OJSC VOLGA TGC

CONSOLIDATED FINANCIAL STATEMENTS,

PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) FOR THE YEAR ENDED 31 DECEMBER 2007

ZAO KPMG
Naberezhnaya Tower Complex, Block C
18 Krasnopresnenskaya Naberezhnaya
Moscow 123317
Russia

Telephone +7 (495) 937 4477
Fax +7 (495) 937 4400/99
Internet www.kpmg.ru

Independent Auditors' Report

To the board of directors of OJSC Volga TGC

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of OJSC Volga TGC (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as of 31 December 2007, and the consolidated statement of income, consolidated statement of changes in shareholders' equity 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 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 misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of 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 principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Basis for Qualified Opinion

We did not observe the counting of inventories stated at RR 1,377,944 as at 1 January 2006 because we were engaged as auditors of the Group only after that date. It was impracticable to satisfy ourselves as to those inventory quantities by other audit procedures. Accordingly, we were unable to determine whether any adjustments might be necessary to cost of sales, taxation expense and net profit for the year ended 31 December 2006.

Qualified Opinion

In our opinion, except for the effects on the corresponding figures of such adjustments, if any, that might have been determined to be necessary had it been practicable to obtain sufficient appropriate audit evidence as described in the Basis for Qualified Opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2007, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO KPMG

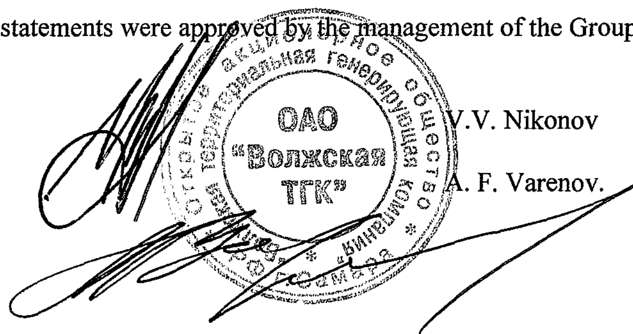
ZAO KPMG
15 April 2008

ZAO KPMG, a company incorporated under the Laws of the Russian Federation and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative.

OJSC Volga TGC
Consolidated Balance Sheet as at 31 December 2007
(in thousands of Russian rubles unless otherwise noted)

	Notes	31 December 2007	31 December 2006
ASSETS			
Non-current assets			
Property, plant and equipment	8	35,224,214	35,012,992
Intangible assets	9	928,361	560,566
Other non-current assets	10	439,587	572,562
Available-for-sale financial assets	11	138,360	365,616
Total non-current assets		**36,730,522**	**36,511,736**
Current assets			
Cash	12	803,251	967,196
Advances to suppliers and prepayments		1,616,743	709,705
Accounts receivable	13	2,794,841	1,807,038
Income tax receivable		9,227	90,812
Value added tax recoverable		204,121	294,935
Available-for-sale financial assets	11	305,131	75,878
Inventories	14	2,663,633	2,693,645
Total current assets		**8,396,947**	**6,639,209**
TOTAL ASSETS		**45,127,469**	**43,150,945**
EQUITY AND LIABILITIES			
Equity			
Ordinary shares (nominal value RR 26,116,076 thousand)	15	26,116,076	26,116,076
Additional paid in capital	15	1,587,056	1,587,056
Retained earnings and other reserves		3,113,339	2,638,999
Total equity		**30,816,471**	**30,342,131**
Non-current liabilities			
Deferred tax liabilities	24	4,758,046	4,910,234
Loans and finance lease liabilities	16	1,000,000	514
Promissory notes	17	119,657	220,780
Employee benefits	18	1,460,364	1,284,650
Other non-current liabilities		4,998	12
Total non-current liabilities		**7,343,065**	**6,416,190**
Current liabilities			
Loans and finance lease liabilities	16	4,111,885	2,885,052
Accounts payable and accrued charges	19	1,973,242	1,977,102
Income tax payable		214,405	177,776
Promissory notes	17	123,669	128,808
Other taxes payable	20	544,732	1,223,886
Total current liabilities		**6,967,933**	**6,392,624**
Total liabilities		**14,310,998**	**12,808,814**
TOTAL EQUITY AND LIABILITIES		**45,127,469**	**43,150,945**

These consolidated financial statements were approved by the management of the Group on 15 April 2008 and were signed on its behalf by:



General Director V.V. Nikonov

Chief Accountant A. F. Varenov.

The accompanying notes on pages 7 to 33 are an integral part of these consolidated financial statements.

	Note	Year ended 31 December 2007	Year ended 31 December 2006
Revenues	21	40,001,388	34,300,600
Operating expenses	22	(38,591,181)	(33,998,401)
Operating profit		**1,410,207**	**302,199**
Other income		(7,864)	122,915
Net finance expense	23	(255,313)	(100,178)
Profit before income tax		**1,147,030**	**324,936**
Income tax expense	24	(616,969)	(180,709)
Net profit for the year		**530,061**	**144,227**
Basic earnings per ordinary share in Russian rubles	25	0,0203	0.0055

The accompanying notes on pages 7 to 33 are an integral part of these consolidated financial statements.

	Year ended 31 December 2007	Year ended 31 December 2006
CASH FLOW FROM OPERATING ACTIVITIES		
Profit before income tax	**1,147,030**	**324,936**
Adjustments for:		
Depreciation	2,576,918	2,475,095
Amortisation of intangible assets	70,181	37,151
Loss on disposal of property, plant and equipment	78,487	960
Increase in liability for defined benefit plans	175,714	183,538
Net finance expense	255,313	100,178
Provision for impairment of accounts receivable	22,591	(148,332)
Reserve for inventory obsolescence	(1,596)	38,431
Gain on sale of non-current assets held for sale	-	(15,048)
Operating cash flows before changes in working capital and profit tax paid	**4,324,638**	**2,996,909**
Increase in trade and other receivables	(1,656,791)	(1,266,784)
Decrease/(increase) in inventories	31,608	(1,354,132)
Increase in other current assets	(41,123)	(76,079)
(Decrease)/increase in trade and other payables	(648,787)	982,220
Interest paid	(299,092)	(109,329)
Income tax paid	(643,364)	(710,385)
Net cash from operating activities	**1,067,089**	**462,420**
CASH FLOW FROM INVESTING ACTIVITIES		
Acquisition of property, plant and equipment	(2,928,686)	(1,876,026)
Acquisition of intangible assets and other non-current assets	(363,284)	(503,629)
Proceeds from sale of property, plant and equipment	62,057	5,852
Interest received	3,967	11,118
Acquisition of available-for-sale financial assets	(73,747)	(589,284)
Repayment of available-for-sale financial assets	100,510	658,528
Loans issued	(27,700)	-
Proceeds from sale of non-current assets held for sale	-	261,000
Net cash used in investing activities	**(3,226,883)**	**(2,032,441)**
CASH FLOW FROM FINANCING ACTIVITIES		
Proceeds from borrowings	15,053,662	5,965,877
Repayment of borrowings	(12,968,825)	(3,742,237)
Payment of finance lease liabilities	(4,034)	8,678
Dividends paid	(84,954)	(35,903)
Net cash from financing activities	**1,995,849**	**2,196,415**
(Decrease)/Increase in cash and cash equivalents	**(163,945)**	**626,394**
Cash at the beginning of the period	**967,196**	**340,802**
Cash at the end of the period	**803,251**	**967,196**

