TGC-4 GROUP

CONSOLIDATED FINANCIAL STATEMENTS
PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)
FOR THE YEAR ENDED 31 DECEMBER 2008

PRICEWATERHOUSECOOPERS

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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 consolidated financial statements of JSC "TGC-4" and its subsidiaries (the "TGC-4 Group") which comprise the consolidated balance sheet as of 31 December 2008 and the consolidated income statement, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 consolidated financial statements present fairly, in all material respects, the financial position of the TGC-4 Group as of 31 December 2008, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation

15 July 2009

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TGC-4 GROUP
Consolidated Balance Sheet as at 31 December 2008
(in thousands of Russian Roubles, unless otherwise stated)

	Notes	31 December 2008	31 December 2007
ASSETS			
Non-current assets			
Property, plant and equipment	8	21,878,279	38,485,791
Intangible assets		61,327	28,769
Investments in associates	5	13,445	13,463
Deferred tax assets	21	542,178	500,931
Long-term accounts receivable and prepayments	11	82,988	100,948
Other non-current assets	9	140,489	121,007
Total non-current assets		**22,718,706**	**39,250,909**
Current assets			
Inventories	10	1,859,247	1,928,123
Accounts receivable and prepayments	11	4,304,594	3,099,321
Current income tax prepayments		1,719	159,031
Deposits in banks	12	4,500,000	-
Cash and cash equivalents	13	4,592,694	198,637
Other current assets		353	16,562
Total current assets		**15,258,607**	**5,401,674**
TOTAL ASSETS		**37,977,313**	**44,652,583**
EQUITY AND LIABILITIES			
Share capital			
Ordinary shares (nominal value)		19,125,056	13,212,020
Preference shares		752,729	752,729
Treasury shares		(1,069)	-
Share premium		10,921,097	959,867
Merger reserve		(1,807,993)	(1,807,993)
Revaluation reserve for property, plant and equipment		3,485,857	10,664,296
Retained earnings		(5,706,177)	2,890,448
Equity attributable to shareholders of TGC-4	14	**26,769,500**	**26,671,367**
Minority interest		3,401	27,388
TOTAL EQUITY		**26,772,901**	**26,698,755**
Non-current liabilities			
Non-current debt	17	1,078,544	5,568,470
Deferred tax liabilities	21	566,698	5,286,975
Pension liabilities	18	805,449	705,187
Total non-current liabilities		**2,450,691**	**11,560,632**
Current liabilities			
Current debt and current portion of non-current debt	16	5,870,626	4,984,707
Accounts payable and accruals	19	1,261,144	1,152,267
Provision for legal claims	26	812,591	38,558
Current income tax liabilities		249,745	3,375
Other taxes payable	20	559,615	214,289
Total current liabilities		**8,753,721**	**6,393,196**
TOTAL LIABILITIES		**11,204,412**	**17,953,828**
TOTAL EQUITY AND LIABILITIES		**37,977,313**	**44,652,583**

General Director — E.Y. Abramov

Chief Accountant — I.A. Lapitskaya

15 July 2009

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

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Revenue	22	29,222,777	24,627,275
Other operating income	22	308,171	219,186
Operating expenses other than impairment related to property, plant and equipment	23	(30,780,849)	(24,843,893)
Impairment (charge) / reversal related to property, plant and equipment	8	(10,600,862)	279,480
Revaluation write down	8	-	(6,257,915)
Operating loss		**(11,850,763)**	**(5,975,867)**
Finance income	24	540,216	10,519
Finance costs	24	(923,267)	(836,412)
Share of result of associates	5	232	7,315
Loss before income tax		**(12,233,582)**	**(6,794,445)**
Income tax benefit	21	2,489,715	1,578,388
Loss for the year from continuing operations		**(9,743,867)**	**(5,216,057)**
Discontinued operations:			
Profit for the year from discontinued operations	6	-	63,465
Loss for the year		**(9,743,867)**	**(5,152,592)**
Attributable to:			
The Group shareholders		(9,719,880)	(5,137,467)
Minority interest		(23,987)	(15,125)
Loss per ordinary share for loss from continuing operations attributable to the Group shareholders – basic and diluted (in Russian Roubles per share)	15	**(0.006)**	**(0.004)**
Earnings per ordinary share for profit from discontinued operations attributable to the Group shareholders – basic and diluted (in Russian Roubles per share)	15	-	**0.00005**

General Director — E.Y. Abramov

Chief Accountant — I.A. Lapitskaya

15 July 2009

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
CASH FLOW FROM OPERATING ACTIVITIES:			
Loss before income tax		**(12,233,582)**	**(6,794,445)**
Profit for the year from discontinued operations	6	-	63,465
Adjustments for other non-cash items			
Depreciation of property, plant and equipment	8, 23	3,444,199	3,191,973
Amortization of intangible assets	23	54,339	8,707
Impairment charge / (reversal of) related to property, plant and equipment	8	10,800,862	(279,480)
Revaluation write down	8	-	6,257,915
Income tax related to discontinued operations		-	(18,431)
Loss on disposal of subsidiary		-	(48,753)
Share of profits of associate	5	(232)	(7,315)
Loss on disposal of associate		-	12,053
Accounts payable written off		(7,977)	(5,078)
Increase of accounts receivable impairment	11, 23	490,104	63,534
Accounts receivable written-off		4,214	744
Increase of inventory impairment provision		278	6,962
Exchange differences		927	13,906
Interest expense	24	864,120	787,217
Interest income	24	(540,216)	(614)
Impairment of available-for-sale financial assets	5	46,268	26,068
Impairment of investments in associate	5	5,155	-
Loss on disposal of property, plant and equipment		1,259	17,237
Pension interest expense	18,24	59,147	49,195
Pension operating expenses/accruals	18,23	88,605	65,430
Provision for legal claims	23,26	787,821	38,558
Other non-cash items		(21,920)	(76,982)
Operating cash flows before working capital changes and income tax paid		**3,643,369**	**3,371,866**
Increase in accounts receivable and prepayments		(1,610,124)	(1,202,791)
Increase in other current assets		-	(39,616)
Decrease in inventories		304,775	94,438
Increase in other non-current assets		(52,586)	(83,835)
Decrease in accounts payable and accruals		(89,129)	(77,340)
Increase in taxes payable other than income tax		345,325	1,445
Cash provided by operating activities before interest and taxes		**2,541,630**	**2,064,167**
Income tax paid		31,173	(340,658)
Interest paid		(881,977)	(731,139)
Interest received		488,863	1,019
Net cash generated from operating activities		**2,179,689**	**993,389**

TGC-4 GROUP
Consolidated Statement of Cash Flows for the year ended 31 December 2008
(in thousands of Russian Roubles, unless otherwise stated)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
CASH FLOW FROM INVESTING ACTIVITIES:			
Purchase of property, plant and equipment and other non-current assets		(5,428,932)	(5,554,276)
Proceeds from sale of property, plant and equipment and other non-current assets		28,264	56,545
Purchase of intangible assets		(86,897)	(18,707)
Proceeds from sale of associates		-	15,100
Purchase of short-term financial investments		(8,000,000)	(31,313)
Proceeds from sale of short-term financial investments		3,500,000	32,000
Disposal of subsidiaries, net of cash disposed		-	93,176
Dividends received		250	1,092
Net cash used in investing activities		**(9,987,315)**	**(5,406,384)**
CASH FLOW FROM FINANCING ACTIVITIES:			
Repayment of finance lease		(165,821)	(167,895)
Proceeds from borrowings		30,815,183	31,327,366
Repayment of debts		(34,228,456)	(31,367,587)
Proceeds from bonds issuance		-	5,000,000
Expenses from bonds issuance		-	(950)
Purchase of treasury shares		(33,463)	-
Proceeds from share issuance		15,822,000	-
Dividends paid		(7,760)	(296,143)
Net cash generated from financing activities		**12,201,683**	**4,494,791**
Increase in cash and cash equivalents		**4,394,057**	**81,796**
Cash and cash equivalents at the beginning of the year		198,637	116,841
Cash and cash equivalents at the end of the year		4,592,694	198,637

General Director E.Y. Abramov

Chief Accountant I.A. Lapitskaya

15 July 2009

Consolidated Statement of Changes in Equity for the year ended 31 December 2008
(in thousands of Russian Roubles, unless otherwise stated)

	Attributable to the shareholders of TGC-4									
	Ordinary share capital	Preference share capital	Treasury shares	Share premium	Merger reserve	Revaluation reserve	Retained Earnings	Total	Minority interest	Total equity
At 1 January 2007	13,212,020	752,729	-	959,867	(1,807,993)	255,720	7,226,863	20,599,206	42,608	20,641,814
Property, plant and equipment:										
Revaluation (Note 8)	-	-	-	-	-	15,146,880	-	15,146,880	-	15,146,880
Transfer of the realised revaluation reserve	-	-	-	-	-	(1,451,386)	1,451,386	-	-	-
Income tax recognised in equity (Note 21)	-	-	-	-	-	(3,635,251)	-	(3,635,251)	-	(3,635,251)
Transfer of income tax recognised in equity	-	-	-	-	-	348,333	(348,333)	-	-	-
Net income/expenses recognised directly in equity	-	-	-	-	-	10,408,576	1,103,053	11,511,629	-	11,511,629
Loss for the year	-	-	-	-	-	-	(5,137,467)	(5,137,467)	(15,125)	(5,152,592)
Total recognised income and expenses for the year	-	-	-	-	-	10,408,576	(4,034,414)	6,374,162	(15,125)	6,359,037
Dividends (Note 14)	-	-	-	-	-	-	(302,001)	(302,001)	(95)	(302,096)
At 31 December 2007	13,212,020	752,729	-	959,867	(1,807,993)	10,664,296	2,890,448	26,671,367	27,388	26,698,755
Share issuance (Note 14)	5,860,000	-	-	9,962,000	-	-	-	15,822,000	-	15,822,000
Purchase of treasury shares (Note 14)	-	-	(14,029)	(19,434)	-	-	-	(33,463)	-	(33,463)
Merger of JSC "TGC-4 Holding"	53,036	-	12,960	18,664	-	-	(3,042)	81,618	-	81,618
Property, plant and equipment: Impairment of property, plant and equipment (Note 8)	-	-	-	-	-	(7,945,855)	-	(7,945,855)	-	(7,945,855)
Income tax recognised in equity (Note 21)	-	-	-	-	-	1,899,300	-	1,899,300	-	1,899,300
Transfer of the realised revaluation reserve	-	-	-	-	-	(1,414,855)	1,414,855	-	-	-
Transfer of income tax recognised in equity	-	-	-	-	-	282,971	(282,971)	-	-	-
Net income/expenses recognised directly in equity	-	-	-	-	-	(7,178,439)	1,131,884	(6,046,555)	-	(6,046,555)

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

	Attributable to the shareholders of TGC-4									
	Ordinary share capital	Preference share capital	Treasury shares	Share premium	Merger reserve	Revaluation reserve	Retained Earnings	Total	Minority interest	Total equity
Loss for the year	-	-	-	-	-	-	(9,719,880)	(9,719,880)	(23,987)	(9,743,867)
Total recognised income and expenses for the year	-	-	-	-	-	(7,178,439)	(8,587,996)	(15,766,435)	(23,987)	(15,790,422)
Dividends (Note 14)	-	-	-	-	-	-	(5,587)	(5,587)	-	(5,587)
At 31 December 2008	19,125,056	752,729	(1,069)	10,921,097	(1,807,993)	3,485,857	(5,706,177)	26,769,500	3,401	26,772,901

General Director E.Y. Abramov

Chief Accountant I.A. Lapitskaya

15 July 2009

Note 1. The Group and its operations

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

As at 31 December 2008 the Group TGC-4 (hereinafter – the Group) incorporates TGC-4 with ten branches located in Belgorod, Bryansk, Voronezh, Kaluga, Kursk, Lipetsk, Oryol, Ryazan, Smolensk and Tula and subsidiaries. The principal subsidiaries are listed in Note 5.

The Company is incorporated in accordance with the Russian Federation legislation.

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

As at 31 December 2008, the number of the Group's employees was 16,462 (as at 31 December 2007 16,892).

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

TGC-4 operates 10 generating branches. The Group's principal activity is generation and sale of electricity (capacity) and heat.

Main developments in the Group's 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 decisions to reorganize the companies in the form of a merger with 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 a merger with TGC-4.
- On 8 April 2006 similar decisions were taken at the extraordinary 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 decisions to reorganize the company in the form of a merger with TGC-4 on the conditions envisaged by the Merger Agreement and to approve the Merger Agreement and the deed of transfer.
- On 21 July 2006 the Board of RAO UES performing the functions of the general meeting of shareholders of TGC-4 took decisions to reorganize the Company in the form of a takeover of its 11 regional generating companies, to approve the Merger Agreement and increase the Group's charter capital by placing additional shares for converting the shares of merged companies in the manner envisaged by the Merger Agreement. Conversion coefficients were determined as well.
- On 15 September 2006 termination of activities of the 11 regional generating companies as a result of the merger with TGC-4 was registered in the Uniform State Register of Legal Entities. Shares of the merged companies were converted and TGC-4 started to operate as a single company.

These developments represented the reorganisation of entities under common control and were accounted for using the predecessor values method (Note 14).

Changes in the Group

- At the extraordinary general meeting held on 31 August 2007 TGC-4's shareholders decided to increase the equity capital of TGC-4 by placing 586,000,000,000 additional ordinary registered shares with a par value of RR 0.01 per share and a total par value of RR 5,860,000 thousand. The placement was executed in May 2008 at the price of RR 0.027 per share as defined by the Board of Directors. As a result of this placement TGC-4 raised cash of RR 15,822,000 thousand (Note 14).

