest	Total equity
At 1 January 2005	-	-	-	4,749,463	-	-	4,749,463	4,943,319	9,692,782
Profit/(loss) for the year*	-	-	-	-	-	188,984	188,984	29,086	218,070
Contribution from shareholders (Note 13)	-	-	-	-	-	60,288	60,288	230,359	290,647
Payment of share capital (Note 13)	4,999	-	5,001	-	-	-	10,000	-	10,000
Dividends	-	-	-	-	-	(155,925)	(155,925)	(161,090)	(317,015)
At 31 December 2005	4,999	-	5,001	4,749,463	-	93,347	4,852,810	5,041,674	9,894,484
Payment of share capital (Note 13)	12,177,856	684,903	(5,001)	(6,557,456)	-	-	6,300,302	(6,300,302)	-
Changes in Group structure	1,029,165	67,826	-	-	959,867	(1,322,203)	734,655	1,322,203	2,056,858
Profit for the year	-	-	-	-	-	8,416,611	8,416,611	-	8,416,611
Dividends	-	-	-	-	-	(18,266)	(18,266)	(20,967)	(39,233)
At 31 December 2006	13,212,020	752,729	-	(1,807,993)	959,867	7,169,489	20,286,112	42,608	20,328,720



General Director

Chief Accountant

(Handwritten signature)

G.A. Kochetkov

I.A. Lapitskaya

25 September 2007

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 1. The Group and its operations

Open Joint-Stock Company "Territorial Generation Company 4" ("TGC-4" or "Company") was established on 18 April 2005 as a subsidiary of OJSC "RAO UES of Russia" ("RAO UES" or "Parent") within the framework of Russian electricity sector restructuring.

The Group TGC-4 (hereinafter – the Group) as at 31 December 2006 for the purposes of preparation of the combined and consolidated financial statements incorporates TGC-4 with eleven branches located in Belgorod, Bryansk, Voronezh, Kaluga, Kursk, Lipetsk, Oryol, Ryazan, Smolensk, Tambov and Tula and subsidiaries. The principal subsidiaries are listed in Note 5.

The branches were formed on base eleven regional generating companies (JSC "Bryansk Generating Company", JSC "Voronezh Generating Company", JSC "Kaluga Generating Company", JSC "Kursk Generating Company", JSC "Oryol Generating Company", JSC "Prioksk Territorial Generating Company", JSC "Ryazan Heat Supply Company", JSC "Smolensk Generating Company", JSC "Lipetsk Generating Company", JSC "Tambov Generating Company" and JSC "Heat Power Company" (Belgorod), whose assets were merged into and with TGC-4 as at 15 September 2006. The merger was a business combination amongst entities under common control (except for JSC "Heat Power Company" (Belgorod) Note 5), and has been accounted for using the predecessor accounting method (see Note 3). As such, these financial statements include all companies for all periods presented.

The Company is incorporated under the law of Russian Federation.

The Company's registered office is located at 99, Timiryazev Str., 300600, Tula, Russia. The Company has branches.

As at 31 December 2006, the number of the Group's employees was 16,841 (as at 1 January 2006 11,537).

The Company's shares are listed in the Russian Trade System.

The TGC-4 operates 11 power plants and its principal activity is electricity and heat generation.

Operating environment

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

Relations with the state and current regulation

As at 31 December 2006 the Russian Federation owned 52.7% of RAO UES of Russia, which in its turn owned 50.02% of voting ordinary shares of TGC-4. The Russian government is the ultimate controlling party of the Company.

The Group's customer base includes large number of entities controlled by or related to the state. Moreover, the state controls a number of the Group's fuel and other suppliers.

The Government of the Russian Federation directly affects the Group's operations through regulation by the Federal Service on Tariffs ("FST"), with respect to its wholesale energy sales, and through regulating by the Regional Services on Tariffs ("RST's"), with respect to retail electricity and heating sales.

The operations of all generating facilities are coordinated by The System Operator – the Central Dispatch Unit of the Unified Energy System ("SO-CDU") in order to meet system requirements in an efficient manner (a subsidiary of RAO UES of Russia).

Tariffs which the Group may charge for sales of electricity and heat are governed by regulations specific to the electricity and heat industry and by regulations applicable to natural monopolies. Historically, such tariffs have been based on a "cost-plus" system, meaning cost of service plus a margin, where costs are determined under the Regulations on Accounting and Reporting of the Russian Federation ("RAR"), a basis of accounting which significantly differs from International Financial Reporting Standards ("IFRS"). In practice, tariff decisions were impacted significantly by social and political considerations, causing

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 1. The Group and its operations (continued)

significant delays in tariff determinations and tariff increases that were lower than required to compensate for cost increases.

As described in Notes 2 and 25, the government's economic, social and other policies could have material effects on the operations of the Group.

Regulatory issues and sector restructuring

The Russian electric utilities industry is presently undergoing a reform process designed to introduce competition into the electricity sector and to create an environment in which the RAO UES Group and its successor companies (including TGC-4) can raise the capital required to maintain and expand current capacity.

- The regulatory framework governing the process of reforming the Russian Federation electric utilities industry and the functioning of the industry, both during the transition period and subsequent to the completion of reforms, is set forth in the following legislation: Federal Law No.35-FZ of 26 March 2003 "On the Electric Utilities of the Russian Federation" and Federal Law No.36-FZ of 26 March 2003 "On the Specifics of the Functioning of Electric Utilities During the Transition Period and the Introduction of Amendments to Certain Russian Federation Legislative Acts and the Invalidation of Certain Russian Federation Legislative Acts in Connection with the Adoption of the Law "On the Electric Utilities of the Russian Federation".
- In September 2003, the Russian Federation Government issued Resolution No. 1254-r "On formation of generation companies of the wholesale electricity market" which approved the composition of wholesale generating companies of the wholesale electricity market, including a list of the 5 power plants to be contributed into the Group.
- In October 2003, the Russian Federation Government issued Resolution No. 643 "On the Rules for the Wholesale Electricity Market during the Transition Period". According to the rules adopted, there will be two sectors within the Federal Wholesale Electricity Market (FOREM): regulated trading sector and free trading sector. Within the free trading sector, electricity suppliers will be able to sell electricity generated with the use of facilities and equipment accounting for 15% of the working capacity. Since November 2003, the non-commercial partnership "Trade System Administrator of the Wholesale Electricity Market", in accordance with the rules for the wholesale electricity market during the transition period, has been holding electricity bidding in the free trading sector. The Group participates in this free trading scheme. According to the laws underlying the electric utilities reform, subsequently free trading will be extended over the whole volume of trading.
- As part of reforming of the operation of the wholesale electricity (power) market in August 2006 the Government issued Resolution No. 529 "On the Improvement of the Operation of the Wholesale Electricity Market" which introduced changes in the Rules for the Wholesale Electricity Market during the Transition Period from 1 September 2006. Effective as of September 2006 there will be changes in pricing and abolition of limitation on sale of power in the free trading sector. Specifically, the Resolution stipulates a gradual reduction (5% to 15% per annum) of the share of electricity sales on the wholesale market at regulated prices (tariffs) and a corresponding increase of trading of electricity at free market prices.
- As at 29 May 2003, the Board of Directors of RAO UES of Russia approved a "Concept of RAO UES of Russia strategy for the period from 2003 through 2008". In February 2006 the Board of Directors approved an Appendix to the Concept of RAO UES Strategy: "Generating companies of the Wholesale Electricity Market (TGCs)". This document provides a detailed description of the major changes that are planned to take place in respect of RAO UES Group companies during the electric utilities reform program.

A crucial step in developing a competitive wholesale electricity (capacity) market was the adoption of the new Wholesale Electric Power (capacity) Market (NOREM) Rules of the Transitional Period approved by Resolution of the Government of the Russian Federation No. 529 dated August 31, 2006 and which came into force on September 1, 2006. Under the new wholesale market framework, electricity and power purchase-and-sale transactions in the regulated market sector are to be governed by a regulated bilateral

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 1. The Group and its operations (continued)

contract system. From 1 September 2006 regulated contracts covered substantial volume of electricity and power produced and consumed.

From 2007 the volumes of electricity (power) traded in the wholesale market at regulated prices will be substantially reduced. The pace of reduction was set by the Russian Federation Government according to socio-economic development forecasts. In 2007 up to 90% of the forecasted production volumes will be traded at regulated prices. The period from 2006 to approximately 2011 is a transition period. After that, it is expected that a fully competitive wholesale market will develop.

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

Main developments in the formation process

- On 28 February 2006 the general shareholders' meetings of 8 regional Generating companies - JSC "Bryansk Generating Company", JSC "Voronezh Generating Company", JSC "Kaluga Generating Company", JSC "Kursk Generating Company", JSC "Oryol Generating Company", JSC "Prioksk Territorial Generating Company", JSC "Ryazan Heat Supply Company" and JSC "Smolensk Generating Company" - took a decision to reorganize the companies in the form of merger with JSC "TGC-4" on the conditions envisaged by the Merger Agreement and to approve the Merger Agreement and deeds of transfer of the companies reorganized in the form of merger with JSC "TGC-4".
- On 8 April 2006 similar decisions were taken at the general meetings of shareholders of JSC "Lipetsk Generating Company" and JSC "Tambov Generating Company".
- On 21 July 2006 the general meeting of shareholders of JSC "Heat Power Company" (Belgorod) took a decision to reorganize the company in the form of merger with JSC "TGC-4" on the conditions envisaged by the Merger Agreement and to approve the Merger Agreement and deed of transfer.
- On 21 July 2006 the Board of RAO UES of Russia performing the functions of the general meeting of shareholders of JSC "TGC-4" took a decision to reorganize the Company in the form of takeover of its 11 regional generating companies, to approve the Merger Agreement and increase the Group's charter capital through the placement of additional shares for the conversion of shares of merged companies in the manner envisaged by the Merger Agreement. Conversion coefficients were determined.
- On 15 September 2006 termination of activities of 11 regional Generating companies through the merger with JSC "TGC-4" was registered in the United State Register of Enterprises and Organizations of Russia. Shares of merged companies were converted and JSC "TGC-4" started to operate as a single company.