	Share capital	Additional paid in capital	Available-for-sale financial assets revaluation reserve	Retained earnings	Total equity
Balance as at 1 January 2006	**26,116,076**	**1,587,056**	**(98,600)**	**2,590,473**	**30,195,005**
Changes in fair value of available-for-sale financial assets	**-**	**-**	38,802	-	**38,802**
Net profit recognized directly in equity	**-**	**-**	38,802	-	**38,802**
Profit for the year	-	-	-	144,227	**144,227**
Total recognized income for the year	-	-	38,802	144,227	**183,029**
Dividends	-	-	-	(35,903)	**(35,903)**
Balance as at 31 December 2006	**26,116,076**	**1,587,056**	**(59,798)**	**2,698,797**	**30,342,131**
Balance as at 1 January 2007	**26,116,076**	**1,587,056**	**(59,798)**	**2,698,797**	**30,342,131**
Changes in fair value of available-for-sale financial assets	-	-	29,233	-	**29,233**
Net profit recognized directly in equity	-	-	29,233	-	**29,233**
Profit for the year	-	-	-	530,061	**530,061**
Total recognized income for the year	-	-	29,233	530,061	**559,294**
Dividends	-	-	-	(84,954)	**(84,954)**
Balance as at 31 December 2007	**26,116,076**	**1,587,056**	**(30,565)**	**3,143,904**	**30,816,471**

Note 1. The Group and its operations

Open Joint Stock Company Volga Territorial Generating Company, (OJSC Volga TGC, or the "Company"), was established on August 1, 2005, within the framework of Russian electricity sector restructuring in accordance with the Resolution of General Shareholders Meetings by OJSC Samaraenergo, OJSC Saratovenergo and OJSC Ulyanovskenergo, the companies ultimately controlled by RAO UES of Russia.

On 1 April 2006 in accordance with the Resolution of General Shareholders Meetings on reorganization in the form of regional generation companies spin-off the following legal entities were spun off from OJSC Samaraenergo, OJSC Saratovenergo and OJSC Ulyanovskenergo: OJSC Samara Territorial Generating Company, OJSC Saratov Territorial Generating Company and OJSC Ulyanovsk Territorial Generating Company, which became the shareholders of the Company.

On 3 July 2007 the final stage of the Company's formation was completed by merging OJSC Samara Territorial Generating Company, OJSC Saratov Territorial Generating Company and OJSC Ulyanovsk Territorial Generating Company into the Company. Their respective shares were transferred to RAO UES of Russia, who became the direct controlling shareholder of the Company.

The Group Volga TGC (the "Group") comprises 17 thermoelectric power stations, 5 heat networks and 2 regional state power stations. The Group consists of OJSC Volga TGC and 3 subsidiaries. The Group's major subsidiary is Open Joint Stock Company Orenburg Heat Generating Company (hereinafter Orenburg TGC).

The Group's principle activity is electricity and heat generation.

The Company's registered office is 15, Mayakovskogo str., 443100, Samara, Russia.

Russian business environment

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

Relations with the state and regulation of the Group

As at 31 December 2007 the following shareholders owned OJSC Volga TGC: RAO UES of Russia (54%), CJSC Deposit-clearing company (33%), other minority shareholders (13%). RAO UES of Russia ("the Parent") is the controlling shareholder of the Group. As at 31 December 2007 the Government of the Russian Federation owned 52.7% of RAO UES of Russia.

Among the consumers of electricity and heat power of the Group are key entities controlled by, or related to, the state. Furthermore, the state controls a number of the Group's fuel and other suppliers (see Note 27).

The government of the Russian Federation directly affects the Group's operations through regulation by the Federal Service on Tariffs ("FST"), with respect to its wholesale energy sales, and by the regional services on tariffs ("RSTs"), with respect to its retail electricity and heat sales. The operations of all generating facilities are coordinated by JSC System Operator – Central Despatch Unit of Unified Energy System ("SO-CDU") in order to meet system requirements in an efficient manner. SO-CDU is controlled by RAO UES of Russia.

Tariffs which Group may charge for sales of electricity and heat are governed both by regulations specific to the electricity and heat industry and by regulations applicable to natural monopolies. As a condition to privatization in 1992, the government of the Russian Federation imposed an obligation on RAO UES entities to provide connection for the supply of electricity and heating to customers in the Russian Federation.

Note 1. The Group and its operations (continued)

Sector restructuring

The Russian electric utilities industry in general and the Group in particular are presently undergoing a reform process designed to introduce competition into the electricity sector and to create an environment in which the Group can raise the capital required to maintain and expand current capacity.

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

From 2007 volumes of electricity (power) traded in the wholesale market at regulated prices began to reduce. The pace of reduction is set by the Russian Federation Government according to socio-economic development forecasts. In 2007 about 92% of the forecasted production volumes was traded at regulated prices. In 2013 it will become possible to launch a fully competitive whole sale market.

As at 29 May 2003, the Board of Directors of RAO UES approved a "Concept of RAO UES strategy for the period from 2003 through 2008" (further- the "Concept of RAO UES Strategy"). In February 2006 the Board of Directors approved Appendixes to the Concept of RAO UES Strategy: "Territorial generating companies ("TGCs") being created on the basis of assets of the Holding Group RAO UES" and "Generating companies of the Wholesale Electricity Market ("WGCs")". These documents provide a detailed description of the major changes that are planned to take place during the electric utilities reform program.

Management believes that as an ultimate result, a stable regulatory regime and a competitive power market will be established, which will allow Group to raise funds for developing its business. However, there can be no complete assurance in this regard.

