**RAO UES GROUP**
**IAS CONSOLIDATED INTERIM FINANCIAL STATEMENTS**
**FOR THE THREE AND NINE MONTHS ENDED 30 SEPTEMBER 2002**

## RAO UES Group

**Consolidated Interim Balance Sheet as at 30 September 2002**

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002)

| | Notes | 30 September 2002 | 31 December 2001 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 8 | 821,518 | 837,857 |
| Investments in associates | 9 | 5,619 | 5,365 |
| Other non-current assets | 10 | 19,977 | 27,435 |
| **Total non-current assets** | | **847,114** | **870,657** |
| | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 11 | 11,074 | 13,959 |
| Accounts receivable and prepayments | 12 | 90,744 | 99,676 |
| Inventories | 13 | 41,600 | 41,328 |
| Loans issued | 1 | 8,635 | 14,713 |
| Other current assets | | 10,922 | 5,259 |
| **Total current assets** | | **162,975** | **174,935** |
| | | | |
| **Total assets** | 6 | **1,010,089** | **1,045,592** |
| | | | |
| **Shareholders' equity and liabilities** | | | |
| | | | |
| **Shareholders' equity** | 14 | | |
| Share capital | | | |
| Ordinary shares (nominal value RR 20,521 million) | | 141,419 | 141,419 |
| Preference shares (nominal value RR 1,038 million) | | 7,354 | 7,354 |
| Treasury shares | | (737) | (731) |
| | | 148,036 | 148,042 |
| Retained earnings and fair value reserve | | 383,986 | 364,098 |
| **Total shareholders' equity** | | **532,022** | **512,140** |
| | | | |
| **Minority interest** | 15 | 207,736 | 211,308 |
| | | | |
| **Non-current liabilities** | | | |
| Deferred profits tax liabilities | 16 | 54,753 | 86,745 |
| Non-current debt | 17 | 9,853 | 25,852 |
| Other non-current liabilities | 18 | 25,551 | 24,260 |
| **Total non-current liabilities** | | **90,157** | **136,857** |
| | | | |
| **Current liabilities** | | | |
| Current debt and current portion of non-current debt | 19 | 52,866 | 38,426 |
| Accounts payable and accrued charges | 20 | 88,986 | 98,158 |
| Taxes payable | 21 | 38,322 | 48,703 |
| **Total current liabilities** | | **180,174** | **185,287** |
| | | | |
| **Total liabilities** | 6 | **270,331** | **322,144** |
| | | | |
| **Total shareholders' equity and liabilities** | | **1,010,089** | **1,045,592** |

Chairman of the Management Board — Chubais A.B.

First Deputy Chairman of the Management Board — Melamed L.B.

21 March 2003

# RAO UES Group

## Consolidated Interim Statement of Operations for the three and nine months ended 30 September 2002

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002)

| | Notes | Three months ended 30 September 2002 | Nine months ended 30 September 2002 | Three months ended 30 September 2001 | Nine months ended 30 September 2001 |
|---|---|---|---|---|---|
| **Revenues** | | | | | |
| Electricity | | 83,011 | 255,857 | 73,125 | 233,206 |
| Heating | | 7,107 | 50,107 | 6,322 | 50,963 |
| Governmental assistance | 22 | 1,818 | 3,903 | 1,091 | 2,915 |
| Other | | 5,178 | 18,557 | 4,520 | 17,949 |
| **Total revenues** | 6 | **97,114** | **328,424** | **85,058** | **305,033** |
| **Costs and other deductions** | | | | | |
| Fuel expenses | | 22,759 | 84,032 | 20,621 | 85,661 |
| Wages and payroll taxes | | 20,042 | 58,129 | 17,900 | 50,537 |
| Depreciation and amortisation | 8 | 14,751 | 45,379 | 15,133 | 44,111 |
| Purchased power | | 13,329 | 43,686 | 16,537 | 39,382 |
| Repairs and maintenance | | 11,605 | 25,977 | 9,816 | 24,325 |
| Taxes other than on income | | 6,234 | 18,746 | 5,331 | 20,254 |
| Other materials | | 4,685 | 11,980 | 3,513 | 11,702 |
| Social expenditures | | 1,273 | 2,564 | 1,593 | 4,114 |
| Water usage expenses | | 1,189 | 3,206 | 769 | 2,017 |
| Doubtful debtors expense / (release) | | 919 | 1,921 | (7,622) | (9,288) |
| Loss / (gain) on disposal of fixed assets and investments | | 259 | 178 | (857) | (984) |
| Other expenses | | 10,511 | 30,502 | 9,126 | 29,496 |
| **Total costs and other deductions** | | **107,556** | **326,300** | **91,860** | **301,327** |
| **(Loss) / income from operations** | 6 | **(10,442)** | **2,124** | **(6,802)** | **3,706** |
| Share of (loss) / income of associates | 9 | (184) | 284 | (193) | 271 |
| Monetary effects and financing items | 23 | (3,145) | (321) | 14,711 | 26,973 |
| **(Loss) / income before profit tax and minority interest** | | **(13,771)** | **2,087** | **7,716** | **30,950** |
| Total profit tax benefit | 16 | 9,688 | 16,599 | 32,435 | 11,376 |
| **(Loss) / income before minority** | | **(4,083)** | **18,686** | **40,151** | **42,326** |
| Minority interest: share of net result | 15 | 7,326 | 2,580 | (8,400) | (9,597) |
| **Net income** | | **3,243** | **21,266** | **31,751** | **32,729** |
| **Earnings per ordinary and preference share – basic and diluted (in Russian Roubles)** | 24 | 0.08 | 0.50 | 0.74 | 0.77 |

Chairman of the Management Board — Chubais A.B.

First Deputy Chairman of the Management Board — Melamed L.B.

21 March 2003

# RAO UES Group

## Consolidated Interim Cash Flow Statement for the nine months ended 30 September 2002

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002)

| | Nine months ended 30 September 2002 | Nine months ended 30 September 2001 |
|---|---|---|
| **CASH FLOW FROM OPERATING ACTIVITIES:** | | |
| **Income before profit tax** | **2,087** | **30,950** |
| Adjustments to reconcile income before taxation to net cash provided by operations: | | |
| Depreciation and amortisation | 45,379 | 44,111 |
| Doubtful debtors expense / (release) | 1,921 | (9,288) |
| Interest and gain on restructuring accounts payable and taxes payable | 5,721 | (13,916) |
| Share of income of associates, before profit tax | (284) | (271) |
| Loss / (gain) on disposal of fixed assets and investments | 178 | (984) |
| Monetary effects on non-operating balances | (3,701) | (3,398) |
| Adjustment for non-cash investing activities | (6,183) | (4,624) |
| Other | 10 | (266) |
| **Operating cash flows before working capital changes and profit tax paid** | **45,128** | **42,314** |
| Working capital changes: | | |
| Decrease in accounts receivable and prepayments | 7,714 | 23,932 |
| (Increase) / decrease in other current assets | (5,666) | 2,531 |
| Decrease in loans issued | 6,078 | - |
| Increase in inventories | (271) | (565) |
| Decrease / (increase) in other non-current assets | 4,907 | (3,532) |
| Decrease in accounts payable and accrued charges | (10,110) | (26,232) |
| Decrease in taxes payable, other than profits tax | (9,317) | (28,494) |
| Increase in other non-current liabilities | 1,293 | 18,108 |
| Profit tax paid (cash) | (15,386) | (19,203) |
| Profit tax paid (non-cash) | (155) | (593) |
| **Net cash provided by operating activities** | **24,215** | **8,266** |
| **CASH FLOW FROM INVESTING ACTIVITIES:** | | |
| Additions to property, plant and equipment | (23,362) | (17,297) |
| Proceeds from sale of property, plant and equipment | 1,422 | 1,214 |
| Purchases of investments, net | (235) | (54) |
| **Net cash used for investing activities** | **(22,175)** | **(16,137)** |
| **CASH FLOW FROM FINANCING ACTIVITIES:** | | |
| Proceeds from issuance of current debt | 84,980 | 54,962 |
| Proceeds from issuance of non-current debt | 4,516 | 1,125 |
| Repayment of debt | (84,841) | (46,215) |
| Interest paid | (6,430) | (1,794) |
| Dividends paid | (1,908) | (1,053) |
| Purchase of treasury shares, net | (6) | - |
| **Net cash (used for) / provided by financing activities** | **(3,689)** | **7,025** |
| Effect of inflation on cash and cash equivalents | (1,236) | (1,175) |
| **Decrease in cash and cash equivalents** | **(2,885)** | **(2,021)** |
| **Cash and cash equivalents at the beginning of the period** | **13,959** | **9,976** |
| **Cash and cash equivalents at the end of the period** | **11,074** | **7,955** |

Chairman of the Management Board — Chubais A.B.

First Deputy Chairman of the Management Board — Melamed L.B.

21 March 2003

# RAO UES Group

**Consolidated Interim Statement of Changes in Shareholders' Equity for the nine months ended 30 September 2002**

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002)

| | Ordinary share capital | Preference share capital | Treasury shares | Retained earnings and fair value reserve | Total shareholders' equity |
|---|---|---|---|---|---|
| **At 31 December 2000, as previously reported** | 141,419 | 7,354 | (731) | 321,130 | 469,172 |
| Adoption of IAS 39 (see Note 3) | - | - | - | (2,530) | (2,530) |
| **At 31 December 2000, as adjusted** | 141,419 | 7,354 | (731) | 318,600 | 466,642 |
| Net income | - | - | - | 32,729 | 32,729 |
| Dividends | - | - | - | (1,134) | (1,134) |
| Change in fair value of available-for-sale investments | - | - | - | 399 | 399 |
| **At 30 September 2001** | 141,419 | 7,354 | (731) | 350,594 | 498,636 |
| | | | | | |
| **At 1 January 2002** | 141,419 | 7,354 | (731) | 364,098 | 512,140 |
| Net income | - | - | - | 21,266 | 21,266 |
| Dividends | - | - | - | (1,328) | (1,328) |
| Change in fair value of available-for-sale investments | - | - | - | (50) | (50) |
| Change in treasury shares, net | - | - | (6) | - | (6) |
| **At 30 September 2002** | 141,419 | 7,354 | (737) | 383,986 | 532,022 |

Chairman of the Management Board — Chubais A.B.

