TGC-2 GROUP
COMBINED AND CONSOLIDATED FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) FOR THE YEAR ENDED 31 DECEMBER 2007

PRICEWATERHOUSECOOPERS

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of Open Joint Stock Company "Territorial Generating Company # 2" (OJSC "TGC-2"):

We have audited the accompanying combined and consolidated financial statements of OJSC "TGC-2" and its subsidiaries (the "Group") which comprise the combined and consolidated balance sheet as at 31 December 2007, the combined and consolidated income statement, combined and consolidated statement of changes in equity and combined and consolidated statement of cash flows 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 combined and consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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INDEPENDENT AUDITOR'S REPORT

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

Opinion

In our opinion, the accompanying combined and consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2007, and 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

24 July 2008

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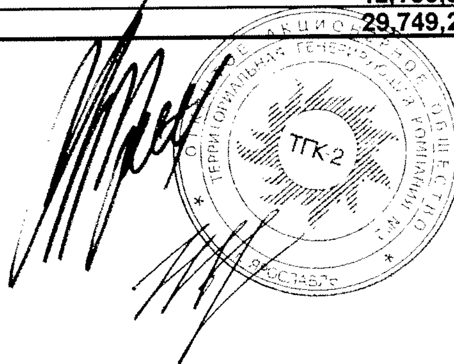
TGC-2 Group
Combined and Consolidated Balance Sheet as at 31 December 2007

(in thousands of Russian Roubles)

	Note	31 December 2007	31 December 2006
Non-current assets			
Property, plant and equipment	8	23,357,065	16,695,862
Other non-current assets	9	531,620	289,436
Total non-current assets		**23,888,685**	**16,985,298**
Current Assets			
Cash and cash equivalents	12	436,068	121,323
Accounts receivable and prepayments	11	3,227,886	2,222,788
Income tax prepayment		36,721	102,980
Inventories	10	2,159,866	1,929,848
Other current assets		-	1,432
Total current assets		**5,860,541**	**4,378,371**
TOTAL ASSETS		**29,749,226**	**21,363,669**
EQUITY AND LIABILITIES			
Share capital	13	11,124,969	7,117,127
Merger reserve	13	(2,750,197)	(335,453)
Other reserves	13,8	7,322,150	-
Retained earnings/(loss)		1,265,423	2,923,874
Equity attributable to parent company		**16,962,345**	**9,705,548**
Minority interest		-	1,771,420
Total equity		**16,962,345**	**11,476,968**
Non-current Liabilities			
Deferred income tax liabilities	14	3,102,828	1,422,691
Non-current borrowings	16	670,000	-
Pension liabilities	15	342,885	198,268
Other non-current liabilities		4,059	9,665
Total non-current liabilities		**4,119,772**	**1,630,624**
Current liabilities			
Current borrowings and current portion of non-current borrowings	16	6,008,900	6,074,231
Accounts payable and accrued liabilities	17	2,318,172	1,779,768
Income tax payable		-	6,330
Other taxes payable	18	340,036	395,748
Total current liabilities		**8,667,109**	**8,256,077**
Total liabilities		**12,786,881**	**9,886,701**
TOTAL EQUITY AND LIABILITIES		**29,749,226**	**21,363,669**



General Director — A.A. Vagner

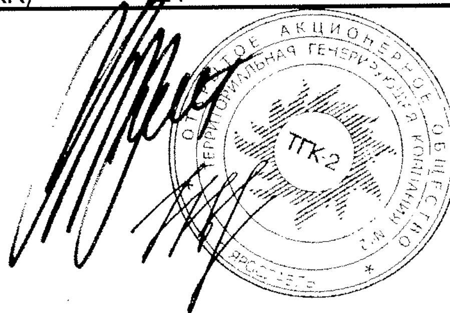
Chief Accountant — Y.V. Ivanova

24 July 2008

TGC-2 Group
Combined and Consolidated Income Statement for the year ended 31 December 2007

(in thousands of Russian Roubles)

	Notes	Year ended 31 December 2007	Year ended 31 December 2006
Revenues			
Sales of electricity	19	9,927,520	6,129,317
Sales of heating	19	9,879,178	8,205,855
Other sales	19	988,093	669,894
Total revenues		**20,794,791**	**15,005,066**
Operating expenses	20	(21,415,331)	(17,769,698)
Other operating income	21	234,147	321,744
Revaluation write down	8	(1,566,891)	-
Release of impairment of property, plant and equipment	8	-	7,579,968
Operating Loss/(Profit)		**(1,953,284)**	**5,137,080**
Finance income		-	1,234
Finance costs	22	(525,630)	(446,775)
Loss/(Profit) before income tax		**(2,478,914)**	**4,691,539**
Income tax charge	14	(191)	(62,204)
Deferred income tax benefit / (charge)	14	642,739	(1,292,494)
Loss/(Profit) for the year		**(1,836,366)**	**3,336,841**
Loss/(profit) attributable to:			
Parent company shareholders		(1,658,044)	3,310,776
Minority interest		(178,322)	26,065
Weighted average earnings per ordinary and preference share – basic and diluted (in RR)	24	(0.002)	0.008



General Director — A.A. Vagner

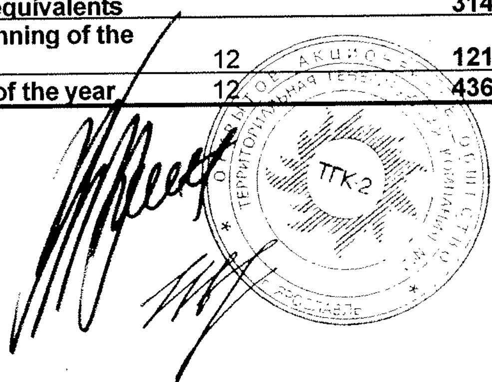
Chief Accountant — Y.V. Ivanova

24 July 2008

TGC-2 Group
Combined and Consolidated Cash Flow Statement for the year ended 31 December 2007

(in thousands of Russian Roubles)

	Notes	Year ended 31 December 2007	Year ended 31 December 2006
CASH FLOW FROM OPERATING ACTIVITIES:			
(Loss) / profit before income tax		**(2,478,914)**	**4,691,539**
Adjustments to reconcile profit before income tax and net cash from operating activities:			
Depreciation of property, plant and equipment	8,20	3,184,956	735,414
Impairment loss reversed during the year		-	(7,579,968)
Provision for impairment of accounts receivable	11,20	(584,782)	303,607
Write off accounts receivable	20	17,363	8,628
Reversal of provision for obsolete inventories		(17,867)	(13,187)
Interest income		-	(10,656)
Finance costs	22	497,503	436,375
Loss on discounting of non-current accounts receivable	20, 21	104,979	229,712
(Gain) / loss on discounting of loans issued to employees		(2,863)	9,606
Loss / (gain) on disposal of subsidiaries	23	5,330	(66,554)
Charge of post-employment benefits obligations	15, 22	28,127	10,400
Loss on disposal of property, plant and equipment		4,734	20,360
Revaluation of fixed assets write down	8	1,566,891	-
Other income		(33,486)	(74,710)
Operating cash flows before working capital changes		**2,291,971**	**(1,299,434)**
Working capital changes:			
(Increase) in accounts receivable		(414,735)	(696,683)
(Increase) in inventories		(204,582)	(722,267)
Increase in accounts payable and accrued liabilities		395,823	609,999
(Increase) / decrease in other non-current assets		(339,804)	31,487
Increase / (decrease) in other non-current liabilities		106,825	(12,858)
(Decrease) in taxes payable other than income tax		(55,712)	(257,184)
Income tax refunded / (paid)		91,583	(207,785)
Net cash generated by/(used for) operating activities		**1,871,369**	**(2,554,725)**
CASH FLOW FROM INVESTING ACTIVITIES:			
Purchase of property, plant and equipment		(1,604,700)	(1,050,775)
Proceeds from sales of property, plant and equipment		201	6,554
Proceeds from disposals of subsidiaries	23	34,399	180,819
Issuing of loans to third parties		(12,090)	-
Advances paid for finance lease		(3,697)	-
Interest received		524	11,233
Net cash used for investing activities		**(1,585,363)**	**(852,169)**
CASH FLOW FROM FINANCING ACTIVITIES:			
Proceeds from borrowings		9,768,707	13,262,912
Repayment of borrowings		(9,163,959)	(9,065,438)
Interest paid		(562,735)	(426,698)
Leasing payments		(13,274)	(9,577)
Dividends paid		-	(359,444)
Cash payment to owners to redeem treasury's shares		-	(420)
Net cash generated by financing activities		**28,739**	**3,401,335**
Increase/(decrease) in cash and cash equivalents		**314,745**	**(5,559)**
Cash and cash equivalents at the beginning of the year	12	**121,323**	**126,882**
Cash and cash equivalents at the end of the year	12	**436,068**	**121,323**



General Director A.A. Vagner

Chief Accountant Y.V. Ivanova

24 July 2008

TGC-2 Group
Combined and Consolidated Statement Of Changes In Equity for the year ended 31 December 2007

(in thousands of Russian Roubles)

	Attributable to the parent's shareholders					Minority interest	Total Equity
	Share capital	Merger reserve	Retained earnings	Other reserve	Total		
At 1 January 2006	**10,000**	**4,286,220**	**(210,651)**	**-**	**4,085,569**	**4,413,355**	**8,498,924**
Profit for the year	-	-	3,310,775	-	3,310,775	26,065	3,336,840
Dividends (Note 13)	-	-	(176,250)	-	(176,250)	(182,127)	(358,377)
Issuance of shares (Note 13)	7,107,127	(4,621,673)	-	-	2,485,454	(2,485,873)	(419)
At 31 December 2006	**7,117,127**	**(335,453)**	**2,923,874**	**-**	**9,705,548**	**1,771,420**	**11,476,968**
At 1 January 2007	**7,117,127**	**(335,453)**	**2,923,874**	**-**	**9,705,548**	**1,771,420**	**11,476,968**
Revaluation of property, plan end equipment, net of tax (Note 8)	-	-	-	6,540,866	6,540,866	814,909	7,355,775
Loss for the year	-	-	(1,658,044)	-	(1,658,044)	(178,322)	(1,836,366)
Dividends (Note 13)	-	-	(407)	-	(407)	-	(407)
Issuance of shares (Note 13)	4,007,842	(2,414,744)	-	814,909	2,408,007	(2,408,007)	-
Provision for buy out shares	-	-	-	(33,625)	(33,625)	-	(33,625)
At 31 December 2007	**11,124,969**	**(2,750,197)**	**1,265,423**	**7,322,150**	**16,962,345**	**-**	**16,962,345**

General Director — A.A. Vagner

Chief Accountant — Y.V. Ivanova

24 July 2008

Note 1. The Group and its operations

Open Joint-Stock Company "Territorial Generating Company-2" ("TGC-2") was established on 19 April 2005 within the framework of Russian electricity sector restructuring in accordance with the Resolution of the Board of directors of OJSC RAO UES of Russia (minutes No. 188 of 25 February 2005) and Instruction of the Chairman of the Management Board of OJSC RAO UES of Russia (minutes No. 93 of 18 April 2005).The structure and principles of foundation of TGC-2 were adopted by the Board of Directors of OJSC RAO UES of Russia on 23 April 2004 (Resolution No. 168).