Note 1. The Group and its operations (continued)

RAO UES's interest in TGC-4 decreased from 50.02% to 34.649% as a result of the additional placement of shares. In June 2008 RAO UES's interest decreased to 0% due to the sale of TGC-4's shares previously owned by RAO UES to ONEXIM HOLDINGS LIMITED and the transfer of 212,754,467,344 shares to JSC "TGC-4 Holding" for subsequent merger of JSC "TGC-4 Holding" with TGC-4.

As at the reporting date ONEXIM HOLDINGS LIMITED who owns 49.999% of the Company's ordinary shares has significant influence over the Company.

- On 29 April 2008 the Board of Directors of TGC-4 approved the decision on the additional issue of the registered non-documentary ordinary shares of TGC-4 amounting to 6,600,255,897 shares with a par value of RR 0.01 each, which are placed when spinning-off JSC "TGC-4 Holding" from RAO UES with a simultaneous merger of JSC "TGC-4 Holding" with TGC-4 by converting the shares of JSC "TGC-4 Holding" into the shares of TGC-4. In total 5,303,612,900 shares with a par value of RR 0.01 each were placed in the merger process (1,296,642,997 shares remained unplaced) (Note 14).

  The reorganization of TGC-4 in the form of a merger with JSC "TGC-4 Holding" was finalized on 1 July 2008. All shares of JSC "TGC-4 Holding" were converted into TGC-4's shares using the conversion ratios set out in the merger agreement.

- 30 June 2008 TGC-4 was reorganized in the form of a merger with its wholly owned subsidiary JSC "Novomoskovskaya GRES", in accordance with decision of TGC-4 shareholders taken on 29 October 2007 at the extraordinary general meeting (Note 5).

Creation of subsidiaries

In November 2007 the Board of Directors made a decision to establish JSC "Orlovskaya Heat Network Company" (TGC-4's interest is 100%) and JSC "Belgorodskaya Heat Network Company" (TGC-4's interest is 100%).

JSC "Orlovskaya Heat Network Company" was registered in November 2007 with the charter capital of RR 10,000 thousand to be paid in cash. Notification of the FFMS Regional Branch on the state registration of the securities' issue and the report on the results of the stock issue of JSC "Orlovskaya Heat Network Company" was provided on 19 February 2008.

JSC "Belgorodskaya Heat Network Company" was registered in December 2007 with the charter capital of RR 3,084,430 thousand of which RR 10,000 thousand are to be paid in cash and RR 3,074,430 thousand to be contributed by other assets (fixed assets at market value determined by an independent appraiser). The charter capital was paid up in February 2008.

Notification of the FFMS Regional Branch on the state registration of the securities' issue and the report on the results of the stock issue of JSC "Belgorodskaya Heat Network Company" was provided on 12 March 2008.

In August 2008 the Board of Directors adopted a decision to establish JSC "Smolenskaya Heat Network Company" (TGC-4's interest is 100%).

JSC "Smolenskaya Heat Network Company" was registered on 19 August 2008 with the charter capital of RR 1,000 thousand to be paid in cash. The charter capital was paid up in October 2008. Notification of the FFMS Regional Branch on the state registration of the securities' issue and the report on the results of the stock issue of JSC "Smolenskaya Heat Network Company" was provided on 7 October 2008.

In September 2008 the Board of Directors adopted a decision to establish JSC "Kurskaya Heat Network Company" (TGC-4's interest is 100%) and in JSC "Smolenskteploenergoremont" (TGC-4's interest is 100%).

JSC "Kurskaya Heat Network Company" was registered in October 2008, with the charter capital of RR 1,000 thousand to be paid in cash. The charter capital was paid up in November 2008. Notification of the FFMS Regional Branch on the state registration of the securities' issue and the report on the results of the stock issue of JSC "Kurskaya Heat Network Company" was provided on 17 February 2009.

Note 1. The Group and its operations (continued)

JSC "Smolenskteploenergoremont" was registered in October 2008, with the charter capital of RR 1,000 thousand to be paid in cash. In November 2008 the charter capital was partially paid up in the amount of RR 20 thousand. Notification of the FFMS Regional Branch on the state registration of the securities' issue and the report on the results of the stock issue of JSC "Smolenskteploenergoremont" was provided on 17 February 2009.

Operating environment

The Russian Federation displays certain characteristics of an emerging market, including inconvertibility of the Russian Rouble in most countries outside of the Russian Federation and relatively high inflation. Despite strong economic growth in recent years, the financial situation in the Russian market significantly deteriorated during 2008, particularly in the fourth quarter. As a result of global volatility in financial and commodity markets, among other factors, there has been a significant decline in the Russian stock market since mid-2008. Since September 2008, there has been increased volatility in currency markets and the Russian Rouble has depreciated significantly against some major currencies. The official US Dollar exchange rate of the Central Bank of the Russian Federation ("CBRF") increased from RR 25.37 at 1 October 2008 to RR 29.38 at 31 December 2008.

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

Management is unable to predict all developments in the economic environment which could have an impact on the Group's operations and consequently what effect, if any, they could have on the financial position of the Group.

Relations with the State and current regulation

As at 31 December 2007 the Russian Federation owned 52.7% of the voting shares of RAO UES. In its turn RAO UES owned 50.02% of the voting ordinary shares of TGC-4.

In June 2008 RAO UES's interest in TGC-4 decreased to 0% as a result of the sale of TGC-4 shares owned by RAO UES to ONEXIM HOLDINGS LIMITED.

The Government directly affects the Group's operations by regulating its wholesale energy sales through the Federal Service on Tariffs ("FST"), and its retail sales of electricity and heat through Regional Energy Commissions ("RECs").

The operations of all generating facilities are coordinated by the System Operator of the Unified Energy System ("SO UES") in order to meet system requirements in a more efficient manner. Operations of SO UES are controlled by the state.

Although certain volumes of electric power and capacity are traded at open prices, tariffs for major volumes of electric and heat power sold by Group entities are governed by regulations specific to the electricity and heat generation 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, a basis of accounting which significantly differs from International Financial Reporting Standards ("IFRS"). In practice, tariff decisions were impacted significantly by social and political considerations, causing significant delays in tariff determinations and tariff increases that were lower than required to compensate for cost increases.

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

Regulatory issues and sector restructuring

The Russian electric utility in general and the Group in particular are presently undergoing a reform process designed to introduce competition into the electricity sector and to create an environment in which energy companies (including TGC-4) can raise the capital required to maintain and expand current capacity. On 28 June 2008 the changes to the Wholesale Electric Power (capacity) Market Rules of the Transition Period (NOREM) were approved by the Resolution of the Government of the Russian Federation No. 476. According to these changes, starting from 1 July 2008 capacity exceeding the

Note 1. The Group and its operations (continued)

regulated contracts, as well as that of new input generating capacities, is traded at non-regulated prices on a wholesale market.

According to the Resolution of the Government of the Russian Federation, capacity can be traded in several ways, including by means of bilateral contracts for the sale of electricity and capacity between the wholesale market participants. Thus, from 1 July 2008 up to 25% of electricity could be sold at market prices and the schedule of the power market liberalization coincides with that of the electricity market liberalization approved by Resolution of the Russian Government No. 643. By 1 January 2011 the schedule envisages that 100% of electricity and power will be sold at market prices.

Note 2. Financial position

As at 31 December 2008 the Group's current assets exceeded its current liabilities by RR 6,504,886 thousand which is explained by the fact that certain parts of the proceeds received from the share issuance in 2008 were deposited with banks (as at 31 December 2007 the Group's current assets were below its current liabilities by RR 991,522 thousand which is explained by the use of short-term borrowings to finance its investments).

As described above, the Group is affected by the Russian government's policy through control of tariffs and other factors. The FST has 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 the 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.

The existing economic situation of the world and Russian economies and a forecast decrease of GDP may affect electricity consumption. Accordingly, the Government of the Russian Federation could revise its forecast of social-economic development during 2009-2012, and that could result in changes to the terms of the liberalisation of wholesale market and plans of electricity tariff indexation as well as the timeline of the Group's investment program that was devised on the basis of electricity consumption growth rate that is not achievable under current circumstances.

Any change of terms of the wholesale market liberalisation and plans of electricity tariff indexation may influence the Group's revenues. Debtors of the Group may be adversely affected by the financial and economic environment which could in turn impact their ability to repay the amounts owed.

Although the Group's current collections of accounts receivable is high enough, the Group continues to experience difficulties in obtaining settlements of accounts receivable, particularly, for heat sales, the majority of which are receivables from housing and utilities entities (Note 11). Also, there still remains a significant level of uncollectible accounts receivable for heat sold in the period prior to restructuring. There is legislation enabling the Group to terminate service to delinquent customers, but certain strategic and political factors make this difficult. The Group has recognised impairment losses against doubtful accounts receivable, as further described in Note 11.

Currently decreasing demand for electricity and heat due to the decline in the Russian economy may have an adverse impact on the group's operations and more tough borrowing terms and conditions may affect the ability of the Group to obtain new borrowings at terms similar to those applied to earlier transactions. Deteriorating economic conditions for the Group's customers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management believes that it has properly reflected revised estimates of expected future cash flows in its assessment of possible impairment of assets (Note 8).

Management is unable to reliably determine the effects on the Group's future financial position of any further deterioration in the Group's operating environment as a result of the ongoing crisis. Management believes it is taking all the necessary measures to support the sustainability and development of the Group's business in the current circumstances, including arrangements to improve the Group's operational efficiency and efficiency of its investment projects as well as measures to optimize its costs, such as:

Note 2: Financial position (continued)

- 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 energy generation assets.

Note 3. Basis of preparation

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and related interpretations adopted by the International Accounting Standards Board ("IASB").

Each Group's entity 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.

The accounting policies have been consistently applied to all periods presented.

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.

New accounting developments

These financial statements have been prepared by applying the accounting policies consistent with those of the annual financial statements for the year ended 31 December 2007.

Certain new interpretations became effective for the Group from 1 January 2008:

- 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); and
- 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).

These interpretations did not have any significant effect on the Group's consolidated financial statements.

"Reclassification of Financial Assets" Amendments to IAS 39, "Financial Instruments: Recognition and Measurement", and IFRS 7, "Financial Instruments: Disclosures and a subsequent amendment", "Reclassification of Financial Assets: Effective Date and Transition". The amendments allow entities the options (a) to reclassify a financial asset out of the held for trading category if, in rare circumstances, the asset is no longer held for the purpose of selling or repurchasing it in the near term; and (b) to reclassify an available-for-sale asset or an asset held for trading to the loans and receivables category, if the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity (subject to the asset otherwise meeting the definition of loans and receivables). The amendments may be applied with retrospective effect from 1 July 2008 for any reclassifications made before 1 November 2008; the reclassifications allowed by the amendments may not be applied before 1 July 2008 and retrospective reclassifications are only allowed if made prior to 1 November 2008. Any reclassification of a financial asset made on or after 1 November 2008 takes effect only from the date when the reclassification is made.

The Group has not elected to make any of the optional reclassifications during the period.

Note 3. Basis of preparation (continued)

The following new standards, amendments to standards and interpretations have been issued and are effective for the financial years beginning after 1 January 2009 and have not been early adopted.

- IFRS 8 "Operating Segments" (effective for annual reporting 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. The Group will apply the new standard from 1 January 2009 and is currently assessing what impact the new IFRS will have on its consolidated financial statements.

- Amendment to IAS 23 "Borrowing Cost" (effective for borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009). The revised IAS 23 was issued in March 2008. The main change to IAS 23 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. An entity is, therefore, required to capitalise such borrowing costs as part of the cost of the asset. The revised standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

- Amendment to IAS 1 "Presentation of Financial Statements" (revised in September 2007, effective for annual reporting periods beginning on or after 1 January 2009). The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its consolidated financial statements starting in 2009.

- Amendment to IAS 32 and IAS 1, "Puttable Financial Instruments and Obligations Arising on Liquidation" (effective for annual periods beginning on or after 1 January 2009). The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability. The Group does not expect the amendment to affect its consolidated financial statements.

- IAS 27, "Consolidated and Separate Financial Statements" (revised January 2008, effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

- Amendments to IFRS 2, "Share-based Payment Vesting Conditions and Cancellations" (effective for annual periods beginning on or after 1 January 2009). The amendment deals with two matters. It clarifies that vesting conditions are service conditions and performance conditions only. Other features of a share-based payment are not vesting conditions. It also specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The Group does not expect the amendment to affect its consolidated financial statements.

- IFRS 3, "Business Combinations" (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application

Note 3. Basis of preparation (continued)

of the acquisition method to business combinations. The requirement to measure at fair value every asset and liability at each step fin a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, in a business combination achieved in stages, the acquirer will have to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss. Acquisition related costs will be accounted for separately from the business combination and, therefore, recognized as expenses rather than included in goodwill. An acquirer will have to recognise at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The Group will apply the new standard to any business combination in 2010.