First Deputy Chairman of the Management Board — Melamed L.B.

21 March 2003

## Note 1: The Group and its operations

The Russian Open Joint Stock Company for Energy and Electrification Unified Energy System of Russia ("RAO UES") was created on 31 December 1992 following the privatisation of certain electricity power generation, transmission and distribution assets formerly under the control of the Ministry of Energy of the Russian Federation. Nuclear generation stations were not transferred to RAO UES.

The RAO UES Group (the "Group") consists of RAO UES and its related subsidiaries as at 30 September 2002. Principal subsidiaries are disclosed in Note 5. The operations of all generating facilities are co-ordinated by the Central Despatch Centre ("CDC") and Regional Despatch Centres, which are all under the control of the Group, in order to meet system requirements in an efficient manner.

All member companies of the Group are incorporated under the laws of the Russian Federation (the "state").

The Group performs the following major activities:

- ***High voltage transmission:*** The high voltage transmission network connects all but a few regions of the Russian Federation. RAO UES charges a transmission fee to users of the network and, together with the Federal Grid Company (a 100 percent owned subsidiary of RAO UES), maintains this network. The CDC, a 100 percent owned subsidiary of RAO UES, is responsible for system despatch and the functioning of the Federal Wholesale Market of Electricity and Capacity ("FOREM");

- ***Regional generation and distribution:*** RAO UES has ownership interests in more than 70 regional power companies ("energos"), responsible for the generation, distribution and sale of heat and electricity. These ownership interests range from 14 percent to 100 percent; and

- ***Stand-alone electricity generation:*** Major generation stations produce electricity and sell it via FOREM. The majority of these sales are within the Group.

At 30 September 2002, the number of employees of the Group was approximately 631,000 (31 December 2001: 648,000). Additionally, the Group's two associates combined had 33,000 employees at 30 September 2002 (31 December 2001: 37,000).

RAO UES's registered office is located at 7, Kitaigorodsky Proezd, 103074, Moscow, Russia.

RAO UES also prepares annual parent company stand-alone financial statements in accordance with International Accounting Standards ("IAS").

***Economic environment in the Russian Federation.*** Whilst there have been improvements in the economic situation in the Russian Federation in recent years, 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, restrictive currency controls, and relatively high inflation.

The prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory, and political developments.

***Relations with the state and current regulation.*** At 30 September 2002, the Russian Federation owned 52.7 percent of RAO UES, which represents 54.9 percent of the ordinary shares issued. As discussed in Note 14, only ordinary shares have voting rights. The Group's customer base includes a large number of entities controlled by, or related to, the state. Furthermore, the state controls a number of the Group's fuel and other suppliers.

The government of the Russian Federation directly affects the Group's operations through regulation by the Federal Energy Commission ("FEC"), with respect to its wholesale energy sales, and by the Regional Energy Commissions ("RECs"), with respect to its retail electricity and heat sales. Tariffs which Group entities 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 privatisation in 1992, the government of the Russian Federation imposed an obligation on Group 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)**

As described above and in Notes 2 and 26, the government's economic, social and other policies could have material effects on the operations of the Group.

***Regulatory and sector restructuring.*** The power sector and the Group are presently undergoing restructuring designed to introduce competition into the electricity sector and to create an environment in which the Group and its successor companies can raise the capital required to maintain and expand current capacity. Under Government Resolution No. 526 dated 11 July 2001 "On the Reform of the Russian Federation Electric Utilities", a non-regulatory market is being set up to sell 5-15 percent of the electricity generated. Subsequently all electricity generated is expected to be sold in a competitive, wholesale market. In accordance with the "Action Plan for the 1st Stage of the Electric Utilities Reform", approved by Government Directive No. 471-p dated 5 April 2002, the following is being undertaken:

- Trade System Administrator ("TSA") – in November 2001, a non-commercial partnership "Trade System Administrator of the Wholesale Electricity Market UES" was created to manage the new wholesale market. The Group controls 50 percent of the votes in the Supervisory Council of the TSA; the other 50 percent is owned by other industry participants;

- Federal Grid Company – OAO "FSK UES" ("FSK") was established in June 2002, as a wholly-owned subsidiary, to manage the transmission operations using the transmission assets obtained and planned to be obtained from RAO UES and its subsidiaries and associates;

- System Operator – "OAO System Operator – Central Dispatch Unit of Unified Energy System" ("SO") – SO was established in June 2002, to carry out the dispatch functions within the Group;

- RAO UES has drafted guidelines that set out the process for establishing wholesale generation companies, including a listing of the power stations included therein. At present, ministries and government agencies of the Russian Federation are considering these guidelines. Further, consultations are being held with heads and representatives of the regions whose power stations are earmarked for integration within the wholesale generation companies; and

- The subsidiaries and associates of RAO UES are drafting plans for reforming the said subsidiaries and associates.

As part of the restructuring process, amendments to Russian laws governing the future structure and foundations of the electricity market are being considered by legislative bodies of the Russian Federation. The State Duma of Russian Federation has passed on third reading bills on the electric utilities that have been introduced by the Russian Federation. The Group's management plays an active role in the development of this new legislation and the amendment of the existing laws.

At this time, the impacts of the industry changes on both the financial results and position of the Group cannot be readily assessed and, accordingly, no provision has been recognised for the effects of the restructuring process.

***Transactions related to the repayment of Russian Federation debt to the Czech Republic.*** In December 2001 the Group entered into a series of transactions in which it participated in the settlement of Russian Federation debt ("RF debt") to the Czech Republic (the "Czech transactions"). By contract, the Ministry of Finance of the Russian Federation ("MinFin") transferred to the Group its obligations regarding the RF debt in exchange for a commitment to repay such debt. The Group obtained a loan of Russian Rouble ("RR") 26,500 million (RR 24,000 million unrestated) from Sberbank (see Note 17) and then made payments totalling RR 26,777 million (RR 24,250 million unrestated) to the Czech Republic's formally appointed representative, Falcon Capital, to buy back the RF debt. MinFin paid RR 44,955 million (RR 40,713 million unrestated) to the Group upon confirmation that the RF debt had been settled and that the tax liability payments from suppliers described below had been received.

**Note 1: The Group and its operations (continued)**

Concurrently, as part of its arrangement with MinFin, the Group issued loans to several of its major suppliers and to its subsidiaries, for RR 16,237 million (RR 14,705 million unrestated) and RR 28,758 million (RR 26,044 million unrestated), respectively. The loans to suppliers were required to be made for one year, with no interest, and repayable in equal, monthly instalments through the end of 2002. As a result of the loans being issued at below market interest rates, the Group recorded a discount of RR 1,524 million (RR 1,380 million unrestated) in December 2001. At 30 September 2002, the balance outstanding on the loans issued was RR 8,635 million. The imputed interest recorded as a result of the amortisation of the discount for the nine months ended 30 September 2002 was RR 1,081 million. Subsequent to the balance sheet date, the repayment terms for the debt of one of the suppliers, Rosenergoatom, amounting to RR 3,002 million at 30 September 2002, were extended with monthly repayments due up to August 2003.

The loans to the subsidiaries were used to make payments to major suppliers as a settlement of a portion of the outstanding trade payables to those suppliers. The Group understands that the suppliers made equivalent payments to the state to settle their outstanding tax liabilities.

The resulting gain on the Czech transactions of RR 16,655 million (RR 15,083 million unrestated) was recorded in December 2001 and was comprised of the proceeds received from MinFin, less the amount paid to Falcon Capital and the discount on the loans issued to suppliers. The related profit tax expense of RR 4,139 million was reflected in the current profit tax charge for the period ended 30 September 2002; it was recorded as a deferred profit tax liability at 31 December 2001.

**Note 2: Financial condition**

At 30 September 2002, the Group's current liabilities exceeded its current assets by RR 17,199 million (31 December 2001: RR 10,352 million; 31 December 2000: RR 97,916 million). Since 2000, the Group has improved its financial position, largely through better cash collections and the restructuring of trade and tax liabilities to long term. The effects of the restructuring of accounts and taxes payable are described in Notes 18, 20 and 21. However, there still remains a significant amount of uncollected accounts receivable from earlier periods. Management continues to aggressively implement collection and restructuring efforts to reduce the outstanding balances. There is legislation enabling the Group to cut off non-payers, but this is only possible to a certain extent due to strategic and political factors. Federal, municipal and other governmental organisations make up a significant proportion of the debtor balance as at 30 September 2002. The Group has provided against doubtful debtors, as further described in Notes 10 and 12.

The Group is affected by government policy through control of tariffs and other factors. The Regional Energy Commissions 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 a Russian statutory basis and, accordingly, exclude additional costs recognised under an IAS basis of accounting. As a result, tariffs do not consistently allow for an adequate return on investment and currently do not provide sufficient funds for the full replacement of property, plant and equipment. Furthermore, the Group also experiences difficulties raising finance for the necessary investment in generation, transmission and distribution assets.

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

- introduction of improved financial budgeting procedures; a strong focus on timely cash collection of current and old debtor balances; restructuring of liabilities for repayment over a longer period;
- discussions with strategic investors, and identification and assessment of projects requiring investment funds;
- negotiations with federal and regional governments and regulators for real increases in tariffs to support adequate long term investment into the Group's generation, transmission and distribution assets; and
- active participation in the restructuring of the electricity sector (see Note 1).

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 2: Financial condition (continued)**

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

As part of its financial restructuring efforts, the Group took on additional debt, as described in Note 1. The ability to repay this debt in accordance with its terms and to continue to meet other cash obligations will be dependent on various factors including: continued efforts to collect old outstanding debtors; further restructuring of current liabilities to long term debt; obtaining additional debt financing; and ultimately real increases in tariffs.