Restructuring of the Group

Upon the formation of the Company, as described above, in August 2005, the founders transferred the ownership of their heat and electricity generating assets as the initial contribution to the Company’s share capital. These assets were subsequently leased back to the original owners until the Company’s own generating activities commenced on 1 January 2006.

In April 2007, the Parent transferred 100% of the shares of Orenburg TGC to the Company in exchange for additional shares issued by the Company as part of the overall restructuring of the Group (see Note 15).

All assets and activities contributed to the group as part of the restructuring are transferred from entities under common control of RAO UES of Russia.

In accordance with the Group’s accounting policy, these consolidated financial statements are presented as if the restructuring described above had been completed prior to 2006.

Note 2. Financial conditions

As discussed above the Group is affected by the Government through control of tariffs and other factors. The FST and RSTs do not always permit tariff increases in line with increases in the Group's costs and thus some tariffs are insufficient to cover all the costs of generation and distribution. Moreover, these tariffs consider costs only on the Russian statutory basis and, accordingly, exclude additional costs recognized under the International Financial Reporting Standards ("IFRS"). As a result, tariffs may not consistently allow for an adequate return on investment and may not provide sufficient funds for the full replacement of property, plant and equipment. However, in 2006 and in 2007, the growing demand for electricity and capacity together with increasing free trading sector of the wholesale electricity market have resulted in a higher rate of revenue growth (see Sector restructuring in Note 1).

Note 2. Financial conditions (continued)

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

- introduction of improved financial budgeting procedures;
- force concentration on timely cash collection of current and expired accounts receivable;
- negotiations with strategic investors, identification and assessment of projects requiring financial investments;
- negotiations with federal and regional governments and regulators concerning the increases in tariffs to support adequate long term investment into the Group's generation assets;

Note 3. Basic approaches for financial statements preparation

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standard ("IFRS").

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that financial investments classified as available-for-sale are stated at fair value; and property, plant and equipment were revalued to determine deemed cost as part of the adoption of IFRSs.

Functional and presentation currency

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

Use of judgments, estimates and assumptions

Management has made a number of judgments, estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with IFRSs. Actual results may differ from those estimates. Judgments and estimates that have the most significant effect on the amounts recognised in the financial statements include:

Impairment provision for accounts receivable

Management has determined the provision for impairment of receivables based on specific customer identification, payment trends and subsequent receipts in order to estimate the fair value of future cash collections. Management believes that the Group 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 (see Note 26).

Property, plant and equipment

Fair value of property, plant and equipment as at 1 January 2005 has been determined by an independent appraiser based on the depreciated replacement cost method as well as estimated income. As described in Note 8 the determination of fair value is based on management assessment of future growth in sales and production. Further, management assesses the useful lives of property, plant and equipment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Carrying value and depreciation of property, plant and equipment are significantly affected by the above estimates, and actual results may differ from those estimates. Any changes to these estimates may have significantly impact on these consolidated financial statements.

Note 4. Summary of significant accounting policies

The significant accounting policies followed by the Group are set out below. Except for certain reclassifications made to prior year balances to conform to the current year presentation, the Group consistently applied accounting policies.

4.1 Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

Transactions among entities under common control

Transfers of interests in entities that are under the control of the shareholder that controls the Company are accounted for as if the transfer had occurred at the beginning of the earliest comparative period presented. For this purpose the assets and liabilities are recognized at their carrying amounts and comparatives are restated. The entities constituting the restructured Group do not prepare individual financial statements under IFRSs. The Group adopted IFRS as of 1 January 2005. As a result, property, plant and equipment were revalued as of that date to determine deemed cost as part of the adoption of IFRSs. Any difference between the carrying amount of transferred net assets and cost of investment is accounted for as an adjustment to equity.

Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Associates are accounted for using the equity method. The consolidated financial statements include the Group’s share of the income and expenses of associates, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group’s share of losses exceeds its interest in an associate, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee.

Transactions eliminated on consolidation

Intra-group balances, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group’s interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

4.2 Foreign currency

Transactions in foreign currencies are translated to Russian rubles at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to Russian rubles at the exchange rate at that date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated to Russian rubles at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments.

Note 4. Summary of significant accounting policies (continued)

4.3 Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity, promissory notes, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs, except as described below. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

Cash comprises cash in hand and cash deposited on demand at banks. Cash equivalents comprise short-term high 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.

Held-to-maturity investments

If the Group has the positive intent and ability to hold investment in financial assets to maturity, then they are classified as held-to-maturity. Held-to-maturity investments are measured at amortised cost using the effective interest method, less any impairment losses.

Available-for-sale financial assets

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

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

Investments at fair value through profit or loss

An instrument is classified as at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value. Upon initial recognition, attributable transaction costs are recognised in profit or loss when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

Other

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses. Investments in equity securities that are not quoted on a stock exchange and where fair value cannot be estimated on a reasonable basis by other means are stated at cost less impairment losses.

Note 4. Summary of significant accounting policies (continued)

4.4 Property, plant and equipment

Recognition and measurement

Items of property, plant and equipment, except for land, are measured at cost less accumulated depreciation and impairment losses. The cost of property, plant and equipment at 1 January 2005, the date of transition to IFRSs, was determined by reference to its fair value at that date ("deemed cost").

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. For the property, plant and equipment which were subject to the independent appraiser as at 1 January 2005, the applied depreciation rate is based on the estimated remaining useful lives as at the valuation date. The useful lives, in years, of property, plant and equipment by type of facility are present as follows:

Type of property, plant and equipment	Useful lives (in years)
Electricity and heat generation	10-30
Heating networks	7-10
Other	3-30

4.5 Intangible assets

Research and development

Expenditure on research activities, undertaken with the prospect of gaining new technical knowledge and understanding, is recognized in profit or loss when incurred.

Development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalized only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Group intends to and has sufficient resources to complete development and to use or sell the asset. The expenditure capitalized includes the cost of materials, direct labour and overhead costs that are directly attributable to preparing the asset for its intended use. Other development expenditure is recognized in profit or loss when incurred.

Capitalized development expenditure is measured at cost less accumulated amortization and accumulated impairment losses.

Other intangible assets

Other intangible assets that are acquired by the Group, which have finite useful lives, are measured at cost less accumulated amortization and accumulated impairment losses.

Note 4. Summary of significant accounting policies (continued)

4.5 Intangible assets (continued)

Subsequent expenditure

Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognized in profit or loss when incurred.