- Amendment to IFRS 1 and IAS 27 "Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate" (revised May 2008; effective for reporting periods beginning on or after 1 January 2009). The amendment allows first-time adopters of IFRS to measure investments in subsidiaries, jointly controlled entities or associates at fair value or at previous GAAP carrying value as deemed cost in the separate financial statements. The amendment also requires distributions from pre-acquisition net assets of investees to be recognised in profit or loss rather than as a recovery of the investment. The amendments will not have an impact on the Group's consolidated financial statements.
- Amendment to IAS 39, "Financial Instruments: Recognition and Measurement" (effective with retrospective application for annual periods beginning on or after 1 July 2009, with earlier application permitted). The amendment to IAS 39 clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The Group is currently assessing the impact of the amendment on its consolidated financial statements.
- IFRIC 13, "Customer Loyalty Programmes" (effective for annual periods beginning on or after 1 July 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. The Group does not operate any loyalty programmes.
- IFRIC 15, "Agreements for the Construction of Real Estate" (effective for annual periods beginning on or after 1 January 2009). The interpretation applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors, and provides guidance for determining whether agreements for the construction of real estate are within the scope of IAS 11 or IAS 18. It also provides criteria for determining when entities should recognise revenue on such transactions. IFRIC 15 is not currently relevant to the Group's operations because it does not have any agreements for the construction of real estate.
- IFRIC 16, "Hedges of a Net Investment in a Foreign Operation" (effective for annual periods beginning on or after 1 October 2008). The interpretation explains which currency risk exposures are eligible for hedge accounting and states that translation from the functional currency to the presentation currency does not create an exposure to which hedge accounting could be applied. The IFRIC allows the hedging instrument to be held by any entity or entities within a group except the foreign operation that itself is being hedged. The interpretation also clarifies how the gain or loss recycled from the currency translation reserve to profit or loss is calculated on disposal of the hedged foreign operation. Reporting entities will apply IAS 39 to discontinue hedge accounting prospectively when their hedges do not meet the criteria for hedge accounting in IFRIC 16. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.
- IFRIC 17, "Distribution of Non-Cash Assets to Owners" (effective for annual periods beginning on or after 1 July 2009, with earlier application permitted). The interpretation clarifies when and how distribution of non-cash assets as dividends to the owners should be recognised. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets will be recognised in profit or loss when the entity settles the dividend payable. The Group will apply IFRIC 17 if it distributes non-cash assets to owners in the future.

Note 3. Basis of preparation (continued)

- IFRS 1, "First-time Adoption of International Financial Reporting Standards" (effective for the first IFRS financial statements for a period beginning on or after 1 July 2009). The revised IFRS 1 retains the substance of its previous version but within a changed structure in order to make it easier for the reader to understand and to better accommodate future changes. The Group concluded that the revised standard does not have any effect on its consolidated financial statements.
- The amendments to the IFRSs which are the part of the IASB's annual improvements project published in May 2008 are effective from 1 January 2009. In 2007, the International Accounting Standards Board decided to initiate an annual improvements project as a method of making necessary, but non-urgent, amendments to IFRS. The amendments issued in May 2008 consist of a mixture of substantive changes, clarifications, and changes in terminology in various standards. The substantive changes relate to the following areas: classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary; possibility of presentation of financial instruments held for trading as non-current under IAS 1; accounting for sale of IAS 16 assets which were previously held for rental and classification of the related cash flows under IAS 7 as cash flows from operating activities; clarification of definition of a curtailment under IAS 19; accounting for below market interest rate government loans in accordance with IAS 20; making the definition of borrowing costs in IAS 23 consistent with the effective interest method; clarification of accounting for subsidiaries held for sale under IAS 27 and IFRS 5; reduction in the disclosure requirements relating to associates and joint ventures under IAS 28 and IAS 31; enhancement of disclosures required by IAS 36; clarification of accounting for advertising costs under IAS 38; amending the definition of the fair value through profit or loss category to be consistent with hedge accounting under IAS 39; introduction of accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting. The Group does not expect the amendments to have any material effect on its consolidated financial statements.
- On 16 April 2009 the IASB issued "Improvements to IFRSs", a collection of amendments to 12 standards as part of its program of annual improvements. The latest amendments were included in exposure drafts published in October 2007, August 2008 and January 2009. Most of the amendments are effective for annual periods beginning on or after 1 January 2010. The Group is assessing the impact of those pronouncements on its consolidated financial statements.
- IFRIC 18, "Transfers of Assets from Customers" (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. IFRIC 18 is not expected to have any impact on the Group's consolidated financial statements.
- Improving Disclosures about Financial Instruments - Amendment to IFRS 7, "Financial Instruments: Disclosures" (issued in March 2009; effective for annual periods beginning on or after 1 January 2009). The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity will be required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment (a) clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and (b) requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk. The Group is currently assessing the impact of the amendment on disclosures in its consolidated financial statements.
- Amendments to IFRIC 9 and IAS 39 "Embedded Derivatives " (effective for annual periods ending on or after 30 June 2009). The amendments clarify that on reclassification of a financial asset out of the "at fair value through profit or loss" category, all embedded derivatives have to be assessed and, if necessary, separately accounted for. The Group is currently assessing the impact of the amendment on disclosures in its consolidated financial statements.

Note 3. Basis of preparation (continued)

- On 9 July 2009 IASB issued an International Financial Reporting Standard designed for use by small and medium-sized entities (IFRS for SMEs). IFRS for SMEs simplified many of the principles of full IFRS for recognising and measuring assets, liabilities income and expense, and the number of required disclosures have been simplified and significantly reduced. IFRS for SMEs is not applicable for the Group's operations.

Going concern

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

Impairment of financial assets carried at amortised cost

Impairment is recognised as a result of the Group's assessment of whether the collectability of specific customer accounts deteriorated compared to prior estimates. The primary factors that the Group considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any portion or instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the counterparty experiences a significant financial difficulty as evidenced by its financial information that the Group obtains;
- the counterparty considers bankruptcy or a financial reorganisation;
- there is adverse change in the payment status of the counterparty as a result of changes in the national or local economic conditions that impact the counterparty; or
- the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

If conditions change and management determines that the collectability of accounts receivable has improved, the impairment is fully or partially reversed. See effect of these critical accounting estimates and assumptions in Note 11.

Impairment of non-financial assets

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 impairment loss is recognised in the income statement to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Accounting for impairment includes impairments of property, plant and equipment, investments in associates and inventory obsolescence.

See effect of these critical accounting estimates and assumptions in Note 5, 8, 10.

Note 3. Basis of preparation (continued)

Provisions for liabilities and charges

The Group accrues provision for legal proceedings when its assessments indicate that it is probable that a liability has been incurred 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.

See effect of these critical accounting estimates and assumptions in Note 26.

Revaluation of property, plant and equipment

Fair value of property, plant and equipment and the remaining useful life of property, plant and equipment of the Group companies have been determined by independent appraisers as at 1 January 2007. The carrying value and depreciation of property, plant and equipment are affected by the estimates of replacement cost, depreciated replacement cost and remaining useful lives. Changes in these assumptions could have a material impact to the fair value of property, plant and equipment (see Note 8).

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. See effect of these critical accounting estimates and assumptions in Note 8.

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. See effect of these critical accounting estimates and assumptions in Note 26.

Note 4. Summary of significant accounting policies

Principles of consolidation

a) Subsidiaries

Subsidiaries are those companies and other entities which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain benefits. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries other than those acquired from parties under common control. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.

The excess of the cost of acquisition over the acquirer's share of the fair value of the net assets of the acquiree at each exchange transaction is recorded as goodwill. The excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is recognised immediately in profit or loss.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest.

Note 4. Summary of significant accounting policies (continued)

Minority interest is that part of the net results and of the net assets of a subsidiary attributable to interests which are not owned, directly or indirectly, by the Company. Minority interest forms a separate component of the Group's equity.

Transactions eliminated on consolidation

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

Purchases of subsidiaries from parties under common control

Purchases of subsidiaries from parties under common control are accounted for using the predecessor values method. Under this method the consolidated financial statements of the combined entity are presented as if the businesses had been combined from the beginning of the earliest period presented or, if later, the date when the combining entities were first brought under common control. The assets and liabilities of the subsidiary transferred under common control are at the predecessor entity's carrying amounts. The predecessor entity is considered to be the highest reporting entity in which the subsidiary's IFRS financial information was consolidated. Related goodwill inherent in the predecessor entity's original acquisitions is also recorded in these consolidated financial statements. Any difference between the carrying amount of net assets, including the predecessor entity's goodwill, and the consideration for the acquisition is accounted for in these consolidated financial statements as an adjustment to merger reserve within equity.

b) Associates

Associates are entities over which the Group has significant influence (directly or indirectly), 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.

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 income statement.

The exchange rates prevailing as at 31 December 2008 as determined by the Central Bank of the Russian Federation, between the RR and the US Dollar ("USD") was RR 29.3804: USD 1.00 (as at 31 December 2007 RR 24.5462: USD 1.00), between the RR and EURO RR 41.4411: EURO 1.00 (as at 31 December 2007 RR 35.9332: EURO 1.00).

Property, plant and equipment

Starting from 1 January 2007 the Group changed its accounting policy for property, plant and equipment which are now stated at revalued amount less any subsequent accumulated depreciation and subsequent accumulated impairment losses. The revaluation model is applied in relation to all classes of PPE except for the following classes of fixed assets: communications; motor vehicles; computer; instruments, tools, measuring equipment; other machinery. Those classes of PPE are measured at costs less accumulated depreciation and accumulated impairment.

Note 4. Summary of significant accounting policies (continued)

Prior to 1 January 2007 property, plant and equipment were stated at cost less accumulated depreciation less accumulated impairment losses. As of the beginning of 2005 property, plant and equipment were stated at the carrying value determined in accordance with the IFRS at the date of their transfer to the Group by the Predecessor entity. 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 were 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 impairment loss is recognised in the income statement to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Property, plant and equipment are subject to revaluation on a regular basis. The frequency of revaluation depends upon the movements in the fair values of the assets being revalued.

Increases in the carrying amount arising on revaluation are credited to revaluation reserve in equity. Decreases that offset previous increases of the same asset are charged against revaluation reserve directly in equity; all other decreases are charged to the consolidated income statement. The revaluation reserve in equity is transferred directly to retained earnings when the surplus is realised either on the retirement or disposal of the asset or as the asset is used by the Group; in the latter case, the amount of the surplus realised is the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on the asset's original cost.

When an item of property, plant and equipment was revalued, any accumulated depreciation at the date of the revaluation was eliminated against the gross carrying amount of the asset and the net amount was restated to the revalued amount of the asset.

Further acquisitions of property, plant and equipment between revaluations 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 loses 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.

Prepayments

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group.

Depreciation

Land is not depreciated. 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.

Useful lives of property, plant and equipment are subject to annual assessment by management and if expectations differ from previous estimates, the changes of useful lives are accounted for as a change in an accounting estimate prospectively.

Note 4. Summary of significant accounting policies (continued)

In 2008 the depreciation on property, plant and equipment was based on the following useful lives in years:

Type of facility	Acquired prior to 31 December 2006	Acquired subsequent to 31 December 2006
Electricity and heat generation	4-54	9-32
Electricity distribution	3-28	9-21
Heating networks	3-36	5-25
Other	1-63	3-28

Intangible assets

The Group's intangible assets have definite useful lives and primarily include capitalised computer software and licenses. Intangible assets are stated at cost, adjusted for subsequent disposal, amortization and impairment.

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

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

Type	Useful lives
Computer software	1-10
Licenses	1-9

If impaired, the carrying amount of intangible assets is written down to the higher of value in use and fair value less costs to sell.

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the net identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of exchange. Goodwill on acquisitions of subsidiaries is presented separately in the consolidated balance sheet. Goodwill on acquisitions of associates is included in the investment in associates. Goodwill is carried at cost less accumulated impairment losses, if any.

The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired. Goodwill is allocated to the cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or groups of units represent the lowest level at which the Group monitors goodwill and are not larger than a segment. Gains or losses on disposal of an operation within a cash generating unit to which goodwill has been allocated include the carrying amount of goodwill associated with the operation disposed of, generally measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit which is retained.

Financial assets

a) Classification of financial assets

The Group classifies its financial assets in the following categories: loans and receivables and available-for-sale. The Group does not have any financial assets held-to-maturity and financial assets at fair value through profit or loss. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. The group's loans and receivables comprise "trade and other receivables" and cash and cash equivalents in the balance sheet (Notes 11 and 13).

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date (Note 9).

Note 4. Summary of significant accounting policies (continued)

b) Recognition and measurement

Financial assets are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Group commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

The Group uses discounted cash flow valuation techniques to determine the fair value of financial assets that are not traded in an active market.

The Group derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

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.

Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method.

Inventory

Inventories are recorded at the lower of cost and net realizable value. Cost of fuel is determined on the weighted average basis, for other groups – specific identification of the individual costs.

Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

Value added tax on purchases and sales

Output VAT related to sales is payable to federal 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 goods and services and the VAT invoice.

The tax authorities allow to offset VAT. VAT related to sales and purchases is recognised 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.

Note 4. Summary of significant accounting policies (continued)

Trade and other receivable

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less impairment. An impairment of trade receivables is established when there is objective evidence that the group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired.

The amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within "operating expenses". If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss.

When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against "operating expenses" in the income statement.

Trade and other payables

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

Provisions for liabilities and charges

Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Guarantees

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 initially 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. This amount is amortised on a straight line basis over the life of the guarantee. Financial guarantees are subsequently measured at the higher of (i) the remaining unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the obligation at the balance sheet date.

Debt

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost, any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowing costs

Prior to 1 January 2009, the Group recognised all borrowing costs as an expense in the period in which they are incurred.