**Note 3: Basis of presentation**

These consolidated interim financial statements have been prepared in accordance with IAS.

Each enterprise of the Group individually maintains its own books of accounts and prepares its statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"). The accompanying financial statements are based on the statutory records, which are maintained under the historical cost convention method, except for revaluations of property, plant and equipment, and adjusted and reclassified for presentation in accordance with IAS.

The preparation of consolidated interim financial statements in accordance with IAS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates have principally been made in respect of the impairment provision on property, plant and equipment, deferred profits taxes, allowance for doubtful debtors and fair values of financial instruments. Actual results could differ from these estimates.

***Inflation accounting.*** The adjustments and reclassifications made to the statutory records for the purposes of IAS presentation include the restatement for changes in the general purchasing power of the Russian Rouble in accordance with IAS 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date.

The conversion factors are derived from the Russian Federation Consumer Price Index (“CPI”) published by the Russian State Committee on Statistics (“Goscomstat”), and from indices obtained from other published sources for years prior to 1992. The indices used to restate the balance sheet, based on 1988 prices, (1988 = 100) as at 30 September 2002, and the respective conversion factors are:

| Date | Index | Conversion Factor |
|---|---|---|
| 31 December 1998 | 1,216,400 | 2.15 |
| 31 December 1999 | 1,661,481 | 1.58 |
| 31 December 2000 | 1,995,937 | 1.31 |
| 31 December 2001 | 2,371,572 | 1.10 |
| 30 September 2002 | 2,618,734 | 1.00 |

The significant guidelines followed in restating these financial statements in accordance with IAS 29 are:

- all amounts, including comparative figures, are stated in terms of the measuring unit current at 30 September 2002;
- monetary assets and liabilities are not restated because they are already expressed in terms of the monetary unit current at 30 September 2002;
- the appraisal values of property, plant and equipment and the impact of any impairment have been restated by applying relevant conversion factors beginning with the appraisal date together with adjustments for additions, disposals and depreciation, all restated by applying the relevant conversion factors;

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 3: Basis of presentation (continued)**

- other non-monetary assets and liabilities (items which are not expressed in terms of the monetary unit current at 30 September 2002) and shareholders' equity, including the share capital, are restated by applying the relevant conversion factors;
- all items in the statements of operations and of cash flows are restated by applying appropriate conversion factors; and
- the effect of inflation on the Group's net monetary position is included in the statement of operations of the current period as a net monetary gain.

The statement of operations includes a net monetary gain of RR 1,236 million and RR 6,982 million for the three and nine months ended 30 September 2002, respectively (three months ended 30 September 2001: monetary gain of RR 161 million; nine months ended 30 September 2001: monetary gain of RR 13,678 million) because, on average, the Group had net monetary liabilities during this period.

As at 31 December 2002 the CPI was 2,730,154 (1988 = 100), representing inflation of 4.3 percent since 30 September 2002.

As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation has ceased, effective from 1 January 2003 the Group no longer applies the provisions of IAS 29.

***Adoption of IAS 39 "Financial Instruments: Recognition and Measurement" ("IAS 39").*** With effect from 1 January 2001, the Group has adopted IAS 39 "Financial Instruments: Recognition and Measurement". The effect of adopting this standard is summarised below, and further information is disclosed in Note 4.

The resulting adjustments of the balances at 1 January 2001, shown below, were taken to opening retained earnings and fair value reserve.

| | Total effect on items measured | Deferred profits tax liabilities | Minority interests | Retained earnings and fair value reserve |
|---|---|---|---|---|
| Available-for-sale investments | (3,564) | - | - | (3,564) |
| Accounts payable and taxes payable | 3,153 | (1,074) | (1,045) | 1,034 |
| | | (1,074) | (1,045) | (2,530) |

The adjustment to available-for-sale investments reflects the assessment by management of the fair value of investments on the balance sheet, which were carried at cost prior to 1 January 2001. The accounts payable and taxes payable adjustment is comprised of specific amounts payable which had, as at 1 January 2001, been renegotiated with creditors for long-term repayment.

**Note 4: Summary of significant accounting policies**

***Principles of consolidation.*** The consolidated financial statements comprise the financial statements of RAO UES and the financial statements of those entities whose operations are controlled by RAO UES. Control is presumed to exist when RAO UES controls, directly or indirectly through subsidiaries, greater than 50 percent of voting rights. The Group consolidates a number of companies in which the Group owns less than 50 percent of the voting shares. Control exists for such entities on the basis of a dominant shareholding combined with other factors which allow the Group to exercise control.

A significant majority of the principal subsidiary Companies described in Note 5 were transferred to RAO UES by the Russian Federation on and after its incorporation into a joint stock company. These transfers represented a reorganisation of assets under common control and, accordingly, are accounted for in a manner similar to uniting of interests from the date of privatisation of each Group entity.

All material inter-group balances and transactions have been eliminated. Separate disclosure is made of minority interests.

## Note 4: Summary of significant accounting policies (continued)

***Associated enterprises.*** Investments in associated enterprises are accounted for using the equity method of accounting, based upon the percentage of ownership held by the Group. Associated enterprises are entities over which RAO UES is presumed to exercise significant influence but which it does not control.

***Investments.*** Investments intended to be held for an indefinite period of time are classified as available-for-sale; these are included in other non-current assets unless management has the 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 classification of its investments at the time of the purchase and re-evaluates such designation on a regular basis.

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

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

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

***Loans issued.*** Loans issued by the Group are measured at amortised cost. Amortised cost is the amount at which the loan was measured at initial recognition minus principal repayments plus the cumulative amortisation of any difference between that initial amount and the maturity amount, and minus any write down for impairment.

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

The official rate of exchange, as determined by the Central Bank of the Russian Federation, between the Russian Rouble and the US Dollar ("US$") at 30 September 2002 was RR 31.64: US$ 1.00 (31 December 2001: RR 30.14: US$ 1.00). Exchange restrictions and controls exist relating to converting the Russian Rouble into other currencies.

***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 either proposed before the balance sheet date or proposed or declared after the balance sheet date, but before the financial statements are authorized for issue.

***Property, plant and equipment.*** Property, plant and equipment as at 30 September 2002 is stated at depreciated replacement cost, based upon values determined by a third party valuation at 31 December 1997, and adjusted for subsequent additions at cost, disposals and depreciation, and restated for the impact of inflation. At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount which is determined as the higher of an asset's net selling price and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the statement of operations. An impairment loss recognised in prior years is reversed if there has been a change in the estimates used to determine an asset's recoverable amount.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 4: Summary of significant accounting policies (continued)**

The amounts determined by the third party valuation represent an estimate of depreciated replacement cost. The third party valuation was performed in order to determine a basis for cost, because the historical accounting records for property, plant and equipment were not readily available. Therefore, this third party valuation is not a recurring feature since it was intended to determine the initial cost basis of property, plant and equipment. The change in carrying value arising from this valuation was recorded directly to retained earnings.

Major renewals and improvements are capitalised and the assets replaced are retired. Costs of borrowing are not capitalised. Maintenance, repairs and minor renewals are expensed as incurred. Minor renewals include all expenditures that do not result in a technical enhancement of an asset beyond its original capability. Gains and losses arising from the retirement of property, plant and equipment are included in the statement of operations as incurred.

Under Russian law, land on which the Group carries out its activities is the property of the state and municipalities and, therefore, is not included in the consolidated balance sheet.

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

| **Type of facility** | **Acquired prior to 31 December 1997** | **Acquired subsequent to 31 December 1997** |
|---|---|---|
| Electricity and heat generation | 3 - 80 | 20 - 80 |
| Electricity transmission | 14 - 40 | 25 - 40 |
| Electricity distribution | 3 - 40 | 25 - 40 |
| Heating network | 3 - 40 | 20 - 40 |
| Other | 8 - 24 | 10 - 40 |

Social assets are not capitalized as they are not expected to result in future economic benefits to the Group. Costs associated with fulfilling the Group’s social responsibilities are also expensed as incurred.

***Cash and cash equivalents.*** Cash comprises cash in hand and cash deposited in banks. Cash equivalents comprise short-term investments that may be readily converted into cash and have a maturity of three months or less.

The statement of cash flows has been prepared in accordance with IAS 7 "Cash Flow Statements" and has been restated for the effects of inflation, in accordance with IAS 29. The Group relies to some extent on non-cash transactions. Investing activities and financing activities, as disclosed in the statement of cash flows, represent actual cash transactions. The total of operating activities also represents actual cash flow from operations. However, individual items within this part of the statement of cash flows are stated inclusive of both cash and non-cash transactions. Management believes that the benefits of providing individual cash items within operating activities is outweighed by the cost of preparation.

***Mutual settlements, barter and non-cash settlements.*** A portion of sales and purchases are settled by mutual settlements, barter and non-cash settlements. These settlements are generally in the form of direct settlement by goods or services with the final customer, cancellation of mutual balances or through a chain of non-cash transactions involving several companies. Non-cash settlements which are expected to be settled within 12 months are recorded as other current assets. These include “veksels” or “bills of exchange” which are negotiable debt obligations. The receivables and payables recorded in the consolidated interim balance sheet, that are expected to be settled by mutual settlements, barter or non-cash settlements, reflect management’s estimate of the fair value to be received or given up in non-cash settlements.

**Note 4: Summary of significant accounting policies (continued)**

***Accounts receivable and prepayments.*** Accounts receivable are recorded inclusive of value added taxes which are payable to tax authorities upon collection of such receivables. Trade and other receivables are 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 market rate of interest for similar borrowers at the date of origination of the receivables.

***Value added tax on purchases and sales.*** Value added tax of 20 percent is applied to the majority of purchases and sales. Value added tax is reclaimable against current value added tax obligations upon payment and receipt of goods or services rendered. These obligations are recorded net of the reclaimed value added tax on purchases. Value added tax on purchases for which either payment has not been made, goods have not been received or construction has not been completed is recorded as an asset in the balance sheet.