Amortization

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The estimated useful lives for the current and comparative periods are as follows:

Type of intangible assets	Useful lives (in years)
Computer software	3-10
Licenses	2-5
Capitalised development costs	1-5

4.6 Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised on the Group’s balance sheet.

4.7 Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories includes all actual acquisition costs and other costs incurred to bring inventories to their existing condition and location. The cost of inventories does not include the cost of borrowings obtained to acquire such inventories. The cost of fuel is determined using the weighted average cost method. The cost of other inventories is determined using the actual cost method.

Net realizable value is the estimated selling price in the ordinary course of business, less selling expenses.

4.8 Impairment

Financial assets

A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial asset is calculated by reference to its current fair value.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in profit or loss. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

Note 4. Summary of significant accounting policies (continued)

4.8 Impairment (continued)

Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

4.9 Employee benefits

Defined contribution plans

In the normal course of business the Group contributes all obligatory payments to the Russian Federation state pension fund on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred and recognized in the Income statement as employee benefit expenses and payroll taxes.

Defined benefit plans and other long-term employee benefits

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and any unrecognised past service costs and the fair value of any plan assets are deducted. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method. When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised in profit or loss on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in profit or loss.

The Group's net obligation in respect of long-term employee benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any related assets is deducted. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed using the projected unit credit method.

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

Note 4. Summary of significant accounting policies (continued)

4.10 Environmental liabilities

Liabilities for environmental remediation are recorded in accounting in the presence of such obligations, when the payment is probable and reliable estimates exist.

4.11 Non-current assets classified as held for sale

Non-current assets or disposal groups are classified in the balance sheet as held for sale when their carrying amount will be recovered principally through a sale transaction and not through their use.

Assets (disposal groups) are classified as held for sale when they can be sold in their present condition and on the terms that are typical for such assets and such sale in itself needs to be highly probable.

Sale can be characterized as highly probable when the management has a firm intention to dispose of the asset, actively searches for potential buyers, has a plan of the asset disposal and works on its execution. An asset becomes a marketable asset for sale at a price comparable to its fair value.

Held for sale assets are measured at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group first is allocated to goodwill, and then to remaining assets on pro rata basis, except that no loss is allocated to inventories, financial assets, deferred tax assets, employee benefit assets, which continue to be measured in accordance with the Group's accounting policy. Impairment losses on initial classification as held for sale and subsequent gains and losses on remeasurement are recognized in the consolidated statement of income. Gains are not recognized in excess of any cumulative impairment loss. Held for sale assets (or disposal groups) are not depreciated or amortised.

4.12 Revenue

Revenue is recognized when the significant risks and rewards of ownership have been transferred to the buyer of electricity and heat or non-utility goods and services.

Revenue is measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, the revenue is measured at the fair value of the goods or services sold/provided. Revenue is stated net of value added tax.

4.13 Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent lease payments are accounted for by revising the minimum lease payments over the remaining term of the lease when the lease adjustment is confirmed.

4.14 Social expenditure

To the extent that the Group's contributions to social programs benefit the community at large and are not restricted to the Group's employees, they are recognized in profit or loss as incurred.

4.15 Finance income and expense

Finance income comprises interest income on funds invested, gains on the disposal of available-for-sale financial assets and foreign currency gains. Interest income is recognised as it accrues, using the effective interest method.

Finance expenses comprise interest expense on borrowings, losses on the disposal of available-for-sale financial assets and foreign currency losses. All borrowing costs are recognised in profit or loss using the effective interest method.

Note 4. Summary of significant accounting policies (continued)

4.16 Income tax expense

Income tax expense comprises current and deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

4.17 Dividends

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

4.18 Earnings per share

Basic earnings per share is determined by dividing the profit attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares in circulation during the reporting period, less the average number of treasury shares held by the Group. The Company has not issued any dilutive instruments.

4.19 Treasury shares

Treasury shares are stated at weighted average cost. The gains or losses arising on the disposal of treasury shares are recorded directly in equity.

4.20 New accounting developments

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2007, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the Group's operations. The Group plans to adopt this pronouncement when it becomes effective.

- IAS 23 *Borrowing costs*. The amendment requires capitalization of borrowing costs directly attributable to qualifying assets and is applicable for annual periods beginning on or after 1 January 2009.

Management believes that this interpretation will not have significant impact on the Group's operations.

Note 5. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and / or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Note 5. Determination of fair values (continued)

Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

Available-for-sale financial assets

Available-for-sale investments principally comprise non-marketable securities, which are not publicly traded or listed on a stock exchange. For these investments, fair value is estimated by reference to a variety of methods including those based on their earnings and those using the discounted value of estimated future cash flows. In assessing the fair value, management makes assumptions that are based on market conditions existing at each balance sheet date.

Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. For finance leases the market rate of interest is determined by reference to similar lease agreements.

Note 6. Financial risk management

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investments.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables based on a specific loss that relates to individually significant exposures.

Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded (see Note 13).

Cash and bank deposits are placed in financial institutions, which are considered to have minimal risk of default.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Typically the Group ensures that it has sufficient cash on demand to meet expected operational expenses, including servicing of financial obligations; this excludes the potential impact of extreme circumstances that can not reasonably be predicted, such as natural disasters.

Note 6. Financial risk management (continued)

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

The Group does not apply hedge accounting in order to manage volatility in profit or loss.

Foreign exchange risk

The Group primarily operates on the territory of the Russian Federation. The majority of the Group's purchases are denominated in Russian rubles. The Group doesn't have cash balances, accounts receivable or bank loans denominated in foreign currency.

Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity. Interest rates are disclosed in Note 16.

Capital management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board of Directors monitors the return on capital, which the Group defines as operating profit for the period divided by total equity. The Board of Directors also monitors the level of dividends to shareholders.

The Board seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position.