Note 4. Summary of significant accounting policies (continued)

Pension and post-employment benefits

In the normal course of business the Group 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.

The Group's entities operate 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 Group 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.

Pension plans are qualified as unfunded plans. Therefore, the balances in the pension accounts of the Fund shall be accounted in the balance sheet within the non-current assets as a separate asset (Note 9).

Current and deferred income tax

Income taxes have been provided for in the financial statements in accordance with legislation enacted or substantively enacted by the balance sheet date. The income tax charge comprises current tax and deferred tax and is recognised in the income statement except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes other than on income are recorded within operating expenses.

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

The Group controls reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains at their disposal. The Group does not recognise deferred tax liabilities on such temporary differences except to the extent that Management expects the temporary differences to reverse in the foreseeable future.

The Group's uncertain tax positions are reassessed by management at every balance sheet date. Liabilities are recorded for income tax positions that are determined by management as more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the balance sheet date and any known court or other rulings on such issues. Liabilities for penalties, interest and taxes other than on income are recognised based on management's best estimate of the expenditure required to settle the obligations at the balance sheet date.

Note 4. Summary of significant accounting policies (continued)

Revenue recognition

Revenue is recognised on the delivery of electricity, capacity and heat during the period. Revenues are measured at the fair value of consideration received or receivable. 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 risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the lease term. The lease term is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

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.

Financial 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 from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate. They are presented in the income statement under a general heading such as "other operating income".

Treasury shares

Where the Company or its subsidiaries purchase the Company's equity instruments, the consideration paid, including any directly attributable incremental costs, net of income taxes, is deducted from equity attributable to the Company's equity holders until the equity instruments are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

Dividends

Dividends are recognized as a liability and deducted from equity at the balance sheet date only if they are declared and approved by shareholders before or on the balance sheet date. Dividends are disclosed when they are declared after the balance sheet date, but before the financial statements are authorized for issue.

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. Preference shares are not redeemable and are considered to be participating shares.

Note 4. Summary of significant accounting policies (continued)

Environmental liabilities

Liabilities for environmental remediation are recorded where there is a present obligation, the payment is probable and reliable estimates can be made. Group regularly pays for normative pollutions and pollutions above norms. All such payments are recorded in the income statement.

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.

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 and receivables 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.

Note 5. Group subsidiaries and associated companies

The Group's consolidated financial statements include the following wholly owned subsidiaries.

		Ownership, %	
Name of subsidiary	Activity	31 December 2008	31 December 2007
JSC "Novomoskovskaya GRES"	Electricity and heat generation	-	100
JSC "Belgorodskaya Heat Network Company"	Heat generation and distribution	100	-
JSC "Orlovskaya Heat Network Company"	Heat generation and distribution	100	-
JSC "Smolenskaya Heat Network Company"	Heat generation and distribution	100	-
JSC "Kurskaya Heat Network Company"	Heat generation and distribution	100	-
JSC "Smolenskteploenergoremont"	Repairs of heat- and electromechanical equipment of power stations	100	-

In the reporting year the Parent company merged with JSC "Novomoskovskaya GRES". In addition, from 2008 the Group also includes the following five newly established 100% owned subsidiaries: JSC "Belgorodskaya Heat Network Company", JSC "Orlovskaya Heat Network Company", JSC "Smolenskaya Heat Network Company", JSC "Kurskaya Heat Network Company", JSC "Smolenskteploenergoremont" (Note1).

Note 5. Group subsidiaries and associated companies (continued)

The Group has the followig associated companies:

Name of associate	Activity	Ownership, % 31 December 2008	31 December 2007
JSC "Energetic Health Centre"	Health and recreation of families and children	49	49
JSC "Technotest-Energo"	Assembly and repair works including facilities controlled by the RF Government Technical Supervision	49	49
JSC "Schekinskiye PGU"	Technical supervision services with respect to design and construction of power generating units	41	13

In the reporting year the Company's interest in the charter capital of JSC "Schekinskiye PGU" changed from 13% as at 31 December 2007 up to 41% as at 31 December 2008 as a result of receiving shares in the process of TGC-4 reorganisation in the form of a merger with JSC "TGC-4 Holding".

As at 31 December 2008 investments in the shares of JSC "Schekinskiye PGU" are recognized on the balance sheet in the zero amount, net of the related impairment. The asset has been impaired due to the bankruptcy procedure of JSC "Schekinskiye PGU".

The table below summarises the movements in the carrying amount of the Group's investment in associates.

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Carrying amount at 1 January	13,463	34,394
Fair value of net assets of associates acquired	5,155	-
Impairment of investments in associates	(5,155)	-
Fair value of net assets of associates disposed	-	(27,154)
Share of profit of associates	232	7,315
Dividends received from associates	(250)	(1,092)
At 31 December	**13,445**	**13,463**

Summarised financial information of associates, including the aggregated amounts of assets, liabilities, revenues and profit or loss is as follows.

JSC "Energetic Health Centre"

Balance Sheet

Narrative	31 December 2008	31 December 2007
Property, plant and equipment	22,204	21,836
Total non-current assets	**22,204**	**21,836**
Cash and cash equivalents	1,587	2,692
Accounts receivable and prepayments	801	389
Inventories	404	306
Total current assets	**2,792**	**3,387**
TOTAL ASSETS	**24,996**	**25,223**
Accounts payable and accruals	7	75
Total current liabilities	**7**	**75**
TOTAL LIABILITIES	**7**	**75**

Income Statement

Narrative	Year ended 31 Decemebr 2008	Year ended 31 December 2007
Revenue	11,965	11,902
Profit/(loss) for the year	**(159)**	**5 473**

Note 5. Group subsidiaries and associated companies (continued)

JSC "Technotest-Energo"

Balance sheet

Narrative	31 December 2008	31 December 2007
Property, plant and equipment	427	695
Total non-current assets	**427**	**695**
Cash and cash equivalents	522	865
Accounts receivable and prepayments	1 832	1,066
Total current assets	**2,354**	**1,931**
TOTAL ASSETS	**2,781**	**2,626**
Deferred tax liabilities	29	28
Total non-current liabilities	**29**	**28**
Accounts payable and accruals	303	271
Total current liabilities	**303**	**271**
TOTAL LIABILITIES	**332**	**299**

Income Statement

Narrative	Year ended 31 Decemebr 2008	Year ended 31 December 2007
Revenue	13,887	17,502
Profit for the year	**633**	**992**

Note 6. Discontinued operations

Operations discontinued in 2007

In 2007 shares of subsidiaries JSC "Ryazanenergoremont" and JSC "Tambovenergospetsremont" were disposed by a competitive sale of shares with the involvement of a specialized agent.

JSC "Ryazanenergoremont"

Income Statement

Narrative	3 months ended 30 March 2007
Revenue	285
Cost of sales	(1,116)
Financial costs	(45)
Income tax expense	17,674
Net profit for the period	**16,798**

Cash Flow Statement

Narrative	3 months ended 30 March 2007
Cash at the beginning of the period	**16**
Operating activities	(7,058)
Investment activities	2,675
Financial activities	4,373
Cash at the end of the period	**6**

Note 6. Discontinued operations (continued)

JSC "Tambovenergospetsremont"

Income statement

Narrative	Period ended 19 June 2007
Revenue	5,094
Cost of sales	(7,937)
Income tax expense	757
Net loss for the period	**(2,086)**

Cash Flow Statement

Narrative	Period ended 19 June 2007
Cash at the beginning of the period	**1,174**
Operating activities	5,333
Investment activities	(210)
Financial activities	(400)
Cash at the end of the period	**5,897**

The following gain from sales of subsidiaries was included in profit from discontinued operations for the year ended 31 December 2007:

Narrative	Year ended 31 December 2007
Gain from sales of subsidiaries	48,753

Note 7. Related parties

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, or the party is a member of the key management personnel of the entity or its parent. 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 2008 and 31 December 2007 is detailed below.

As at 31 December 2007 50.02% of the voting ordinary shares were owned by the state-controlled RAO UES. Therefore, the related parties of the Group in 2007 included RAO UES and its subsidiaries as well as other entities controlled by the State.

In June 2008 RAO UES's interest decreased to 0% as a result of the sale TGC-4 shares to ONEXIM HOLDINGS LIMITED.

As at the reporting date ONEXIM HOLDINGS LIMITED who owns 49.999% of the Company's ordinary shares has significant influence over the Company.

Transactions with subsidiaries of RAO UES related to sales of electric power and other sales as well as purchases of electric power and other purchases for 2008 have been disclosed for the period from the year beginning till 30 June 2008.

The table below shows related party transactions for the periods ended 31 December 2008 and 31 December 2007 and balances with related parties as at 31 December 2008 and 31 December 2007.

Note 7. Related parties (continued)

Transactions with subsidiaries of JSC RAO UES of Russia

Transactions with subsidiaries of RAO UES were as folows:

Narrative	Period from 1 January to 30 June 2008	Year ended 31 December 2007
Income		
Sales of heat and electricity	1,583,682	4,576,389
Other sales	-	37,633
Expenses		
Purchase of electricity	130,436	364,040
Repairs and technical maintenance	43,612	94,974
NOREM services	129,887	153,499
Other expenses	14,680	223,521
Interest expense	-	8,633

There are no balances related to transactions with subsidiaries of RAO UES for the year ended 31 December 2008.

Narrative	Year ended 31 December 2007
Accounts receivable and prepaymets, gross	83,919
Provision for impairment of accounts receivable	(46,765)
Accounts receivable, net	37,154
Accounts payable and accruals	44,413

Significant transactions with other related parties represent transactions with JSC "Tulskaya distrubution company" which is related to the Group by the same member of the key management personel as of the Group.

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Income		
Sales of heat and electricity	2 289 471	2 387 294
Expenses		
Purchase of electricity	8 477	-

There are no balances related to transactions with JSC "Tulskaya distrubution company" for the year ended 31 December 2008.

The Group does not have any transactions with companies controlled by ONEXIM Group for the year ended 31 December 2008.

Products sold to related parties on standard commercial terms at market prices. The cost of sold electric and heat energy was determined at the tariffs established by the regulatory authority for each station.

Goods, products, work and services from related parties were bought on standard commercial terms at market prices, except for prices of goods and services that are regulated by the tariff legislation.

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 the Russian statutory financial statements. The compensation is approved by the Board of Directors. In addition, members of the Management Board are paid discretionary bonuses, which are approved by the Chairman of the Management Board based on his assessment 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.

Note 7. Related parties (continued)

Key management received the following remuneration during the years ended 31 December 2008 and 31 December 2007:

Narrative	Year ended 31 December 2008		Year ended 31 December 2007	
	Expenses	Liabilities	Expenses	Liabilities
Salaries	21,005	736	15,600	1,072
Bonuses	44,651	-	21,566	-
Compensation	4,701	-	4,827	-
Other	4,794	-	4,177	-
Contributions under pension agreements	459	-	414	-
Total	**75,610**	**736**	**46,584**	**1,072**

At 31 December 2008 there were 11 members of the Board of Directors and 3 members of the Management Board.

Termination benefits

In May 2008 TGC-4 entered into additional agreements to employment contracts with the General Director and members of the Company's Management Board. These agreements set out the procedure, terms and conditions for termination benefits payable to members of the Company's top management. The amount of such benefits depends on the cause and date of the termination. Under these agreements, termination benefits are only paid on termination taking place within the period from 1 May 2008 through to 1 June 2009. The amount paid to key management personnel in the reporting year totalled RR 25,994 thousand. The amount to be paid by the Company varies from zero to RR 8,870 thousand.

The Group has no other compensation programs.

Note 8. Property, plant and equipment

Property, plant and equipment

Narrative	Electricity & heat generation	Electricity distribution	Heating networks	Other	Construction in progress	Total
Cost						
Balance as at 31 December 2007	20,996,159	721,052	9,245,983	6,444,862	4,426,130	41,834,186
Additions	217,976	-	5,589	47,574	5,230,351	5,501,490
Transfers	867,175	51,044	818,011	361,030	(2,097,260)	-
Disposals	(18,114)	(126)	(1,015)	(18,869)	(88,459)	(126,583)
Balance as at 31 December 2008	22,063,196	771,970	10,068,568	6,834,597	7,470,762	47,209,093
Accumulated depreciation (including impairment)						
Balance as at 31 December 2007	(1,654,203)	(67,524)	(971,720)	(654,948)	-	(3,348,395)
Impairment loss	(8,839,815)	(239,716)	(5,115,414)	(2,676,383)	(1,675,389)	(18,546,717)
Charge for the period	(1,728,811)	(77,802)	(1,045,010)	(592,576)	-	(3,444,199)
Disposals	2,539	68	122	5,768	-	8,497
Balance as at 31 December 2008	(12,220,290)	(384,974)	(7,132,022)	(3,918,139)	(1,675,389)	(25,330,814)
Net book value as at 31 December 2007	19,341,956	653,528	8,274,263	5,789,914	4,426,130	38,485,791
Net book value as at 31 December 2008	9,842,906	386,996	2,936,546	2,916,458	5,795,373	21,878,279

Note 8. Property, plant and equipment (continued)

Property, plant and equipment

Narrative	Electricity & heat generation	Electricity distribution	Heating networks	Other	Construction in progress	Total
Cost						
Balance as at 31 December 2006	23,556,876	1,045,469	9,405,046	7,540,417	2,178,450	43,726,258
Revaluation – reclassification of accumulated depreciation	(7,092,865)	(451,190)	(4,089,947)	(5,099,181)	-	(16,733,183)
Revaluation increase	6,189,760	197,158	4,422,322	3,166,250	1,171,390	15,146,880
Revaluation write-down	(4,030,812)	(164,615)	(1,360,014)	(402,488)	(299,986)	(6,257,915)
Additions	575,435	108	70,543	94,480	5,289,081	6,029,647
Transfers	1,808,721	95,393	801,865	1,156,749	(3,862,728)	-
Disposals	(10,956)	(1,271)	(3,832)	(11,365)	(50,077)	(77,501)
Balance as at 31 December 2007	20,996,159	721,052	9,245,983	6,444,862	4,426,130	41,834,186
Accumulated depreciation (including impairment)						
Balance as at 31 December 2006	(7,339,262)	(474,534)	(4,089,947)	(5,268,648)	-	(17,172,391)
Reversal of impairment loss	231,679	20,241	-	27,560	-	279,480
Revaluation – reclassification of accumulated depreciation	7,092,865	451,190	4,089,947	5,099,181	-	16,733,183
Charge for the period	(1,640,091)	(64,783)	(972,483)	(514,616)	-	(3,191,973)
Disposal	606	362	763	1,575	-	3,306
Balance as at 31 December 2007	(1,654,203)	(67,524)	(971,720)	(654,948)	-	(3,348,395)
Net book value as at 31 December 2006	16,217,614	570,935	5,315,099	2,271,769	2,178,450	26,553,867
Net book value as at 31 December 2007	19,341,956	653,528	8,274,263	5,789,914	4,426,130	38,485,791

Note 8. Property, plant and equipment (continued)

The Group changed its accounting policies related to revaluation of property, plant and equipment from 1 January 2007 (Note 4).