***Inventories.*** Inventories are valued at the lower of net realisable value and weighted average cost, restated for the effects of inflation. Provision is made for potential losses on obsolete or slow-moving inventories, taking into account their expected use and future realisable value.

***Deferred profit taxes.*** Deferred profit tax assets and liabilities are calculated in respect of temporary differences using a balance sheet liability method. Deferred profit tax is provided for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. A deferred profit tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred profit tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred profit tax is not provided for the undistributed earnings of subsidiaries, as the Group requires profits to be reinvested, and only insignificant dividends are declared. Deferred profit tax is provided for the undistributed earnings of associated enterprises.

***Accounts payable and accrued charges.*** Accounts payable are stated inclusive of value added tax which is reclaimable from the tax authorities upon the later of receipt of goods and services and the payment of the associated payable.

If accounts payable are restructured and the fair value of the restructured payable differs by more then ten percent from the original liability, then the fair value of the restructured payable is measured as the present value of the future cash flows discounted at the interest rate available to the Group at the date of the restructuring. The amount of the discount is credited to the statement of operations (monetary effects and financing items) as a gain on restructuring, and the non-current portion of the discounted payable is reclassified to other non-current liabilities. The discount is amortised over the period of the restructuring as an interest expense.

***Debt.*** Debt is recognised initially at the fair value of the proceeds received, net of transaction costs incurred. Fair value is determined with reference to market interest rates applicable to the Group when the debt was incurred. In subsequent periods, debt is stated at amortised cost; any difference between the fair value of the proceeds (net of transaction costs) and the redemption amount is recognised in the statement of operations as an interest expense over the period of the debt obligation.

***Minority interest.*** Minority interest represents the minority shareholders' proportionate share of the equity of the Group's subsidiaries. This has been calculated based upon the minority interests' ownership percentage of these subsidiaries. Specific rights on dissolution for preference shareholders are included in the calculation of minority interests. RAO UES does not own any preference shares in subsidiaries.

**Note 4: Summary of significant accounting policies (continued)**

***Pension and post-employment benefits***. Group entities' mandatory contributions to the governmental pension scheme are expensed when incurred. Discretionary pension and other post-employment benefits are not material.

***Environmental liabilities.*** Liabilities for environmental remediation are recorded where there is a present obligation, the payment is probable and reliable estimates exist.

***Revenue recognition***. Revenue is recognised on the delivery of electricity and heat and on the despatch of non-utility goods and services through the end of the period. Revenue amounts are presented exclusive of value added tax and other similar compulsory payments.

Revenue is based on the application of authorised tariffs for electricity and heat sales as approved by the regional RECs.

***Earnings per share.*** Preference shares are considered to be participating shares as their dividend may not be less than that given to ordinary shares. 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.

***Treasury shares.*** Where RAO UES or its subsidiaries purchase RAO UES's equity share capital, the consideration paid, including any attributable transaction costs, net of income taxes, is deducted from total shareholders' equity as treasury shares until they are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity. Treasury shares are stated at weighted average cost, restated for inflation as at the balance sheet date.

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

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

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 5: Principal subsidiaries

The following are the significant subsidiary enterprises which have been consolidated into the Group's financial statements. All subsidiaries are incorporated and operate in Russia.

***Regional generation and distribution companies***

| Name | Ownership % | Voting % | Name | Ownership % | Voting % |
|---|---|---|---|---|---|
| ***Centre*** | | | ***South*** | | |
| Astrakhanenergo | 49.0 | 49.0 | Dagenergo | 51.3 | 51.3 |
| Belgorodenergo | 49.0 | 65.3 | Experimentalnaya TETS | 74.9 | 100.0 |
| Bryanskenergo | 49.0 | 65.2 | Kabbalkenergo | 50.3 | 59.8 |
| Ivenergo | 49.7 | 56.6 | Kalmenergo | 96.4 | 96.4 |
| Kalugaenergo | 49.0 | 49.0 | Karachaevo-Cherkesskenergo | 100.0 | 100.0 |
| Kostromaenergo | 49.0 | 65.3 | Kubanenergo | 49.0 | 49.0 |
| Kurskenergo | 49.4 | 59.8 | Rostovenergo | 48.4 | 62.8 |
| Lipetskenergo | 49.0 | 49.0 | Sevkavkazenergo | 49.0 | 49.0 |
| Mosenergo | 50.9 | 50.9 | Stavropolenergo | 55.1 | 71.9 |
| Orelenergo | 49.5 | 60.6 | | | |
| Ryazanenergo | 49.0 | 49.0 | ***Ural*** | | |
| Smolenskenergo | 48.7 | 59.3 | | | |
| Tambovenergo | 49.0 | 56.0 | Chelyabenergo | 49.0 | 58.1 |
| Tulaenergo | 49.0 | 49.0 | Kirovenergo | 48.2 | 64.0 |
| Tverenergo | 49.0 | 65.3 | Kurganenergo | 49.0 | 53.8 |
| Vladimirenergo | 49.0 | 49.0 | Orenburgenergo | 100.0 | 100.0 |
| Volgogradenergo | 49.0 | 61.3 | Permenergo | 49.0 | 64.4 |
| Vologdaenergo | 49.0 | 49.0 | Sverdlovenergo | 49.0 | 65.3 |
| Voronezhenergo | 49.0 | 65.3 | Tumenenergo | 100.0 | 100.0 |
| Yarenergo | 47.8 | 60.3 | Udmurtenergo | 49.0 | 55.4 |
| ***North-West*** | | | ***Siberia*** | | |
| Arkhenergo | 49.0 | 59.1 | Altaienergo | 54.7 | 72.2 |
| Karelenergo | 100.0 | 100.0 | Buryatenergo | 47.6 | 47.6 |
| Kolenergo | 49.2 | 65.5 | Chitaenergo | 49.0 | 62.2 |
| Komienergo | 50.1 | 50.3 | Khakasenergo | 100.0 | 100.0 |
| Lenenergo | 49.0 | 57.4 | Krasnoyarskenergo | 51.8 | 66.4 |
| Novgorodenergo | 49.0 | 62.9 | Kuzbassenergo | 49.0 | 49.0 |
| Pskovenergo | 49.0 | 49.0 | Omskenergo | 49.0 | 60.4 |
| Yantarenergo | 100.0 | 100.0 | Tomskenergo | 52.0 | 59.9 |
| ***Middle Volga*** | | | ***East*** | | |
| Chuvashenergo | 100.0 | 100.0 | Amurenergo | 53.1 | 61.1 |
| Marienergo | 64.4 | 70.1 | Dalenergo | 49.0 | 65.3 |
| Mordovenergo | 54.7 | 54.7 | Geotherm | 82.7 | 87.3 |
| Nizhnovenergo | 49.0 | 62.3 | Khabarovskenergo | 48.8 | 60.8 |
| Penzaenergo | 49.0 | 60.2 | Kolymaenergo | 97.1 | 97.1 |
| Samaraenergo | 49.2 | 56.3 | Kamchatskenergo | 49.0 | 59.2 |
| Saratovenergo | 49.8 | 64.6 | Magadanenergo | 49.0 | 64.4 |
| Ulyanovskenergo | 49.0 | 65.3 | Sakhalinenergo | 49.0 | 49.0 |
| | | | Sakhaenergo | 49.0 | 100.0 |
| | | | Yakutskenergo | 49.0 | 58.1 |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 5: Principal subsidiaries (continued)

### *Hydrogenerating companies*

| Name | Ownership % | Voting % | Name | Ownership % | Voting % |
|---|---|---|---|---|---|
| Bureyskaya GES | 76.9 | 78.4 | Volzhskaya GES (Volzhsk) | 83.3 | 86.4 |
| Kabbalk GES | 74.3 | 98.0 | Volzhskaya GES (Zhigulevsk) | 85.0 | 88.1 |
| Kamskaya GES | 100.0 | 100.0 | Votkinskaya GES | 59.8 | 74.2 |
| Kaskad Verhnevolzhskih GES | 100.0 | 100.0 | Zaramagskie GES | 90.8 | 92.9 |
| Sayano-Shushenskaya GES | 78.9 | 82.8 | Zeiskaya GES | 56.9 | 72.5 |
| Sulakenergo | 99.2 | 99.2 | Zelenchugskie GES | 97.3 | 97.3 |
| Taimyrenergo | 100.0 | 100.0 | | | |

### *Thermal generating companies*

| Name | Ownership % | Voting % | Name | Ownership % | Voting % |
|---|---|---|---|---|---|
| Berezovskaya GRES –1 | 100.0 | 100.0 | North-West Station | 53.5 | 60.5 |
| Cherepetskaya GRES | 55.8 | 55.8 | Novocherkasskaya GRES | 100.0 | 100.0 |
| Gusinoozerskaya GRES | 100.0 | 100.0 | Pechorskaya GRES | 51.0 | 51.0 |
| Konakovskaya GRES | 51.0 | 51.0 | Permskaya GRES | 100.0 | 100.0 |
| Kostromskaya GRES | 51.0 | 51.0 | Pskovskaya GRES | 50.0 | 50.0 |
| Krasnoyarskaya GRES –2 | 100.0 | 100.0 | Ryazanskaya GRES | 100.0 | 100.0 |
| Kuban GRES | 79.8 | 99.9 | Shekinskie PGU | 92.1 | 98.9 |
| Kaliningradskaya TETS –2 | 92.1 | 92.1 | Stavropolskaya GRES | 51.0 | 51.0 |
| Lutek | 56.3 | 56.3 | Troitskaya GRES | 100.0 | 100.0 |
| Nevinomysskaya GRES | 100.0 | 100.0 | | | |

### *Construction companies*

| Name | Ownership % | Voting % | Name | Ownership % | Voting % |
|---|---|---|---|---|---|
| Boguchanskaya GES | 65.4 | 69.4 | Cherkeigesstroi | 100.0 | 100.0 |
| Bureyagesstroy | 100.0 | 100.0 | Zeyagesstroi | 100.0 | 100.0 |

### *Other*

| Name | Ownership % | Voting % | Name | Ownership % | Voting % |
|---|---|---|---|---|---|
| Central Despatch Centre | 100.0 | 100.0 | Inter RAO UES | 100.0 | 100.0 |
| Federal Grid Company | 100.0 | 100.0 | Neftianoy Dom | 75.0 | 75.0 |
| Insurance company LIDER | 100.0 | 100.0 | System Operator | 100.0 | 100.0 |
| Centre of Settlement Optimisation | 100.0 | 100.0 | | | |

The Group controls Centre for Assistance in Restructuring the Electricity Sector, a non-commercial partnership.