In accordance with the above Resolution:

- On 19 April 2005 TGC-2 was established;
- On 13 April 2006 the OJSC RAO UES Board of Directors approved the share conversion ratios estimated by independent valuators for the regional generating companies (hereinafter – RGC's) being merged into and with TGC-2;
- On 27, 28 February, 09, 13 and 27 March and 10 April 2006 TGC-2 and six of the RGC's held general shareholders' meetings at which the decisions were taken on reorganization of TGC-2 in the form of a merger with OJSC Arkhangelskaya Generating Company (Arkhangelskaya GC), OJSC Yaroslavskaya Energy Company (Yaroslavskaya EC), OJSC Tverskaya Generating Company (Tverskaya GC), OJSC Novgorodskaya Generating Company (Novgorodskaya GC), OJSC Kostromskaya Generating Company (Kostromskaya GC), OJSC Vologodskaya HePP (Vologodskaya HePP).
- For share conversion purposes, the TGC-2 declared additional issuance and placement of 1,095,996,358,137 ordinary shares with the par value of 0.01 Russian Rouble and 16,500,533,681 preference shares with the par value of 0.01 Russian Rouble for total amount of RR 11,124,969 thousand. As a result of converting to a single share, the shareholders of RGC's became the shareholders of the united single company TGC-2, and the minority interest was removed at the TGC-2 level;
- On 1 July 2006 Yaroslavskaya GC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP, on 3 May 2007 Arkhangelskaya GC had ceased operating as legal entities and their assets had merged into and with TGC-2;

During the merger OJSC Kostromaenergoremont, OJSC Novgorodenergoservice, OJSC HePP Belyi Ruchei and OJSC Arkhenergoremont being the subsidiaries of Kostromskaya GC, Novgorodskaya GC, Vologodskaya HePP and Arkhangelskaya GC, respectively, became the subsidiaries of TGC-2:

Name	% owned	Location	Activities
OJSC Kostromaenergoremont	100%	Kostroma	Repair and construction
OJSC Novgorodenergoservice	100%	Novgorod	Repair and construction
OJSC HePP Belyi Ruchei	87.14%	Vologda	Generation of electricity and heat
OJSC Arkhenergoremont	100%	Arkhangelsk	Repair and construction

OJSC Kostromaenergoremont, OJSC Arkhenergoremont and OJSC Novgorodenergoservice were sold in November 2006 and April 2007 respectively (see Note 23).

As at 31 December 2006 the 1st stage of the process of merger of assets of the RGC's into and with TGC-2 and forming of the united Group TGC-2 (hereinafter - "the Group") has been completed.

The merger of assets of Arkhangelskaya Generating Company into and with TGC-2 in course of the 2nd and the last stage of forming the united Group TGC-2 was completed in May 2007.

The TGC-2 Company as at 31 December 2007 for the purpose of preparation of the combined and consolidated accounts financial statements includes TGC-2 and five regional branches - Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP, whose assets were merged into and with TGC-2 as at 1 July 2006, and Arkhangelskaya GC whose assets were merged into and with TGC-2 as at 3 May 2007, and its' subsidiary, OJSC HePP Belyi Ruchei.

The Group principal activity is generation of electricity and heat in the Central and North Russia.

The Group owns 16 electric power stations, 13 boiler plants and 5 heating distribution companies. Total installed electric power capacity of the Group is 2,582.5 MW; total heating capacity – 12,473.195 Gkal/h.

Note 1. The Group and its operations (continued)

The Group is registered with the Inspectorate of the Russian Federal Tax Service for the Leninsky District, the city of Yaroslavl.

The Group's registered office is located at 42, prospekt Octyabrya, Yaroslavl, Russian Federation.

TGC-2 shares are trading on Russian Stock Exchanges – MICEX and RTS.

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

Relations with the state and current regulation. As at 31 December 2007 the OJSC RAO UES of Russia (the Parent) owns 49.36 % of voting ordinary shares of TGC-2. The Company is controlled by the Parent on the basis of a significant shareholding combined with other factors which allow the company to exercise control, namely: RAO UES has the majority in the Board of Directors, RAO UES control over the company operations through its ownership and operation of the Unified Energy System. The Russian Government is the ultimate controlling party of the Group.

The Group customer base includes a large number of entities controlled by or related to the Government of the Russian Federation. Moreover, the state controls a number of the Group fuel and other suppliers (see Note 7). The Government of the Russian Federation directly affects the Group operations through regulating by the Federal Service on Tariffs (FST), with respect to their wholesale energy sales, and through regulating by the regional services on tariffs (RST's), with respect to retail electricity and heating sales.

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

Tariffs which the Group may charge for sales of electricity are governed by regulations specific to the electricity industry and by regulations applicable to natural monopolies. Historically, such tariffs have been based on a "cost-plus" system, meaning cost of service plus a margin, where costs are determined under the Regulations on Accounting and Reporting of the Russian Federation ("RAR"), a basis of accounting which significantly differs from International Financial Reporting Standards ("IFRS"). In practice, tariff decisions were impacted significantly by social and political considerations, causing significant delays in tariff determinations and tariff increases that were lower than required to compensate for cost increases. The tariff structure in the Russian electric utilities industry is undergoing a liberalization process, which should lead to a competitive market-based tariff structure. Also, as described in Notes 26, the Russian government's economic, social and other policies could have material effect on the operations of the Group.

The Group restructuring. On 26 October 2007 the Extraordinary General Meeting of Shareholders of RAO UES took a decision to spin-off JSC TGC-2 from RAO UES as follows:

- on 1 July 2008 OJSC TGC-2 Holding has been formed by the way of spin-off from RAO UES as a new legal entity, which has held ordinary shares of TGC-2 and certain property owned at the moment by RAO UES;
- simultaneously (the same day – on 1 July 2008) with its formation, OJSC TGC-2 Holding has been merged with TGC-2, which is the surviving entity. All assets of OJSC TGC-2 Holding, consisting of the ordinary shares of TGC-2 and other property, has been transferred to the Company;
- upon the merger, OJSC TGC-2 Holding has ceased to exist and its shares have been converted into TGC-2' shares;
- each holder of RAO UES shares:
  - on the day of formation of OJSC TGC-2 Holding – is entitled to a number of shares in the OJSC TGC-2 Holding in proportion to the number of RAO UES shares held by such holder as at 6 June 2008;
  - upon the conversion of OJSC TGC-2 Holding' shares – becomes a shareholder of TGC-2.

On 05 December 2007 the Extraordinary General Meeting of Shareholders of TGC-2 approved additional number of authorized shares in the quantity of 2,705,952,526 shares with par value of RR 0.01 each. The reason for this decision was the share swap which should take place during the merger of OJSC "TGC-2 Holding" with and into TGC-2.

Note 1. The Group and its operations (continued)

Industry restructuring. Electric power as a component of the energy and utilities sector is one of the primary industries and its contribution into the country's GDP is 10–11%. Similar to other sectors of energy and utilities, electric power currently dominates in the production sphere.
In 2007 RAO UES of Russia initiated a surge of its assets sales which have been completed with the energy holding liquidation on 1 July 2008. Strategic investors entered the energy industry in 2007 and 11 generating companies were sold by the end of the year.

Federal Law No.35-FZ "On Electric Utilities" was amended in 2007 confirming that the reform will be continued and RAO UES of Russia will be liquidated. The amendments also tightened state control over electricity suppliers' activities in terms of price manipulation in the free market and their dominance.

In 2007 the wholesale market still operated under the NOREM rules set out by Resolution of the Russian Government No. 529 dated 31.08.2006, the liberalisation rate was 5% and 10% in the first and second half of the year, respectively, with the specifics in terms of electricity volumes supplied to the population taken into account, and by 2011 liberalisation rate will reach 100%.

It is expected that in 2008 a Resolution of the Russian Government will be issued on the launch of the capacity market where available capacity volumes will be allowed to be traded at the transition auctions providing for the supplies during 2009-2011 and long-term auctions for 10 years supplies, given they pass through the competitive selection procedure in their respective free power flow zone. For the first time, the wholesale market agents will have the possibility of concluding non-regulated contracts for capacity supply.

The wholesale electricity market is expected to be fully liberalised at the end of the transition period by 2011.

Recent volatility in global financial markets. Since the second half of 2007 there has been a sharp rise in foreclosures in the US subprime mortgage market. The effects have spread beyond the US housing market as global investors have re-evaluated their exposure to risks, resulting in increased volatility and lower liquidity in the fixed income, equity, and derivative markets. The volume of wholesale financing by Russian companies has significantly reduced since August 2007. Such circumstances may affect the ability of the Group to obtain new borrowings and refinance its existing borrowings at terms and conditions that applied to similar transactions in recent periods. Debtors of the Group may also be affected by the lower liquidity situation which could in turn impact their ability to repay their amounts owed. Management is unable to reliably estimate the effects on the Group's financial position of any further possible deterioration in the liquidity of the financial markets and their increased volatility.

Note 2. Financial condition

At 31 December 2007 the Group current liabilities exceeded its current assets by RR 2,806,568 thousand (as at 31 December 2006: current liabilities exceeded its current assets by RR 3,877,706 thousand).

As at 31 December 2007 the Group net assets were positive and amounted to RR 16,962,345 thousand (at 31 December 2006: RR 11,476,968 thousand).

As discussed in Note 1, the Group is significantly affected by government policy through control of tariffs and other factors. In recent years the Regional Energy Commissions have not always permitted tariff increases in line with inflation and thus some tariffs are insufficient to cover all the costs of generation. Moreover, these tariffs consider costs only on Russian statutory basis and, accordingly, exclude significant additional costs recognized under IFRS basis of accounting. As a result, tariffs often do not allow for an adequate return or provide sufficient funds for the full replacement of property, plant and equipment. However, during 2006 and 2007 the growing demand for electricity and capacity together with increasing the free trading sector of the wholesale electricity market have resulted in a higher rate of revenue growth (see Sector restructuring in Note 1 and impairment reserve reversal in Note 8).