For each revalued class of property, plant and equipment stated at revalued amount in these financial statements, the carrying amount that would have been recognized as at 31 December 2008 had the assets been carried under the cost model is as follows.

	Electricity & heat generation	Electricity distribution	Heating networks	Other	Construction in progress	Total
Net book value as at 31 December 2008	8,765,233	358,138	1,630,412	1,910,236	5,640,482	18,304,501
Net book value as at 31 December 2007	17,275,346	647,561	5,648,336	5,214,778	1,751,466	30,537,487

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 2008 such advances amounted to RR 4,502,718 thousand (as at 31 December 2007 – RR 2,130,936 thousand).

Other property, plant and equipment include motor roads, coolers, chimneys, vehicles, computers, office fixtures and other equipment.

There are no pledged property, plant and equipment.

Impairment provision for property, plant and equipment

As described in Note 2, the ongoing global financial and economic crisis continues to effect the Group, in particular:

- the financial crisis has resulted in a higher volatility of stock markets, severe reduction of liquidity in Russian economy and aggravated terms of raising funds in Russia;
- mid-term prognoses of such macroeconomic indicators as GDP and inflation index have changed significantly;
- decline in prices for commodities, in particular for oil, stable gas condensate, liquified gas and oil products is the evidence of the reduced demand from consumers;
- lower liquidity levels led to reduced production at some Russian entities and consequently to reduced demand for electricity;
- significant reduction of TGC-4's market capitalization in the fourth quarter 2008.

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. Branches and subsidiaries of TGC-4, including power stations and heat network assets were used as the relevant 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. 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:

- Cash flows were projected based on actual operating results for 2008 and the business plan for 2009. Projected future cash flows from operating activity as at reporting date are lower then estimated as at 1 January 2007 particularly due to the growth of operating expenses and the decrease of sales volumes, partially because of the influence of financial crisis. Regulated tariffs established for JSC "Belgorodskaya Heat Network Company", which was separated from TGC-4, do not recover all current expenses of that subsidiary, and consequently result in the projection of negative cash flows from 2009;
- A post-tax discount rate of 15.87% was applied in determining the recoverable amount of the generating units. The discount rate was calculated based on the weighted average cost of capital. A post-tax discount rate of 13.89% was used for the revaluation in 2007;

Note 8. Property, plant and equipment (continued)

- The forecast period for existent capacity is 12-14 years. The forecast period for the revaluation in 2007 was set up to the year 2025 (18 years);
- The values assigned to the key assumptions represent management's assessment of future trends in the business and are based on both external sources and internal sources;
- Annual increase in electricity tariffs is estimated by management to be at the level of gas prices growth (principal technological fuel);
- Annual increase in heat tariffs is estimated by management in the part related to fuel – at the level of gas prices increase and in the part related to direct component – at the level of inflation rates;
- Annual increase in capacity tariffs is estimated by management to be in line with the inflation rate.
- The forecast of electricity, capacity and heat prices in revaluation model in the year 2007 for the period 2007-2010 were based on Scenario forecast of development of electric utility industry in Russia, but since 2011 appraiser used assumption that prices should be set at the level which could lead the company to EBITDA/Revenue ratio equal to 20.57% which is average for emerging markets in energy sector. Such assumption was not used in 2008;
- Annual growth of gas prices is estimated by the management as 26% per annum ("p.a.") in 2009-2010; 37% p.a. in 2011; 30% p.a. in 2012; 20% p.a. in 2013, 10% p.a. in 2014, 3-7% starting from 2015. For the 2007 revaluation gas prices were assumed to grow as 27% p.a. in 2009-2010, 29% in 2011, 8% p.a. in 2012-2015 and 3% p.a. starting from 2016;
- Annual growth of coal prices is estimated by the management as 3-6% p.a. starting from 2009. For the 2007 revaluation coal prices were assumed to grow at 3-10% p.a.;
- Growth of mazut prices is estimated as 1-5% p.a. from 2009. For the 2007 revaluation mazut prices were assumed to grow at 3-10% p.a.;
- Annual growth of inflation is estimated by the management as 10% p.a. in 2009; 9.4% p.a. in 2010 ; 8% p.a. in 2011, 7.2% p.a. in 2012, 7% p.a. in 2013, 3-6% starting from 2014. For the 2007 revaluation the following inflation rates were used: 6% p.a. in 2009-2013, 5% p.a. in 2014-2015; 4% p.a. in 2016-2018 and 3 % p.a. starting from 2019.
- The assumption was made that production volumes of electricity and heat will remain at the current level for the whole impairment test period (investment program is not included);
- Increase of other cost (except of fuel) will not exceed the inflation rate.

The impairment loss recognised against each of the cash generating units is presented below:

Narrative	Total impairment loss	Charged to equity	Charged to the income statement
JSC "Belgorodskaya Heat Network Company"	(2,706,270)	(981,895)	(1,724,375)
JSC "Tulenergocomplect"	(33,499)	-	(33,499)
Bryanskaya regional generation	(352,141)	(66,295)	(285,846)
Voronezhskaya regional generation	(939,020)	(336,567)	(602,453)
Kaluzhskaya regional generation	(133,820)	(9,963)	(123,857)
Kurskaya regional generation	(2,268,961)	(921,608)	(1,347,353)
Vostochnaya regional generation	(5,682,950)	(2,252,098)	(3,430,852)
Ryazanskaya regional generation	(301,150)	(154,264)	(146,886)
Tulskaya regional generation	(5,677,113)	(3,207,581)	(2,469,532)
Impairment of corporate assets	(40,840)	(15,584)	(25,256)
Impairment of advances to construction	(410,953)	-	(410,953)
Total	**(18,546,717)**	**(7,945,855)**	**(10,600,862)**

Note 8. Property, plant and equipment (continued)

The following table as at 31 December 2008 presents sensitivities of profit and loss and equity to reasonably possible changes in the post-tax discount rate, inflation rate and annual growth of gas prices applied at the balance sheet date relative to the impairment assumptions made by the Group, with all other variables held constant:

Expected impact	Change forecast scenario factor					
	WACC		Inflation		Gas prices growth	
	-1%	+1%	-1%	+1%	-1%	+1%
Impact on profit and loss	1,166,633	(1,443,008)	(1,267,790)	995,503	686,193	(1,046,641)
Impact on equity	360,894	(570,381)	(264,504)	180,463	245,978	(1,206,107)

The impairment test resulted in an imparment loss of RR 18,546,717 thousand being recognised (as at 31 December 2007 – RR 0 thousand).

Finance lease

The Group leases property, plant and equipment on the basis of finance lease agreements. At the end of each lease transaction 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 2008	31 December 2007
Electricity and heat generation	850,361	917,435

Finance lease rentals are payable as follows:

Maturity table for finance lease (discounted minimum lease payments)	31 December 2008	31 December 2007
Maturity		
not later than one year	170,298	169,855
from 1 to 5 years	220,240	390,537
Total	**390,538**	**560,392**

Maturity table for finance lease (undiscounted minimum lease payments)	31 December 2008	31 December 2007
Maturity		
not later than one year	284,876	346,866
from 1 to 5 years	277,213	562,088
Total	**562,089**	**908,954**

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 under operating lease terms.

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

As at 31 December 2008

Narrative	Land lease	Lease of buildings and structures	Lease of other property, plant and equipment	Total
Under one year	133,235	16,979	6,911	157,125
From 1 to 5 years	378,639	44,988	15,731	439,358
From 5 years	1,556,070	56,496	37,421	1,649,987
Total	**2,067,944**	**118,463**	**60,063**	**2,246,470**

Note 8. Property, plant and equipment (continued)

As at 31 December 2007

Narrative	Land lease	Lease of buildings and structures	Lease of other property, plant and equipment	Total
Under one year	125,934	22,448	4,405	152,787
From 1 to 5 years	404,171	65,739	14,707	484,617
From 5 years	1,455,739	56,426	37,650	1,549,815
Total	**1,985,844**	**144,613**	**56,762**	**2,187,219**

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

Management of the Group believes, that after the expiration of the land lease agreements they will be renegotiated onto additional periods.

Note 9. Other non-current assets

Narrative	31 December 2008	31 December 2007
Available-for-sale investments in the fund	83,667	76,002
Letter of credit	28,328	38,538
Available-for-sale investments	28,494	6,467
Total	**140,489**	**121,007**

At 31 December 2008 the assets recorded on joint accounts and on individual accounts in non-state pension fund in respect of current employees in amount of RR 83,667 thousand (RR 76,002 thousand at 31 December 2007) are intended to be used for settlement of defined benefit pension obligations.

The Group has an irrevocable letter of credit for equipment delivery amounting to RR 28,328 thousand as at 31 December 2008 (RR 38,538 thousand as at 31 December 2007). The decrease of the letter of credit amount during the period ended 31 December 2008 related to the payment to a supplier and reduced total amount of the letter of credit according to the contract.

As at 31 December 2008 available-for-sale investments included the shares of JSC "RusHydro" in the amount of RR 27,182 thousand (45,227,455 shares at the market value RR 0.601) received by TGC-4 as a result of a merger with JSC "TGC-4 Holding".

Note 10. Inventories

Narrative	31 December 2008	31 December 2007
Fuel stock	1,368,541	1,396,867
Raw and materials	303,475	338,222
less impairment	(4,490)	(3,873)
Other inventories	200,145	205,672
less impairment	(8,424)	(8,765)
Total	**1,859,247**	**1,928,123**

As at 31 December 2008 fuel stock of RR 1,260,739 thousand were pledged as collateral according to loan agreements.

As at 31 December 2007 no inventories were pledged as collateral.

Note 11. Accounts receivable and prepayments

Accounts receivable (payments expected after 12 months of the reporting date)

Narrative	31 December 2008	31 December 2007
Long-term trade receivables	4,019	248,808
less impairment	(2,089)	(204,603)
Other long-term receivables	19,031	19,399
less impairment	(6,011)	(7,535)
Total financial assets	**14,950**	**56,069**
Advances issued to suppliers and prepayments	58,667	39,206
less impairment	-	-
Long-term VAT due from the budget	9,371	5,673
Total non-financial assets	**68,038**	**44,879**
Total	**82,988**	**100,948**

Accounts receivable (payments expected within 12 months of the reporting date)

Narrative	31 December 2008	31 December 2007
Trade receivables	3,108,860	1,826,466
less impairment	(627,880)	(170,141)
Other accounts receivable	166,356	104,947
less impairment	-	-
Total financial assets	**2,647,336**	**1,761,272**
Advances issued to suppliers and prepayments	1,641,075	1,252,049
less impairment	-	-
Other taxes prepaid	3,116	55,916
VAT reimbursable	13,067	30,084
Total non-financial assets	**1,657,258**	**1,338,049**
Total	**4,304,594**	**3,099,321**

The above accounts receivable and prepayments include receivables from related parties (Note 7).

The individually impaired receivables mainly relate to Housing and utilities infrastructure, which are in unexpectedly difficult economic situations. It was assessed that a portion of the receivables is expected to be recovered.