Differences between ownership interest and voting interest normally represent the effect of preference shares. RAO UES does not hold any preference shares of its subsidiaries. Such preference shares do not have any voting rights, unless dividends have not been declared fully at the Annual Shareholders' meeting.

**Note 5: Principal subsidiaries (continued)**

In August 2001, the Group acquired a controlling interest in OOO Media-Holding REN-TV, an entity which holds television broadcasting equipment and licenses. This investment was acquired and held exclusively with a view to its subsequent disposal in the near future. Accordingly, it has not been consolidated and is classified as an available-for-sale investment in other current assets.

During the period ended 30 September 2002 there were certain other changes in RAO UES' ownership percentage of several of its subsidiaries, which had an immaterial impact on the statement of operations.

**Note 6: Segment information**

***Primary reporting segments - business segments.*** The Group is organised into four main business segments; this classification is consistent with the disclosure in the prior year's consolidated financial statements.

- ***"RAO UES segment"*** this segment principally comprises RAO UES and FSK, which maintain and operate the high voltage electricity transmission grid. Transmission fees paid by energos are set by the FEC;

- ***"Energos segment"*** consists of regional electricity & heat generation and distribution. The majority of electricity generated by energos is sold within the regions in which the energo operates at tariffs set by RECs. Certain energos have surplus generation and sell electricity via FOREM. Tariffs in FOREM are set by the FEC;

- ***"Hydro and thermal generating stations segment"*** consists of entities that sell electricity to energos through FOREM, at tariffs set by the FEC; and

- ***"Construction segment"*** consists of construction entities.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 6: Segment information (continued)

| Three months ended 30 September 2002 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Gross revenues | 13,729 | 96,313 | 10,702 | 1,191 | - | 121,935 |
| Intra-group revenues | (10,661) | (3,161) | (9,948) | (1,051) | - | (24,821) |
| Net revenues | 3,068 | 93,152 | 754 | 140 | - | 97,114 |
| Segment income / (loss) | 4,952 | (13,563) | (1,167) | (378) | (286) | (10,442) |
| Capital expenditures | 2,092 | 7,761 | 2,316 | 168 | - | 12,337 |
| Depreciation and amortisation | 2,306 | 10,841 | 1,562 | 42 | - | 14,751 |
| Doubtful debtors expense / (release) | 162 | (108) | 798 | 67 | - | 919 |

| Nine months ended 30 September 2002 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Gross revenues | 40,628 | 321,883 | 29,279 | 3,452 | - | 395,242 |
| Intra-group revenues | (31,462) | (6,650) | (25,887) | (2,819) | - | (66,818) |
| Net revenues | 9,166 | 315,233 | 3,392 | 633 | - | 328,424 |
| Segment income / (loss) | 16,956 | (7,780) | (6,259) | (498) | (295) | 2,124 |
| Capital expenditures | 5,437 | 19,594 | 5,184 | 1,013 | - | 31,228 |
| Depreciation and amortisation | 7,424 | 33,170 | 4,668 | 117 | - | 45,379 |
| Doubtful debtors expense / (release) | 640 | 496 | 1,024 | (239) | - | 1,921 |

| Three months ended 30 September 2001 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Gross revenues | 9,827 | 82,236 | 10,068 | 2,085 | - | 104,216 |
| Intra-group revenues | (7,591) | (3,002) | (6,488) | (2,077) | - | (19,158) |
| Net revenues | 2,236 | 79,234 | 3,580 | 8 | - | 85,058 |
| Segment income / (loss) | 2,403 | (6,859) | 328 | (1,980) | (694) | (6,802) |
| Capital expenditures | 1,443 | 5,968 | 2,207 | 142 | - | 9,760 |
| Depreciation and amortisation | 2,434 | 11,447 | 1,232 | 20 | - | 15,133 |
| Doubtful debtors expense / (release) | 71 | (6,877) | (1,076) | 260 | - | (7,622) |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 6: Segment information (continued)

| Nine months ended 30 September 2001 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Gross revenues | 30,659 | 295,863 | 32,721 | 3,050 | - | 362,293 |
| Intra-group revenues | (23,109) | (5,026) | (27,048) | (2,077) | - | (57,260) |
| Net revenues | 7,550 | 290,837 | 5,673 | 973 | - | 305,033 |
| Segment income / (loss) | 9,013 | (6,277) | 194 | (419) | 1,195 | 3,706 |
| Capital expenditures | 4,679 | 16,491 | 6,535 | 674 | - | 28,379 |
| Depreciation and amortisation | 7,425 | 31,904 | 4,695 | 87 | - | 44,111 |
| Doubtful debtors expense / (release) | 474 | (7,858) | (2,067) | 163 | - | (9,288) |

| As at 30 September 2002 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Segment total assets | 525,130 | 702,457 | 118,682 | 10,769 | (352,568) | 1,004,470 |
| Associates | - | 5,619 | - | - | - | 5,619 |
| Total assets | 525,130 | 708,076 | 118,682 | 10,769 | (352,568) | 1,010,089 |
| Segment liabilities | 19,665 | 131,524 | 29,180 | 3,930 | (31,440) | 152,859 |
| Unallocated liabilities | | | | | | 117,472 |
| Total liabilities | | | | | | 270,331 |

| As at 31 December 2001 | RAO UES | Energos | Hydro and thermal generating stations | Construction | Consolidation adjustments | Total |
|---|---|---|---|---|---|---|
| Segment total assets | 407,628 | 731,168 | 122,186 | 10,763 | (231,518) | 1,040,227 |
| Associates | - | 5,365 | - | - | - | 5,365 |
| Total assets | 407,628 | 736,533 | 122,186 | 10,763 | (231,518) | 1,045,592 |
| Segment liabilities | 20,754 | 146,543 | 27,937 | 3,582 | (27,695) | 171,121 |
| Unallocated liabilities | | | | | | 151,023 |
| Total liabilities | | | | | | 322,144 |

All items that reconcile segment income or loss to the Group's net income or loss are not allocatable except for the Group's share of income or loss from associates which is attributable to the Energos segment.

***Secondary reporting segments - geographical segments.*** The Group operates in seven geographical areas within the Russian Federation. These geographical areas correspond to the regions established for system operation. Group entities have been aggregated within these geographical areas based on the area where their assets are located, with the exception of the RAO UES segment. The transmission grid, owned by RAO UES and FSK, is located throughout the territory of the Russian Federation, but is recorded in the books of these without details of geographic location. Accordingly, it is not practicable to split the assets of RAO UES on a geographical basis. The Group's assets generate revenues primarily within the geographical region where they are located.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 6: Segment information (continued)

| | Revenue | | | |
|---|---|---|---|---|
| | **Three months ended 30 September 2002** | **Nine months ended 30 September 2002** | **Three months ended 30 September 2001** | **Nine months ended 30 September 2001** |
| RAO UES segment | 13,729 | 40,628 | 9,827 | 30,659 |
| Centre | 31,886 | 99,133 | 28,386 | 95,001 |
| North-West | 9,021 | 36,654 | 6,833 | 33,183 |
| Urals | 25,372 | 81,346 | 21,901 | 76,272 |
| Siberia | 12,589 | 42,618 | 11,264 | 40,038 |
| Middle Volga | 10,084 | 33,725 | 9,105 | 31,082 |
| East | 10,701 | 35,203 | 8,797 | 29,903 |
| South | 8,553 | 25,935 | 8,103 | 26,155 |
| | 121,935 | 395,242 | 104,216 | 362,293 |
| Consolidation adjustments | (24,821) | (66,818) | (19,158) | (57,260) |
| Total | 97,114 | 328,424 | 85,058 | 305,033 |

| | Total assets | | Capital expenditures | | | |
|---|---|---|---|---|---|---|
| | **30 September 2002** | **31 December 2001** | **Three months ended 30 September 2002** | **Nine months ended 30 September 2002** | **Three months ended 30 September 2001** | **Nine months ended 30 September 2001** |
| RAO UES segment | 525,130 | 407,628 | 2,092 | 5,437 | 1,443 | 4,679 |
| Centre | 240,974 | 254,025 | 2,318 | 6,330 | 1,494 | 5,806 |
| North-West | 67,569 | 70,262 | 1,128 | 2,713 | 964 | 3,786 |
| Urals | 187,916 | 193,830 | 1,938 | 4,390 | 1,572 | 3,401 |
| Siberia | 117,174 | 121,913 | 1,399 | 3,456 | 1,332 | 3,218 |
| Middle Volga | 64,518 | 68,641 | 402 | 1,279 | 288 | 1,143 |
| East | 95,718 | 96,282 | 2,029 | 5,231 | 1,683 | 4,153 |
| South | 63,658 | 64,529 | 1,031 | 2,392 | 984 | 2,193 |
| | 1,362,657 | 1,277,110 | 12,337 | 31,228 | 9,760 | 28,379 |
| Consolidation adjustments | (352,568) | (231,518) | - | - | - | - |
| Total | 1,010,089 | 1,045,592 | 12,337 | 31,228 | 9,760 | 28,379 |

Nizhnovenergo was reclassified from the Center geographical region to the Middle Volga geographical region in accordance with the manner in which the Group reports geographical segments internally to top management. Comparative figures for these segments have been adjusted accordingly.