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

- introduction of improved financial analysis and budgeting procedures; a strong focus on timely cash collection of current debtor balances;
- discussions with strategic investors, and identification and assessment of projects requiring investment funds;

Note 2. Financial condition (continued)

- negotiations with federal and regional governments and regulators for real increases in tariffs to support adequate long term investment into the Group generation assets;
- in regard to significant amount of current liabilities, the Group has approved financial plans for 2008 and agreed provisions of credit lines with several Russian banks. Cash received from those banks will be sufficient to re-finance current liabilities. The Group management believes that it will be able to obtain necessary financing in the future.

During 2006 the Arkhangelsk branch has experienced significant losses due to significant increases in price for mazut, the main fuel used by the Arkhangelsk branch.

The Group has agreed an increase in sales tariffs for Arkhangelsk branch for 2007 with the Regional Energy Commission. The 2007 tariff has been increased on average by 25 % for heat sales and by 120 % for electricity sales.

Russian Federation Law No.41-FZ dated 14 April 1995 On State Regulation of Heat and Electricity Tariffs in the Russian Federation and Russian Government Regulation No.109 dated 26 February 2004 on Pricing of Electricity and Heat in the Russian Federation set out the procedure according to which the income shortage of a state-regulated company shall be compensated via regulation of future period tariffs. The Group invoked this right, and therefore 2006 losses were taken into account when establishing tariffs for 2007 and will be taken into account for the future periods.

The Group's management believe that it will be able to negotiate further increases in tariffs with regional government and regulators.

In addition, in April 2007 the Board of Directors of TGC-2 approved an investment programme. As a part of this programme the plan is that the Arkhangelsk branch's power stations are modernized in a way that allows usage of coal or gas as an alternative for mazut.

Management believes, that growing demand for electricity and capacity together with measures discussed above will result in a higher rate of revenue growth (see Sector restructuring in Note 1) and the Group and will be able to raise needed capital to sustain the business.

Note 3. Basis of preparation

Statement of compliance. These combined and consolidated financial statements (hereinafter – the 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 company of the Group individually maintains its own books of accounts and prepares its statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. 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 Group has the date of transition of 1 January 2005. The Group did not previously prepare Russian GAAP financial statements as a separate reporting entity and accordingly no meaningful reconciliations from Russian GAAP to IFRS can be provided.

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

Predecessor Accounting. In June 2006 OJSC RAO UES of Russia (hereinafter - the Parent) transferred to the Group 49.18% of ordinary shares of the following companies: Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC and Vologodskaya HePP.

In May 2007 the Parent transferred to the Group 48.99% of ordinary shares of Arkhangelskaya GC.

Those companies were controlled by the Parent on the basis of a significant shareholding combined with other factors which allow the company to exercise control, namely: RAO UES has the majority in the Board of Directors, RAO UES is the dominant owner or RAO UES has control over the company operations through its ownership and operation of the Unified Energy System.

Note 3. Basis of preparation (continued)

In this combined and consolidated financial statements, the Group accounted for these business combination amongst entities under common control using the predecessor values method. Accordingly, assets and liabilities of the transferred entities were accounted for at their carrying value, as determined by the Parent in its IFRS consolidated financial statements. Statements in respect of the comparative period has been restated as if the business combination took place at the beginning of the earliest period presented.

Thus, starting from 1 January 2005: Yaroslavskaya EC, Tverskaya GC, Novgorodskaya GC, Kostromskaya GC, Vologodskaya HePP and starting from 1 January 2006 Arkhangelskaya GC are aggregated into the Group financial statements as branches of TGC-2.

Reclassifications. The following reclassifications have been made to prior year data to conform with the current year presentation.

Before 31 December 2006, property, plant and equipment were divided into groups, according to their function, such as electricity and heat generation. This classification was considered appropriate when the Predecessor group was comprised of vertically integrated entities carrying out activities from generation to final consumer sales. However, considering the restructuring processes in the industry, dividing of property, plant and equipment according to their functional area no longer provides useful information.

Management considers that classifying property, plant and equipment by their nature rather than by their function provides more useful information and is more representative of the new structure of industry. Comparative information for 2006 and 2005 has been restated in line with the new classification.

PPE groups for IFRS purposes (in accordance with previously adopted classification)	As at 31 December 2006	As at 31 December 2005
Electricity and heat generation	10,803,874	5,029,964
Electricity distribution	595,895	270,777
Heating networks	2,395,240	1,245,493
Construction in progress	2,100,722	1,663,550
Other	800,131	452,178
Total	**16,695,862**	**8,661,962**

PPE groups for IFRS purposes (in accordance with newly adopted classification)	As at 31 December 2006	As at 31 December 2005
Production buildings	4,986,328	2,301,614
Hydrotechnical buildings	222,074	103,787
Equipment and assembling units	4,434,628	2,050,131
Substations & power equipment	1,718,186	822,590
Electricity grids and equipment	38,553	22,619
Heat grids	2,395,240	1,245,493
Construction in progress	2,100,722	1,663,550
Other	800,131	452,178
Total	**16,695,862**	**8,661,962**

Accounting for the effects of hyperinflation. Prior to 1 January 2003 the adjustments and reclassifications made to the statutory records for the purpose of IFRS presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with International Accounting Standard 29 ("IAS") "Financial Reporting in Hyperinflationary Economies". IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy should be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicated that hyperinflation ceased, effective from 1 January 2003 the Group no longer applied the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current as of 31 December 2002 are treated as the basis for the carrying amounts in the consolidated financial statements for subsequent periods.

Going concern.This financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. The accompanying financial statements do not include any adjustments should the Group be unable to continue as a going concern.

Note 4. Summary of significant accounting policies

Principles of consolidation. The Financial Statements comprise the financial statements of TGC-2 and the financial statements of those entities whose operations are controlled by TGC-2. Control is presumed to exist when TGC-2 controls, directly or indirectly through subsidiaries, more than 50% of voting rights.

A) Subsidiaries
The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. The minority interest has been presented as part of equity.

B) Transactions eliminated on consolidation
Inter-company balances and transactions, and any unrealised gains arising from inter-company transactions, are eliminated in preparing the consolidated financial statements.

C) Transactions with minority interest
The Group applies a policy of treating transactions with minority interest as transactions with the owners in their capacity of owners. In case of purchases of minority interest, the difference between any consideration paid and the relevant share of the carrying value of net assets of the subsidiary acquired is recognised in equity.

Transfers of subsidiaries from parties under common control. Contributions to share capital of shares in subsidiaries from parties under common control are accounted for using the predecessor values method. Under this method the financial statements of the combined entity are presented as if the businesses had been combined from the beginning of the earliest period presented. Any difference between the carrying amount of net assets and the nominal value of share capital and other considerations contributed is accounted for in the combined and consolidated financial statements as an adjustment to equity.

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

Financial assets. The Group holds only financial assets classified as loans and receivables. 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 receivable comprise 'trade and other receivable' and 'cash and cash equivalents' in the balance sheet.
Loans and receivables are carried at amortised cost using the effective interest method.

Property, plant and equipment. Starting from 1 January 2007 the Group changed its accounting policy to revalue property, plant and equipment on a regular basis. Prior to 1 January 2007 property, plant and equipment were stated at depreciated cost less impairment. 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. 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 estimated the recoverable amount which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognized as a decrease of revaluation reserve in the equity. An impairment loss recognized in prior years is reversed if there have been a change in the estimates used to determine an asset's recoverable amount. Reversal of impairment is credited to the equity statement under the heading of revaluation reserve. If an impairment loss on the revalued asset was previously recognized in the income statement, a reversal of that impairment loss is also recognized in the income statement.

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 of property, plant and equipment are credited to revaluation reserves in equity. Decreases that offset previous increases of the same asset are charged against revaluation reserves directly in equity; all other decreases are charged to the income statement. Any accumulated depreciation at the date of revaluation is eliminated against the gross amount of the asset, and the net amount is restated to the revalued amount of the asset.

Note 4. Summary of significant accounting policies (continued)

The Group records deferred taxes in respect of revaluation of property, plant and equipment directly to equity.

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

Depreciation on 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.

Prior to 31 December 2006 for the property, plant and equipment which were subject to the third party valuation as at 31 December 1997, the depreciation rate applied was based on the estimated remaining useful lives as at the valuation date. The useful lives, in years, of assets by type of facility were as follows:

Type of facility	Acquired prior to 31 December 1997	Acquired subsequent to 31 December 1997
Electricity and heat generation	12-50	20-50
Electricity distribution	6-26	25-30
Heating grids	6-13	20-25
Other	8	10

The useful lives, in years, of assets by type of facility (after reclassification) were as follows:

Type of facility	Acquired prior to 31 December 1997	Acquired subsequent to 31 December 1997
Production buildings	30	50
Hydrotechnical buildings	39	50
Equipment and assembling units	19	20
Substations & power equipment	8-10	25-30
Electricity grids and equipment	18	25
Heat grids	9	20
Other	8	10

Beginning from 1 January 2007 the depreciation rate applied is based on the estimated remaining useful lives as at valuation date. If estimated useful lives had not been changed from 1 January 2007, the depreciation for 2007 year had been reduced by RR 1,637, 784 thousand. Effect of change in the useful lives for the future periods has not been assessed as management considers such estimation impracticable.

The revised useful lives, in years, of revalued assets by type of facility (after reclassification) were as follows:

Type of facility	Revised starting from 1 January 2007
Production buildings	2-59
Hydrotechnical buildings	2-92
Equipment and assembling units	1-40
Substations & power equipment	2-39
Electricity grids and equipment	2-30
Heat grids	2-29
Other	1-59

Operating lease. 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 period of the lease.

The lease payments receivable under operating lease contracts (less allowances provided by the lessor) are recognized in the income statement on a straight-line basis over the lease term.

Finance lease. 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. Each lease payment is allocated between the liability and finance charges so as to

Note 4. Summary of significant accounting policies (continued)

achieve a constant rate on the finance balance outstanding.The corresponding rental obligations, net of future finance charges, are included in debts. The interest cost is charged to the income statement over the lease period using the effective interest method. The assets acquired under finance lease 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.

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

Inventories. Inventories are recorded at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses. Cost of inventory is determined on the weighted average basis. Provision is made for potential losses on obsolete or slow-moving inventories, taking into account their expected use and future realizable value.