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

Note 7. Segment reporting

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

Note 8. Property, plant and equipment

	Electricity and heat generation	Heating networks	Construction-in-progress, including advances	Other	Total
Cost/Deemed cost					
Balance at 1 January 2007	31,078,672	7,009,959	982,218	672,352	39,743,201
Additions	32,065	8,917	2,754,516	132,813	2,928,311
Transfers	1,428,372	599,589	(2,044,948)	16,987	-
Disposals	(117,542)	(14,880)	(17,937)	(49,058)	(199,417)
Balance at 31 December 2007	32,421,567	7,603,585	1,673,849	773,094	42,472,095
Depreciation					
Balance at 1 January 2007	(3,188,044)	(1,371,404)	-	(170,761)	(4,730,209)
Depreciation for the period	(1,708,539)	(745,626)	-	(122,753)	(2,576,918)
Disposals	28,040	1,808	-	29,398	59,246
Balance at 31 December 2007	(4,868,543)	(2,115,222)	-	(264,116)	(7,247,881)
Carrying amounts					
At 1 January 2007	27,890,628	5,638,555	982,218	501,591	35,012,992
At 31 December 2007	27,553,024	5,488,363	1,673,849	508,978	35,224,214

	Electricity and heat generation	Heating networks	Construction-in-progress, including advances	Other	Total
Cost/Deemed cost					
Balance at 1 January 2006	29,647,303	6,583,210	1,068,524	512,716	37,811,753
Additions	505,590	116,386	1,170,533	164,937	1,957,446
Transfers	937,908	310,363	(1,251,952)	3,681	-
Disposals	(12,129)		(4,887)	(8,982)	(25,998)
Balance at 31 December 2006	31,078,672	7,009,959	982,218	672,352	39,743,201
Depreciation					
Balance at 1 January 2006	(1,507,167)	(660,047)		(94,470)	(2,261,684)
Depreciation for the period	(1,683,992)	(711,357)		(79,746)	(2,475,095)
Disposals	3,115	-	-	3,455	6,570
Balance at 31 December 2006	(3,188,044)	(1,371,404)		(170,761)	(4,730,209)
Carrying amounts					
At 1 January 2006	28,140,136	5,923,163	1,068,524	418,246	35,550,069
At 31 December 2006	27,890,628	5,638,555	982,218	501,591	35,012,992

At 31 December 2007 construction in progress includes advance prepayments for property, plant and equipment of RR 95,945 thousand (31 December 2006: RR 72,996 thousand).

Note 9. Intangible assets

Cost	Computer software	Licenses	Development costs	Total
Balance at 1 January 2007	281,395	766	318,264	600,425
Additions	121,598	4,465	311,913	437,976
Disposals	(53)	-	-	(53)
Balance at 31 December 2007	402,940	5,231	630,177	1,038,348
Amortisation				
Balance at 1 January 2007	(35,906)	(172)	(3,781)	(39,859)
Amortisation for the period	(51,830)	(791)	(17,560)	(70,181)
Amortisation disposal in the period	53	-	-	53
Balance at 31 December 2007	(87,683)	(963)	(21,341)	(109,987)
Carrying amounts				
At 1 January 2007	245,489	594	314,483	560,566
At 31 December 2007	315,257	4,268	608,836	928,361

Cost	Computer software	Licenses	Development costs	Total
Balance at 1 January 2006	172,233	162	22,735	195,130
Additions	109,252	604	295,529	405,385
Disposals	(90)	-	-	(90)
Balance at 31 December 2006	281,395	766	318,264	600,425
Amortisation				
Balance at 1 January 2006	(2,786)	(12)	-	(2,798)
Amortisation for the period	(33,210)	(160)	(3,781)	(37,151)
Amortisation disposal in the period	90	-	-	90
Balance at 31 December 2006	(35,906)	(172)	(3,781)	(39,859)
Carrying amounts				
At 1 January 2006	169,447	150	22,735	192,332
At 31 December 2006	245,489	594	314,483	560,566

Development costs represent the implementation of SAP software.

Note 10. Other non-current assets

	31 December 2007	31 December 2006
Restructured trade receivables (Note 13)	264,959	250,112
Trade and other receivables	50,738	145,432
Provision for impairment of accounts receivable	-	(47,902)
Advances for implementation of SAP software	34,162	110,158
Long-term VAT recoverable	8,469	66,762
Loans issued	27,700	-
Other	53,559	48,000
Total	**439,587**	**572,562**

Note 11. Available-for-sale financial assets

	31 December 2007	31 December 2006
Non-current investments		
Bank promissory notes	138,360	365,616
Total	**138,360**	**365,616**
Current investments		
Bank promissory notes	305,131	75,878
Total	**305,131**	**75,878**

The fair value of available-for-sale investments of RR 443,491 thousand as at 31 December 2007 (31 December 2006: RR 398,630 thousand) was determined by using 6.3-9.7% (31 December 2006: 8.7-9.4%) discount rate and with reference to their maturity. The nominal value of these interest free promissory notes is RR 474,057 thousand (31 December 2006: RR 458,431 thousand).

The Group's exposure to credit risks related to available-for-sale financial assets is disclosed in note 26.

Note 12. Cash

	31 December 2007	31 December 2006
Petty cash	214	79
Bank balances	803,037	967,117
Total	**803,251**	**967,196**

Note 13. Accounts receivable

	31 December 2007	31 December 2006
Trade receivables	3,870,128	3,102,318
Restructured accounts receivable	21,563	45,674
Tax prepayments	4,510	37,153
Other receivables	127,330	204,763
Provision for impairment of accounts receivable	(1,228,690)	(1,582,870)
Total	**2,794,841**	**1,807,038**

Certain trade receivables have been restructured and as a result are due to be realised more than one year from the balance sheet date (see Note 10). Expected future principle and interest cash flows from these receivables were discounted at 10.13%. The effect of discounting is included in net finance expenses (see Note 23).

The Group's exposure to credit and impairment losses related to trade and other accounts receivable are disclosed in note 26.

Note 14. Inventories

	31 December 2007	31 December 2006
Fuel supplies	1,618,184	1,697,816
Raw materials and supplies	646,145	620,261
Spare parts	452,462	432,845
Finished goods and other	10,701	8,178
Reserve for obsolescence	(63,859)	(65,455)
Total	**2,663,633**	**2,693,645**

At 31 December 2007 and 31 December 2006 inventories with a carrying amount of RR 961,914 thousand where pledged as collateral for bank loans (see Note 16).

Note 15. Equity

	31 December 2007	31 December 2006
Ordinary shares	26,116,076,165	26,116,076,165
Par value (in RR)	1.00	1.00

The charter capital of the Company formed upon its foundation was RR 22,830,000 thousand and consisted of 22,830,000,000 ordinary shares with nominal value of 1 ruble each.

In July 2007 the Company registered the results of 23,426,150,308 ordinary shares issue which were placed by conversion upon merger of regional generation companies (see Note 1).

In April 2007 the Company issued 2,689,925,857 additional ordinary shares with a par value of RR 1.00, which were placed by close subscription to the Parent. In payment for this additional share the Company received 100% of shares of Orenburg TGC. The fair value of shares of Orenburg TGC in the amount of RR 4,276,982 thousand was determined by independent appraiser. The amount in excess of par value is accounted for as additional paid in capital.