Accounts receivable by groups as at 31 December 2008:

	Industrial consumers	Housing and utilities infrastructure	Population	Other	Total
Not yet due accounts receivable	130,474	1,012,594	124,507	1,053,411	**2,320,986**
Overdue accounts receivable not impaired	3,029	185,354	22,484	115,483	**326,350**
Including by dates of delay					
from 1 to 60 days	1,711	155,111	7,846	48,840	**213,508**
from 61 to 150 days	57	16,905	4	11,258	**28,224**
from 151 to 330 days	1,261	8,481	14,471	54,181	**78,394**
from 331 to 1050 days	-	4,037	-	823	**4,860**
over 1051 days	-	820	163	381	**1,364**
Overdue accounts receivable impaired	39,640	415,996	48,372	123,872	**627,880**
Including by dates of delay					-
from 1 to 60 days	-	-	-	-	-
from 61 to 150 days	66	34,668	414	58,066	**93,214**
from 151 to 330 days	3,378	192,466	9,615	13,599	**219,058**
from 331 to 1050 days	25	178,680	34,855	48,298	**261,858**
over 1051 days	36,171	10,182	3,488	3,909	**53,750**
less impairment of overdue receivables	(39,640)	(415,996)	(48,372)	(123,872)	(627,880)
Total	**133,503**	**1,197,948**	**146,991**	**1,168,894**	**2,647,336**

Note 11. Accounts receivable and prepayments (continued)

Accounts receivable by groups as at 31 December 2007:

	Industrial consumers	Housing and utilities infrastructure	Population	Other	Total
Not yet due accounts receivable	27,075	568,615	89,166	458,165	**1,143,021**
Overdue accounts receivable not impaired	14,597	428,017	55,759	119,878	**618,251**
Including by dates of delay					
from 1 to 60 days	1,495	110,659	24,714	38,513	**175,381**
from 61 to 150 days	37	44,643	2,132	6,750	**53,562**
from 151 to 330 days	1,405	137,272	8,329	31,196	**178,202**
from 331 to 1050 days	3,741	125,847	20,584	43,029	**193,201**
over 1051 days	7,919	9,596	-	390	**17,905**
Overdue accounts receivable impaired	49,328	45,410	11,310	64,093	**170,141**
Including by dates of delay					
from 1 to 60 days	-	1,996	2,215	316	**4,527**
from 61 to 150 days	-	4,492	-	-	**4,492**
from 151 to 330 days	17	12,194	2,305	30,825	**45,341**
from 331 to 1050 days	10,261	18,134	6,159	22,920	**57,474**
over 1051 days	39,050	8,594	631	10,032	**58,307**
less impairment of overdue receivables	(49,328)	(45,410)	(11,310)	(64,093)	**(170,141)**
Total	**41,672**	**996,632**	**144,925**	**578,043**	**1,761,272**

Management has determined the impairment based on the specific customer identification, customer payment trends, subsequent receipts and settlements and analyses of expected future cash flows.

The Group's management believes that the Group's entities will be able to realize the net receivable amount through direct collections and other non-cash settlements, and therefore, the recorded value approximates their fair value. Long term restructured receivables are recognised at amortised cost. The discounting effect is included in impairment.

Movements of impairment are presented below:

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
At the beginning of the period, including discounting effect	382,279	346,059
Impairment charge	521,648	87,596
Accounts receivable written-off as bad debts	(236,403)	(27,314)
Impairment reversal	(16,365)	(8,198)
Discounting effect - net	(15,179)	(15,864)
At the end of the period	**635,980**	**382,279**

Movements of impairment by groups of receivables for the year ended 31 December 2008:

Narrative	Industrial consumers	Housing and utilities infrastructure	Population	Other	Total
At the beginning of the period, including discounting effect	49,328	45,410	11,310	276,231	**382,279**
Impairment charge	5,879	394,170	37,062	84,537	**521,648**
Accounts receivable written-off as bad debts	(15,567)	(20,416)	-	(200,420)	**(236,403)**
Impairment reversal	-	(3,168)	-	(13,197)	**(16,365)**
Discounting effect - net	-	-	-	(15,179)	**(15,179)**
At the end of the period	**39,640**	**415,996**	**48,372**	**131,972**	**635,980**

Note 11. Accounts receivable and prepayments (continued)

Movements of impairment by groups of receivables for the year ended 31 December 2007

Narrative	Industrial consumers	Housing and utilities infrastructure	Population	Other	Total
At the beginning of the period, including discounting effect	44,963	36,167	7,603	257,326	**346,059**
Impairment charge	4,397	42,150	3,707	37,342	**87,596**
Accounts receivable written-off as bad debts	(32)	(26,557)	-	(725)	**(27,314)**
Impairment reversal	-	(6,350)	-	(1,848)	**(8,198)**
Discounting effect - net	-	-	-	(15,864)	**(15,864)**
At the end of the period	**49,328**	**45,410**	**11,310**	**276,231**	**382,279**

Note 12. Deposits in banks

Financial assets comprised short-term bank deposits in Russian Rouble in amount of RR 4,500,000 thousand as at 31 December 2008 (there were no short-term RR bank deposits as at 31 December 2007).

Bank	Rating	Rating agency	Effective interest rate, %	31 December 2008	31 December 2007
JSC Sberbank of Russia	BBB	Fitch	9.5%	1,500,000	-
JSC "AKB ROSBANK"	BB+	Standard & Poor's	9.7%	3,000,000	-
Total				**4,500,000**	-

The deposit in Sberbank of Russia with an initial maturity on 8 June 2010 for the amount of RR 1,500,000 thousand was actually redeemed on 15 January 2009 with an effective interest rate of 9.1%. The deposit in JSC "AKB ROSBANK" with the initial maturity on 19 May 2009 for the amount of RR 3,000,000 thousand was actually redeemed on 23 January 2009 with an effective an interest rate of 9.45%.

Note 13. Cash and cash equivalents

Narrative	31 December 2008	31 December 2007
Cash at bank and in hand	2,597,783	198,463
Cash equivalents in RR	1,994,911	174
Total	**4,592,694**	**198,637**

Cash included cash balances in RR in bank accounts and in hand of RR 157,035 thousand as at 31 December 2008 (RR 198,463 thousand as at 31 December 2007), cash balances denominated in US Dollars was of USD 83,074 thousand as at 31 December 2008 which equals RR 2,440,748 thousand at the exchange rate effective at 31 December 2008 (there were no USD denominated balances at 31 December 2007).

Cash equivalents comprised short-term USD bank deposit of USD 67,889 thousand as at 31 December 2008 which equals RR 1,994,596 thousand at the exchange rate effective at 31 December 2008 (as at 31 December 2007 there were no short-term USD bank deposits) and cash on corporate cards. The effective interest rate for the above deposit was 0.2%. The original maturity of bank deposits is from 30 December 2008 to 11 January 2009.

The Group has no restricted cash balances.

Note 13. Cash and cash equivalents (continued)

Cash and cash equivalents are deposited in Russian banks as follows:

Bank	Rating	Rating agency	31 December 2008	31 December 2007
Foreign currency bank deposits				
JSC "AKB ROSBANK"	BB+	Standard & Poor's	1,994,596	-
Total foreign currency bank deposits			**1,994,596**	**-**
Cash in bank accounts				
JSC Bank VTB	BBB	Fitch	74,060	17,172
JSC Sberbank of Russia	BBB	Fitch	30,620	20,891
JSC "Alfa-Bank"	BB-	Fitch	19,142	277
JSC "MInB"	-	-	14,332	74
JSC "Bank of Moscow"	BBB-	Fitch	12,292	6,598
JSC "AKB ROSBANK"	BB+	Standard & Poor's	4,593	66
GAZPROMBANK (JSC)	BB+	Standard & Poor's	990	137,020
Prio-Vneshtorgbank (JSC)	-	-	432	2,062
NKO "RTS clearing House" (LLC)	-	-	-	13,692
JSC "Promsvyazbank"	B+	Fitch	-	189
other	-	-	574	422
Total cash in bank accounts			**157,035**	**198,463**
Foreign currency bank accounts				
GAZPROMBANK (JSC)	BB+	Standard & Poor's	2,440,748	-
Total foreign currency bank accounts			**2,440,748**	**-**
Cash on corporate cards				
JSC Sberbank of Russia	BBB	Fitch	23	13
JSC Bank VTB	BBB	Fitch	167	60
GAZPROMBANK (JSC)	BB+	Standard & Poor's	57	60
other	-	-	68	41
Total cash on corporate cards			**315**	**174**

Ratings are shown in accordance to international rank.

Note 14. 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, 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.

Sharehoders' equity

At the extraordinary general meeting held 31 August 2007 TGC-4 shareholders decided to increase the equity capital of TGC-4 by placing 586,000,000,000 additional ordinary registered shares with the par value of RR 0.01 per share and the total par value of RR 5,860,000 thousand. The placement was executed in May 2008 by public subscription (certificate on the corresponding entry made in the Unified State Register of the legal entities № 2087154220240 of 20 May 2008).

On 29 April 2008 the Board of Directors approved the decision on the additional issue of the registered non-documentary ordinary shares of TGC-4 amounting to 6,600,255,897 shares with a nominal par value of RR 0.01 each, which were placed when spinning-off JSC "TGC-4 Holding" from RAO UES with subsequent merger of JSC "TGC-4 Holding" into TGC-4 by converting the shares of JSC "TGC-4 Holding" into the shares of TGC-4. In the framework of the merger, 5,303,612,900 shares with a nominal value of RR 0.01 each for the total amount of RR 53,036 thousand were issued (certificate on the corresponding entry made in the Unified State Register of the legal entities № 2087154358124 dated 25 August 2008).

Note 14. Equity (continued)

The information about the Group's shareholders' equity is presented below

Narrative	Total number	Nominal value
Ordinary shares as at		
1 January 2008	1,321,201,964,859	13,212,020
31 December 2008	1,912,505,577,759	19,125,056
Preference shares as at		
1 January 2008	75,272,938,838	752,729
31 December 2008	75,272,938,838	752,729
TOTAL as at		
1 January 2008	**1,396,474,903,697**	**13,964,749**
31 December 2008	**1,987,778,516,597**	**19,877,785**

In 2007 the Group did not place additional shares.

Narrative	Total number	Nominal value
Ordinary shares as at		
1 January 2007	1,321,201,964,859	13,212,020
31 December 2007	1,321,201,964,859	13,212,020
Preference shares as at		
1 January 2007	75,272,938,838	752,729
31 December 2007	75,272,938,838	752,729
TOTAL as at		
1 January 2007	**1,396,474,903,697**	**13,964,749**
31 December 2007	**1,396,474,903,697**	**13,964,749**

Ordinary shares and preference shares

Preference shares have no right of conversion or redemption, but are entitled to a minimum annual dividend of 10.0 percent of net statutory profit. The dividend is declared entirely at the discretion of the shareholders. In total the preference dividend may not be less than the ordinary dividend and is not cumulative. Preference shares carry no voting rights except when annual Shareholders' meeting has not decided on dividends payment or decided on partial dividends payments, in which case the preference shares acquire voting rights. In liquidation preference shareholders are first paid any declared unpaid dividends and then the nominal value of the shares ("liquidation value"). Following this, preference shareholders participate equally in the distribution of remaining assets with ordinary shareholders.

Treasury shares

Treasury shares were bought back from shareholders of TGC-4 in February 2008 in the framework of the mandatory reorganisation procedure, including 1,296,246,581 ordinary shares at the buy-back price of RR 0.0244 for the total amount of RR 31,628 thousand, and 106,634,280 preference shares at the buy-back price of RR 0.0172 for the total amount of RR 1,834 thousand. According to the agreement on the merger of JSC "TGC-4 Holding" 1,296,044,491 ordinary shares of TGC-4 were used for the purpose of converting JSC "TGC-4 Holding" shares in the merger process.

Share premium

The share premium of RR 9,962,000 thousand was received from the placement of 586,000,000,000 ordinary shares (with the par value of RR 0.01 per share) at a price of RR 0.027 per share, as approved by the Board of Directors on 24 April 2008 (Note 1).

Merger reserve

The merger reserve represents the difference between the IFRS carrying value of the contributed net assets of 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" and JSC "Tambov Generating Company" merged into the Group and the minority interest. The merger reserve was subsequently adjusted by the

Note 14. Equity (continued)

share capital issued by TGC-4 to reflect the transfer of businesses owned by the entities under common control.

Dividends

In accordance with Russian legislation the Group distributes profits as dividends on the basis of the financial statements prepared in accordance with the Russian Accounting Rules. The statutory accounting reports are the basis for profit distribution and other appropriations. The 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 that currently, it would not be appropriate to disclose the distributable reserves in these financial statements.

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

Narrative	Year ended 31 December 2008		Year ended 31 December 2007	
	Declared dividends, in thousands of RR	Dividends per share, RR	Declared dividends, in thousands of RR	Dividends per share, RR
JSC "Territorial Generation Company 4" – for year 2006	-	-	252,001	RR 0.000180455 per ordinary and preference share
JSC "Territorial Generation Company 4" – for 6 months 2007	-	-	50,000	RR 0.0000358044 per ordinary and preference share
JSC "Tulenergocomplect"– for year 2006	-	-	95	RR 0.2274 per ordinary share
JSC "Territorial Generation Company 4" – for year 2007	5,587	RR 0.00007432577 per preference share	-	-

In June 2009 TGC-4 announced the dividends on preference shares of RR 1,763 thousand based on the performance results for the year ended 31 December 2008 (Note 28).

Note 15. Basic and diluted earnings per share

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Loss attributable to the shareholders of TGC-4 (RR thousand)	(9,719,880)	(5,137,467)
Less profit from discontinued operations	-	63,465
Loss from continuing operations	(9,719,880)	(5,200,932)
Weighted average number of ordinary shares issued (thousands of shares)	1,664,262,546	1,321,201,965
Loss per ordinary share from contining operations attributable to shareholders of the Group – basic and diluted (in RR per share)	(0.006)	(0.004)
Earings per ordinary share from discontinued operations attributable to shareholders of the Group - basic and diluted (in RR per share)	-	0.00005

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

Narrative	Effective interest rate, %	31 December 2008	31 December 2007
GAZPROMBANK (JSC), Tula Branch	7.9 – 15.0	1,800,094	1,507,848
JSC Sberbank of Russia, Tula branch № 8604	7.0 – 13.0	785,110	1,451,483
JSC "AKB ROSBANK", Mid-Russian branch	8.5 – 16.5	475,879	245,500
"Royal bank of Scotland" (CJSC) (in 2007 - ABN AMRO Bank (CJSC)	8.35	-	1,483,868
JSC "Alfa-Bank", Tula Branch	9.0 – 9.2	-	100,123
Interest on bonded loan	7.6	14,750	26,030
Current portion of non-current debt, including			
- bonded loan	7.6	2,624,495	-
- finance lease		170,298	169,855
Total		**5,870,626**	**4,984,707**

The current debts are denominated in Russian Roubles.