Value added tax on purchases and sales. Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) transfer of ownership for the goods to customers. Input VAT is generally recoverable against output VAT on the cash basis. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is disclosed separately as a current asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Accounts receivables and prepayments. Accounts receivable are recorded inclusive of value added taxes. Trade and other receivables are adjusted for an allowance made for impairment of these receivables. Such an allowance for doubtful debtors is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the allowance is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the original effective rate of interest. The amount of the provision is recognised in the consolidated income statement. The primary factors that the Group considers whether a receivable is impaired is 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 of the receivable 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;
- the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

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

Deferred income tax. 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 entities 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.

Note 4. Summary of significant accounting policies (continued)

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

Borrowings. Borrowings are recognised initially at their fair value. Fair value is determined using the prevailing market rates of interest for similar instruments, if significantly different from the interest rates under the loan received. In subsequent periods, borrowings are stated at amortised cost using the effective interest method; any difference between the amount at intitial recognition and the redemption amount is recognised in the income statement as an interest expense over the period of the debt obligation.

Borrowing costs are recognised as an expense in the period in which they are incurred.

Provisions. Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, when 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.

Pension benefits and other social obligations. In the normal course of business the Group contributes to the Russian Federation state pension scheme on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred. Additional pension payments and other post-employment benefits to the employees are included within salaries, employee benefit expenses and payroll taxes in the income statement.

The Group operate defined benefit plans with respect to the majority of the Group employees. 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 the defined benefit pension plans is the present value of defined benefit obligations at the balance sheet date less the fair value of plan assets, including adjustments related to unrecognised actuarial gains and losses.The defined benefit obligations are calculated using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality government bonds denominated in the same currency as pension benefits, with terms to maturity approximating the terms of the related pension liability.

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

Revenue recognition. Revenue is recognised on the delivery of electricity and heat and on the dispatch of non-utility goods and services within the reporting period. Revenue amounts are presented exclusive of value added taxes.

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

Earnings per share. Preference shares are considered to be participating shares as their dividend may not be less than that given with respect to ordinary shares. The earnings per share is determined by dividing the net income attributable to ordinary and preference shareholders by the weighted average number of ordinary and preference shares outstanding during the reporting period, excluding the average number of treasury shares held by the Group. Preference shares participate in losses.

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

Segment reporting. The Group operates in a single geographical area and industry – generation of electricity and heat in the territory of the Russian Federation. The generation of electricity and heat are related activities and are subject to similar risks; therefore they are reported as one business segment.

Note 5. Critical accounting estimates and assumptions

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

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 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).

Impairment provision for accounts receivable. The impairment provision for accounts receivable is based on the Group assessment of wether the collectibility of specific customer accounts worsened compared to prior estimates. If there is deterioration in a major customer's creditworthiness or actual collections from customers are different form the estimates, the actual accounts receivable could differ from these estimates. Account receivable which has been assessed as uncollectible during the period is being written-off against impairment provision to the extent of impairment charge recognised against that receivable. If amount being written-off is greater than impairment recognised in prior periods, remaining amount is being written-off directly to operating expenses.

Impairment of non-financial assets. At each balance sheet date the Group assesses whether there is any indication that the carrying amount of the Group assets exceeds their recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. When such indication of impairment is identified, the carrying amount is reduced to the recoverable amount. The amount of the impairment is recorded in the income statement in the period when the impairment is actually identified. If conditions change and management determines that the assets' value has increased, the impairment provision will be fully or partially reversed. Accounting for impairment includes provisions against property, plant and equipment and inventory obsolescence, calculated based on assumptions made by the Group (see 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 tax positions cannot be sustained, an appropriate amount is accrued in these IFRS financial statements (see Note 26).

Note 6 (a). Adoption of new or revised Standards and Interpretations

These new or amended standards and interpretations that are in force for the year beginning on 1 January 2007 and their impact on the current period or any prior period are described below:

- IFRS 7 *Financial Instruments: Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures* (effective from 1 January 2007). This IFRS introduced new disclosures to improve the information about financial instruments, including about quantitative aspects of risk exposures and the methods of risk management. The new quantitative disclosures provide information about the extent of exposure to risk, based on information provided internally to the entity's key management personnel. Qualitative and quantitative disclosures cover exposure to credit risk, liquidity risk and market risk including sensitivity analysis to market risk. IFRS 7 replaced IAS 30, *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*, and some of the requirements in IAS 32, *Financial Instruments: Disclosure and Presentation.* The Amendment to IAS 1 introduced disclosures about the level of an entity's capital and how it manages capital. The new disclosures are made in these consolidated financial statements;

Note 6 (a). Adoption of new or revised Standards and Interpretations (continued)

- IFRIC 7, *Applying the Restatement Approach under IAS 29* (effective for periods beginning on or after 1 March 2006, that is from 1 January 2007);
- IFRIC 8, *Scope of IFRS 2* (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007);
- IFRIC 9, *Reassessment of Embedded Derivatives* (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10, *Interim Financial Reporting and Impairment* (effective for annual periods beginning on or after 1 November 2006).

The effect of adoption of the above new standard and interpretations (except IFRS 7) on the Group's financial position at 31 December 2007 and 31 December 2006 and on the results of its operations for the periods ended on the specified dates was not significant.

IFRS 7 introduces new disclosures relating to financial instruments. This standard does not have any impact on the classification and valuation of the Group's financial instruments.

Note 6 (b). New Accounting Pronouncements

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2008 or later periods and which the Group has not early adopted:

- ***IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009)***. The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. The Group is currently assessing what impact the standard will have on segment disclosures in the consolidated financial statements.
- ***Puttable financial instruments and obligations arising on liquidation – IAS 32 and IAS 1 Amendment (effective from 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 23, Borrowing Costs (revised March 2007; effective for annual periods beginning on or after 1 January 2009).*** The revised IAS 23 was issued in March 2007. 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 financial statements.
- ***IAS 1, Presentation of Financial Statements (revised September 2007; effective for annual 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 financial statements but to have no impact on the recognition or measurement of specific transactions and balances.
- ***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

Note 6 (b). New Accounting Pronouncements (continued)

- 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.
- ***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 on the same basis as US GAAP (at fair value). The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, goodwill will be measured as the difference at acquisition date between the fair value of any investment in the business held before the acquisition, the consideration transferred and the net assets acquired. Acquisition-related costs will be accounted for separately from the business combination and therefore recognised 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 is currently assessing the impact of the amended standard on its consolidated financial statements.
- ***Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment (issued in January 2008; effective for annual periods beginning on or after 1 January 2008).*** The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.
- ***IFRIC 13, Customer loyalty programmes (issued in June 2007; 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. IFRIC 13 is not relevant to the Group's operations because no Group companies operate any loyalty programmes.

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

- IAS 27 (Revised), Consolidated and Separate Financial statements (effective for annual periods beginning on or after 1 July 2009);
- IFRIC 11, *IFRS 2 – Group and Treasury Share Transactions* (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12, *Service Concession Arrangements* (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 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);
- 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. (The Group is currently assessing the impact of the interpretation on its consolidated financial statements);
- 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

Note 6 (b). New Accounting Pronouncements (continued)

- 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 (IFRIC 16 does not have an impact on these consolidated financial statements as the Group does not apply hedge accounting).

Improvements to International Financial Reporting Standards (issued in May 2008). 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, including ***IFRS 5, Non-current Assets Held for Sale and Discontinued Operations (and consequential amendments to IFRS 1) (effective for annual periods beginning on or after 1 July 2009).*** The amendment clarifies that an entity committed to a sale plan involving loss of control of a subsidiary would classify the subsidiary's assets and liabilities as held for sale. The revised guidance should be applied prospectively from the date at which the entity first applied IFRS 5.

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Group's financial statements.

Note 7. Related parties

Related parties are defined in IAS 24, *Related Party Disclosures*. Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties include shareholders, who have significant influence or control over the Group, directors, subsidiaries and enterprises controlled by the state.

OJSC RAO UES as at 31 December 2007 is the main shareholder of TGC-2 and has a control over the Group's activity.

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions during the year ended 31 December 2007 and the year ended 31 December 2006 or had significant balances outstanding at 31 December 2007 and 31 December 2006 are detailed below.

Parent company

Balances with OJSC RAO UES were as follows:

	31 December 2007	31 December 2006
Short-term accounts payable	2,431	-
Borrowings	-	28,130

Transactions with OJSC RAO UES were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Interest expense	17,874	94,225

Transactions with OJSC RAO UES subsidiaries and associates

Transactions with the Parent's subsidiaries and associates were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Sales of electricity and heat	6,565,785	4,507,301
Other income	62,882	60,750

Note 7. Related parties (continued)

	Year ended 31 December 2007	Year ended 31 December 2006
Electricity purchases	111,780	236,302
Heat purchases	85,422	-
Electricity dispatching services	122,735	110,643
Repairs and maintenance services	988	27,325
Rent expenses	14,205	12,922
Other expenses	2,033	742

Balances with the Parent's subsidiaries and associates at the end of the period were as follows:

	31 December 2007	31 December 2006
Accounts receivable	1,134,340	522,486
Accounts payable	(15,153)	(9,157)

State controlled entities

In the normal course of business the Group enters into transactions with other entities under Government control. The prices for natural gas, electricity and heat are based on tariffs established by FTS and RST. Bank loans are obtained under market rates. Taxes are charged and paid under the Russian tax legislation.

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

	Year ended 31 December 2007	Year ended 31 December 2006
Fuel purchases	(5,102,595)	(4,675,759)
Sales of electricity and heat	5,815,610	3,453,936
Interest expense	(372,717)	(140,822)

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

	31 December 2007	31 December 2006
Cash	393,425	19,565
Current accounts receivable and prepayments	1,161,017	529,482
Borrowings	(6,667,600)	(3,263,512)
Accounts payable and accrued liabilities	(62,922)	(176,897)

Tax balances are disclosed in the balance sheet and Notes 11 and 18. Tax transactions are disclosed in Group combined and consolidated income statement and Note 20.

Transactions with Board of Directors and key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

Total remuneration accrued and paid to the members of the Board of Directors and Management Board for the year ended 31 December 2007 and for the year ended 31 December 2006 was as follows:

	Year ended 31 December 2007		Year ended 31 December 2006	
	Expense	Accrued liability	Expense	Accrued liability
Remuneration	45,866	39,597	28,292	18,603
Retirement benefit obligation	676	1,226	138	660

Note 7. Related parties (continued)

At 31 December 2007 there were 11 members of the Board of Directors and 7 members of the Management Board.

Termination Benefits. The Group entered into additional agreements to employment contracts with the General Director and members of the Group's Management Committee after the balance sheet date. These agreements set out the procedure, terms and conditions for termination benefits payable to members of the Group's senior 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 March 2008 through 14 March 2011. The amount to be paid by the Group varies from zero to RR 121,000 thousand.