In accordance with the Group's accounting policy for business combinations under common control, the restructuring, including the share issuance, is presented as if the restructuring was completed before the earliest period presented.

Dividends

In accordance with Russian legislation the Company's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with Russian Accounting Principles. The Company had retained earnings of RR 3,292,323 thousand for the year ended 31 December 2007 (31 December 2006: RR 570,489 thousand).

The Annual General Meeting of the shareholders on 29 May 2007 approved dividends on ordinary shares in respect of the year ended 31 December 2006 in the amount of 0.0030878 Russian rubles per share for the amount of RR 14,650 thousand. The dividends were paid in May, 2007.

The General Meeting of the shareholders on 9 October 2007 approved dividends on ordinary shares in respect of the six months ended 30 June 2007 year in the amount of 0.002692 Russian rubles per share for the amount of RR 70,304 thousand. The dividends were paid in November 2007.

Note 16. Loans and finance lease liabilities

	31 December 2007	31 December 2006
Non-current		
Unsecured bank loans	1,000,000	
Finance lease liabilities	-	514
Total	**1,000,000**	**514**
Current		
Secured bank loans	3,109,840	1,630,400
Unsecured bank loans	1,002,045	1,253,550
Finance lease liabilities	-	1,102
Total	**4,111,885**	**2,885,052**

Note 16. Loans and finance lease liabilities (continued)

	Currency	Interest rate	Year of maturity	31 December 2007	31 December 2006
Secured bank loans	RUR	Mosprime+2.5%-3%	2008	2,008,843	-
Secured bank loans	RUR	Mosprime+3%	2008	847,197	-
Secured bank loans	RUR	11%	2008	253,800	-
Secured bank loans	RUR	Mosprime+3%	2007	-	1,500,000
Secured bank loans	RUR	12%	2007	-	130,400
Unsecured bank loans	RUR	9,8%	2009	1,000,000	
Unsecured bank loans	RUR	10,3%-11,5%	2008	638,122	-
Unsecured bank loans	RUR	Mosibor +4,3%	2008	363,923	-
Unsecured bank loans	RUR	9.46%-9.72%	2007	-	1,200,000
Unsecured bank loans	RUR	13.2%	2006-2007	-	3,550
Unsecured bank loans	RUR	12%	2007	-	50,000
Total				**5,111,885**	**2,883,950**

The bank loans in the amount of RR 2,856,040 thousand (31 December 2006: RR 1,500,000 thousand) are secured over inventories in the amount of RR 961,914 thousand (see Note 14).

The bank loans in the amount of RR 253,800 thousand (31 December 2006: RR 130,400 thousand) are secured by cash flows on certain power supply contracts.

Note 17. Promissory notes

	31 December 2007	31 December 2006
Non-current		
Long-term promissory notes	243,326	295,143
Current portion of long-term promissory notes	(123,669)	(74,363)
Total	**119,657**	**220,780**
Current		
Current portion of long-term promissory notes	123,669	74,363
Short-term promissory notes	-	54,445
Total	**123,669**	**128,808**

	Currency	Year of maturity	31 December 2007	31 December 2006
Promissory notes	RUR	2007	-	128,808
Promissory notes	RUR	2008	123,669	112,591
Promissory notes	RUR	2009	111,505	100,818
Promissory notes	RUR	2010	8,152	7,371
Total			**243,326**	**349,588**

Promissory notes with the carrying value of RR 243,326 thousand as at 31 December 2007 (31 December 2006: RR 347,605 thousand) represent promissory notes issued by the Group in 2005 to OAO Mezhtopenergobank. The nominal value of these interest free promissory notes as at 31 December 2007 is RR 269,000 thousand (31 December 2006: RR 399,000 thousand). Expected future principal cash flows were discounted at rates of between 9.6 and 10.6%. These rates were not materially different from current financing rate of the Group.

Note 18. Employee benefits

The Group has defined benefit pension and other long-term defined benefit plans that cover most full-time and retired employees. Defined post-employment benefits consist of several unfunded plans providing for lump-sum payments upon retirement, financial support for current pensioners, death benefits, jubilee benefits, old age life pension program.

	31 December 2007	31 December 2006
Present value of unfunded obligations	2,004,396	1,698,341
Unrecognized net actuarial losses	(229,876)	(73,029)
Unrecognized past service cost	(314,156)	(340,662)
Total employee benefits	**1 460 364**	**1,284,650**

	31 December 2007	31 December 2006
Defined benefit obligation	2,004,396	1,698,341
Deficit	2,004,396	1,698,341
Experience adjustments on plan liabilities	31,983	82,685

Movement in the present value of the defined benefit obligations

	31 December 2007	31 December 2006
As at 1 January	1,698,341	1,475,675
Interest cost on benefit obligation	114,638	99,608
Current service cost	119,768	103,395
Past service cost	15,632	3,736
Benefits paid	(115,956)	(66,758)
Actuarial (gains)/losses on obligation	171,973	82,685
As at 31 December	**2,004,396**	**1,698,341**

Movements in the net liability recognized in the balance sheet

	31 December 2007	31 December 2006
Net liability at 1 January	1,284,650	1,101,112
Benefits paid	(115,956)	(66,757)
Expense recognized in income statement (see below)	291,670	250,295
Net liability at 31 December	**1,460,364**	**1,284,650**

Expense recognized in the income statement

	Year ended 31 December 2007	Year ended 31 December 2006
Current service cost	119,768	103,395
Interest cost	114,638	99,608
Net actuarial loss recognized in the period	15,126	9,656
Past service cost	42,138	37,636
	291,670	**250,295**

Note 18. Employee benefits (continued)

The expense is recognized in the line item “Operating expenses” of the income statement.