## Note 7: Related parties

***Associates.*** The following transactions were carried out with associates, the majority of which are based on tariffs set by the FEC:

| | **Three months ended 30 September 2002** | **Nine months ended 30 September 2002** | **Three months ended 30 September 2001** | **Nine months ended 30 September 2001** |
|---|---|---|---|---|
| Transmission fee income | 152 | 488 | 123 | 396 |
| Electricity revenues | 78 | 147 | 28 | 47 |
| Rental fee income | 10 | 29 | 12 | 33 |
| Purchased power expense | 62 | 131 | 105 | 175 |

**Note 7: Related parties (continued)**

***Directors' compensation.*** Compensation is paid to members of the management board of RAO UES for their services in full time management positions. The compensation is made up of a contractual salary, non-cash benefits, and a performance bonus depending on results for the year according to Russian statutory financial statements. The compensation is approved by the board of directors. Discretionary bonuses are also payable to members of the management board, which are approved by the Chairman of the managing board according to his perception of the value of their contribution.

No fees, compensation or allowances are paid to members of the board of directors of RAO UES for their services in that capacity, or for attending board meetings.

Salary and bonuses paid to members of the management board by RAO UES, included in wages and payroll taxes in the statement of operations, amounted to RR 16 million and RR 60 million for the three and nine months ended 30 September 2002, respectively (three months ended 30 September 2001: RR 16 million, nine months ended 30 September 2001: RR 42 million). In addition, certain amounts were paid to members of the management board of RAO UES by RAO UES' subsidiaries in respect of management duties at those companies.

***Eurofinance.*** A member of the management board of RAO UES was elected to the Supervisory Board of Eurofinance in 2000. RAO UES Board of Directors did not authorise his participation in the managing bodies of Eurofinance; as a result he was not entitled to and did not participate in Eurofinance's Supervisory Board. Further, he was not re-elected to Eurofinance's Supervisory Board in April 2002 and, consequently, Eurofinance is not a related party of the Group.

The commission and the interest charged by Eurofinance to RAO UES was RR 7 million for the three months ended 31 March 2002 (for the three months ended 31 March 2001: RR 42 million). Commission and interest approximate market rates. As at 31 March 2002, when Eurofinance ceased to be a related party, RAO UES held RR 664 million of promissory notes of Eurofinance (31 December 2001: nil). The balance outstanding due to RAO UES from Eurofinance was RR nil as at 31 March 2002 (31 December 2001: RR 315 million).

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 8: Property, plant and equipment

**Appraised value or cost**

| | Electricity and heat generation | Electricity transmission | Electricity distribution | Heating networks | Construction in progress | Other | Total |
|---|---|---|---|---|---|---|---|
| Opening balance as at 31 December 2001 | 655,396 | 205,477 | 654,891 | 117,686 | 232,262 | 224,010 | 2,089,722 |
| Additions | 739 | 34 | 545 | 37 | 27,774 | 2,099 | 31,228 |
| Transfers | 12,738 | 4,373 | 5,479 | 621 | (28,556) | 5,345 | - |
| Disposals | (2,006) | (53) | (1,913) | (283) | (2,748) | (3,614) | (10,617) |
| Closing balance as at 30 September 2002 | 666,867 | 209,831 | 659,002 | 118,061 | 228,732 | 227,840 | 2,110,333 |

**Accumulated depreciation (including impairment)**

| | Electricity and heat generation | Electricity transmission | Electricity distribution | Heating networks | Construction in progress | Other | Total |
|---|---|---|---|---|---|---|---|
| Opening balance as at 31 December 2001 | (400,889) | (105,528) | (451,112) | (80,147) | (63,426) | (150,763) | (1,251,865) |
| Charge for the period | (11,274) | (5,337) | (12,226) | (3,185) | - | (13,357) | (45,379) |
| Transfers | (4,684) | (1,585) | (2,378) | (215) | 10,904 | (2,042) | - |
| Disposals | 1,535 | 53 | 1,840 | 268 | 1,375 | 3,358 | 8,429 |
| Closing balance as at 30 September 2002 | (415,312) | (112,397) | (463,876) | (83,279) | (51,147) | (162,804) | (1,288,815) |
| Net book value as at 30 September 2002 | 251,555 | 97,434 | 195,126 | 34,782 | 177,585 | 65,036 | 821,518 |
| Net book value as at 31 December 2001 | 254,507 | 99,949 | 203,779 | 37,539 | 168,836 | 73,247 | 837,857 |

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

Depreciation is charged once an asset is available for service.

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

A portion of fixed asset additions has been settled through mutual settlement, barter and other non-cash means. Non-cash transactions in respect of property, plant and equipment are:

| | Nine months ended 30 September 2002 | Nine months ended 30 September 2001 |
|---|---|---|
| Non-cash acquisitions | 7,866 | 7,623 |
| Non-cash proceeds from the sale of property, plant and equipment | 588 | 2,833 |

The majority of the non-cash purchase acquisitions related to construction in progress.

***Impairment***. For the period ended 30 September 2002, management has assessed the adequacy of its existing impairment provision and concluded that the amount is appropriate. Accordingly, no further adjustment has been recorded. The impairment provision included in the accumulated depreciation balance as at 30 September 2002 is RR 744,448 million.

Management has used various assumptions in the calculation of the recoverable value of property, plant and equipment. Variations in these assumptions may give rise to a significantly different amount for the impairment provision. In management's opinion, the existing provision represents the best estimate of the impact of impairment as a result of the current economic conditions in the Russian Federation.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 9: Investments in associates**

The Group has investments in the following associated enterprises, both of which are incorporated and operate in Russia:

| | 30 September 2002 | | 31 December 2001 | |
|---|---|---|---|---|
| **Enterprise name** | **% Ownership** | **% Voting** | **% Ownership** | **% Voting** |
| Bashkirenergo | 21.3 | 22.3 | 21.3 | 22.3 |
| Novosibirskenergo | 14.2 | 16.9 | 14.2 | 16.9 |

| | Bashkir-energo | Novosibirsk-energo | Total |
|---|---|---|---|
| Carrying value as at 31 December 2001 | 3,962 | 1,403 | 5,365 |
| Share of income of associates | 330 | (46) | 284 |
| Share of associates' tax (charge) / benefit | (67) | 37 | (30) |
| Carrying value as at 30 September 2002 | 4,225 | 1,394 | 5,619 |

The Group's interest in associated enterprises is shown in the consolidated interim balance sheet at its proportion of net assets attributable to the Group at the date of transfer from the Russian Federation plus the Group's share of post-acquisition earnings and losses and other changes in the enterprise's equity, restated in terms of purchasing power of the Russian Rouble as at 30 September 2002.

**Note 10. Other non-current assets**

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Available-for-sale investments | 8,268 | 15,257 |
| Advances to contractors | 9,275 | 6,901 |
| Restructured trade receivables (Net of allowance for doubtful debtors of RR 5,321 million as at 30 September 2002 and RR 10,958 million as at 31 December 2001) | 2,069 | 4,266 |
| Other | 365 | 1,011 |
| | 19,977 | 27,435 |

**Note 11: Cash and cash equivalents**

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Cash at bank and in hand | 10,489 | 13,832 |
| Foreign currency accounts | 585 | 127 |
| | 11,074 | 13,959 |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 12: Accounts receivable and prepayments

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Trade receivables (Net of allowance for doubtful debtors of RR 49,883 million as at 30 September 2002 and RR 54,921 million as at 31 December 2001) | 35,240 | 49,020 |
| Value added tax recoverable | 19,332 | 18,072 |
| Advances to suppliers and prepayments | 13,835 | 11,121 |
| Receivables from associates | 820 | 607 |
| Other receivables (Net of allowance for doubtful debtors of RR 7,054 million as at 30 September 2002 and RR 6,516 million as at 31 December 2001) | 21,517 | 20,856 |
| | 90,744 | 99,676 |

Management has determined the allowance for doubtful debtors based on specific customer identification, customer payment trends, subsequent receipts and settlements and analyses of expected future cash flows. Based on the expected collection rate, discount rates of 20 - 29 percent have been used in the estimate of fair value of future cash flows. The effects of discounting are reflected in the doubtful debtor allowance and expense. The management of the Group believes that Group entities will be able to realise the net receivable amount through direct collections and other non-cash settlements.

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). The loss on restructuring is included in doubtful debtors expense.

For the nine months ended 30 September 2002, approximately 21 percent (the nine months ended 30 September 2001: 26 percent) of the settlements of the Group's accounts receivables and prepayments were made via non-cash settlements.

## Note 13: Inventories

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Materials and supplies | 25,293 | 25,836 |
| Fuel production stocks | 14,624 | 13,157 |
| Other inventories | 1,683 | 2,335 |
| | 41,600 | 41,328 |

The above inventory balances are recorded net of an obsolescence provision of RR 2,230 million and RR 2,767 million as at 30 September 2002 and 31 December 2001, respectively.

At 30 September 2002 and 31 December 2001, the inventory balance included RR 9,906 million and RR 11,440 million, respectively, of inventory pledged as collateral under loan agreements.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 14: Shareholders' equity

***Share Capital***

| | Number of shares issued and fully paid | 30 September 2002 | 31 December 2001 |
|---|---|---|---|
| Ordinary shares | 41,041,753,984 | 141,419 | 141,419 |
| Preference shares | 2,075,149,384 | 7,354 | 7,354 |
| | | 148,773 | 148,773 |

The authorised number of ordinary and preference shares are 47,509,289,488 and 2,075,149,384 respectively, both with a nominal value per share of 0.5 Russian Roubles. All authorised preference shares have been issued. The value of the share capital is stated in terms of the purchasing power of the Russian Rouble at the consolidated interim balance sheet date.

***Ordinary shares and preference shares.*** Preference shares have no right of conversion or redemption, but are entitled to a minimum annual dividend of 10 percent of net statutory profit. 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. In liquidation preference shareholders are first paid any declared unpaid dividends and then the nominal value of the shares ("liquidation value"). Following this, preference shareholders participate equally in the distribution of remaining assets with ordinary shareholders.

On 7 May 1998 the law number 74-FZ "On the Peculiarities of Share Distribution of UES" was signed by the President of the Russian Federation. This law stipulates that a minimum of 51 percent of voting shares in RAO UES be held by the government of the Russian Federation and that foreign investors are limited to owning not more than 25 percent of the voting shares of the company. The practical implications of this foreign ownership limitation for RAO UES or its shareholders are unclear.