The Group has no other compensation programs.

(in thousands of Russian Roubles)

Note 8. Property, plant and equipment

	Production buildings	Hydrotechnical buildings	Equipment and assembling units	Substations & power equipment	Electricity grids and equipment	Heat grids	Construction in progress	Other	Total
Cost									
Opening balance as at 1 January 2007	**7,825,422**	**286,925**	**7,090,161**	**3,071,826**	**48,329**	**7,011,921**	**2,100,722**	**4,939,227**	**32,374,533**
Elimination of accumulated depreciation	(3,169,332)	(221,092)	(2,716,670)	(1,401,509)	(25,397)	(4,721,134)	-	(3,423,537)	(15,678,671)
Assets revaluation	1,890,268	230,449	548,530	25,030	10,459	2,841,842	753,379	3,378,694	9,678,651
Revaluation write down	(5,312)	-	(318,784)	(862,256)	(3,544)	-	(237,796)	(139,199)	(1,566,891)
Additions	12,652	-	20,918	339	-	-	1,679,373,	59,438	1,772,720
Transfers	251,258	31,207	753,637	294,530	6,222	121,332	(1,782,235)	324,049	-
Disposals	(14,585)	-	(2,186)	(1,001)	(562)	(621)	(53)	(19,670)	(38,678)
Closing balance as at 31 December 2007	**6,790,371**	**327,489**	**5,375,606**	**1,126,959**	**35,507**	**5,253,340**	**2,513,390**	**5,119,002**	**26,541,664**
Accumulated depreciation									
Opening balance as at 1 January 2007	**(3,169,332)**	**(221,092)**	**(2,716,670)**	**(1,401,509)**	**(25,397)**	**(4,721,134)**	**-**	**(3,423,537)**	**(15,678,671)**
Elimination of accumulated depreciation	3,169,332	221,092	2,716,670	1,401,509	25,397	4,721,134	-	3,423,537	15,678,671
Charge for the period	(700,219)	(5,971)	(535,559)	(156,159)	(8,653)	(908,028)	-	(870,391)	(3,184,980)
Disposals	-	-	-	46	-	86	-	249	381
Closing balance as at 31 December 2007	**(700,219)**	**(5,971)**	**(535,559)**	**(156,113)**	**(8,653)**	**(907,942)**	**-**	**(870,142)**	**(3,184,599)**
Net book value as at 1 January 2007	**4 656 090**	**65 833**	**4 373 491**	**1 670 317**	**22 932**	**2 290 787**	**2 100 722**	**1 515 690**	**16 695 862**
Net book value as at 31 December 2007	**6 090 152**	**321 518**	**4 840 047**	**970 846**	**26 854**	**4 345 398**	**2 513 390**	**4 248 860**	**23 357 065**

(in thousands of Russian Roubles)

Note 8. Property, plant and equipment (continued)

	Production buildings	Hydrotechnical buildings	Equipment and assembling units	Substations & power equipment	Electricity grids and equipment	Heat grids	Construction in progress	Other	Total
Cost									
Opening balance as at 1 January 2006	**7,673,038**	**334,548**	**6,837,255**	**3,894,963**	**87,529**	**7,336,325**	**1,663,550**	**3,405,223**	**31,232,431**
Additions	15,159	-	3,100	2,658	-	52,385	1,106,866	89,032	1,269,200
Transfers	41,764	-	81,226	80,723	271	110,688	(656,454)	341,782	-
Disposals	(60,349)	-	(818)	(429)	-	-	(13,240)	(52,262)	(127,098)
Closing balance as at 31 December 2006	**7,669,612**	**334,548**	**6,920,763**	**3,977,915**	**87,800**	**7,499,398**	**2,100,722**	**3,783,775**	**32,374,533**
Accumulated depreciation (including impairment)									
Opening balance as at 1 January 2006	**(5,371,424)**	**(230,761)**	**(4,787,124)**	**(3,072,373)**	**(64,910)**	**(6,090,832)**	**-**	**(2,953,045)**	**(22,570,469)**
Charge for the period	(106,178)	(3,903)	(154,577)	(118,522)	(2,958)	(202,964)	-	(146,312)	(735,414)
Disposals	27,991	-	542	447	-	-	-	18,264	47,244
Release of impairment loss	2,766,327	122,190	2,455,024	930,719	18,621	1,189,638	-	97,449	7,579,968
Closing balance as at 31 December 2006	**(2,683,284)**	**(112,474)**	**(2,486,135)**	**(2,259,729)**	**(49,247)**	**(5,104,158)**	**-**	**(2,983,644)**	**(15,678,671)**
Net book value as at 1 January 2006	**2,301,614**	**103,787**	**2,050,131**	**822,590**	**22,619**	**1,245,493**	**1,663,550**	**452,178**	**8,661,962**
Net book value as at 31 December 2006	**4,986,328**	**222,074**	**4,434,628**	**1,718,186**	**38,553**	**2,395,240**	**2,100,722**	**800,131**	**16,695,862**

Note 8. Property, plant and equipment (continued)

Construction in progress represents the carrying amount of property, plant and equipment that has not yet been put into operation.

Depreciation is charged once an asset is available for use.

Other property, plant and equipment include motor vehicles, computers, office furniture and other equipment.

Revaluation. Starting from 1 January 2007 the Group changed its accounting policy to revalue property, plant and equipment on a regular basis (see Note 4). Asset values were determined by independent appraisers primarily based on the depreciated replacement cost method. The replacement cost of buildings, constructions, machinery and equipment and transfer devices has been estimated based on technical characteristics, unit construction cost and construction estimates. The replacement cost of equipment was estimated based on data of aggregative replacement cost of heat-power station, current purchase contracts and price-list of producers and trading companies. Economic obsolescence was estimated based on profitability test results for each cash-generating unit – Yaroslavl branch, Tver branch, Vologda branch, Novgorod branch, Kostroma branch, Arkhangelsk branch. The discount rate used in profitability test was 14.23 percent, except for Arkhangelsk branch, which was 15.96 percent. The forecast period is 19 years. The long-term rate of growth in sales volumes is approximately 3 percent.

As a result of the revaluation, the Group equity increased by RR 7,355,775 thousand, comprising an increase in carrying value of property, plant and equipment of RR 9,678,651 thousand, net of a related deferred tax liability of RR 2,322,876 thousand. As a consequence of recognizing the results of the revaluation a revaluation write down of RR 1,566,891 thousand was recognized in the income statement. Revaluation loss has been recognized for those assets whose fair values are lower than their respective net book value as at 1 January 2007. The remaining effect of the revaluation, RR 7,355,775 thousand was recognized directly in equity as a other reserve.

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 had the assets been carried under the cost model is as follows:

	Production buildings	Hydrotechnical buildings	Equipment and assembling units	Substations & power equipment	Electricity grids and equipment	Heat grids	Assets under construction	Other	Total
Net book value as at 31 December 2007	4,435,886	95,622	4,660,735	1,632,320	21,765	2,032,164	2,022,276	1,585,456	16,486,224
Net book value as at 31 December 2006	4,986,328	222,074	4,434,628	1,718,187	38,553	2,395,240	2,100,722	800,131	16,695,862

As at 31 December 2007 and at 31 December 2006 no property, plant equipment balances were pledged as collateral according to loan agreements.

Impairment release as at 31 December 2006. As at 31 December 2006 management considered recent favorable changes in operation of the Russian electricity market and reassessed recoverable amount of the Group's property, plant and equipment as at 31 December 2006 to its value in use.

Such positive changes include:

1. upward revisions, based on recent trends, in the expected growth of demand for electricity and heat in the regions in which the Group operates;

2. higher degree of certainty about the free trading sector for electricity, which has been enacted by the government of the Russian Federation in August 2006 (see Note 1).

These developments have resulted in a change to the assumptions that were used to determine the value in use of the assets included in each cash generating unit. An impairment review has been carried out by comparing the recoverable amount of the each cash generating unit to its net book value. The recoverable amount was based on value in use, which was calculated based on estimated future cash flows using various assumptions including the following significant assumptions:

- annual increase in electricity tariffs is estimated by the management as 6%-27% p.a. in 2008-2011 and 3%-5% p.a. in 2012 and onwards;
- annual increase in heat tariffs is estimated by the management as 17%-18% p.a. in 2008-2011, 3%-5% p.a. in 2012 and onwards;

Note 8. Property, plant and equipment (continued)

- annual growth of gas prices is estimated by the management as 23%-26% p.a. in 2008-2011; 4% p.a. in 2012 and onwards;
- annual growth of coal prices is estimated by the management as 5%-11% p.a. in 2008-2011; 3% p.a. in 2012 and onwards;
- growth of mazut prices set for the Group were on average 5-6% in 2008-2011 and 3%-5% p.a. in 2012 and onwards;
- growth of peat prices set for the Group were on average 5-7% in 2008-2011 and 4% p.a. in 2012 and onwards;
- the assumption was made that production volumes of electricity and heat will remain at the current level for the whole impairment test period (investment programme is not included);
- increase of major cost (except of fuel) will not exceed the inflation rate;
- weighted average cost of capital of 14.23 percent for TGC-2 and 15.96 percent for Arkhangelskaya GC was applied for discounting future operating cash flows generated by the Group for all cash generating units;
- the Group's restructuring did not change the manner of recovery of the assets – the regulator allocated previously single tariffs for electricity and heat set for a vertically integrated power companies among newly created generating businesses.

Impairment assessment as at 31 December 2007. Management believes that there were no indications of impairment of the Group's principal operating assets at 31 December 2007, due to the following reasons:

- higher than expected growth of demand for electricity and heat in regions in which the Group operates, which is based on recent trends;
- higher certainty about the free trading sector for electricity, which has been enacted by the government of the Russian Federation as of August 2006;
- the tariffs on electricity and heat are increased leading to increase of revenue (see Note 2);
- there is no evidence of significant adverse changes in the market, economic, technological, legal environment during reporting period and in the foreseeable future;
- the Group is not planning to sell a significant part of PPE;
- there have not been changes in the activity of the Group which can lead to adverse effect on value of PPE;
- there is no evidence of obsolescence or physical damage of PPE;
- there have not been any significant changes in the market interest rates.

Operating lease. The Group leases a number of land areas and facilities owned by local governments under operating lease. Land lease payments are determined by lease agreements.