Short-term loans issued to the Group were secured by inventories totalling RR 1,260,739 thousand and zero as at 31 December 2008 and as at 31 December 2007 respectively (Note 10).

Note 17. Non-current debt

Narrative	Effective interest rate, %	Maturity date	31 December 2008	31 December 2007
GAZPROMBANK (JSC), Tula Branch	11.0 – 11.2	2012	692,818	-
JSC Sberbank of Russia, Tula branch № 8604	8.4 – 9.4	2010	165,486	32,035
JSC "AKB ROSBANK"	10.6	2009	-	145,898
Bonded loan	7.6	2010	2,624,495	5,000,000
Finance lease			390,538	560,392
Total non-current debt			**3,873,337**	**5,738,325**
Less current portion of non-current debt			(2,624,495)	-
Less current portion of finance lease			(170,298)	(169,855)
Total			**1,078,544**	**5,568,470**

Maturity schedule for non-current debt (except for finance lease)	31 December 2008	31 December 2007
Maturity		
From 1 to 2 years	165,486	177,933
From 2 to 5 years	692,818	5,000,000
Total	**858,304**	**5,177,933**

The Group uses fixed rate loans. The Group has not entered into any hedging arrangements in respect of interest rate exposures.

The currency of all non-current borrowings is the Russian Roubles.

As at 31 December 2008 obligations under the bonded loan were recognised within current debts in the amount of the offer that was executed on 10 June 2009 for RR 2,624,495 thousand (Notes 16, 28).

As at 31 December 2008 the estimated fair value of the non-current debt approximates its carrying value.

The non-current debt was not secured by any pledged property.

Note 18. Pension liabilities

The tables below provide information about the benefit obligations and actuarial assumptions used for the year ended 31 December 2008 and the year ended 31 December 2007.

Amounts recognised in the consolidated balance sheet are as follows:

Narrative	31 December 2008	31 December 2007
Present value of defined benefit obligations (DBO)	891,630	863,322
Fair value of plan assets	-	-
Present value of unfunded obligations	891,630	863,322
Unreconised net actuarial losses	(5,276)	(67,974)
Unrecognised past service cost	(80,905)	(90,161)
Net liability in the balance sheet	**805,449**	**705,187**

Amounts recognised in the consolidated statement of operations are as follows:

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Current service cost	73,365	60,563
Interest cost	59,147	49,195
Expected return on plan assets	-	-
Net actuarial (gain)/ loss recognised in the period	5,985	(363)
Amortisation of past service cost	9,255	9,255
Curtailment gain	-	(39,081)
Immediate recognition of vested prior service cost	-	35,056
Net expense recognized in the Income Statement	**147,752**	**114,625**

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

Narrative	31 December 2008	31 December 2007
Present value of defined benefit obligations (DBO) at beginning of year	863,322	746,645
Current service cost	73,365	60,563
Interest cost	59,147	49,195
Actuarial (gains)/ loss	(56,713)	62,405
Past service cost	-	36,301
Benefits paid	(47,490)	(52,416)
Curtailment gain	-	(39,371)
Present value of defined benefit obligations (DBO) at year end	**891,631**	**863,322**

Curtailment gain received in 2007 related to reduction of lump sum on retirement.

Principal actuarial assumptions are as follows:

Narrative	31 December 2008	31 December 2007
Nominal discount rate	9.00%	6.75%
Wage growth rate	8.0%	7.0%
Inflation rate	7.0%	6.0%
Mortality table	Russia 1998	Russia 1998

The Group expects to contribute RR 53,091 thousand to the defined benefit plan during the year beginning 1 January 2009.

Note 19. Accounts payable and accruals

Narrative	31 December 2008	31 December 2007
Trade payables	650,659	408,387
Total financial liabilities	**650,659**	**408,387**
Wages and salaries payable	374,935	338,185
Advances received	139,981	155,567
Income payable to participants	12,244	20,014
Other payables	83,325	230,114
Total non-financial liabilities	**610,485**	**743,880**
Total	**1,261,144**	**1,152,267**

Trade payables are classified as financial liabilities. Contractual maturity date of trade payable is less than one year.

Note 20. Other taxes payable

Narrative	31 December 2008	31 December 2007
Property tax	75,788	64,149
Unified social tax	78,132	78,871
Personal income tax	32,353	26,758
Land tax	13,940	14,639
VAT	338,395	106
Fines and penalties	5	-
Other taxes	21,002	29,766
Total	**559,615**	**214,289**

Note 21. Income tax benefit

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Current income tax charge	372,509	260,417
Deferred income tax benefit	(2,862,224)	(1,838,805)
Total	**(2,489,715)**	**(1,578,388)**

During the year ended 31 December 2008 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 end 31 December 2008	Year end 31 December 2007
Loss before profit tax	**(12,233,582)**	**(6,794,445)**
Theoretical income tax charge at an average statutory tax rate of 24%	2,936,060	1,630,667
Tax effect of items which are not deductible for taxation purposes	(162,200)	(52,279)
Effect from changes in tax rate	(223,046)	-
Unrecognised tax asset	(61,099)	-
Total	2,489,715	1,578,388

Note 21. Income tax benefit (continued)

Deferred income tax

Differences between IFRS accounting principles 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.

During the year ended 31 December 2008 the Group's taxable profit was subject to income tax rate of 24%. In line with Russian Tax law, starting from 1 January 2009 the income tax charge shall be calculated at the rate of 20%. In accordance with the accounting policies (Note 4) deferred tax assets and liabilities are measured at 20 percent, the rate expected to be applicable when the assets or liabilities will be realized.

The tax effect of temporary differences that resulted in formation of deferred tax assets and liabilities is shown below:

Deferred tax assets	31 December 2008	Charged to the income statement	Charged to the income statement effect of the rate change from 24% to 20%	31 December 2007
Other non-current liabilities	161,090	24,063	(32,218)	169,245
Non-current debt	44,048	(40,871)	(8,810)	93,729
Accounts receivable and prepayments	93,563	(19,468)	(18,711)	131,742
Accounts payable and accruals	241,874	184,035	(48,376)	106,215
Inventories	1,603	1,923	(320)	-
Deferred tax assets as at year end	**542,178**	**149,682**	**(108,435)**	**500,931**

Deferred tax liabilities	31 December 2008	Charged to the income statement	Charged directly to equity	Charged directly to equity effect of the rate change from 24% to 20%	Charged to the income statement effect of the rate change from 24% to 20%	31 December 2007
Property, plant and equipment	540,070	(2,940,056)	(1,671,350)	(227,950)	119,937	5,259,489
Other non-current assets	16,733	1,840	-	-	(3,347)	18,240
Inventories	-	(1,478)	-	-	-	1,478
Other	9,895	4,106	-	-	(1,979)	7,768
Deferred tax liabilities as at year end	**566,698**	**(2,935,588)**	**(1,671,350)**	**(227,950)**	**114,611**	**5,286,975**

The Group has unrecognised deferred tax assets in the amount of RR 247,295 thousand for the period ended 31 December 2008 (for the period ended 31 December 2007 RR zero) and related deductable temporary differences in the amount of RR 1,236,475 thousand (for the period ended 31 December 2007 RR zero); these occurred mainly due to the impairment of property plant and equipment in JSC "Belgorodskaya Heat Network Company" as future economic profit of this subsidiary is not probable.

Note 21. Income tax benefit (continued)

The comparative information for deferred tax assets and liabilities is shown below:

Deferred tax assets	31 December 2007	Charged to the income statement	Charged directly to equity	31 December 2006
Other non-current liabilities	169,245	14,930	-	154,315
Property, plant and equipment	-	(138,820)	-	138,820
Non-current debt	93,729	10,118	-	83,611
Accounts receivable and prepayments	131,742	4,885	-	126,857
Accounts payable and accruals	106,215	28,830	-	77,385
Inventories	-	(518)	-	518
Deferred tax assets as at year end	**500,931**	**(80,575)**	**-**	**581,506**

Deferred tax liabilities	31 December 2007	Charged to the income statement	Charged directly to equity	31 December 2006
Property, plant and equipment	5,259,489	(1,945,205)	3,635,251	3,569,443
Other non-current assets	18,240	18,232	-	8
Inventories	1,478	1,478	-	-
Other	7,768	6,115	-	1,653
Deferred tax liabilities as at year end	**5,286,975**	**(1,919,380)**	**3,635,251**	**3,571,104**

The deferred tax assets and liabilities expected to be recovered within 12 months

Narrative	Deferred tax liabilities	Deferred tax assets
Property, plant and equipment	(34,808)	-
Accounts payable and accruals	-	(241,874)
Other non-current liabilities	-	(10,618)
Accounts receivable and prepayments	-	(93,563)
Deferred tax assets and liabilities expected to be recovered in 2009	**(34,808)**	**(346,055)**
Deferred tax assets and liabilities expected to be recovered from 2009	**(531,893)**	**(196,123)**

Note 22. Revenue, other operating income

Revenue

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Electricity and capacity	14,973,092	12,399,817
Heat energy	13,431,258	11,429,726
Other	818,427	797,732
Total	**29,222,777**	**24,627,275**

Other operating income

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Exchange differences	165,790	-
Income from fines and penalties recognised	84,812	33,704
Income from property, plant and equipment sales	21,392	29,741
Income from property, plant and equipment written-off	18,719	49,270
Accounts payable written-off	7,977	5,078
Stock surplus	7,689	51,420
Compensation of interest expenses on loans taken for fuel purchases	3,202	47,348
Other income	18,590	2,625
Total other operating income	**308,171**	**219,186**

Note 23. Operating expenses other than impairment related to property, plant and equipment

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Fuel expense	14,510,652	11,811,133
Employee benefit	3,981,975	3,396,523
Depreciation of property, plant and equipment and amortisation of intangible assets	3,498,538	3,200,680
Purchased electricity	2,429,482	1,830,713
Repairs and maintenance	1,159,138	1,045,848
Other raw materials and supplies (including chemical agents)	866,721	834,801
Provision (changes in provision) against legal claims	787,821	38,558
Water usage expenses (including payments to water treatment systems)	597,642	598,697
Changes of accounts receivable impairment	490,104	63,534
Taxes other than income tax	441,336	379,487
Rent payments	256,078	247,150
NOREM services	228,831	161,066
Security	164,411	142,687
Pension plan expenses	88,605	65,430
Insurance cost	83,671	86,827
Transportation services	55,878	37,606
Consulting, legal and audit services	48,987	84,325
Impairment of available-for-sales investment	46,268	26,068
Social expenses	36,862	35,321
Losses from property, plant and equipment disposal	22,651	46,549
Utilities	21,965	9,111
Impairment of investment in associate	5,155	-
Environmental payments	3,126	25,773
Changes in inventory impairment provision	276	6,962
Other expenses	954,676	669,044
Total	**30,780,849**	**24,843,893**

Employee benefits include

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Salaries and wages, payroll taxes	3,790,354	3,233,159
Financial assistance to employees and retired employees	164,230	152,672
Defined benefit pension plan expenses	88,605	65,430
Defined contribution pension plan expenses	27,391	10,692
Total	**4,070,580**	**3,461,953**

Note 24. Finance income, finance costs

Finance income

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Interest income	540,216	10,519
Итого	**540,216**	**10,519**

Finance costs

Narrative	Year ended 31 December 2008	Year ended 31 December 2007
Interest expense	864,120	778,584
Pension interest expense	59,147	49,195
Discounting effect	-	8,633
Total	**923,267**	**836,412**

Note 25. 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 JSC "Centre for Financial Settlements", retail companies and large industrial customers.

Purchase commitments

The Group entities concluded a number of long-term contracts with JSC "Gazprom" for the supply in 2008-2012 of the limited gas with guaranteed volumes and delivery terms. The principal suppliers of fuel are JSC "Gazprom" subsidiaries: LLC "Belregiongaz", LLC "Bryanskregiongaz", LLC "Voronezhregiongaz", LLC "Kalugaregiongaz", LLC "Kurskregiongas", LLC "Lipetskregiongaz", LLC "Oryolregiongaz", LLC "Ryazanregiongaz", LLC "Smolenskregiongaz", LLC "Tambovregiongaz" and LLC "Tularegiongaz". Purchase volumes are determined on the basis of estimated production demands. The purchase price of gas is determined by Federal Service of Tariffs. The gas demand that is not covered by the limited volumes set up by OJSC Gazprom shall be satisfied by commercial gas purchases under short-term (up to one months) supply contracts entered into following results of tenders held on the electronic platform of LLC "Mezhregiongaz" and at prices determined by the tender.

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 18,396,958 thousand as at 31 December 2008 (31 December 2007 RR 7,882,096 thousand).

The major part of future capital expenditures under contractual obligations as at 31 December 2008 are related to the following stations: enlargement of Novomoskovskaya GRES in amount of RR 7,669,759 thousand; reconstruction of Dyagilevskaya TETs in amount of RR 5,781,021 thousand; reconstruction of the boiler in North-West region of the town of Kursk in amount of RR 1,974,691 thousand; reconstruction of Voronezhskaya TETs-2 in amount of RR 1,802,725 thousand.