Note 2. Financial condition

At 31 December 2006, the Group's current assets exceeded its current liabilities by RR 251,090 thousand (at 31 December 2005: the Group's current liabilities exceeded its current assets by RR 282,773 thousand).

As discussed above, the Group is affected by Government policy through control of tariffs and other factors. The FST have not always permitted tariff increases in line with the Group's costs and thus some tariffs are insufficient to cover all the costs of generation. Moreover, increases in these tariffs consider costs only on a Russian statutory basis and, accordingly, exclude additional costs recognised under an IFRS basis of accounting. As a result, tariffs may not consistently allow for an adequate return on investment and currently do not provide sufficient funds for the full replacement of property, plant and equipment. However, during 2006 and to date in 2007 the growing demand for electricity and capacity together with the increasing free trading sector of the wholesale electricity market have resulted in a higher rate of revenue growth, received from the sale of electricity and heat generated by own stations

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 2. Financial condition (continued)

(see Regulatory issues and sector restructuring in Note 1 and Impairment provision for property, plant and equipment in Note 8).

Although the Company's current collections of accounts receivable is high enough, the Company continues to experience difficulties in obtaining settlements of accounts receivable, particularly, for heat sales, the majority of which are receivables from state-controlled entities. Also, there still remains a significant level of uncollectible accounts receivable for heat sales for earlier periods. There is legislation enabling the Company to terminate service to delinquent customers, but certain strategic and political factors make this difficult. The Company has created impairment provision against doubtful accounts receivable, as further described in Note 12.

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

- introduction of improved financial budgeting procedures;
- discussions with strategic investors, and identification and assessment of projects requiring investment funds;
- negotiations with federal and regional governments and regulators for real increases in tariffs to support adequate long term investment into the Group's generation assets; and
- raising long-term debt/equity financing for investments in new generating assets.

Note 3. Basis of preparation

Statement of compliance

These are the first combined and consolidated financial statements ("Financial Statements") that have been prepared in accordance with International Financial Reporting Standards ("IFRS") and related interpretations adopted by the International Accounting Standards Board ("IASB"). There are no previous GAAP financial statements from which reconciliation can be prepared.

Each enterprise of the Group individually maintains its own books of accounts and prepares its statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"). The accompanying financial statements are based on the statutory records and adjusted and reclassified for the purpose of fair presentation in accordance with IFRS.

Functional and presentation currency

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

Predecessor Accounting

In these combined and consolidated financial statements, the Group accounted for the merger with others entities as business combinations amongst entities under common control under an accounting policy using the predecessor values method. Accordingly, assets and liabilities of the contributed entity were accounted for at the carrying value, as determined by RAO UES in its IFRS consolidated financial statements. Information in respect of the comparative period and opening balances as at 1 January 2005 has been restated as if the business combination took place at the beginning of the earliest period presented. Therefore JSC "Bryansk Generating Company", JSC "Voronezh Generating Company", JSC "Kaluga Generating Company", JSC "Kursk Generating Company", JSC "Oryol Generating Company", JSC "Prioksk Territorial Generating Company", JSC "Ryazan Heat Supply Company" and JSC "Smolensk Generating Company", JSC "Lipetsk Generating Company", JSC "Tambov Generating Company" and JSC "Heat Power Company" (Belgorod) were accounted in the Group's combined and consolidated financial statements effective from 1 January 2005.

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 3. Basis of preparation (continued)

The difference between the consideration paid and the predecessor carrying values of the net assets relating to the acquisition of a business from an entity under common control is recorded in equity, as a merger reserve.

Minority interest represents the difference between the net assets and results of each merged companies and net assets and results carved out from their predecessors and RAO UES proportionate share of the respective net assets and results until the merger into the Company. Minority interest forms a separate component of the Company's equity.

Accounting for the effects of hyperinflation

The Russian Federation has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 "Financial Reporting in Hyperinflationary Economies" ("IAS 29"). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. Hyperinflation in the Russian Federation ceased effective from 1 January 2003. Restatement procedures of IAS 29 are therefore only applied to assets acquired or revalued and liabilities incurred or assumed prior to that date. For these balances, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts of these financial statements.

New accounting developments

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

- IAS 39 (Amendment) "The Fair Value Option";
- IFRIC 4 "Determining whether an Arrangement contains a Lease";
- IAS 39 (Amendment) "Cash Flows Hedge Accounting of Forecast Intragroup Transactions";
- IAS 39 (Amendment) "Financial Guarantee Contracts";
- IAS 21 (Amendment) "Net Investment in a Foreign Operation";
- IAS 19 (Amendment) "Employee Benefits";
- IFRIC 5 "Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds";
- IFRIC 6 "Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment";
- IFRS 6 "Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006)".

The effect of adoption of the above new or revised standards and interpretations on the Group's financial position at 31 December 2006 and 31 December 2005 and on the results of its operations for the years then ended was not significant.

Other new standards or interpretations

The Group has not early adopted the following other new standards or interpretations:

- IFRS 7 "Financial Instruments". Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007). The IFRS introduces new disclosures to improve the information disclosed in respect of financial instruments. The volume of disclosures will increase significantly with an emphasis on quantitative aspects of risk exposures and the methods of risk management. The quantitative disclosures will provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity's key management personnel. Qualitative and quantitative disclosures will cover exposure to credit risk, liquidity risk and market risk including

Note 3. Basis of preparation (continued)

sensitivity analysis to market risk. IFRS 7 replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and some of the requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The Amendment to IAS 1 introduces disclosures about level of an entity's capital and how it manages capital. The Group is currently assessing what impact the new IFRS and the amendment to IAS 1 will have on disclosures in its financial statements;

- IFRS 8 "Operating Segments" (effective for annual periods beginning on or after 1 January 2009). The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information;
- IFRIC 7 "Applying the Restatement Approach under IAS 29" (effective for periods beginning on or after 1 March 2006, that is from 1 January 2007);
- IFRIC 8 "Scope of IFRS 2" (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007);
- IFRIC 9 "Reassessment of Embedded Derivatives" (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10 "Interim Financial Reporting and Impairment" (effective for annual periods beginning on or after 1 November 2006);
- IFRIC 11 "IFRS 2 Group and Treasury Share Transactions" (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12 "Service Concession Arrangements" (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 13 "Customer Loyalty Programmes" (effective for annual periods beginning on or after 1 July 2008);
- IFRIC 14 "IAS 19 The limit on a Defined Benefit Asset, Minimum Funding Requirements and their interaction" (effective for annual periods beginning on or after 1 January 2008);
- IAS 23 "Borrowing Cost" (Amendment, applies to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009). The main change from the previous version is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale.

Going concern

The accompanying combined and consolidated financial statements have been prepared on a going concern basis, which contemplates the realisation of assets and the satisfaction of liabilities in the normal course of business. The recoverability of the Group's assets, as well as the future operations of the Group, may be significantly affected by the current and future economic environment. The accompanying financial statements do not include any adjustments should the Group be unable to continue as a going concern.

Critical accounting estimates and assumptions

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

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 3. Basis of preparation (continued)

significant effect on the amounts recognized in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Provision for impairment of accounts receivable

Provision for impairment of accounts receivable is based on the Group's assessment of whether the collectibility of specific customer accounts deteriorated compared to prior estimates. If there is a deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates, the actual results could differ from these estimates (see Note 12). If conditions change and management determines that the collectibility of accounts receivable has improved, the provision for impairment is fully or partially reversed.

Impairment of other assets and accounting for provisions

At each balance sheet date the Group assesses whether there is any indication that the recoverable amount of the Group's assets has declined below the carrying value. The recoverable amount of property, plant and equipment is the higher of an asset's fair value less costs to sell and its value in use. When such a decline is identified, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recorded in the consolidated statement of income in the period in which the reduction is identified. If conditions change and management determines that the value of an asset other than goodwill has increased, the impairment provision will be fully or partially reversed (see Note 8).

Accounting for impairment includes provisions against property, plant and equipment, investments, other non-current assets and inventory obsolescence. The provisions for liabilities and charges primarily include provisions for environmental and pension liabilities, legal proceedings. The Group records impairment or accrues these provisions when its assessments indicate that it is probable that a liability has been incurred or an asset will not be recovered, and an amount can be reasonably estimated. The Group's estimates for provisions for liabilities and charges are based on currently available facts and the Group's estimates of the ultimate outcome or resolution of the liability in the future. Actual results may differ from the estimates, and the Group's estimates can be revised in the future, either negatively or positively, depending upon the outcome or expectations based on the facts surrounding each exposure.

Tax contingencies

Russian tax legislation is subject to varying interpretations and changes, which can occur frequently. Where the Group management believes it is probable that their interpretation of the relevant legislation and the Group's tax positions cannot be sustained, an appropriate amount is accrued for in these IFRS financial statements.

Useful lives of property, plant and equipment

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

Carve-out methodologies

These consolidated and combined financial statements include the carved out financial statements of JSC "Lipetsk Generating Company", JSC "Tambov Generating Company", JSC "Ryazan Heat Supply Company", JSC "Kursk Generating Company", JSC "Smolensk Generating Company", JSC "Prioksk Territorial Generating Company", JSC "Oryol Generating Company" for the period and from the predecessor legal entities as outlined in the table below.