Operating lease rentals under non-cancellable leases are payable as follows:

	31 December 2007	31 December 2006
not later than one year	171,578	161,851
later than one year and not later than five years	529,881	340,495
later than five years	7,048,500	1,836,470
Total	**7,749,959**	**2,338,816**

The land areas leased by the Group are the territories on which the Group's electric power stations, heating stations and other assets are located. Some contracts for land lease are concluded for 49 years, other contracts are concluded for one year with prolongation. Lease payments are reviewed regularly to reflect market rentals.

Note 8. Property, plant and equipment (continued)

Finance lease. As at 31 December 2007 assets under finance lease which are included in the "Other" category within property, plant and equipment were as follows:

	31 December 2007	31 December 2006
Cost of finance leased assets	164,735	164,735
Accumulated depreciation	(51,984)	(36,556)
Net book value	**112,751**	**128,179**

The maturity table and information about minimum lease payments of finance lease liability as follows:

	31 December 2007	31 December 2006
not later than one year	3,067	10,206
later than one year and not later than five years	3,300	6,005
later than five years	155	430
Lease payments	**6,522**	**16,641**

Assets under the financial lease agreements were received from LLC «RosBusinesLeasing», LLC «Verhnevolzhskaya Lease Company», LLC «Art Leasing», LLC «Centroenergo-consulting», LLC «Petroenergoleasing».

Note 9. Other non-current assets

	Effective interest rate,%	31 December 2007	31 December 2006
Long-term loans issued	12	16,821	19,182
Non-current account receivables (due 2009-2029)	12	353,474	155,839
Total financial assets	**-**	**370,295**	**175,021**
Non-current input VAT (to be recovered more than one year after reporting date)	-	13,109	74,898
Other	-	148,216	39,517
Other non-current assets	**-**	**531,620**	**289,436**

Long-term loans issued represent non-current portion of the Group's employees' receivables on flat payments by installments, on 12% annual interest loans provided by Group.

Non-current account receivable as at 31 December 2007 and 31 December 2006 represents restructured receivable from OJSC Tver Utilities.

Note 10. Inventories

	31 December 2007	31 December 2006
Fuel	1,411,974	1,306,185
Spare parts	296,831	346,879
Other inventories	451,061	276,784
Total inventories	**2,159,866**	**1,929,848**

Other inventories are presented net of provision for obsolescence of RR 17,867 thousand at 31 December 2006 (31 December 2007: nil).

As at 31 December 2007 and 31 December 2006, the inventory balance included RR 1,216,734 thousand and RR 581,573 thousand, respectively, of inventory pledged as collateral under loan agreements.

Note 11. Accounts receivable and advances issued

	31 December 2007	31 December 2006
Trade receivables (net of allowance for doubtful debtors of RR 742,404 thousand as at 31 December 2007 and RR 1,245,891 thousand as at 31 December 2006)	1,945,900	1,504,994
Other receivables (net of allowance for doubtful debtors of RR 6,903 thousand as at 31 December 2007 and RR 106,583 thousand as at 31 December 2006)	272,520	242,857
Total financial assets	**2,218,420**	**1,747,851**
Advances to suppliers (net of allowance for doubtful debtors of RR 19,321 thousand as at 31 December 2007 and RR 936 thousand as at 31 December 2006)	545,769	260,568
Value added tax recoverable	410,920	199,257
Prepayments to the budget (other than income tax)	52,777	15,112
Total trade and other receivable	**3,227,886**	**2,222,788**

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

Certain trade receivables and other accounts receivable have been restructured and are due to be realized more than one year from the balance sheet date (see Note 9).

The Group manages accounts receivable and analyses of contractors' credit risk (see Note 2). The Group analyses its debt by the classes presented in the table below. Management determines two main classes – Electricity and Heat. Electricity is sold in an open and highly regulated market to other energy companies that sell that electricity further to the final customers. Heat is sold to resellers and also to final customers. Debtors within these classes are quite homogeneous regarding their credit quality and other characteristics.

Accounts receivable current and not impaired:

	31 December 2007	31 December 2006
Electricity	175,102	20,060
Heat	773,817	659,934
Other	148,479	148,887
Total current and not impaired	**1,097,398**	**828,881**

As at 31 December 2007 trade and other receivable of RR 1,121,022 thousand (as at 31 December 2006: RR 918,970 thousand) were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The ageing analysis of these trade receivables is shown in the table below:

Trade and other receivables past due but not impaired as at 31 December 2007:

	1-3 months	3-6 months	6-12 months	1-5 years	More than 5 years	Total amount
Electricity	7,017	2,786	1,836	4,729	689	17,057
Heat	598,522	36,321	215,057	130,023	-	979,923
Other	6,211	-	92,384	14,917	10,530	124,042
Total past due but not impaired	**611,750**	**39,107**	**309,277**	**149,669**	**11,219**	**1,121,022**

Trade and other receivables individually determined to be impaired (gross):

	31 December 2007	31 December 2006
Electricity	77,741	105,151
Heat	664,663	1,140,740
Other	6,903	106,583
Total individually impaired	**749,307**	**1,352,474**

Note 11. Accounts receivable and advances issued (continued)

All impaired trade and other receivables have been provided for. The movement of provision is shown in the table below:

Impairment of trade and other receivables for the year ended 31 December 2007:

	Electricity	Heat	Other	Total amount
As at 1 January	105,151	1,140,740	106,583	1,352,474
Charge for the year	-	352,432	6,903	359,335
Trade and other receivables written-off during the year as uncollectible	-	(23,706)	-	(23,706)
Unused amounts reversed	(27,410)	(804,803)	(106,583)	(938,796)
As at 31 December	**77,741**	**664,663**	**6,903**	**749,307**

Impairment of trade and other receivables for the year ended 31 December 2006:

	Electricity	Heat	Other	Total amount
As at 1 January	105,151	837,133	106,583	1,048,867
Charge for the year	-	306,110	-	306,110
Trade and other receivables written-off during the year as uncollectible	-	(2,503)	-	(2,503)
Unused amounts reversed	-	-	-	-
As at 31 December	**105,151**	**1,140,740**	**106,583**	**1,352,474**

Note 12. Cash and cash equivalents

	31 December 2007	31 December 2006
Cash in bank and in hand	234,068	81,822
Cash equivalents	202,000	39,501
Total Cash and Cash equivalents	**436,068**	**121,323**

Cash equivalents comprise certificates of overnight deposit.

Bank deposits	Rating	Rating agency	31 December 2007	31 December 2006
OJSC "VTB Bank"	Baa2	Moody's	202,000	-

All cash and cash equivalents are denominated in Russian Roubles.

Note 13. Equity

Basis of presentation of movements in equity. The Group was formed by the combination of a number of businesses under common control. Because of the consequent use of the predecessor basis (see Note 2), the principal component of the net equity recognized 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. As the Group was formed as a result of share issue completed after 01 January 2005, the equity statement reflects additions to share capital in the amount equal to the statutory nominal value of the shares issued which is based on the fair value of the net assets of the businesses contributed. In accordance with the predecessor basis of accounting, the effect of such addition to equity is offset by a corresponding increase in the merger reserve and reduction in minority interest.

Note 13. Equity (continued)

Share capital

	31 December 2007	31 December 2006
Number of ordinary and preference shares authorized, issued and fully paid	1,112,496,891,818	711,712,704,501
Par value (in RR)	0.01	0.01
Total share capital (in thousand RR)	**11,124,969**	**7,117,127**

As at 19 April 2005, the date that the Group was established, the number of issued ordinary shares amounted to 1,000,000,000 with a par value of RR 0.01 each.

Contributions to the Group's share capital in amount of RR 10,000 thousand were paid in cash in the year 2005.

As of 29 June 2006 the Group increased it's share capital by RR 7,107,127 thousand by conversion of ordinary and preference shares of OJSC Vologodskaya HePP, OJSC Kostromskaya GC, OJSC Novgorodskaya GC, OJSC Tverskaya GC and OJSC Yaroslavskaya EC into the ordinary shares of TGC-2.

As of 3 May 2007 the Group increased it's share capital by RR 4,007,842 thousand by conversion of ordinary and preference shares of OJSC Arkhangelskaya GC into the ordinary shares of TGC-2.

As a result, OJSC RAO UES shareholdings (49.18% of OJSC Vologodskaya HePP, OJSC Kostromskaya GC, OJSC Novgorodskaya GC, OJSC Tverskaya GC and OJSC Yaroslavskaya EC, 48.99% of Arkhangelskaya GC) and minorities' shareholdings (50.82% and 51.01% for Arkhangelskaya GC) were exchanged for the shares of TGC-2.

Share capital in the Statement of Changes in Equity as at 31 December 2007 includes number of issued ordinary shares amounted to 1,095,996,358,137 with a par value of RR 0.01 each and number of preference shares amounted to 16,500,533,681 a par value of RR 0.01 each.

Ordinary shares and preference shares. Preference shares have no right of conversion or redemption. 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 dividends on preference shares have not been declared fully at the Annual Shareholders' meeting. At liquidation, preference shareholders are first paid any declared unpaid dividends and then the nominal value of the shares ("liquidation value"). Following this, preference shareholders then participate equally in the distribution of remaining assets with ordinary shareholders.

Merger reserve. Merger reserve of RR (335,454) thousand as at 1 January 2007 represents the difference between IFRS carrying value of the contributed net assets merged into the Group, totaling RR 11,476,968 thousand, and the minority interest of RR 1,771,420 thousand, share capital of RR 7,117,127 thousand, retained earnings of RR 2,923,875 thousand. The merger reserve was subsequently adjusted by the share capital issued by TGC-2 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 financial statements prepared in accordance with Russian Accounting Rules. The statutory accounting reports are the basis for the annual profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit. However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and, accordingly, management believes at present it would not be appropriate to disclose an amount for the distributable reserves in this financial statements.

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

Note 13. Equity (continued)

	Year ended 31 December 2007		Year ended 31 December 2006	
	Declared dividends, in thousand of RR	Dividends per share, RR	Declared dividends, in thousand of RR	Dividends per share, RR
OJSC Yaroslavskaya EC in respect of the year ended 31 December 2005	-	-	76,620	3.538605
OJSC Kostromskaya GC in respect of the year ended 31 December 2005	-	-	60,000	0.110025
OJSC Novgorodskaya GC in respect of the year ended 31 December 2005	-	-	16,222	0.076311
OJSC Tverskaya GC in respect of the year ended 31 December 2005	-	-	25,540	0.05534
OJSC Yaroslavskaya EC in respect of three months ended 31 March 2006	-	-	90,241	4.1680015
OJSC Kostromskaya GC in respect of three months ended 31 March 2006	-	-	23,241	0.042629
OJSC Novgorodskaya GC in respect of three months ended 31 March 2006	-	-	11,100	0.052216
OJSC Tverskaya GC in respect of three months ended 31 March 2006	-	-	33,703	0.073027
OJSC Vologodskaya HePP in respect of three months ended 31 March 2006	-	-	21,709	1.0675684
OJSC TGC-2 in respect of the year ended 31 December 2006	407	0.000000751		
Total dividends	**407**	-	**358,376**	-

On 22 May 2008 the Annual General Meeting declared dividends for the year ended 31 December 2007 of RR 0.0000073465 per share for the total of RR 8,173 thousand and for the first quarter 2008 of RR 0.0001662926 per share for the total of RR 185,000 thousand. These dividends will be paid during the year 2008 and deduct from equity at 31 December 2008.