Note 26. 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

Since April 2008 TGC-4 is a defendant an arbitration processes with JSC "Tambov Utilities" ("TKS") in connection with a number of claims demanding settlement of a debt for water supplies. The claims cover the period of 2006-2008 and totaled RR 664,392 thousand.

Note 26. Contingencies (continued)

The essence of the claim is as follows: TKS and consumers (managing entities, legal entities and other consumers) concluded contracts on the supply of water and on acceptance of waste water, at the same time TGC-4 has contracts with the same consumers on supply of heat in the form of hot water. Water for the purposes of hot water supply is delivered by TKS to Central Heating Points ("CHP") owned by TGC-4, then this water is heated and delivered to consumers via TGC-4's networks. Consumers pay TGC-4 only for the cost of energy used to heat the water. Consumers are supposed to pay TKS for the cost of the water. The volume of water, the payment of which is claimed by TKS, has been calculated in the submitted claims as the difference between the volume of water input to CHP and the volume of water sold by TKS to final consumers, determined based on consumption norms, contracted capacities and other parameters set up in the town of Tambov.

TGC-4 disputes the claims and has taken action to challenge them. As at 31 December 2008 a provision was formed for this legal contingency.

In addition, the Group is a defendant in a number of arbitration proceedings the risk of incurring loss in which is assessed as high, as at the reporting date such claims amounted to RR 148,199 thousand.

The Company created a provision of RR 812,591 thousand against the full amount of possible claims as at the reporting date, the execution of which is expected in 2009.

Management believes that other currently existing claims or suits to entities of the Group (not stated above) and final decisions taken on them do not include any that could have significant adverse impact on the financial position of the Group.

Entities of the Group submitted a number of court claims related to their disputes with the customers (utilities) regarding the scope of provided heat supply services. The court claims to the above companies in part have already been satisfied, under the established court practice disputes regarding the sope of provided heat supply services are generally resolved in favor of the Group. The Group does not expect any losses in connection with these claims.

Movements of provision for legal claims are presented below:

Narrative	31 December 2007	Provision used	Provision reversal	Provision charge	31 December 2008
Provision for legal claims	38,558	(13,788)	(14,518)	802,339	812,591

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 way of accounting for tax purposes of water tax, deductibility of certain expenses 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.

In addition, tax and other legislation do not address specifically all the aspects of the Group's reorganisation related to reforming of the electric utilities industry. As such there may be tax and legal challenges to the various interpretations, transactions and resolutions that were a part of the reorganisation and reform process.

As at 31 December 2008 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.

Note 26. Contingencies (continued)

Environmental matters

Group 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 2008 the Group issued guarantees in respect of the borrowings drawn down by related and other parties in accordance with the contracts of guarantees in the total amount of RR 428,441 thousand (31 December 2007 RR 341,810 thousand).

Counterparty	Debtor	Nature of relationship	31 December 2008	31 December 2007
JSC "Russian Bank of Development"	LLC "IR Leasing"	Guarantee for credit agreement	190,032	315,532
GAZPROMBANK (JSC)	JSC "Energocascade"	Guarantee for letter of credit agreement	230,166	-
GAZPROMBANK (JSC)	JSC "Gazprombank Leasing"	Guarantee for credit agreement	8,243	26,278
Total			**428,441**	**341,810**

Note 27. 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 collectability of receivables. The Group does not have any risk policy to hedge its financial exposures.

Liquidity risk

Prudent liquidity risk management includes maintaining sufficient level of cash and liquidity of securities, availability of funding from an adequate amount of committed credit facilities and the ability to close positions on financial markets.

The Group adheres to the balanced model of financing of working capital – both at the expense of short-term and long-term sources. Temporarily available funds are placed into short-term financial instruments, mainly bank deposits.

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

Note 27. Financial instruments and financial risk factors (continued)

31 December 2008	Less than 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Total
Bonds including future principal and interest payments	-	-	2,729,520	-	2,729,520
Bank loans including future principal and interest payments	93,529	1,784,358	1,420,194	1,075,967	4,374,048
Finance lease liability	29,572	42,623	212,681	277,213	562,089
Trade payables	599,864	34,331	16,464	-	650,659
Total future payments	**722,965**	**1,861,312**	**4,378,859**	**1,353,180**	**8,316,316**
31 December 2007					
Bonds including future principal and interest payments	26,030	-	2,643,170	2,729,520	5,398,720
Bank loans including future principal and interest payments	506,074	976,692	3,434,875	192,530	5,110,171
Finance lease liability	37,168	52,018	257,680	562,088	908,954
Trade payables	408,387	-	-	-	408,387
Total future payments	**977,659**	**1,028,710**	**6,335,725**	**3,484,138**	**11,826,232**

The Group aims to maintain flexibility in its funding requirements by monitoring its cash position (through budgeting) and keeping committed credit lines available.

In 2008 TGC-4 attracted RR 15,822,000 thousand, issuing additional shares (Note 1). Management believes that as at 31 December 2008 the Group does not have any significant liquidity risk as its current assets sufficiently exceed its current liabilities.

Decision on the Group's debt structure is made based on minimization of the debt's cost, availability of borrowings and profit maximizing.

Interest rate risk

The Group's operating profits and cash flows from operating activity are independent from changes in market interest rates. The Group is exposed to interest rate risk through market value fluctuations of interest bearing long-term and short-term borrowings (Notes 16,17). Substantially all of the Group's long-term and short-term borrowings are at fixed interest rates and credit lines are available in several credit organizations at the same time.

As at 31 December 2008 the maximum interest rate on received loans was 16.5% p.a.on the actual debt amount, however the loan interest rates may be increased by the bank unilaterally, including in connection with a higher refinance rate of Central Bank of the Russian Federation. This increases adverse effect of potential interest rate changes.

Proceeds received from the issue of additional shares (Note 1) allowed to reduce the volume of debt which mitigates the interest rate risk.

The Group has significant assets represented by interest bearing deposits. These deposits are not subject to significant interest rate risk as they are short-term and corresponding deposit agreements do not provide for any unilateral change of interest rates by banks.

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.

Credit risk arises from cash and cash equivalents, deposits with banks, as well as credit exposures to wholesale and retail customers, including outstanding receivables and committed transactions.

Note 27. Financial instruments and financial risk factors (continued)

Group's financial assets, which are exposed to credit risk, are follows:

Narrative	31 December 2008	31 December 2007
Cash and cash equivalents	4,592,694	198,637
Bank deposits	4,500,000	-
Trade receivables less impairment	2,480,980	1,656,325
Other accounts receivable less impairment	166,356	104,947
Guarantee	428,441	341,810
Maximum exposure to credit risks	**12,168,471**	**2,301,719**

Group holds cash in the most safe Russian banks, according the ratings given by rating agencies and considers it enough to present ratings to assess the credit quality of bank balances as actually the ratings are high in comparison with other banks in Russia.

Financial assets which potentially subject the Group entities to concentrations of credit risk consist principally of trade and other receivables.

Credit risks, related to trade and other receivables, are systematically reviewed for possibility of creation of impairment provision against trade and other receivables. Trade and other receivables balance netted with trade and other receivables impairment provision represents maximum exposure to credit risks, relating to receivables. Despite the fact that cash collection is subject to influence of different economic factors, Management of the Group believes that there is no significant risk of losses exceeding recognized trade and other receivables impairment provision.

There are no significant contactors who constitutes more than 10% of the Group revenue, consequently there is no concentration of credit risk for the Group from the management point of view.

The Group has developed and approved credit policy, ensuring the maintenance of debt position levels and cost of debts levels. Credit risk is managed on the Group basis. For customers there is no independent rating and therefore the Group assesses the credit quality of the customer, taking into account its financial position, past experience and other factors.

Fair value

Management believes that the fair value of its financial assets and liabilities approximates their carrying amounts. The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values due to the short-term nature of trade receivables. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available for Group for similar financial instruments.

The maximum exposure for each risk is limited to the fair value of each class of financial instrument.

Financial instruments categories

Financial instruments include the following categories of financial assets and liabilities:

31 December 2008	Loans and receivables	Available-for-sale financial assets	Other financial liabilities	Total
Assets				
Long-term accounts receivable	14,950	-	-	14,950
Other non-current assets	28,328	112,161	-	140,489
Accounts receivable	2,647,338	-	-	2,647,338
Bank deposits	4,500,000	-	-	4,500,000
Cash and cash equivalents	4,592,694	-	-	4,592,694
Total assets	**11,783,308**	**112,161**	-	**11,895,469**

Note 27. Financial instruments and financial risk factors (continued)

31 December 2008	Loans and receivables	Available-for-sale financial assets	Other financial liabilities	Total
Liabilities				
Non-current debt	-	-	1,078,544	1,078,544
Current debt and current portion of non-current debt	-	-	5,870,626	5,870,626
Trade accounts payable	-	-	650,659	650,659
Total liabilities	-	-	**7,599,829**	**7,599,829**
31 December 2007				
Assets				
Long-term accounts receivable	56,069	-	-	56,069
Other non-current assets	38,538	82,469	-	121,007
Accounts receivable	1,761,272	-	-	1,761,272
Other current assets	16,209	-	-	16,209
Cash and cash equivalents	198,637	-	-	198,637
Total assets	**2,070,725**	**82,469**	-	**2,153,194**
Liabilities				
Non-current debt	-	-	5,568,470	5,568,470
Current debt and current portion of non-current debt	-	-	4,984,707	4,984,707
Trade accounts payable		-	408,387	408,387
Total liabilities	-	-	**10,961,564**	**10,961,564**

Currency risks

Electric power produced by the Group is sold on the internal market of the Russian Federation with prices fixed in the currency of the Russian Federation. Hence, the Group's net exposure to currency risk on operating activity that are denominated in a currency other than the Russian Roubles is kept at minimum level. The financial condition of the Company, its liquidity, financing sources and the results of activities do not considerably depend on currency rates as the Group activities are planned to be performed in such a way that its liabilities be denominated in the national currency. That is why the influence of foreign currency rates fluctuations on the financial position of the Group is estimated as insignificant.

However the Group is exposed to foreign exchange risk arising from currency accounts and deposit balances (Note 13). The following table as at 31 December 2008 presents sensitivities of profit and loss and equity to reasonably possible changes in exchange rates applied at the balance sheet date relative to the functional currency of the Group, with all other variables held constant.

Expected impact	Change on US dollar exchange rate against the Russian Rouble			
	-30%	-20%	+20%	+30%
Impact on profit and loss	(1,330,588)	(887,059)	887,059	1,330,588
Impact on capital	-	-	-	-

The exposure was calculated only for deposits and cash balances denominated in currency other than Russian Rouble.

Capital risk

Capital risk management relates to the compliance with the Russian legislation and credit policy implementation to maintain an optimal capital structure and reduce the cost of capital.

The following capital requirements have been established for joint stock companies by the legislation of the Russian Federation:

- share capital can not be lower than 1,000 minimum salaries on the date of the company registration;
- if the share capital of the entity is greater than statutory net assets of the entity, such entity must decrease its share capital to the value not exceeding its net assets.

Note 27. Financial instruments and financial risk factors (continued)

- if the minimum allowed share capital is greater than statutory net assets of the entity, such entity is subject to liquidation.

As at 31 December 2008 the Group entities were in compliance with the above share capital requirements.

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

Consistent with other companies in the industry, the Group monitors capital on the basis of the gearing ratio, and ensures that the ratio is not more than 1.0. This ratio is calculated as debt divided by total capital. Debt is calculated as total borrowings, as shown in the consolidated balance sheet. Total capital is calculated as equity, as shown in the consolidated balance sheet.

Gearing ratios were 0.21 as at 31 December 2008, 0.28 as at 31 December 2007, respectively.

Narrative	31 December 2008	31 December 2007
Non-current and current debts	6,949,170	10,553,177
Equity	26,769,500	26,671,367
Gearing ratio	**0.21**	**0.28**

The Group's policy of capital risk management is based on the following financial ratios: debt to EBITDA ratio and interest payments coverage by EBITDA. EBITDA equal to earnings before the deduction of interest expense and financing items, non-cash impairment and disposal charges, income taxes and depreciation.

The debt to EBITDA ratios were 3.09 as at 31 December 2008 and 3.29 as at 31 December 2007.

Interest expense coverage by EBITDA were 2.60 for year ended 31 December 2008 and 4.11 for the year ended 31 December 2007.

Narrative	31 December 2008	31 December 2007
Operating loss	(11,850,763)	(5,975,867)
Revaluation write down	-	(6,257,915)
Impairment (charge) / reversal related to property, plant and equipment	(10,600,862)	279,480
Depreciation of property, plant and equipment	3,498,538	3,200,680
EBITDA	**2,248,637**	**3,203,248**
Non-current and current debts	6,949,170	10,553,177
Non-current and current debts / EBITDA	**3.09**	**3.29**
Interest expense	864,120	778,584
EBITDA / Interest expense	**2.60**	**4.11**

Note 28. Subsequent event

Dividends

The annual dividend amount per preference share for 2008 was approved by the TGC-4 general meeting of shareholders on 11 June 2009 and equals to RR 0.00002342143 per share. At the same time the TGC-4 general meeting of shareholders decided not to pay any dividends on the ordinary shares. The total amount of declared annual dividends for 2008 is RR 1,763 thousand.