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 3. Basis of preparation (continued)

Generating Company	Predecessor legal entity	Period requiring carve-out accounting
JSC "Lipetsk Generating Company"	OJSC "Lipetskenergo"	11 days ended 11 January 2005
JSC "Tambov Generating Company"	OJSC "Tambovenergo"	11 days ended 11 January 2005
JSC "Ryazan Heat Supply Company"	OJSC "Ryazan'energo"	11 days ended 11 January 2005
JSC "Kursk Generating Company"	OJSC "Kurskenergo"	1 month ended 31 January 2005
JSC "Smolensk Generating Company"	OJSC "Smolenskenergo"	1 month ended 31 January 2005
JSC "Prioksk Territorial Generating Company"	OJSC "Tulenergo"	3 months ended 30 March 2005
JSC "Oryol Generating Company"	OJSC "Oryolenergo"	3 months ended 30 March 2005

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

- electricity and heat sales were based on actual electricity and heat power production volume multiplied by actual tariffs approved by RSTs for the power stations after their spin-off from the predecessor legal entities for the year 2005;
- direct operating expenses were determined on actual basis as recorded in accounting of predecessors attributable to each power station;
- depreciation of property, plant and equipment was calculated on IFRS predecessor values;
- general and administrative overheads were not allocated but were determined on an actual basis, i.e. only those expenses that can be directly attributed to assets/liabilities belonging to generation were carved out;
- current profit tax was determined using the effective profit tax rate of the predecessor entities;
- property, plant and equipment were based on IFRS predecessor values and rolled back to 1 January 2005 taking into account additions and disposals in the stations before their spin-off;
- accounts receivable, inventory, accounts payable, borrowings, which were mostly accounted for by the predecessor entities for vertically integrated businesses and not split by division, have been accounted for based on the actual balances and amounts transferred by the predecessors to respective spun-off entities.

Because of the various determinations used in carving out revenues and expenses, those revenues and expenses related to the electricity and heat generation operations within the former structure of the business may not be indicative of revenues expected to be earned and costs expected to be incurred on a prospective basis for the electricity and heat generation operations within the Company as a separate business and, as such, these financial statements may not be indicative of future results of operations and trends.

As a result of determinations used to proceed with the spin-offs and, consequently, determinations used for preparation of carved out data the difference arose between the amount of net assets at the date of spin off and the amount of net assets as at 1 January 2005 adjusted for the net profit carved out for the periods ended at spin-off dates. The difference of RR 290,647 thousands was accounted as Contribution from shareholders within equity (Note 13).

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 4. Summary of significant accounting policies

Principles of consolidation

The Financial Statements comprise the financial statements of TGC-4 and the financial statements of those entities whose operations are controlled by TGC-4. Control is presumed to exist when TGC-4 controls, directly or indirectly through subsidiaries, more than 50 % of voting rights.

A) Subsidiaries

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

Transactions eliminated on consolidation

Inter-company balances and transactions, and any unrealised gains arising from inter-company transactions, are eliminated in preparing the combined and consolidated financial statements.

B) Associates

Associates are entities over which the Group has significant influence, but not control, generally accompanying a shareholding of between 20 % and 50 % of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group's share of the post-acquisition profits or losses of associates is recorded in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Transfers of subsidiaries from parties under common control

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

Foreign currency

Monetary assets and liabilities, which are held by the Group entities and denominated in foreign currencies at the balance sheet date, are translated into RR at the exchange rates prevailing at that date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transaction. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of operations.

As at 31 December 2006, the official rate of exchange, as determined by the Central Bank of the Russian Federation, between the RR and the US Dollar ("USD") was RR 26.33: USD 1.00 (31 December 2005: RR 28.78: USD 1.00), between the RR and EURO RR 34.70: EURO 1.00 (31 December 2005: RR 34.19: EURO 1.00).

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 4. Summary of significant accounting policies (continued)**Property, plant and equipment**

In 2005 property, plant and equipment were recognised at the carrying value determined in accordance with IFRS at the date of their transfer to the Company from the Predecessor entity.

Property, plant and equipment are stated at depreciated costs less impairment. Deemed cost was initially determined by a third party valuation at 31 December 1997 and restated for the impact of inflation until 31 December 2002. Adjustments are made for additions, disposals and depreciation charges.

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

The amounts determined by the third party valuation represent an estimate of depreciated replacement cost. The third party valuation was performed in order to determine a basis for cost, because the historical accounting records for property, plant and equipment were not readily available, in accordance with paragraph 16 of IAS 29. Therefore, this third party valuation is not a recurring feature since it was intended to determine the initial cost basis of property, plant and equipment and the Group has not adopted a policy of revaluation on subsequent measurement. The change in carrying value arising from this valuation was charged directly to retained earnings. The policy of revaluation will be adopted from 1 January 2007 as described in Note 27.

Further acquisitions of property, plant and equipment are recognized at their actual cost.

Renewals and improvements are capitalized and the assets replaced are retired. The cost of repair and maintenance are expensed as incurred. Gains and losses arising from the retirement of property, plant and equipment are included in the income statement as incurred.

Gain or loss from sale or other retirement of property, plant and equipment is determined as the difference between the sales proceeds and book value and is recognized in the income statement.

Depreciation

Depreciation of property, plant and equipment is calculated on a straight-line basis over the estimated useful life of the asset when it is available for use. For the property, plant and equipment which were subject to the third party valuation as at 31 December 1997, the depreciation rate applied is based on the estimated remaining useful lives as at the valuation date. The remaining useful lives are reviewed annually. The useful lives, in years of assets by type of facility are as follows:

Type of facility	Acquired prior to 31 December 1997	Acquired subsequent to 31 December 1997
Electricity and heat generation	5-63	20-50
Electricity distribution	6-28	25
Heating network	4-31	20
Other	8	10

Useful lives of property, plant and equipment are reviewed on a regular basis to ensure their consistency with previous assessments. Depreciation accrued for the accounting period is properly adjusted, if necessary.

Intangible assets

Intangible assets are stated at cost, adjusted for subsequent disposal, amortisation and impairment.

Amortisation of intangible assets is calculated on a straight-line basis over the shorter of useful life or validity period of legal rights.

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 4. Summary of significant accounting policies (continued)

Goodwill

Goodwill is recognised on acquisitions of subsidiaries, associates and jointly controlled entities. Goodwill arising on the acquisitions represents any excess of the purchase consideration over the acquirer's interest in the net fair value of identifiable assets, liabilities and contingent liabilities. Goodwill is recognised at cost less impairment losses. The carrying amount of goodwill is assessed for impairment on an annual basis. In respect of associates and a jointly controlled entity, the carrying amount of goodwill is included in the carrying amount of the investment.

Any excess of the fair value of the net identifiable assets acquired over the cost of acquisition is recognised immediately in the statement of operations.

Investments

Investments intended to be held for an indefinite period of time are classified as available-for-sale; these are included in other non-current assets unless management has the express intention of holding the investment for less than 12 months from the balance sheet date, they will need to be sold to raise operating capital or they mature within 12 months, in which case they are included in other current assets. Management determines the appropriate categorisation, current or non-current, at the time of the purchase and re-evaluates it based on maturity at each reporting date.

Available-for-sale investments include non-marketable securities, which are not publicly traded or listed on the Russian stock exchange. For these investments, fair value is estimated by reference to a variety of methods including those based on their earnings and those using the discounted value of estimated future cash flows. In assessing the fair value, management makes assumptions that are based on market conditions existing at each balance sheet date. Investments in equity securities that are not quoted on a stock exchange and where fair value cannot be estimated on a reasonable basis by other means are stated at cost less impairment losses.

Regular way purchases and sales of investments are initially measured at fair value and recognised on the settlement date, which is the date that the investment is delivered to or by the Group. Cost of purchase includes transaction costs. The available-for-sale investments are subsequently carried at fair value. Gains and losses arising from changes in the fair value of these investments are included in the fair value reserve in shareholders' equity in the period in which they arise. Realised gains and losses from the disposal of available-for-sale investments are included in the statement of operations in the period in which they arise.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of available-for-sale investments. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through current period's profit or loss.

The Group does not hold any investments held-to-maturity or for trading purposes.

Cash and cash equivalents

Cash comprises cash in hand and cash deposited on demand at banks. Cash equivalents comprise short-term highly liquid investments that are readily convertible into cash and have a maturity of three months or less from the date of acquisition and are subject to insignificant changes in value.

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**(in thousands of Russian Roubles)

Note 4. Summary of significant accounting policies (continued)**Inventory**

Inventories are valued at the lower of acquisition cost and net realizable value. Acquisition cost of inventory is determined on the weighted average basis.

Provision is made for potential losses on obsolete or slow-moving inventories, taking into account their expected useful life and future realizable value.

Value added tax on purchases and sales

Starting 1 January 2006 output VAT related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice.

Before 1 January 2006 there were other tax rules applied for output and input VAT. Output VAT related to sales was generally payable to tax authorities on the collection of the receivables from customers. The related deferred VAT liability was maintained until the underlying debtor is recovered or written off for tax purposes. Input VAT was generally recoverable against output VAT upon payment for purchases made.

There are also some transition rules applied for output and input VAT incurred before 1 January 2006 and which were not settled as at 1 January 2006. Generally, according to the rules these output and input VAT will be settled during 2006-2007 but not later than the first tax period of year 2008.

The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognized in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Accounts receivable

Accounts receivable are recorded inclusive of value added taxes which are payable to tax authorities upon collection of such receivables. Trade and other receivables are recognized in amounts presented to contractors for payment and are adjusted for an allowance made for impairment of these receivables. Such an allowance for doubtful debtors is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables.

The amount of the allowance is the difference between the carrying and recoverable amount, being the present value of the expected cash flows, discounted at the market rate of interest for similar borrowers at the date of origination of the receivables.

Accounts payable and accruals

Accounts payable are stated inclusive of value added tax. Trade payables are recognized initially at fair value and subsequently measured at amortised cost using the effective interest rate method. If accounts payable are restructured and the fair value of the restructured payable determined using the original effective interest rate differs by more than ten percent from the original liability, then the fair value of the restructured payable is measured as the present value of the future cash flows discounted at the interest rate available to the Group at the date of the restructuring.

The amount of the discount is credited to the income statement (finance costs - net) as a gain on restructuring, and the non-current portion of the discounted payable is reclassified to other non-current liabilities. The discount is amortized over the period of the restructuring as an interest expense.

Note 4. Summary of significant accounting policies (continued)

Guarantee

Financial guarantees are contracts where the Group is required to make payments to reimburse a lender when a specific debtor fails to make payment when due in accordance with a debt instrument. Financial guarantee contracts issued by the entity are accounted for at fair value. Fair value is determined using the interest rate differentials method, which provides a suitable basis for estimating the fair value of guarantees. Under this method the fair value of guarantee represents the difference in the present value of the interest payments charged on the guaranteed loan and what would have been charged had the loan not been guaranteed over the period of the guarantee.