Provision for buy out shares. As described in Note 1, on 5 December 2007, the Extraordinary shareholder's meeting of TGC-2 approved the basic structure for the third (final) phase of the Group reorganization. Those shareholders who voted against approval of the reorganization or did not participate in that shareholders meeting had the right to demand that TGC-2 buy back its shares within 45 days of the shareholders meeting date. The re-purchase price was calculated by an independent appraiser and approved by the TGC-2 Board of Directors at the level of RR 0.02067 per ordinary share and RR 0.01736 per preference share.

As at 28 January 2008 TGC-2 Board of Directors approved report on shareholders claims to buy-out its shares, in accordance with which 300,043,370 ordinary and 1,579,684,034 preference shares would be repurchased by TGC-2. The total amount of cash to be paid was RR 33,625 thousand. These shares had to be re-purchased by TGC-2 by 19 February 2008.

As at 31 December 2007 TGC-2 had not repurchased any shares. Based on requirements of IAS 37 "Provisions, contingent liabilities and contingent assets" as at 31 December 2007 TGC-2 accrued a provision for the cost of the shares to be bought back from the shareholders in the amount of RR 33,625 thousand in equity in the line "Provision for buy out shares".

Note 14. Income tax

Income tax charge

	Year ended 31 December 2007	Year ended 31 December 2006
Current income tax charge	(191)	(62,204)
Deferred income tax benefit / (charge)	642,739	(1,292,494)
Income tax benefit / (charge)	**642,548**	**(1,354,698)**

In year ended 31 December 2007 and 2006 the Group companies were subject to a 24% income tax rate on taxable profits.

Reconciliation between the expected and the actual tax charge is provided below:

	Year ended 31 December 2007	Year ended 31 December 2006
Profit before tax	**(2,478,914)**	**4,691,538**
Theoretical tax charge at the statutory tax rate of 24%	594,939	(1,125,969)
Tax effect of items which are not deductible or assessable for taxation purpose	47,609	(228,729)
Total income tax charge	**642,548**	**(1,354,698)**

Deferred tax assets and liabilities

Differences between IFRS and Russian statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets and liabilities are measured at the rate of 24% which is expected to be applied to the period when the assets are realized and liabilities are settled.

In the context of the Group's current structure, tax losses and current tax assets of different consolidated entities may not be offset against current tax liabilities and taxable profits of other consolidated entities and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

As at 31 December 2007, deferred tax assets and liabilities of all branches were offset within TGC-2 as a single entity, resulting in a net liability of RR 3,102,828 thousand.

	31 December 2006	Movement for the year recognized in Income Statement	Movement for the year recognized in Statement of Changes in Equity	31 December 2007
Tax losses	589,208	(168,613)	-	420,595
Trade accounts receivable and prepayments	291,295	(124,203)	-	167,092
Accounts payable and accrued liabilities	37,645	23,419	-	61,064
Pension liabilities	50,121	32,171	-	82,292
Other	5,983	(5,983)	-	-
Deferred tax assets	**974,252**	**(243,209)**	**-**	**731,043**
Property, plant and equipment	(2,384,129)	897,714	(2,322,876)	(3,809,292)
Other	(12,814)	(11,766)	-	(24,580)
Deferred tax liabilities	**(2,396,943)**	**885,948**	**(2,322,876)**	**(3,833,872)**
Net deferred tax liabilities	**(1,422,691)**	**642,739**	**(2,322,876)**	**(3,102,828)**

Note 14. Income tax (continued)

	31 December 2005	Movement for the year recognized in Income Statement	Movement for the year recognized in Statement of Changes in Equity	31 December 2006
Tax losses	103,164	486,044	-	589,208
Trade receivables and prepayments	257,399	33,896	-	291,295
Accounts payable and accrued liabilities	21,613	16,032	-	37,645
Pension liabilities	43,675	6,446	-	50,121
Other	24,635	(18,652)	-	5,983
Deferred tax assets	**450,486**	**523,766**	**-**	**974,252**
Property, plant and equipment	(569,203)	(1,814,926)	-	(2,384,129)
Other	(11,480)	(1,334)	-	(12,814)
Deferred tax liabilities	**(580,683)**	**(1,816,260)**	**-**	**(2,396,943)**
Net deferred tax assets/(liabilities)	**(130,197)**	**(1,292,494)**	**-**	**(1,422,691)**

The Group has not recorded a deferred tax liability in respect of taxable temporary differences associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

Note 15. Pension liabilities

The Group operates defined benefit and defined contribution pension plans. The Group has contract with a pension fund "Non-state pension fund of electrical energy industry" ("NPFE"), which is a separate legal entity; the other plans are operated by the Group without engaging pension funds.

The defined benefit pension plan through NPFE provides for monthly pension benefit paid upon retirement. Annual contributions are made by the Group to the non-state pension fund. The amount of the contribution is defined by TGC-2 budget and is considered to be sufficient at least to finance ongoing pension benefits. No part of this contribution is recognised as plan asset as far as TGC-2 can recall this money back and the plan is considered as unfunded thereat. Contributions to the NPFE are made on 'pay-as-you-go' basis.

Additionally to the NPFE pension plan, the Group provides financial support, of a defined benefit nature, to former employee old-age pensioners, who have completed certain years of service for the Group, and other post-employment benefit such as lump-sum payments upon retirement and lump-sum material aid.

The non-statutory pension plan providing monthly pensions had approximately 8,258 active participants as at 31 December 2007 and 2,435 pensioners receiving financial support from the employer.

The tables below provide information about the benefit obligations, plan assets and actuarial estimations used for the years ended 31 December 2007 and 31 December 2006.

Amounts recognized in the balance sheet:

	31 December 2007	31 December 2006
Defined benefit obligations	688,150	288,821
Unrecognised net actuarial losses	(281,321)	(35,933)
Unrecognised past service cost	(63,944)	(54,620)
Net liability on balance sheet	**342,885**	**198,268**

Amounts recognized in the income statement:

	Year ended 31 December 2007	Year ended 31 December 2006
Current service cost	35,010	11,930
Interest cost	28,127	14,527
Net actuarial loss recognized in year	-	318
Amortisation of past service cost	5,976	-
Immediate recognition of vested prior service cost	116,479	-
Total	**185,592**	**26,775**

Note 15. Pension liabilities (continued)

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

	31 December 2007	31 December 2006
Benefit obligations		
Benefit obligations as at the beginning of the period	288,821	207,535
Current service cost	35,010	11,930
Interest cost	28,127	14,527
Past service cost	131,780	54,620
Benefits paid	(40,975)	(10,484)
Actuarial losses	245,388	10,693
Benefit obligations as at the end of the period	**688,151**	**288,821**

Principal actuarial estimations are as follows:

	31 December 2007	31 December 2006
Discount rate for benefits at accumulation phase	6.75%	6.75%
Future Salary increase	7.0%	7.0%
Future inflation rate	6.0%	5.0%

Note 16. Borrowings

Non-current borrowings

Creditor	Currency	Effective interest rate,%	Rating	31 December 2007	31 December 2006	Rating agency
OJSC Sberbank (due 2007 – 2010)	RR	8,44-8,55	BBB+	670,000	-	Fitch Ratings
Total non-current borrowings				670,000	-	

Current borrowings

Creditor	Currency	Effective interest rate,%	Rating	31 December 2007	Rating	31 December 2006	Rating agency
OJSC Vneshtorgbank	RR	8.3-8.6	BBB+	1,500,000	BBB+	2,216,381	Fitch Ratings
OJSC Alfa-Bank	RR	-	-	-	BB	898,685	S&P
OJSC TransCreditBank	RR	10.5	BB	11,300	BB-	758,101	S&P
OJSC Sberbank *	RR	9.0	BBB+	1,297,600	BBB+	655,927	Fitch Ratings
OJSC Vnesheconombank	RR	9.0	BBB+	1,000,000	-	-	Fitch Ratings
OJSC Nomosbank	RR	10.75	B+	200,000	B+	1,317,500	Fitch Ratings
OJSC Rosbank	RR	9.0	A-	2,000,000	A-	199,507	Fitch Ratings
RAO UES	RR	34.00	-	-	-	28,130	-
Total current borrowings				**6,008,900**		**6,074,231**	

* - inventory pledged as collateral under loan agreements (see Note 10).

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

Note 17. Accounts payable and accrued liabilities

	Currency	31 December 2007	31 December 2006
Trade payables	RR	1,454,638	1,005,609
Total financial liabilities		**1,454,638**	**1,005,609**
Payables to employees	RR	329,861	199,158
Advances from the buyers	RR	270,244	170,648
Payables to the capital construction contractors	RR	181,812	208,547
Accrued liabilities and other payables	RR	66,292	175,248
Dividends	RR	15,325	20,558
Total		**2,318,172**	**1,779,768**

Trade payables are classified as financial liabilities. Total amount of financial liabilities as at 31 December 2007 comprises RR 8,133,538 thousand (as at 31 December 2006: RR 7,079,840 thousand) and includes, beside trade payables, non-current borrowing (Note 16) and current borrowings (Note 16).

Management believes that the majority of suppliers, balances of which are included into trade payables, comprise the single class, as they bear the same characteristics. Those suppliers are mainly providers of repair and maintenance services.

Note 18. Taxes other than income tax

	31 December 2007	31 December 2006
Value added tax	117,663	244,499
Property tax	50,025	52,817
Unified social tax	101,637	46,740
Water tax	19,266	25,565
Other taxes	51,445	26,127
Total	**340,036**	**395,748**

The value added tax amount represent deferred VAT, which only becomes payable to the authorities when the underlying receivable balances are either recovered or written off.