Actuarial assumptions

	2007	2006
Discount rate (accumulation phase)	6,75%	6,75%
Future salary increases	8%	7%
Inflation rate	6%	5%

Note 19. Accounts payable and accrued charges

	31 December 2007	31 December 2006
Trade payables	816,412	737,342
Advances received	514,223	411,512
Wages and salary	352,637	300,899
Other payables	262,557	498,329
Provision for holidays	27,413	29,020
Total	**1,973,242**	**1,977,102**

Note 20. Other taxes payable

	31 December 2007	31 December 2006
Deferred VAT	-	803,838
Property tax	110,604	112,387
Value added tax	185,046	94,675
Employee taxes	106,301	92,909
Other taxes	142,781	120,077
Total	**544,732**	**1,223,886**

Note 21. Revenues

	Year ended 31 December 2007	Year ended 31 December 2006
Electricity	18,568,531	15,460,662
Heating	18,326,924	15,775,620
Other	3,105,933	3,064,318
Total	**40,001,388**	**34,300,600**

Note 22. Operating expenses

	Year ended 31 December 2007	Year ended 31 December 2006
Fuel	20,283,200	17,910,729
Third party services	4,051,122	3,201,922
Employee benefits	5,278,316	4,611,070
Depreciation	2,576,918	2,475,095
Material expenses	1,454,068	1,635,515
Taxes other than income tax	719,858	705,200
License fee	358,019	299,528
Purchased power	1,214,129	1,034,845
Provision for impairment of accounts receivable	22,591	(148,332)
Insurance	255,859	234,346
Bank services	181,617	158,109
Rental expenses	337,961	233,119
Water usage expenses	1,023,337	890,231
Amortization of intangible assets	70,181	37,151
Other expenses	764,005	719,873
Total	**38,591,181**	**33,998,401**

Employee benefits expenses comprise the following:

	Year ended 31 December 2007	Year ended 31 December 2006
Salaries and wages, benefits and payroll taxes	5,167,793	4,516,205
Non-governmental pension fund expenses	110,523	94,865
Employee benefits	**5,278,316**	**4,611,070**

Note 23. Net finance expense

	Year ended 31 December 2007	Year ended 31 December 2006
Interest income	16,255	11,118
Interest expense	(308,450)	(105,537)
Effect of discounting	36,882	(5,759)
Total	**(255,313)**	**(100,178)**

Note 24. Income tax expense

	Year ended 31 December 2007	Year ended 31 December 2006
Current income tax expense	769,157	715,437
Deferred income tax benefit	(152,188)	(534,728)
Total income tax expense	**616,969**	**180,709**

	Year ended 31 December 2007	Year ended 31 December 2006
Profit before income tax expense	1,147,030	324,936
Theoretical profit tax charge at an average statutory tax rate of 24%	275,287	77,985
Tax effect of items which are not deductible or taxable for taxation purposes	341,682	102,724
Total income tax expense	**616,969**	**180,709**

Note 24. Income tax expense (continued)

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 or profit tax purposes. Deferred profit tax assets and liabilities are measured at 24%, the rate expected to be applicable when the assets or liabilities will reverse.

The temporary differences associated with undistributed earnings of subsidiaries amount to RR 408,408 thousand at 31 December 2007 (31 December 2006: RR 431,654 thousand). A deferred tax liability on these temporary differences was not recognized because management controls the timing of the reversal of the temporary differences and they will not reverse in the foreseeable future.

Changes in deferred tax liabilities and assets for the year ended 31 December 2006 are presented in the table below:

	1 January 2006	Recognized in profit and loss	31 December 2006
Deferred tax liabilities			
Property, plant and equipment	(5,955,781)	583,879	(5,371,902)
Promissory notes	(20,162)	7,827	(12,335)
Total deferred tax liabilities	**(5,975,943)**	**591,706**	**(5,384,237)**
Deferred tax assets			
Accounts receivable	497,492	(78,780)	418,712
Provisions	28,784	21,517	50,301
Other	4,705	285	4,990
Total deferred tax assets	**530,981**	**(56,978)**	**474,003**
Net deferred tax liabilities	**5,444,962**	**534,728**	**4,910,234**

Changes in deferred tax liabilities and assets for the year ended 31 December 2007 are presented in the table below:

	1 January 2007	Recognized in profit and loss	31 December 2007
Deferred tax liabilities			
Property, plant and equipment	(5,371,902)	341,911	(5,029,991)
Promissory notes	(12,335)	6,173	(6,162)
Total deferred tax liabilities	**(5,384,237)**	**348,084**	**(5,036,153)**
Deferred tax assets			
Accounts receivable	418,712	(236,734)	181,978
Provisions	50,301	26,882	77,183
Loss carry forward	-	10,770	10,770
Other	4,990	3,186	8,176
Total deferred tax assets	**474,003**	**(195,896)**	**278,107**
Net deferred tax liabilities	**4,910,234**	**(152,188)**	**4,758,046**

Note 25. Earnings per share

	Year ended 31 December 2007	Year ended 31 December 2006
Weighted average number of ordinary shares issued (quantity) (See Note 15)	26,116,076,165	26,116,076,165
Net profit for the year	530,061	144,227
Earnings per ordinary share – basic (in Russian rubles)	0.0203	0.0055

Note 26. Financial instruments

Credit risk

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk as of the reporting date was:

		Carrying amount	
	Note	31 December 2007	31 December 2006
Restructured trade receivables	10	264,959	250,112
Trade and other long-term receivables	10	50,738	97,530
Loans issued	10	27,700	-
Available-for-sale financial assets	11	443,491	441,494
Cash	12	803,251	967,196
Trade accounts receivable	13	2,663,001	1,565,122
Other accounts receivable	13	127,330	204,763
		4,380,470	**3,526,217**

The maximum exposure to credit risk for trade and other accounts receivable at the reporting date by type of customer was:

	Carrying amount	
	31 December 2007	31 December 2006
Accounts receivables on electricity	138,020	132,506
Accounts receivables on heat	2,524,981	1,432,616
Other accounts receivable	127,330	204,763
	2,790,331	**1,769,885**

The Group's most significant customer, OAO Samaraenergo, accounts for RR 2,820 thousand of the trade receivables carrying amount as of 31 December 2007 (31 December 2006: 0).

Impairment losses

The aging of trade and other receivables at the reporting date was:

	Gross 2007	Impairment 2007	Gross 2006	Impairment 2006
Not past due	2,108,670	-	1,588,402	-
Past due 0-45 days	600,054	-	32,019	-
Past due 46-90 days	41,765	-	103,790	-
More than 90 days	1,268,532	1,228,690	1,628,544	1,582,870
	4,019,021	**1,228,690**	**3,352,755**	**1,582,870**

The movements in the provision for impairment in respect of trade and other receivables during the year was as follows:

	31 December 2007	31 December 2006
Balance at 1 January	1,630,772	1,779,104
Impairment loss recognized/(reversed)	22,591	(148,332)
Use of reserve	(424,673)	-
Balance at the end of the period	**1,228,690**	**1,630,772**

Note 26. Financial instruments (continued)

Based on historic default rates, the Group believes that no impairment allowance is necessary in respect of receivables not past due or past due by up to 90 days.