Debt

Debt is recognized initially at its fair value. Fair value is determined using the prevailing market rate of interest for a similar instrument, if significantly different from the transaction price. In subsequent periods, debt is stated at amortized cost using the effective yield method; any difference between the fair value of the proceeds (net of transaction costs) and the redemption amount is recognized in the income statement as an interest expense over the period of the debt obligation.

Borrowing Costs

The Company applies the benchmark treatment of IAS 23 "Borrowing costs" and recognises all borrowing costs as an expense in the period in which they are incurred.

Pension and post-employment benefits

In the normal course of business the Company contributes to the Russian Federation defined contribution state pension scheme on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred and included in employee benefit expenses and payroll taxes in the income statement.

Company also operates defined benefit plans. Benefit plans define the amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. The liability recognised in the balance sheet in respect of defined benefit pension plans operated by the Company is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses. The defined benefit obligations are calculated using the projected unit credit method. The present value of the defined benefit obligations are determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid associated with the operation of the plans, and that have terms to maturity approximating the terms of the related pension liabilities.

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

Income tax

The income tax represents the sum of the tax currently payable and deferred income tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit before tax 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 by the balance sheet date.

Note 4. Summary of significant accounting policies (continued)

Deferred income tax

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

Deferred tax movements are recorded in the income statement except when they are related to the items directly charged to the shareholders' equity. In this case deferred taxes are recorded as part of the shareholders' equity.

Revenue recognition

Revenue is recognized on the delivery of electricity and heat during the period. Revenue amounts are represented exclusive of value added tax.

Operating leases

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

When assets are leased out under an operating lease, the lease payments receivable are recognised as rental income on a straight-line basis over the lease term.

Finance leases

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

Government grants

Grants related to income are recognized as income in the same periods as the related expenses. They are presented in the income statement under a general heading such as "Other income".

Dividends

Dividends are recognized as a liability and deducted from equity at the balance sheet date only if they are declared (approved by shareholders) before or on the balance sheet date. Dividends are disclosed when

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 4. Summary of significant accounting policies (continued)

they are declared after the balance sheet date, but before the Financial Statements are authorized for issue.

Earnings per share

The earnings per share are determined by dividing the profit attributable to ordinary shareholders of the Parent Company of the Group by the weighted average number of ordinary shares outstanding during the reporting period.

Environmental liabilities

Liabilities for environmental remediation are recorded where there is a present obligation, the payment is probable and reliable estimates can be made.

Segment reporting

The Group operates predominantly in a single geographical area and industry, the generation of electric power and heat in the Russian Federation. The generation of electricity and heat are related activities and are subject to similar risks and returns; therefore they are reported as one business segment.

Minority interest

Minority interest represents the minority shareholders' proportionate share of the equity and results of operations of the Group's subsidiaries. This has been calculated based upon the minority interest's ownership percentage of these subsidiaries.

In purchases of minority interest, difference, if any, between the carrying amount of a minority interest and the amount paid to acquire it is recorded directly in equity.

Interest

Interest income and expense are recognized in the income statement for all debt instruments on an accrual basis using the effective rate of interest method. Interest income includes nominal interest and amortised discount and premium. When loans become doubtful of collection, they are written down to their recoverable amounts and interest income is thereafter recognized based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

Seasonality

Demand for electricity and heat is influenced by both the season of the year and the relative severity of the weather. Revenues from heating are concentrated within the months of October to March. A similar, though less severe, concentration of electricity sales occurs within the same period. The seasonality of electricity and heat production has a corresponding impact on the usage of fuel and the purchase of power.

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

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 5. Group subsidiaries and associated companies

The financial statements consolidate the Group with its subsidiaries which are presented in the table below.

Subsidiaries	Activity	Ownership, %	
		31 December 2006	31 December 2005
JSC "Novomoskovskaya GRES"	Electricity and heat generation	100	100
JSC "Ryazanenergoremont"	Servicing of electrical and heating networks	100	100
JSC "Tambovenergospetsremont"	Repairs, renewal and reconstruction of heating and electrical equipment	100	100
JSC "Tulaenergocomplect"*	Supply of material resources, storage and cargo transportation	50	50
JSC "Voronezhenergoremont"	Servicing of electrical and heating networks	-	100
JSC "Kurskenergospetsremont"	Repairs, renewal and reconstruction of heating and electrical equipment	-	100
JSC "Engineering and Production Centre"	Research, development and design works	-	100
JSC "Tulaenergoremont"	Servicing of electrical and heating networks	-	82

*Control is exercised by means of majority of votes on the Board of JSC Tulaenergocomplect.

In 2006 the shares of repair companies: JSC "Voronezhenergoremont", JSC "Kurskenergospetsremont", JSC "Engineering and Production Centre" and JSC "Tulaenergoremont" owned by regional Generating companies were sold.

The shares were sold by way of competitive sale in 2006. The carrying amount of assets and liabilities disposed was the following:

Narrative	JSC "Voronezh- energoremont"	JSC "Kurskenergospetsremont"	JSC "Engineering and Production Centre"	JSC "Tulaenergoremont"
	14 September 2006	30 June 2006	30 June 2006	30 June 2006
Property, plant and equipment	107,130	16,966	5,143	23,124
Deferred tax assets	130	24	-	896
Other non-current assets	533	101	1,050	3,155
Cash and cash equivalents	1,629	3,424	1,281	802
Accounts receivable and prepayments	17,976	9,136	6,881	31,845
Other current assets	-	-	-	10,550
Inventories	3,781	7,644	12,609	6,640
Accounts payable and advances received	(24,731)	(15,278)	(6,653)	(28,955)
Non-current debt	-	(1,700)	(153)	(354)
Taxes payable	-	-	-	-
Deferred tax liabilities	(8,797)	(1,442)	-	(10,826)
Net assets	97,651	18,875	20,158	36,877

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 5. Group subsidiaries and associated companies (continued)

The Group has the following associated companies:

Associated company	Activity	Ownership, %	
		31 December 2006	31 December 2005
JSC "Energetic Health Centre"	Health and recreation of families and children	49	49
JSC "TechnotestEnergо"	Assembly and repair works including facilities controlled by the RF Government Technical Supervision	49	49
JSC "Belgorodenergосervice"	Repair of electronic devices and heat and electrical meters	25	-
JSC "Heat Power Company" (Belgorod)*	Heat and electricity generation	-	25

***Business combinations with JSC "Heat Power Company" (Belgorod)**

JSC "Heat Power Company" (Belgorod) was accounted within the Group till 30 June 2005. In July 2005 JSC "Heat Power Company" (Belgorod) issued the additional shares and merged municipally owned JSC "BelTEK" that resulted in the decrease of RAO UES ownership share from 49% to 25.1%. The loss resulting from the decrease of RAO UES ownership share in JSC "Heat Power Company" (Belgorod) net assets amounted to RR 405,069 thousand. As at 31 December 2005 JSC "Heat Power Company" (Belgorod) was accounted for as the investment in the associated company amounting to RR 414,128 thousand.

On 15 September 2006 following TGC-4 restructuring the Group obtained the full control over JSC "Heat Power Company" (Belgorod). As a result the Group's revenue increased by RR 1,429,187 thousand and the net income decreased by RR 482,481 thousand.

If the merger had occurred as at 1 January 2006, the Group's revenue would have increased by RR 2,123,065 thousand, and an additional income before allocation would have been recognized of RR 225,399 thousand.

The fair value of TGC-4 shares issued for exchange of JSC "Heat Power Company" (Belgorod) net assets was based on the first published share price (December 2006).

Details of net assets acquired and goodwill are as follows:

Narrative	Value
Total purchase consideration	2,056,858
Provisional estimation net assets acquired value	1,414,063
Goodwill	642,795

No formal valuation of assets and liabilities of JSC "Heat Power Company" (Belgorod) has been completed due to the lack of economic feasibility for valuation performing in the year ended 31 December 2006. The management anticipates this valuation will be finalized before the issue of the next annual financial statements of the Group.

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(in thousands of Russian Roubles)

Note 5. Group subsidiaries and associated companies (continued)

The provisional values of the assets and liabilities at the date of obtaining control over JSC "Heat Power Company" (Belgorod) are as follows:

Narrative	Provisional value
Property, plant and equipment	3,279,216
Investments	18,021
Deferred tax assets	77,093
Accounts receivable and prepayments	422,600
Inventories	95,413
Cash	163,923
Non-current debt	(1,185,370)
Pension liabilities	(165,549)
Deferred tax liability	(253,526)
Current debt and current portion of non-current debt	(370,465)
Accounts payable and accruals	(195,165)
Provisional value of net assets	1,886,191

Note 6. Assets held for sale and discontinued operations**Assets held for sale**

As at 31 December 2006 assets held for sale are shown as follows:

Narrative	31 December 2006	31 December 2005
Assets of the subsidiaries	66,087	42,551
JSC "Ryazanenergoremont"	24,192	-
JSC "Tambovenergospetsremont"	41,895	42,551
Liabilities of the subsidiaries	30,474	9,941
JSC "Ryazanenergoremont"	22,459	-
JSC "Tambovenergospetsremont"	8,015	9,941

In 2005 Board of Directors of JSC "Tambov Generating Company" (decision #9 dated 02 June 2005) approved disposal of 100% of JSC "Tambovenergospetsremont" (the Group subsidiary) shares. The transaction was not completed within one year.

In 2006 Board of Directors of TGC-4 (decision #12/30 dated 14 November 2006 and 02/35 dated 14 February 2007) approved disposal of 100% of the following subsidiaries' shares:

- JSC "Ryazanenergoremont";
- JSC "Tambovenergospetsremont".

Disposal of subsidiaries was established by competitive sale of shares with the involvement of specialized agent.

In order to carry out the planned transaction to withdraw the Group's interest in subsidiaries a market value of the Group's interest was determined by independent appraisers.