Note 19. Revenues

Revenues	**Year ended 31 December 2007**	**Year ended 31 December 2006**
Electricity	9,927,520	6,129,317
Heating	9,879,178	8,205,855
Heat transportation	387,658	239,484
Water circulation	256,768	231,143
Electricity grids connection fee	95,828	25,025
Rent	23,528	15,235
Other	224,311	159,006
Total revenues	**20,794,791**	**15,005,066**

Approximately 3 % of sales of electricity for the year ended 31 December 2007 relates to resale of purchased power on wholesale market NOREM (for the year ended 31 December 2006 – 1%).

Note 20. Operating expenses

	Year ended 31 December 2007	Year ended 31 December 2006
Fuel expenses	11,244,389	10,639,728
Depreciation	3,184,956	735,414
Employee benefits	2,787,395	2,061,269
Repair & maintenance costs	1,130,922	643,278
Purchased power	472,713	375,357
Raw materials	401,506	535,999
Gas transportation expenses	388,608	178,573
Water usage expenses	279,959	170,281
Taxes other than income tax	225,541	377,127
Rent expenses	205,298	156,031
Effect on discounting of non-current accounts receivable	150,236	284,617
Transportation services	141,667	146,795
Security services	135,554	71,174
Subscription fee RAO UES	122,735	84,000
Costs of heat & electricity's transfer	98,999	134,981
Consulting, legal and audit services	75,551	40,257
Pollution fee	75,235	126,925
Insurance cost	68,724	58,362
Write off accounts receivable	17,363	8,628
Bank and agent services	34,603	13,779
Communication services	25,376	7,003
Effect on discounting of loans issued to employees	-	9,606
(Reversal) / charge of provision for impairment of trade and other receivables	(584,782)	303,607
Other expenses	732,783	606,907
Total operating expenses	**21,415,331**	**17,769,698**

Note 21. Other operating income

	Year ended 31 December 2007	Year ended 31 December 2006
Gain on discounting of non-current accounts receivable	45,256	54,905
Gain on discounting of loans issued to employees	2,863	-
Loss / gain on disposal of subsidiaries	(5,330)	145,327
Other income	191,358	121,512
Total other operating income	**234,147**	**321,744**

Note 22. Finance income and costs

Finance costs

	Year ended 31 December 2007	Year ended 31 December 2006
Interest expense	493,239	430,037
Interest cost for pension obligation (see Note 15)	28,127	10,400
Interest expense (leasing)	4,264	6,338
Total finance costs	**525,630**	**446,775**

All finance costs relate to financial liabilities measured at amortised cost.

Note 23. Disposal of subsidiaries

In April 2007 the Group has sold 100% share of its non-core subsidiary OJSC "Novgorodenergoservis" for RR 34,733 thousands. Loss on the disposal was RR 5,330 thousands and was included in "Other operating income". Net assets of OJSC " Novgorodenergoservis" at the date of sale were the following:

	OJSC "Novgorodenergoservice" net assets
Current assets	7,637
Property, plant and equipment	33,425
Other non-current assets	937
Current liabilities	(1,588)
Non-current liabilities	(348)
Net assets	**40,063**
% of ownership	100%
The Group's share in net assets disposed of	40,063
Consideration received, paid in cash	34,733
Loss on disposal of subsidiaries	**(5,330)**

Note 24. Earnings per share

	Year ended 31 December 2007	Year ended 31 December 2006
Weighted average number of ordinary shares issued (thousand)	973,745,892	355,631,722
Weighted average number of preference shares issued (thousand)	3,392,219	5,770,059
Weighted average number of ordinary and preference shares outstanding (thousand)	977,138,111	361,401,782
Profit / (loss) attributable to the shareholders of TGC-2	(1,658,044)	2,952,399
Weighted average earnings per ordinary and preference share – basic and diluted (in RR)	(0.002)	0.008

Note 25. Commitments

Sales commitments. The Group entities sell electricity (capacity) on the two wholesale market sectors: free trading sector and regulated trading sector. The tariffs for the electricity sold/purchased in the regulated trading sector (including the sector of deviations) are set by the Federal Service on Tariffs.
The Group has entered into a number of annual electricity sales agreements with OJSC "Center for Financial Settlements", retail companies and large industrial customers.

Fuel commitments. The following long-term contracts on delivery of gas for the needs of production were concluded by the Group:

- for the Novgorod branch - for delivery of the «limited» gas for a term of 5 years (2008-2012) with the regional gas company of OJSC «Gazprom» - LLC «Novgorodregiongas», price is to be fixed each year by separate agreement;
- for the Yaroslavl branch - for delivery of the «limited» gas for a term of 5 years (2008-2012) with the regional gas company of OJSC «Gazprom» - LLC «Yaroslavskay regionalnay kompaniy po realizacii gaza», price is to be fixed each year by separate agreement;
- for the Tver branch - for delivery of the «limited» gas for a term of 5 years (2008-2012) with the regional gas company of OJSC «Gazprom» - LLC «Tverregiongas»», price is to be fixed each year by separate agreement;
- for the Kostroma branch - for delivery of the «limited» gas for a term of 5 years (2008-2012) with the regional gas company of OJSC «Gazprom» - LLC «Kostromaregiongas»», price is to be fixed each year by separate agreement;

Note 25. Commitments (continued)

- for the Vologda branch - for delivery of the «limited» gas for a term of 5 years (2008-2012) with the regional gas company of OJSC «Gazprom» - LLC «Vologodskay regionalnay kompaniy po realizacii gaza»», price is to be fixed each year by separate agreement;

The Group concluded the long-term contracts (2008 - 2015) for delivery of coal with OJSC "Kuzbasskaya toplivnaya kompaniya" and OJSC "UK "Kuzbassrazrezugol" for delivery approximately tonne 5,200 thousand per year, price is to be fixed each year by separate agreement;

Capital commitments. Future capital expenditure for which contracts have been signed amounted to RR 1,501,823 thousand at 31 December 2007 (at 31 December 2006: nil).

Note 26. Contingencies

Political environment. The operations and earnings of the 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 Russia.

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

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

Tax contingency. Russian tax, currency and customs legislation is subject to varying interpretation, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities in particular the existing way of calculation of water tax, settlement via agents. 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 preceding the year of review. Under certain circumstances review may cover longer periods.

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

As at 31 December 2007 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.

In addition, tax and other legislation do not address specifically all the aspects of the Group's reorganization 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 reorganization and reform process.

Environmental matters. The Group entities and their predecessor entities have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. 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.

Note 27. Financial instruments and financial risk factors

Financial risk factors. The Group activities expose it to a variety of financial risks, including the effects of, changes in interest rates, and the collectibility of receivables. The Group does not have a risk policy to hedge its financial exposures.
Power and heat produced by the Group is sold on the internal market of Russian Federation with prices fixed in the currency of Russian Federation. Hence, the Group is not significant exposed foreign currency exchange risk. The financial condition of the Group, 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 assets and liabilities be denominated in the national currency. Moreover, the Group does not plan to perform activities on the international market.

Credit risk. Credit risk – is the risk of financial loss for the Group in the case of non-fulfilment of obligations of Counterparty to a financial instruments under the proper contract. Financial assets on which the Group has the significant credit risk are represented by the accounts receivable of buyers and customers (in amount of RR 2,571,894 thousand), long-term loans issued (in amount of RR 16,821 thousand) and cash (in amount of RR 436,068 thousand), totalling RR 3,024,763 thousand. Although collection of receivables may be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the receivables already provided for as impaired.

Cash has been deposited in the financial institutions with no more than minimal exposure to default risk at the time of account opening. The Group constantly evaluates the financial condition, ratings assigned by independent agencies, background and other factors.
The table in Note 12 presents the overnight deposits with a major bank Counterparty and the rating of that bank at the balance sheet date.

Despite the fact that certain companies and banks do not have the international credit rating, they are considered as reliable counterparties that have stable positions in the financial market of the Russian Federation and meet the commonly used criteria of credit status and solvency.

Liquidity risk. Prudent liquidity risk management includes maintaining sufficient cash and the availability of funding from an adequate amount of committed credit facilities.

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. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
At 31 December 2007				
Borrowings	6,008,900	-	803,530	-
Accounts payable and accrued charges	2,318,172	-	-	-
At 31 December 2006				
Borrowings	6,074,231	-	-	-
Accounts payable and accrued charges	1,779,768	-	-	-

Interest rate risk. The Group's operating profits and cash flows from operating activity are largely not dependent on the changes in market interest rates. The majority of interest rates on current and non-current borrowings are fixed, these are disclosed in Note 16.

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

- Share capital can not be lower than 1,000 minimum salaries on the date of 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 2007, the Group has been 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 others in the industry, the Group monitors capital on the basis of the gearing ratio and financial leverage ratio calculated based on Russian Accounting Standards financial statements.

During the year ended 31 December 2007, the Group's strategy, which was unchanged from 2006, was to maintain a leverage ratio exceeding 40% and capitalization rate less than 1.5. The gearing ratios and capitalization rate at 31 December 2007 and at 31 December 2006 were as follows:

	31 December 2007	31 December 2006
Leverage ratio (based on RAR figures)	57%	52%
Capitalization rate (based on RAR figures)	0.74	0.95

Reconciliation of Classes of Financial Instruments with Measurement Categories. For the purposes of measurement, IAS 39, Financial Instruments: Recognition and Measurement, classifies financial assets into the following categories: (a) loans and receivables; (b) available-for-sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value through profit or loss ("FVTPL").

As of 31 December 2007 the Group has the loan and receivables class of financial assets only.

Fair values. Management believes that the fair values of its financial assets and liabilities approximates their carrying amount. 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 Group's deposits in banks are short-term and their carrying amount approximates fair value.

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

Note 28. Subsequent events

Sale of TGC-2 shares by Parent**.** On 14 March 2008 RAO UES of Russia announced the results of the open auction held for the sale of its 33.42% shareholding in TGC-2 (percentage is given without taking into account additional share issue placed by the Group). LLC "Kores Invest" has been declared the winner of the auction.

Additional share issue. On 7 May 2008 the Group has announced results of additional share placement and submitted official notification to the Federal Service for Financial Markets. Shares have been placed through public offering. The Group has placed 360,000,000,000 ordinary shares with nominal value of RR 0.01 per share and total value RR 3,600,000 thousand. Shares have been placed by RR 0.025 per share, total amount of cash received is RR 9,000,000 thousand.

Lost of control by Parent. As a result of disposal of shares held in TGC-2 and additional the share issue held by the Group, on 9 June 2008 RAO UES of Russia lost control over TGC-2 and LLC "Kores Invest" acquired ownership of more than 43% of the Group.

Merger with TGC-2 Holding. On 1 July 2008 OJSC TGC-2 Holding has merged with the Group. (See Note 13).