Liquidity risk

The following are the contractual maturities of financial liabilities, including estimated interest payments:

31 December 2007:

	Carrying amount	Contractual cash flows	12 months or less	1-2 years	2-5 years
Secured bank loans	3,109 840	3,208,874	3,208,874	-	-
Unsecured bank loans	2,002 045	2,222,384	1,127,874	1,094,510	-
Long-term promissory notes	119,567	139,000	130,000	130,000	9,000
Current portion of long-term promissory notes	123,669	130,000	130,000	-	-
Trade and other payables	1,078,969	1,078,969	1,078,969	-	-
	6,434,090	**6,779,227**	**5,675,717**	**1,224,510**	**9,000**

31 December 2006:

	Carrying amount	Contractual cash flows	12 months or less	1-2 years	2-5 years
Secured bank loans	1,630,400	1,680,387	1,680,387	-	-
Unsecured bank loans	1,253,550	1,273,633	1,273,633	-	-
Long-term promissory notes	220,780	269,000	-	130,000	139,000
Short-term promissory notes and current portion of long-term promissory notes	128,808	131,983	131,983	-	-
Trade and other payables	1,038,241	1,038,241	1,038,241	-	-
	4,271,779	**4,393,244**	**4,124,244**	**130,000**	**139,000**

Interest rate risk

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	31 December 2007	31 December 2006
Fixed rate instruments		
Financial assets	27,700	-
Financial liabilities	(1,891,922)	(1,383,950)
	(1,864,222)	**(1,383,950)**
Variable rate instruments		
Financial liabilities	(3,219,963)	(1,500,000)
	(3,219,963)	**(1,500,000)**

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit and loss. Therefore a change in interest rates at the reporting date would not affect net profit.

As of 31 December 2007, if interest rates had been 10 basis points higher with all other variables held constant, net profit and equity would have been RR 3,885 thousand (31 December 2006: RR 2,192 thousand) lower mainly as a result of higher interest expense on variable rate borrowings.

Note 26. Financial instruments (continued)

Fair values

The fair value of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows:

	31 December 2007		31 December 2006	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Restructured trade receivables	264,959	249,608	250,112	239,484
Trade and other receivables	50,738	50,738	97,530	97,530
Loans issued	27,700	27,700	-	-
Available-for-sale financial assets	443,491	443,491	441,494	441,494
Cash	803,251	803,251	967,196	967,196
Trade accounts receivable	2,663,001	2,663,001	1,565,122	1,565,122
Other accounts receivable	127,330	127,330	204,763	204,763
Secured bank loans	(3,109,840)	(3,109,840)	(1,630,400)	(1,630,400)
Unsecured bank loans	(2,002,045)	(1,980,424)	(1,253,550)	(1,253,550)
Long-term promissory notes	(119,657)	(120,885)	(220,780)	(228,271)
Short-term promissory notes and current portion of long-term promissory notes	(123,669)	(123,661)	(128,808)	(128,379)
Trade and other payables	(1,078,969)	(1,078,969)	(1,038,241)	(1,038,241)
	(2,053,710)	**(2,048,660)**	**(745,562)**	**(763,252)**

Interest rates used for determining fair value

	2007	**2006**
Other long-term receivables	11.5%	12.5%
Loans and borrowings	11.5%	-
Promissory notes	9.9-13%	8.5-11.4%

Note 27. Related parties

The Group's related parties transactions are disclosed below:

Parent's subsidiaries

Transactions with the Parent's subsidiaries were as follows:

	Year ended 31 December 2007	**Year ended 31 December 2006**
Purchase of electricity	1,599,037	808,566
License fee	347,632	299,528
Rent expense	183,056	6

	31 December 2007	**31 December 2006**
Accounts receivable and prepayments	143,167	86,177
Accounts payable and accrued charges	323,843	107,354

Note 27. Related parties (continued)

State-controlled entities

In the normal course of business the Group enters into transactions with other entities under Government control, including Gazprom, Russian railways, and various governmental bodies. Prices for natural gas, electricity and heat are based on tariffs set by FST and RST. Bank loans are provided on the basis of market rates. Taxes are accrued and settled in accordance with Russian tax legislation.

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

	Year ended 31 December 2007	Year ended 31 December 2006
Electricity and heat sales	23,833,326	22,309,799
Purchase of gas	15,531,796	12,831,482
Interest income	685	14,201
Rent expense	142,460	44,241

	31 December 2007	31 December 2006
Accounts receivable and prepayments	1,001,871	732,897
Accounts payable and accrued charges	220,575	236,971

Tax balances are disclosed in the balance sheet and Notes 20 and 24. Tax transactions are disclosed in the income statement and Notes 22 and 24.

Compensations to the Board of Directors and key management

Compensations are paid to members of the Management Board and Board of Directors for their services in full time management positions. The compensation is made up of a contractual salary, non-cash benefits, and performance bonuses depending on results for the period according to Russian statutory financial statements.

For the 12 months 2007 the following compensations were made to the Management Board and Board of Directors:

	Year ended 31 December 2007	Year ended 31 December 2006
Wages, salaries and bonuses	50,141	46,149
Total	**50,141**	**46,149**

Note 28. Operating leases

Operating leases payable

Operating lease rentals are payable as follows:

	31 December 2007	31 December 2006
Less than one year	15,262	37,058
Between one and five years	38,235	21,419
More than five years	34,001	-
Total	**87,498**	**58,477**

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

Note 28. Operating leases (continued)

Operating leases receivable

Operating lease rentals are receivable as follows:

	31 December 2007	31 December 2006
Less than one year	35,342	62,815
Between one and five years	73,361	46,179
More than five years	1,534	1,450
Total	**110,237**	**110,444**

Note 29. Commitments

Purchase commitments

The Group has a number of outstanding contracts to purchase natural gas. After 31 December 2007 the evaluated volume of supplies under the current contracts will be approximately equal to RR 18,787,215 thousand.

In 2006-2007 long-term gas contracts (until December 2010-2011) were concluded with OJSC Novatek.

Capital commitments

In the normal course of business, the Group has outstanding commitments under the contracts for the purchase and construction of property, plant and equipment for RR 5,193,603 thousand.

Note 30. Contingencies

Insurance

The insurance industry in the Russian Federation is in a developing state. The Group does not have full coverage for its stations, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

Legal proceedings

Group is 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, which, upon final disposition, will have a material adverse effect on the financial position of the Group.

Taxation

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

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

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.

Note 30. Contingencies (continued)

Environmental matters

The Group and its predecessors have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group entities periodically evaluate their obligations under environmental regulations.

Potential liabilities might arise as a result of changes in legislation and regulation or civil litigation. The impact of these potential changes cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.