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 6. Assets held for sale and discontinued operations (continued)**JSC "Ryazanenergoremont"**

Balance Sheet	
Narrative	31 December 2006
Property, plant and equipment	20,555
Deferred tax assets	9
Other non-current assets	2
Total non-current assets	20,566
Cash	16
Accounts receivable and prepayments	3,056
Inventories	554
Total current assets	3,626
TOTAL ASSETS	24,192
Deferred tax liabilities	11,162
Total non-current liabilities	11,162
Current debt and current portion of non-current debt	1,000
Accounts payable and accruals	4,035
Other taxes payable	6,262
Total current liabilities	11,297
TOTAL LIABILITIES	22,459

JSC "Tambovenergospetsremont"

Balance Sheet		
Narrative	31 December 2006	31 December 2005
Property, plant and equipment	22,405	25,514
Deferred tax assets	14	236
Other non-current assets	33	20
Total non-current assets	22,452	25,770
Cash	1,174	6
Accounts receivable and prepayments	12,134	9,635
Inventories	6,135	7,140
Total current assets	19,443	16,781
TOTAL ASSETS	41,895	42,551
Deferred tax liabilities	2,635	3,674
Total non-current liabilities	2,635	3,674
Current debt and current portion of non-current debt	400	-
Accounts payable and accruals	2,884	3,901
Other taxes payable	2,096	2,366
Total current liabilities	5,380	6,267
TOTAL LIABILITIES	8,015	9,941

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 6. Assets held for sale and discontinued operations (continued)

Discontinued operations

As part of a coordinated plan for all RAO UES entities to dispose of service subsidiaries in order to decrease affiliation with them the Group sold its investments in the following companies.

JSC "Ryazanenergoremont"

Statement of Operations		
Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Revenue	5,810	26,601
Cost of sales	(10,397)	(31,603)
Finance costs	(150)	(150)
Income tax expense	7,823	(5,009)
Profit/(loss) for the year	3,086	(10,161)

Cash Flow Statement		
Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	48	792
Operating activities	(864)	(1,342)
Investment activities	723	(252)
Financing activities	109	850
Cash at the end of the year	16	48

JSC "Tambovenergospetsremont"

Statement of Operations		
Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Revenue	13,715	34,925
Cost of sales	(12,402)	(24,583)
Finance costs	-	(25)
Income tax expense	(43)	(2,106)
Profit/(loss) for the year	1,270	8,211

Cash Flow Statement		
Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	6	468
Operating activities	(1,973)	(656)
Investment activities	2,741	194
Financing activities	400	-
Cash at the end of the year	1,174	6

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 6. Assets held for sale and discontinued operations (continued)**JSC "Voronezhenergoremont"**

Statement of Operations		
Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Revenue	10,138	37,701
Cost of sales	(7,552)	(53,488)
Finance costs	-	-
Income tax expense	(551)	19,595
Profit/(loss) for the period	2,035	3,808

Cash Flow Statement		
Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	71	83
Operating activities	3,969	1,402
Investment activities	(2,866)	(1,414)
Financing activities	-	-
Cash at the end of the period	1,174	71

JSC "Kurskenergoremont"

Statement of Operations		
Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Revenue	22,257	55,011
Cost of sales	(22,861)	(59,908)
Finance costs	-	-
Income tax expense	(67)	480
Profit/(loss) for the period	(671)	(4,417)

Cash Flow Statement		
Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	8,839	4,322
Operating activities	(5,415)	4,623
Investment activities	-	(106)
Financing activities	-	-
Cash at the end of the period	3,424	8,839

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

(in thousands of Russian Roubles)

Note 6. Assets held for sale and discontinued operations (continued)**JSC "Tulaenergoremont"****Statement of Operations**

Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Revenue	26,750	86,373
Cost of sales	(22,383)	(80,493)
Finance costs	1,229	(1,525)
Income tax expense	(2,263)	(7,472)
Profit/(loss) for the period	3,333	(3,117)

Cash Flow Statement

Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	2,060	1,296
Operating activities	171	7,490
Investment activities	(1,959)	(6,196)
Financing activities	530	(530)
Cash at the end of the period	802	2,060

JSC "Inzhenerno-proizvodstvennyy centr"**Statement of Operations**

Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Revenue	26,623	43,141
Cost of sales	(26,136)	(38,728)
Finance costs	-	(6)
Income tax expense	517	(1,345)
Profit/(loss) for the period	1,004	3,062

Cash Flow Statement

Narrative	Part of the year ended 31 December 2006	Year ended 31 December 2005
Cash at the beginning of the year	443	250
Operating activities	838	193
Investment activities	-	-
Financing activities	-	-
Cash at the end of the period	1,281	443

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

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Note 7. Related parties

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

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

At 31 December 2006 50.02% of the voting ordinary shares were owned by the state-controlled RAO UES. Thus, the related parties of the Group include RAO UES and its subsidiaries as well as other entities controlled by the State.

The table below shows related party transactions for the periods ended 31 December 2006 and 31 December 2005 and balances with related parties as at 31 December 2006 and 31 December 2005.

RAO UES

As at 31 December 2006 the Company had an outstanding balance on a loan received from the RAO UES (Centre of Power Sector Reform Promotion) of RR 87,111 thousand (31 December 2005: RR 157,813 thousand) (see Note 16).

Transactions and balances with the Parent's subsidiaries and associates

Transactions with subsidiaries of RAO UES were as follows:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Electricity and heating revenues	7,256,225	7,379,042
Other sales	105,588	298,769
Purchase of electricity	415,799	199,698

Balances with subsidiaries of RAO UES were as follows:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Accounts receivable, gross	98,702	280,793
Provision for impairment of accounts receivable	20,675	-
Accounts receivable, net	78,027	280,793
Accounts payable	69,334	137,147

State-controlled entities

In the normal course of business the Group enters into transactions with other entities under government control. Prices for natural gas, electricity and heat are based on tariffs set by FST and RSTs. Bank loans are granted at market rates. Taxes are charged and paid under the Russian tax legislation.

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

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Electricity and heating revenues	389,862	288,490
Purchase of fuel	6,854,833	7,618,143
Interest expense	250,540	68,123

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 7. Related parties (continued)

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

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Accounts receivable and prepayments	504,988	247,730
Accounts payable and accruals	88,111	54,177

Tax balances are disclosed in the balance sheet and Note 19. Tax transactions are disclosed in the income statement and Note 20.

Transactions with key management

Compensation is paid to members of the Management Board of the Group for their services in full time management positions. The compensation is made up of a contractual salary, non-cash benefits, and a performance bonus depending on results for the period according to Russian statutory financial statements. The compensation is approved by the Board of Directors. Also members of the Management Board are paid discretionary bonuses, which are approved by the Chairman of the Management Board according to his perception of the value of each Board member's contribution.

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

Key management received the following remuneration during the years ended 31 December 2006 and 31 December 2005:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Salaries	11,487	6,001
Bonuses	25,609	277
Compensations	3,169	4,053
Other	4,261	3,966
TOTAL	44,526	14,297

The Group has no other compensation programs.

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005
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Note 8. Property, plant and equipment

Description	Electricity & heat generation	Electricity distribution	Heating networks	CIP	Other	Total
Cost						
Opening balance as at 31 December 2005	20,987,635	837,309	6,341,149	1,576,904	7,220,259	36,963,256
Additions	2,148,032	191,945	1,154,972	2,372,714	522,068	6,389,731
Transfers	360,805	20,541	945,840	(1,665,783)	338,597	-
Disposals	(25,347)	(1,018)	(14,655)	(105,279)	(734,346)	(880,645)
Transfers due to reclassifications as Assets held for sale	-	-	-	(106)	(83,985)	(84,091)
Closing balance as at 31 December 2006	23,471,125	1,048,777	8,427,306	2,178,450	7,262,593	42,388,251
Accumulated depreciation (including impairment)						
Opening balance as at 31 December 2005	(15,650,210)	(648,301)	(5,089,412)	(12,457)	(6,122,209)	(27,522,589)
Charge for the period	(332,425)	(12,780)	(165,862)	-	(260,025)	(771,092)
Reversal of impairment loss	8,646,572	188,701	1,197,174	12,457	475,604	10,520,508
Disposals	10,767	378	11,750	-	601,145	624,040
Transfers due to reclassifications as Assets held for sale	-	-	-	-	63,148	63,148
Closing balance as at 31 December 2006	(7,325,296)	(472,002)	(4,046,350)	-	(5,242,337)	(17,085,985)
Net book value as at 31 December 2005	5,337,425	189,008	1,251,737	1,564,447	1,098,050	9,440,667
Net book value as at 31 December 2006	16,145,829	576,775	4,380,956	2,178,450	2,020,256	25,302,266

Note 8. Property, plant and equipment (continued)

Description	Electricity & heat generation	Electricity distribution	Heating networks	CIP	Other	Total
Cost						
Opening balance as at 31 December 2004	21,073,701	854,245	6,696,341	1,565,441	7,598,379	37,788,107
Additions	181,069	1,755	3,063	1,582,208	42,597	1,810,692
Transfers	491,471	42,254	420,433	(1,161,514)	207,356	-
Disposals	(758,606)	(60,945)	(778,688)	(409,231)	(545,787)	(2,553,257)
Transfers due to reclassifications as Assets held for sale	-	-	-	-	(82,286)	(82,286)
Closing balance as at 31 December 2005	20,987,635	837,309	6,341,149	1,576,904	7,220,259	36,963,256
Accumulated depreciation (including impairment)						
Opening balance as at 31 December 2004	(15,597,815)	(671,166)	(5,335,663)	(12,457)	(5,921,780)	(27,538,881)
Charge for the period	(292,693)	(17,527)	(291,916)	-	(611,105)	(1,213,241)
Disposals	240,298	40,392	538,167	-	350,897	1,169,754
Transfers due to reclassifications as Assets held for sale	-	-	-	-	59,779	59,779
Closing balance as at 31 December 2005	(15,650,210)	(648,301)	(5,089,412)	(12,457)	(6,122,209)	(27,522,589)
Net book value as at 31 December 2004	5,475,886	183,079	1,360,678	1,552,984	1,676,599	10,249,226
Net book value as at 31 December 2005	5,337,425	189,008	1,251,737	1,564,447	1,098,050	9,440,667

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

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Note 8. Property, plant and equipment (continued)

Construction in progress represents the carrying amount of property, plant and equipment that has not yet been available for use in production, including generating stations under construction, and advances to construction companies and suppliers of property, plant and equipment. As at 31 December 2006 such advances amounted to RR 446,386 thousand (as at 31 December 2005 – RR 114,482 thousand).