***Dividends.*** The annual statutory accounts of the parent company, RAO UES, are the basis for the annual profit distribution and other appropriations. The specific Russian legislation identifies the basis as the net profit for the year. For 2001, the statutory profit for the parent company, RAO UES, as reported in the published statutory reporting forms, was RR 12,777 million (unrestated). 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 these financial statements.

A dividend was declared in respect of the year ended 31 December 2001 of RR 0.0287 per ordinary share (RR 0.0260 per ordinary share unrestated) (in 2001 in respect of 2000: RR 0.0265 per ordinary share, RR 0.0200 per ordinary share unrestated) and RR 0.1308 per preference share (RR 0.1185 per preference share unrestated) (in 2001 in respect of 2000: RR 0.0968 per preference share, RR 0.0738 per preference share unrestated).

***Fair value reserve.*** The fair value reserve, relating to the changes in the fair value of available-for-sale investments, at 30 September 2002 was a debit of RR 3,024 million (31 December 2001: RR 2,974 million), and is included in retained earnings and fair value reserve.

***Treasury shares***. The Group periodically purchases and sells treasury shares. Treasury shares as at 30 September 2002 represent 400,938,211 (31 December 2001: 399,883,789) ordinary shares and 17,701,098 (31 December 2001: 17,587,446) preference shares.

| | Cost as at 31 December 2001 | Purchases and disposals, net | Cost as at 30 September 2002 |
|---|---|---|---|
| Ordinary shares | 674 | 6 | 680 |
| Preference shares | 57 | - | 57 |
| | 731 | 6 | 737 |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 15: Minority interest**

| | Nine months ended 30 September 2002 | Nine months ended 30 September 2001 |
|---|---|---|
| Opening balance, beginning of year | 211,308 | 196,480 |
| Adoption of IAS 39 (see Note 3) | - | 1,045 |
| Change in fair value of available-for-sale investments | (629) | - |
| Share of net result | (2,580) | 9,597 |
| Acquisitions and changes in Group structure | 977 | (153) |
| Dividends | (1,340) | (1,167) |
| Closing balance, end of period | 207,736 | 205,802 |

**Note 16: Profit tax**

***Profit tax expense***

| | Three months ended 30 September 2002 | Nine months ended 30 September 2002 | Three months ended 30 September 2001 | Nine months ended 30 September 2001 |
|---|---|---|---|---|
| Current profit tax charge | (3,539) | (15,363) | (3,668) | (16,276) |
| Deferred profit tax benefit / (charge) | 13,323 | 31,992 | 2,163 | (5,917) |
| Share of associate profit tax (charge) / benefit (see Note 9) | (96) | (30) | 279 | (92) |
| Effect of tax rate reduction on deferred taxes | - | - | 33,661 | 33,661 |
| **Total profit tax benefit** | 9,688 | 16,599 | 32,435 | 11,376 |

During the year ended 31 December 2001, most members of the Group were subject to profit tax rates of 35 percent on taxable profit. As a result of changes in the Russian tax legislation which were enacted in August 2001, effective 1 January 2002, the profit tax rate has been changed to 24 percent.

In the context of Russian tax legislation, tax losses in different Group companies may not be relieved against taxable profit of other Group companies. Accordingly profit tax may accrue even where there is a net consolidated tax loss.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 16: Profit tax (continued)**

Net income before profit tax for financial reporting purposes is reconciled to profit tax expenses as follows:

| | Three months ended 30 September 2002 | Nine months ended 30 September 2002 | Three months ended 30 September 2001 | Nine months ended 30 September 2001 |
|---|---|---|---|---|
| **(Loss) / income before profit tax** | (13,771) | 2,087 | 7,716 | 30,950 |
| Theoretical profit benefit / (charge) at an average statutory tax rate of 24 percent (2001: 35 percent) | 3,305 | (501) | (2,701) | (10,833) |
| Tax effect of items which are not deductible or assessable for taxation purposes: | | | | |
| Tax interest and penalties | (291) | (1,911) | (902) | (3,180) |
| Non-temporary elements of monetary gains / losses | (2,114) | (18,349) | (2,622) | (33,319) |
| Doubtful debtors (expense) / release | (220) | (461) | 2,265 | 2,849 |
| Other non-deductible expenses, net | (422) | (5,540) | (1,083) | (3,463) |
| Inflation effect on deferred tax balance at beginning of the period | 943 | 8,186 | 1,026 | 13,040 |
| Effect of tax rate reduction on deferred taxes | - | - | 33,661 | 33,661 |
| Effect of statutory revaluation on tax base | 8,643 | 40,184 | (43) | 6,915 |
| Non-recognised deferred tax assets movements | 652 | (3,353) | 4,397 | 8,803 |
| Other | (808) | (1,656) | (1,563) | (3,097) |
| **Total profit tax benefit** | 9,688 | 16,599 | 32,435 | 11,376 |

The non-temporary elements of monetary gains and losses reflect the effect of the theoretical tax charge on inflation with respect to non-monetary items of a non-temporary nature (e.g. shareholders' equity, minority interests and deferred profit tax liabilities).

As described in Note 1, RAO UES established a wholly-owned subsidiary, Federal Grid Company ("FSK"), to hold and manage the high voltage transmission assets. The property, plant and equipment transferred to FSK by RAO UES was revalued at market values. This valuation is used for Russian statutory and tax accounting purposes. Consequently, included within the effect of statutory revaluation for the period to 30 September 2002 is a deferred tax benefit of RR 13,020 million in respect of the revaluation of assets transferred to FSK prior to that date.

***Deferred profit tax.*** Differences between IAS and Russian statutory taxation regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. Deferred profit tax assets and liabilities are measured at 24 percent, the rate applicable when the asset or liability will reverse.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 16: Profit tax (continued)

### Deferred profit tax liability

| | 30 September 2002 | Movement for the period | 31 December 2001 |
|---|---|---|---|
| Trade receivables | (1,455) | (2,261) | 806 |
| Property, plant and equipment | 50,163 | (25,459) | 75,622 |
| Accounts payable | 5,732 | (4,872) | 10,604 |
| Inventories | (202) | 350 | (552) |
| Other | 515 | 250 | 265 |
| | 54,753 | (31,992) | 86,745 |
| Deferred profit tax assets | 15,254 | 3,353 | 11,901 |
| Less non-recognised deferred tax asset | (15,254) | (3,353) | (11,901) |
| | 54,753 | (31,992) | 86,745 |

Revisions to the Russian tax legislation were approved in 2002 which provide clarification of the tax law enacted as at 1 January 2002. In accordance with these revisions, statutory revaluations on property, plant and equipment of up to 30 percent of the statutory carrying value as at 1 January 2001 are deductible for profit tax purposes through depreciation. Previous revisions of the profit tax legislation did not provide clear guidance regarding the deductibility of these revaluations. Consequently, the Group had not recognised the impact resulting from these statutory revaluations until these clarifications were provided in 2002. The effect of the revaluations is to increase the tax base of property, plant and equipment, thereby decreasing the temporary differences between their carrying value for financial and tax purposes.

A deferred profit tax asset has not been recognised for the Group's unused profit tax losses either as at 30 September 2002 or 31 December 2001.

## Note 17: Non-current debt

| | Currency | Effective interest rate | Due | 30 September 2002 | 31 December 2001 |
|---|---|---|---|---|---|
| Central and regional government loans | RR | 21.0% - 35.0% | 2002 and thereafter | 2,307 | 2,558 |
| Central and regional government loans | US$ | LIBOR + 3.0% | 2003 and thereafter | 2,536 | 2,484 |
| Eurobond | US$ | 8.0% | 2002 | 3,479 | 5,020 |
| Bonds issued by subsidiaries | RR / US$ * | 8.0% | 2003 | 4,183 | 4,102 |
| Bonds – RAO UES | RR / US$ * | 7.0% | 2002-2003 | 3,373 | 3,549 |
| Bank debt from foreign banks | Euro | EURIBOR + 4.1% | 2002-2005 | 2,306 | - |
| Bank debt from foreign banks | US$ | LIBOR + 3.5% | 2002 and thereafter | 1,245 | 1,496 |
| Bank debt from Russian banks | Euro | 8.0% - 10.0% | 2002 and thereafter | 54 | 171 |
| Bank debt from Russian banks | RR ** | 19.0% - 35.0% | 2002 and thereafter | 16,409 | 26,887 |
| Other long-term debt | | | | 775 | 719 |
| Total non-current debt | | | | 36,667 | 46,986 |
| Less: current portion of non-current debt | | | | (26,814) | (21,134) |
| | | | | 9,853 | 25,852 |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 17: Non-current debt (continued)**

* For both interest payments and the redemption of these bonds, the Russian Rouble amount is adjusted to reflect any currency movements between the Russian Rouble and the US$ from the date of issuance of the bonds.

** This category includes the loan described in Note 1, whereby in December 2001 the Group received a RR 26,500 million loan from Sberbank. The loan is payable in equal quarterly instalments through 2004. The annual interest rate varies and is 19 percent if RAO UES maintains a volume of monthly transactions in its cash account with Sberbank of greater than RR 800 million, and 21.5% if the volume of transactions is below RR 800 million.

| *Maturity table* | 30 September 2002 | 31 December 2001 |
|---|---|---|
| **Due for repayment** | | |
| Between one and two years | 6,488 | 18,692 |
| Between two and five years | 1,418 | 4,099 |
| After five years | 1,947 | 3,061 |
| | 9,853 | 25,852 |

Except as otherwise noted, the majority of the above bank debt is obtained at a variable interest rate.

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

The Group has not entered into any hedging arrangements in respect of its foreign currency obligations or interest rate exposures.

At the interim balance sheet date, the estimated fair value of total non-current debt (including the current portion) was RR 36,182 million, which is estimated by discounting the future contractual cash flows at the estimated current market interest rates available to the Group for similar financial instruments.