Other property, plant and equipment include motor vehicles, computer equipment, office fixtures and other equipment.

The following table shows the net book value of assets pledged as collateral under loan agreements.

Narrative	As at 31 December 2006	As at 31 December 2005
Electricity and heat generation	2,082,265	-
Heating network	822,470	-
Other	20,840	-
Total	2,925,575	-

Finance leasing

The Group leases property, plant and equipment on the basis of finance lease agreements. At the end of each lease operation the Group buys property, plant and equipment at repurchase price.

The following table shows the net book value of assets under finance lease.

Narrative	31 December 2006	31 December 2005
Electricity and heat generation	692,367	-

Finance lease rentals are payable as follows:

Maturity table for finance lease (discounted minimum lease payments)	31 December 2006	31 December 2005
Maturity		
Under one year	374,831	-
From 1 to 5 years	684,817	-
From 5 years	135	-
Total	1,059,783	-

Maturity table for finance lease (undiscounted minimum lease payments)	31 December 2006	31 December 2005
Maturity		
Under one year	428,244	-
From 1 to 5 years	1,001,266	-
From 5 years	32,132	-
Total	1,461,642	-

Operating lease

The Group use land on which the Group's buildings and facilities are located. The land is a property of local state authorities and the Group uses it on operating lease terms.

Lease payments for land and other property, plant and equipment determined based on the lease agreements terms are as follows:

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Note 8. Property, plant and equipment (continued)**As at 31 December 2006**

Narrative	Land lease	Lease of buildings and structures	Lease of other property, plant and equipment	Total
Under one year	156,205	61,349	39,317	256,871
From 1 to 5 years	614,920	42,727	36,855	694,502
From 5 years	4,067,508	52,965	39,425	4,159,898
Total	4,838,633	157,041	115,597	5,111,271

As at 31 December 2005

Narrative	Land lease	Lease of buildings and structures	Lease of other property, plant and equipment	Total
Under one year	47,810	-	29,120	76,930
From 1 to 5 years	617,395	93,394	66,958	777,747
From 5 years	4,221,238	63,647	48,639	4,333,524
Total	4,886,443	157,041	144,717	5,188,201

The above mentioned lease agreements are usually concluded for 1-49 years with prolongation right. The lease payments are subject to regular review that may result in adjustment to reflect the market conditions.

Impairment provision for property, plant and equipment

The impairment provision included in accumulated depreciation balance as at 31 December 2006 is RR 279,480 thousand (as at 31 December 2005 – RR 11,445,981 thousand).

Management has concluded that at the reporting date there were indications for reversing previously recognised impairment losses based on significant changes with a favorable effect on the Group that have occurred or are expected to occur in the near future in the market and economic environment in which the Group operates. Such changes include:

1. upward revisions, based on recent trends, in the expected growth of demand for electricity and heat in the regions in which the Group operates;
2. higher degree of certainty about the free trading sector for electricity, which has been enacted by the government of the Russian Federation as of August 2006 (see Note 1).

These developments have resulted in a change to the assumptions that were used to determine the value in use of the assets that comprise the cash generating units. An impairment review has been carried out by comparing the recoverable amount of the individual cash generating units with their net book values. For the purposes of the review, each of the Group's power plants was used as the relevant cash generating unit. The recoverable amount was generally based on value in use, which was calculated based on estimated future cash flows using various assumptions including the following:

- annual increase in electricity tariffs is estimated by the management as 13%-18% p.a. in 2008-2011 and 3% p.a. in 2012 and onwards;
- annual increase in heat tariffs is estimated by the management as 15%-18% p.a. in 2008-2011; 3% p.a. in 2012 and onwards;
- annual growth of gas prices is estimated by the management as 25%-28% p.a. in 2008-2011; 3% p.a. in 2012 and onwards;
- annual growth of coal prices is estimated by the management as 10% p.a. in 2008-2011; 3-6% p.a. in 2012 and onwards;

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

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Note 8. Property, plant and equipment (continued)

- growth of mazut prices set for the Company were on average 5-6% in 2008-2011 and 3-6% p.a. in 2012 and onwards;
- growth of peat prices set for the Company were on average 5-7% in 2008-2011 and 4% p.a. in 2012 and onwards;
- the assumption was made that production volumes of electricity and heat will remain at the current level for the whole impairment test period (investment programm is not included);
- increase of major cost (except of fuel) will not exceed the inflation rate;
- weighted average cost of capital of 13.90 % was applied for discounting future operating cash flows generated by the Company for all cash generating units;
- the Company's restructuring did not change the manner of recovery of the assets – the regulator allocated previously single tariffs for electricity and heat set for a vertically integrated power companies among newly created generating businesses.

Management's assessment indicates that value in use of property, plant and equipment will not be lower than its net book value including effect of reversal of impairment provision for all generating units. Consequently, the Group has recorded a reversal of the previously recognised impairment loss in the amount of RR 10,520,508 thousand. The impairment reversal and the corresponding deferred tax expense of RR 2,524,922 thousand were recognised in the income statement for the year ended 31 December 2006.

As from 1 January 2007 the Group intends to change its accounting policy from using of historic cost to revaluation for its property, plant and equipment (see Note 27); any change in the carrying values as a result of the revaluation will be recognised in the financial statements for 2007.

Note 9. Other non-current assets

Narrative	31 December 2006	31 December 2005
Investments in other entities	31,222	31,222
Non-current trade accounts receivable (Net of allowance for doubtful debtors of RR 192,296 thousand as of 31 December 2006, Net of allowance for doubtful debtors of RR 190,702 thousand as of 31 December 2005)	132,187	141,096
Non-current value added tax	21,902	37,017
Letter of credit	355,473	-
Other non-current assets	30,889	149
Total	571,673	209,484

As at 31 December 2006, Group issued an irrevocable letter of credit for equipment amounting to RR 355,473 thousand. Bank performed payment on the letter of credit in full amount after the equipment was supplied in 2007.

Note 10. Cash

Narrative	31 December 2006	31 December 2005
Cash at bank and in hand	116,623	207,089
Cash equivalents	218	225
Total	116,841	207,314

Cash equivalents comprise short-term investments in bank promissory notes. The Group has no restricted cash balances. All cash balances are in Russian Roubles.

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

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Note 11. Inventories

Narrative	31 December 2006	31 December 2005
Fuel production costs	1,427,717	395,358
Raw materials and supplies	335,507	287,464
Other inventories	223,082	215,638
Net of provision for obsolete stock	(5,676)	-
Total	1,980,630	898,460

Inventories balances as at 31 December 2006 included RR 1,195,265 thousand of inventories which were pledged as collateral according to loan agreements (As at 31 December 2005 - RR 13,249 thousand).

Note 12. Accounts receivable and prepayments

Narrative	31 December 2006	31 December 2005
Trade receivables (Net of allowance for doubtful debtors of RR 114,908 thousand as of 31 December 2006, Net of allowance for doubtful debtors of RR 175,675 thousand as of 31 December 2005)	1,073,702	1,021,364
Advances to suppliers and prepayments (Net of allowance for doubtful debtors of RR nil thousand as of 31 December 2006, Net of allowance for doubtful debtors of RR 23,871 thousand as of 31 December 2005)	613,754	283,361
Other receivables (Net of allowance for doubtful debtors of RR nil thousand as of 31 December 2006, Net of allowance for doubtful debtors of RR 26,282 thousand as of 31 December 2005)	294,571	325,582
VAT due from budget	69,495	186,576
Total	2,051,522	1,816,883

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

The above accounts receivable and prepayments include balances due from related parties (see Note 7).

Part of the accounts receivables have been classified as long-term due to the fact that it is due after more than one year from the balance sheet date.

Note 13. Equity**Basis of presentation of movements in equity**

The Group was formed by the combination of a number of businesses under common control. Because of the consequent use of the predecessor basis of accounting (see Note 3), the principal component of the net equity recognised for the Group is based on the historic carrying value of the net assets of the businesses contributed as recorded in the IFRS financial records of the predecessor enterprises, rather than the fair values of those net assets. Similarly, for the purpose of comparability, the equity of the

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 13. Equity (continued)

Group has been presented for comparative periods and as at 1 January 2005 as if the current Group structure had existed from 1 January 2005 (see Note 3). As the Group was formed as a result of a series of share issues completed after 1 January 2005, the equity statement reflects additions to share capital in the amount equal to the statutory nominal value of the shares issued which is based on the fair value of the net assets of the businesses contributed. In accordance with the predecessor basis of accounting, the effect of such additions to equity is offset by a corresponding increase in the merger reserve. In addition, the equity statement also reflects the impact of distributing the minority interest to the parent company of the Group.

Share capital

On 31 August 2006 the Group registered an additional issue of ordinary and preference shares placed by means of conversion of shares of merged companies into the shares of TGC-4 with conversion coefficients approved by merger agreement. The shares were converted at the date of completion of reorganization, i.e. 15 September 2006.

Narrative	Total number	Nominal value (in RR)
Ordinary shares as at		
1 January 2006	1,000,000,000	10,000,000
31 December 2006	1,321,201,964,859	13,212,019,649
Preference shares as at		
1 January 2006	-	-
31 December 2006	75,272,938,838	752,729,388
TOTAL as at		
1 January 2006	1,000,000,000	10,000,000
31 December 2006	1,396,474,903,697	13,964,749,037

Merger reserve

Merger reserve of RR 4,749,463 thousand as at the opening date represents the difference between IFRS carrying value of the contributed net assets merged into the Group, totaling RR 9,894,484 thousand, and the minority interest of RR 5,041,674 thousand. The merger reserve was subsequently adjusted by the share capital issued by TGC-4 to reflect the transfer of businesses owned by the entities under common control.

Contribution from shareholders

As described in Note 3, the income and related expenses for the 1st quarter 2005 for JSC "Priorsk Territorial Generating Company", JSC "Oryol Generating Company", for the 1st month 2005 for JSC "Kursk Generating Company", JSC "Smolensk Generating Company" and for the 11 days 2005 for JSC "Lipetsk Generating Company", JSC "Tambov Generating Company", JSC "Ryazan Heat Supply Generating Company" were carved out from RAO UES statements and included in the Group's financial statements. The net results of operations in the amount of RR 290,647 thousand were recorded as a contribution from shareholders in the equity statement during the year ended 31 December 2005.

Dividends

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

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 13. Equity (continued)

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

Branches	Year ended 31 December 2006		Year ended 31 December 2005	
	Declared dividends, in thousands of RR	Dividends per share, RR	Declared dividends, in thousands of RR	Dividends per share, RR
JSC "Bryansk Generating Company" for year 2005	10	-	1,289	0.0978 – per ordinary share; 0.11402 – per preferred share
JSC "Voronezh Generating Company" - for 6 months 2005	-	-	45,107	0.60249
JSC "Voronezh Generating Company" - for the year ended 31 December 2004	-	-	52,117	0.69612
JSC "Kursk Generating Company" - for year 2005	-	-	31,887	0.0230194
JSC "Lipetsk Generating Company" - for 6 months 2005	-	-	91,771	0.590084
JSC "Lipetsk Generating Company" - for 2005	4,937	0.031745	-	-
JSC "Lipetsk Generating Company" - for 3 months 2006	21,000	0.135029	-	-
JSC "Orel Generating Company" - for year 2005	1,478	0.006233	-	-
JSC "Ryazan Heat Supply Company" - for 6 months 2005	-	-	7,579	0.036624
JSC "Smolensk Generating Company" - for 6 months 2005	-	-	29,708	0.12242
JSC "Tambov Generating Company" - for year 2005	11,809	0.005649 – per ordinary share; 0.014630 – per preferred share	-	-
JSC "Prioksk Territorial Generating Company" - for 6 months 2005	-	-	36,587	0.023353
JSC "Prioksk Territorial Generating Company" - for 9 months 2005	-	-	20,669	0.013193

As disclosed in Note 27 Subsequent events in May 2007 TGC-4 declared additional RR 252,000 thousand dividends for the results of the year ended 31 December 2006.

Note 14. Basic and diluted earnings per share

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Profit/(loss) attributable to the shareholders of TGC-4 (thousands of RR)	8,416,611	249,272
Weighted average number of ordinary shares issued (thousands of shares)	391,638,399	6,259,860
Earning/(loss) per ordinary share for profit/(loss) attributable to the shareholders of TGC-4 – basic and diluted (in RR)	0.021	0.040

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

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Note 15. Non-current debt

Name	Effective interest rate, %	Maturity date	31 December 2006	31 December 2005
JSC "Sberbank RF", Central-Chernozem Branch	11.5	2013	812,390	-
JSC "Sberbank RF", Central-Chernozem Branch	11.5	2009	330,000	-
JSC "Alfa-Bank", Tula Branch	10.5	2008	400,000	-
JSB "Gazprombank", Tula Branch	9.8	2008	1,156,532	-
Smolensk Branch 8609 of JSC "Sberbank" Russia	11.0	2008	30,140	63,107
RAO UES (Centre of Power Sector Reform Promotion)	Interest-free	2007	-	157,813
Finance lease		2010	489,656	-
Total non-current debt			3,218,718	220,920
Less: current portion of non-current debt			-	(87,111)
Less: current portion of non-current finance lease			(129,421)	-
Total			3,089,297	133,809

The currency of all non-current debts is Russian Roubles.

Maturity schedule for non-current debt (except for finance lease)	31 December 2006	31 December 2005
Maturity		
Under one year	-	87
From 1 to 2 years	1,586,672	103,582
From 2 to 5 years	1,142,390	30,140
Total	2,729,062	133,809

The effective interest rate is the market interest rate applicable to the loan at the date of origination for fixed rate loans or the current market rate for floating rate loans.

As at 31 December 2006 estimated fair value of the long-term loans (including current portion of non-current debt) approximates its carrying value.

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 16. Current debt and current portion of non-current debt

Name	Effective interest rate, %	31 December 2006	31 December 2005
JSC "Alfa-Bank"	8.2	19,861	-
JSC "Alfa-Bank", Tula Branch	9.2	100,152	-
JSC "Alfa-Bank", Voronezh Branch	9.5-12	100,188	-
JSC "Alfa-Bank", Lipetsk Branch	9-11.5	-	13,020
JSCB "ROSBANK"	9.25-10.5	113,251	-
JSCB "ROSBANK", Tula Branch	8.5-12.75	498,536	-
JSB "Gazprombank"	10.5-10.6	-	53,659
JSB "Gazprombank", Tula Branch	10.6	-	102,423
JSB "Gazprombank", Lipetsk Branch	9.8	221,992	-
JSB "Gazprombank", Tula Branch	7.9-12	601,241	551,052
JSC "IMB"	10.45-10.75	200,115	-
JSC "Sberbank RF", Central-Chernozem Branch	11.5	112,577	-
JSC "Vneshtorgbank"	10-10.5	95,635	-
JSC "Vneshtorgbank", Tambov Branch	13.5	-	55,000
JSC "Prio-Vneshtorgbank"	11	-	1,000
JSC "Sberbank RF", Smolensk Branch # 8609	9.2-11	106,047	32,880
JSC "Uralsib", Voronezh Branch	12.0	-	65,000
RAO UES (Centre of Power Sector Reform Promotion)	Interest-free	87,111	-
Current portion of non-current debt			
- debt		-	87,111
- finance lease		129,421	
Total		2,386,129	961,145

The currency of all current debts is Russian Roubles.

Short term loans issued to the Group were secured as at 31 December 2006 by inventories totaling RR 1,195,265 thousand (see Note 11).

Note 17. Pension liabilities

The tables below provide information about the benefit obligations, plan assets and actuarial assumptions used for the year ended 31 December 2006 and 2005. Amounts recognised in the Combined and Consolidated Balance Sheet are as follows:

Narrative	31 December 2006	31 December 2005
Present value of defined benefit obligations (DBO)	746,645	463,423
Present value of unfunded obligations	746,645	463,423
Unrecognised actuarial gains/(losses)	(5,497)	(19,530)
Unrecognised past service (cost)/asset	(98,170)	(85,846)
Net liability in the balance sheet	642,978	358,047

Amounts recognized in the Combined and Consolidated Statement of Operations are as follows:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Current service cost	30,861	30,695
Interest cost	36,143	37,718
Amortisation of past service cost	7,142	7,142
Curtailment (gain)/loss	-	(69,084)
Immediate recognition of vested prior service cost	64,023	-
Net expense recognised in the Statement of Operations	138,169	6,471

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

(in thousands of Russian Roubles)

Note 17. Pension liabilities (continued)

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

Narrative	31 December 2006	31 December 2005
Present value of defined benefit obligations (DBO) at beginning of year	463,423	482,884
Service cost	30,861	30,695
Interest cost	36,143	37,718
Actuarial (gain)/loss	(14,034)	19,531
Past service cost	83,489	97,638
Benefits paid	(18,786)	(20,690)
Curtailment (gain)/loss	-	(82,494)
Sale of entity under common control (Belgorod)	-	(101,859)
Business combination (Belgorod)	165,549	-
Present value of defined benefit obligations (DBO) at the end of year	746,645	463,423

Principal actuarial assumptions are as follows:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Nominal discount rate	6.75%	7.00%
Wage growth rate	7.0%	7.0%
Inflation Rate	5.0%	5.0%

There were no changes in actuarial assumptions during 2005 - 2006.

Note 18. Accounts payable and accruals

Narrative	31 December 2006	31 December 2005
Trade payables	560,960	289,844
Wages and salaries payable	300,671	105,358
Advances received	165,044	157,387
Income payable to participants	14,061	125,866
Future period expenses provision	39,470	52,195
Promissory Notes Payable	-	1,686
Accounts Payable of associates	-	8,257
Accounts Payable on construction agreements	-	42,932
Other creditors	248,965	368,513
Total	1,329,171	1,152,038

Note 19. Other taxes payable

Narrative	31 December 2006	31 December 2005
Value added tax	24,605	310,973
Fines and interest	349	333
Property tax	69,096	55,225
Employee taxes	34,440	27,749
Other taxes	66,409	40,545
Total	194,899	434,825

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Note 20. Income tax expense

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Current income tax charge	335,176	474,644
Deferred income tax charge	2,545,444	(108,951)
Other similar payments	(151)	4,481
Total	2,880,469	370,174

During the year ended 31 December 2006 the Group entities were subject to a 24% income tax rate on taxable profits.

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

Net profit before income tax for financial reporting purposes is reconciled to theoretical income tax (statutory profit tax rate – 24%) as follows:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Profit before income tax	11,287,023	881,505
Theoretical income tax charge at an average statutory tax rate of 24 percent	(2,708,886)	(211,561)
Tax effect of items which are not deductible or taxable for taxation purposes	(171,583)	(158,613)
Total	(2,880,469)	(370,174)

Deferred income tax

Differences between IFRS and Russian statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes. The tax effect of temporary differences that resulted in formation of deferred assets and liabilities is shown below:

Deferred tax assets	31 December 2006	Movement for the year recognized in the statement of operations	31 December 2005
Other non-current liabilities	154,315	68,294	86,021
Property, plant and equipment	138,820	(74,636)	213,456
Non-current debt	83,611	83,611	-
Accounts receivable and prepayments	78,376	(25,005)	103,381
Accounts payable and accruals	77,385	40,489	36,896
Other non-current assets	48,481	46,370	2,111
Inventories	518	(3,744)	4,262
Deferred tax assets as at year end	581,506	135,379	446,127

Deferred tax liabilities	31 December 2006	Movement for the year recognized in the statement of operations	31 December 2005
Property, plant and equipment	3,273,730	2,879,816	393,914
Other non-current assets	8	(7,229)	7,237
Other	1,653	(15,332)	16,985
Deferred tax liabilities as at year end	3,275,391	2,857,255	418,136

During the year 2006 JSC "Heat Power Company" (Belgorod) merged the Group as a result of Business combination (Note 5). Consequently Deferred tax liability increased by RR 253,525 thousand and Deferred tax asset increased by RR 77,093 thousand.