**Note 18: Other non-current liabilities**

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Taxes payable | 28,393 | 25,233 |
| Trade payables and other creditors | 2,523 | 6,037 |
| Other | 1,392 | 1,691 |
| Total other non-current liabilities | 32,308 | 32,961 |
| Less: current portion of restructured liabilities | (6,757) | (8,701) |
| | 25,551 | 24,260 |

In accordance with Government Resolution No. 1002 dated 3 September 1999, most members of the Group have restructured taxes including fines and interest to be repaid over a period of up to 10 years. Non-adherence to certain payment schedules could result in the gross amount of taxes payable including fines and interest becoming due on demand. Additionally, a number of Group entities have restructured trade payables to be repaid over a period of up to five years. Based on the contractual dates of repayment, discount rates of 21 – 24 percent have been used in the estimate of the fair value of these liabilities.

The discounting of the restructured payable amounts gives rise to a gain, as disclosed in Note 23.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 18: Other non-current liabilities (continued)**

The maturity profile is as follows:

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Between one and two years | 7,171 | 10,959 |
| Between two and five years | 10,656 | 7,822 |
| After five years | 7,724 | 5,479 |
| | 25,551 | 24,260 |

**Note 19: Current debt and current portion of non-current debt**

| | Effective interest rate | 30 September 2002 | 31 December 2001 |
|---|---|---|---|
| Current debt | 14.0% - 30.0% | 26,052 | 17,292 |
| Current portion of non-current debt | | 26,814 | 21,134 |
| | | 52,866 | 38,426 |

**Note 20: Accounts payable and accrued charges**

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Trade payables | 57,239 | 61,316 |
| Accrued liabilities and other creditors | 26,356 | 31,140 |
| Bills of exchange payable | 1,864 | 859 |
| Dividends payable | 1,673 | 960 |
| Payables to associates | 138 | 72 |
| Current portion of trade payables and other creditors restructured to long-term | 1,716 | 3,811 |
| | 88,986 | 98,158 |

For the nine months ended 30 September 2002, approximately 18 percent (nine months ended 30 September 2001: 29 percent) of the Group's settlements of accounts payable and accrued charges were settled via non-cash settlements.

Restructured trade payables which are payable more than one year from the balance sheet date are reflected within other non-current liabilities as described in Note 18. The details of the gain on restructuring the trade payables is included in Note 23.

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

## Note 21: Taxes payable

| | 30 September 2002 | 31 December 2001 |
|---|---|---|
| Value added tax | 10,708 | 13,519 |
| Fines and interest | 9,034 | 14,012 |
| Profit tax | 2,957 | 3,456 |
| Property tax | 2,905 | 2,024 |
| Employee taxes | 2,800 | 2,984 |
| Turnover taxes | 2,188 | 6,487 |
| Other taxes | 2,691 | 1,331 |
| Current portion of taxes restructured to long-term | 5,039 | 4,890 |
| | 38,322 | 48,703 |

Included in the balances above are certain amounts which only become payable to the authorities when the underlying receivables balance is recovered, namely:

- in Value added tax – RR 8,358 million (31 December 2001: RR 9,905 million); and
- in Turnover taxes – RR 150 million (31 December 2001: RR 764 million).

Substantially all accrued taxes above, excluding the amounts which have been restructured, incur interest at the refinance rate of the Central Bank of the Russian Federation. As at 30 September 2002 the refinance rate was 21 percent (31 December 2001: 25 percent). Interest does not accrue on tax penalties and interest.

Restructured taxes, including fines and interest, which are payable more than one year from the balance sheet date are reflected within other non-current liabilities as described in Note 18. The gain in restructuring the taxes payable is included in Note 23.

For the nine months ended 30 September 2002, approximately 1 percent (nine months ended 30 September 2001: 3 percent) of the Group's settlements of taxes payable were settled via non-cash settlements.

## Note 22: Governmental assistance

During the three and nine months ended 30 September 2002 the Federal government of the Russian Federation and regional governments gave financial assistance equal to RR 1,546 million and RR 3,089 million, respectively (three months ended 30 September 2001: RR 879 million; nine months ended 30 September 2001: RR 2,181 million), for certain entities in the Far East region and RR 272 million and RR 814 million for the three and nine months ended 30 September 2002, respectively (three months ended 30 September 2001: RR 212 million; nine months ended 30 September 2001: RR 734 million) for other Group entities. The assistance in respect of these periods has been recorded as revenue to the statement of operations.

## Note 23: Monetary effects and financing items

| | Three months ended 30 September 2002 | Nine months ended 30 September 2002 | Three months ended 30 September 2001 | Nine months ended 30 September 2001 |
|---|---|---|---|---|
| Gain on restructuring accounts payable and taxes payable | 28 | 6,906 | 16,830 | 18,276 |
| Monetary gain | 1,236 | 6,982 | 161 | 13,678 |
| Imputed interest income | 220 | 1,081 | - | - |
| Interest expense | (4,505) | (13,708) | (2,162) | (4,360) |
| Foreign exchange loss | (124) | (1,582) | (118) | (621) |
| | (3,145) | (321) | 14,711 | 26,973 |

(in millions of Russian Roubles expressed in terms of the purchasing power of the Russian Rouble as at 30 September 2002, except as disclosed)

**Note 23: Monetary effects and financing items (continued)**

The discounting of restructured payable amounts gives rise to gains. The discount is amortized over the period of the restructuring as an expense; RR 2,205 million and RR 6,946 million of such amortisation was included in interest expense for the three and nine months ended 30 September 2002, respectively (three months ended 30 September 2001: RR 501 million; nine months ended 30 September 2001: RR 993 million). Further information on the restructuring of accounts payable and taxes payable is contained in Notes 18, 20 and 21.

Imputed interest income is recorded as a result of the amortisation of the discount recognised in December 2001 on loans issued at below market interest rates. These loans issued are further discussed in Note 1.

**Note 24: Earnings per share**

| | Three months ended 30 September 2002 | Nine months ended 30 September 2002 | Three months ended 30 September 2001 | Nine months ended 30 September 2001 |
|---|---|---|---|---|
| Weighted average number of ordinary shares outstanding (thousands) | 41,041,754 | 41,041,754 | 41,041,754 | 41,041,754 |
| Weighted average number of preference shares outstanding (thousands) | 2,075,149 | 2,075,149 | 2,075,149 | 2,075,149 |
| Adjusted for weighted average number of treasury shares (thousands) | (418,272) | (418,140) | (418,015) | (418,256) |
| Weighted average number of ordinary and preference shares outstanding (thousands) | 42,698,631 | 42,698,763 | 42,698,888 | 42,698,647 |
| Net income | 3,243 | 21,266 | 31,751 | 32,729 |
| **Earnings per ordinary and preference share – basic and diluted (in Russian Roubles)** | 0.08 | 0.50 | 0.74 | 0.77 |

**Note 25: Commitments**

***Sales commitments.*** The Group entered into two export contracts with Fortum Power and Heat Oy ("Fortum"), a shareholder of Lenenergo, and one contract with Pohjolan Voima Oy. One contract with Fortum is for the supply of a minimum of 1.6 million MWh of electricity per year, at prices between Euro 12.15 and Euro 20.50 per MWh. This contract expires at the end of 2007. The second contract with Fortum is for the supply of between 0.35 million and 0.50 million MWh of electricity per year at Euro 17.25 per MWh, through to the end of 2008.

The contract with Pohjolan Voima Oy is for the supply of a minimum of 2.7 million MWh of electricity per year, at prices between Euro 16.20 and Euro 16.70 per MWh. This contract expires at the end of 2004.

***Fuel commitments.*** Group entities have numerous fuel contracts. These fuel contracts represent less than the total annual fuel requirement of the Group. Additional fuel requirements are purchased through short-term agreements and on a spot basis from a variety of suppliers. Prices under the Group's natural gas and coal contracts are generally determined by reference to base amounts adjusted to reflect provisions for changes in regulatory prices, published inflation indices and current market prices.

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

***Capital commitments.*** Future capital expenditures for which contracts have been signed amount to RR 35,503 million at 30 September 2002 and RR 42,068 million at 31 December 2001.

## Note 26: Contingencies

***Political environment.*** The operations and earnings of Group entities continue, from time to time and in varying degrees, to be affected by political, legislative, fiscal and regulatory developments, including those related to environmental protection, in 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 for those risks for which it does not have insurance.

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

***Taxation.*** Russian tax legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result, transactions may be challenged by tax authorities and the Group's entities may be assessed additional taxes, penalties and interest, which can be significant. Periods remain open to review by the tax and customs authorities with respect to tax liabilities for three years.

***Environmental matters.*** Group entities and their predecessor entities have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. 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, other than any amounts which have been accrued in the accompanying consolidated interim balance sheet.

## Note 27: Financial instruments and financial risk factors

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

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

***Foreign exchange risk.*** The Group primarily operates within the Russian Federation, with minimal exports of electricity. The majority of the Group's purchases are denominated in Russian Roubles. The major concentration of foreign exchange risk is in relation to foreign currency denominated sales and purchase commitments, as disclosed in Note 25, and foreign currency denominated debt and Russian Rouble denominated debt linked to US Dollar currency movements, as disclosed in Note 17.

***Interest rate risk.*** As discussed in Note 17, except as otherwise noted, the majority of interest rates on remaining debt are variable. Interest rates on Russian Rouble denominated debt are reset when the underlying Central Bank re-financing rate changes. Assets are generally non-interest bearing.

## Note 28: Subsequent events

***Bonds.*** In October 2002, the Group issued 3 million bonds with a nominal value of RR 1,000 per bond. The bonds yield an effective interest of 15 percent and mature in October 2005. Interest is payable semi-annually for the first two years, with a final interest payment due on the bond maturity date.

***Loan.*** After the balance sheet date, the Group obtained a US$ 70 million loan from the European Bank for Reconstruction and Development ("EBRD"). The stated interest rate for the loan is LIBOR plus 4.25%. Interest and a portion of principal are repayable semi-annually up to the expiry of the loan in 2007.