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

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Note 20. Income tax expense (continued)

Deferred tax assets	31 December 2005	Movement for the year recognized in the statement of operations	31 December 2004
Property, plant and equipment	213,456	48,207	165,249
Accounts receivable and prepayments	103,381	48,844	54,537
Other non-current liabilities	86,021	(23,496)	109,517
Accounts payable and accruals	36,896	3,739	33,157
Inventories	4,262	(12,421)	16,683
Other non-current assets	2,111	(49,879)	51,990
Deferred tax assets as at year end	446,127	14,994	431,133

Deferred tax liabilities	31 December 2005	Movement for the year recognized in the statement of operations	31 December 2004
Property, plant and equipment	393,914	(162,898)	556,812
Accounts payable and other accruals	6,454	(2,645)	9,099
	17,768		5,338
Other		12,430	
Deferred tax liabilities as at year end	418,136	(153,113)	571,249

During the year 2005 RAO UES lost control over JSC "Heat Power Company" (Belgorod). In result Deferred tax liability decreased by RR 98,073 thousand and Deferred tax asset decreased by RR 38,917 thousand.

Note 21. Revenue

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Electricity	9,490,257	8,741,434
Heating	8,745,863	7,154,489
Other	735,820	418,592
Total	18,971,940	16,314,515

TGC-4 GROUP**Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005**

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Note 22. Cost of sales

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Fuel expenses	10,113,566	9,151,602
Employee benefits	2,329,636	1,682,580
Repairs and maintenance	1,413,544	985,910
Purchased electricity	1,033,962	413,082
Depreciation and impairment of property, plant and equipment	771,092	1,213,242
Taxes other than income tax	339,202	330,356
Water usage expenses (including payments to water treatment plants)	280,684	380,228
Other raw materials and supplies (including chemical agents)	318,706	297,568
Subscription fee in favour of RAO UES of Russia, FGC UES, CDU UES System Operator	165,909	-
Rent and lease payments	126,090	178,675
Guarding expenses	113,362	97,676
Insurance cost	86,770	56,318
Utilities	39,468	18,727
Consulting, legal and audit services	36,332	29,086
Other transportation services	75,837	54,322
Social expenses	31,970	18,818
Environmental payments	23,486	19,380
Other expenses	633,474	661,338
Total	17,933,090	15,588,907

Employee benefits expenses are comprised of the following:

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Salaries and wages, payroll taxes	2,067,288	1,565,414
Financial assistance to employees and pensioners	139,998	94,288
Non-governmental pension fund expenses	122,350	22,878
Employee benefits	2,329,636	1,682,580

Note 23. Finance costs

Narrative	Year ended 31 December 2006	Year ended 31 December 2005
Discounting effects	18,961	(52,904)
Interest expense/(income)	374,792	102,982
Pension interest expenses	36,143	37,718
Total	429,896	87,796

Note 24. Commitments**Sales commitments**

The Group sells electricity on the two wholesale electricity (capacity) market sectors: free trading sector and regulated trading sector.

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

Note 24. Commitments (continued)

Fuel commitments

The Group entities concluded a number of contracts for fuel supply. The principal suppliers of fuel are JSC "Gazprom" subsidiaries: LLC "Bryanskregiongaz", LLC "Voronezhregiongaz", LLC "Kalugaregiongaz", LLC "Kurskregiongas", LLC "Lipetskregiongaz", LLC "Oryolregiongaz", "Ryazanregiongaz", LLC "Smolenskregiongaz", LLC "Tambovregiongaz" and LLC "Tularegiongaz". Supplies are carried out under the terms of annual agreements. Purchase volumes are determined on the basis of estimated production demands. The purchase price of gas is determined by Federal Service of Tariffs.

Social commitments

The Group contributes to the maintenance and upkeep of the local infrastructure and the welfare of its employees, including contributions toward the development and maintenance of housing, hospitals, transport services, recreation and other social needs in the geographical areas in which it operates.

Capital commitments

Future capital expenditure for which contracts have been signed amounted to RR 2,604,517 thousand at 31 December 2006 (31 December 2005: RR 45,869 thousand).

Note 25. Contingencies

Political environment

The operations and earnings of Group entities continue, from time to time and in varying degrees, to be affected by political, legislative, fiscal and regulatory developments, including those related to environmental protection, in the Russian Federation.

Insurance

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

Legal proceedings

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

Tax contingency

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

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

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Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

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Note 25. Contingencies (continued)

No disclosure has been made in respect of the possible financial effect of potential claims or disputes on these matters, as this might seriously prejudice the position of the Group.

As at 31 December 2006 management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued for in these Financial Statements.

Environmental matters

Group entities and their predecessor entities have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group entities periodically evaluate their obligations under environmental regulations. Potential liabilities might arise as a result of changes in legislation and regulation or civil litigation. The impact of these potential changes cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

Guarantees

Guarantees are irrevocable assurances that the Group will make payments in the event that another party cannot meet its obligations. As at 31 December 2006 the Group issued guarantees in respect of the borrowings drawn down by the third parties in accordance with the contracts of guarantees in total amount of RR 585,950 thousand (31 December 2005 nil).

Note 26. Financial instruments and financial risk factors

Financial risk factors

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

Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out finance market position.

The Group aims at maintaining flexibility in funding by means of monitoring of cash position (through budgeting) and keeping borrowings available.

Interest rate risk

The Group's operating profits and cash flows from operating activity are largely not dependent on the changes in market interest rates. The Group is only exposed to fair value interest rate risk as all of its borrowings are at fixed interest rates; these are disclosed in Note 15. The Group has no material interest-bearing assets.

Fair values

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

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

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Note 26. Financial instruments and financial risk factors (continued)

Credit risk

The credit risk represents the risk of default by the Group contractors of their obligations to the Group when due and in full.

Financial assets which potentially subject the Group entities to concentrations of credit risk consist principally of trade receivables from related parties (see Note 6). Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance for doubtful debtors already recorded.

The Group has developed and approved Credit policy, ensuring the maintenance of debt position levels and cost of debts levels. Decision on the Group's debt structure is made based on minimization of the debt's cost, availability of borrowings and income maximizing.

Foreign exchange risk

The Group operates within the Russian Federation. The Group's purchases and borrowings are denominated in Russian Roubles.

Note 27. Subsequent events

Shares sale

Pursuant to RAO UES strategy to decrease affiliation of repair and maintenance companies, approved by RAO UES Board of Directors the Group executed sale of repair and maintenance organisations stock.

The Group terminated its participation in JSC "Ryazanenergoremont" in May 2007. 57,263,900 shares with par value of RR 1 each were sold to LLC "Bites" for RR 55,678 thousand.

The Group terminated its participation in JSC "Tambovenergospetsremont" in June 2007. 42,534,000 shares with par value of RR 1 each were sold to LLC "Teploenergomontazh" for RR 43,000 thousand.

On 31 July 2007 Board of Directors of the Group approved the decision to terminate participation of JSC "TGC-4" in JSC "Belgorodenergосervice" by sale of its shares at the public auction at a price not lower than the fair value defined by the independent appraiser (RR 30,200 thousand).

Dividends

Annual dividend amount per share was approved by the TGC-4 general meeting of shareholders on 15 May 2007 and equals to RR 0.000180455 per ordinary share and RR 0.000180455 per preference share. Total amount of declared dividends is RR 252,000 thousand.

On 17 August 2007 Board of Directors recommended to the extraordinary general meeting of shareholders to approve interim dividends in accordance with 6 months of 2007 results in the amount of 0.0000358045 per ordinary share and RR 0.0000358045 per preference share.

Revaluation of property, plant and equipment

The Group changed its accounting policy to revaluing its property, plant and equipment from 1 January 2007. Independent appraisers engaged by the Group have estimated fair value of the Group's property, plant and equipment (except property, plant and equipment of the following subsidiaries: JSC "Novomoskovskaya GRES", JSC "Ryazanenergoremont", JSC "Tambovenergospetsremont", JSC "Tulaenergocomplex") at RR 32,799 thousand as at 1 January 2007.

Bond issue

On 7 June 2007 TGC-4 issued 5 million bonds with par value of RR 1,000 each with 5 years maturity by public subscription at Moscow Interbank Stock Exchange (MMVB).

TGC-4 GROUP

Notes to the Combined and Consolidated Financial Statements for the years ended 31 December 2006 and 31 December 2005

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Note 27. Subsequent events (continued)

Equity issue

TGC-4 shareholders on extraordinary general meeting held 31 August 2007 decided to increase equity capital of TGC-4 by placing 586,000,000 additional ordinary shares with par value of RR 0.01 with the total value of RR 5,860,000 thousand. The placement will be conducted by public subscription at a price defined by the Board of Directors of TGC-4 after expiration of pre-emptive right. Increase in share capital through additional shares placement will be conducted for cash attraction in amount up to RR 18,000,000 thousand.

Joint activity

On 28 August 2007 Board of Directors of TGC-4 agreed Memorandum of principal provisions of joint venture creation (JV) between ČEZ – leading Czech electric company and JSC "TGC-4". It contains parties' intentions to study possibilities and terms of joint participation in the Project of new generating power capacities creation on the basis of Shchekinskaya GRES.

Structural changes

In order to increase effectiveness of operational activity of the Group integration of JSC "TGC-4" branches is conducted. In accordance with the Board of Directors decision dated 1 September 2007 Eastern Regional generation branch of JSC "TGC-4" which combined Lipetsk and Tambov branches started to operate.