

Open joint stock company Lenenergo

Consolidated financial statements
prepared in accordance with
International Financial Reporting Standards

For the year ended 31 December 2010

Ernst & Young

Open joint stock company Lenenergo

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Consolidated financial statements

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Independent auditors' report

To the Shareholders and Board of Directors of OJSC Lenenergo

We have audited the accompanying consolidated financial statements of OJSC Lenenergo and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2010, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

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

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

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



Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

22 April 2011
St. Petersburg, Russia

OJSC LENENERGO
Consolidated statement of financial position
as at 31 December 2010
(in thousands of Russian Rubles)

| | Note | 31 December 2010 | 31 December 2009 |
|--|------|---------------------|---------------------|
| ASSETS | | | |
| Non-current assets | | | |
| Intangible assets | 4 | 601,184 | 696,275 |
| Property, plant and equipment | 5 | 83,621,575 | 73,332,231 |
| Advances for construction of property, plant and equipment | 6 | 2,317,079 | 4,135,536 |
| Available-for-sale investments | 7 | 30,000 | 525,913 |
| Other non-current assets | 8 | 440,430 | 272,310 |
| Total non-current assets | | 87,010,268 | 78,962,265 |
| Current assets | | | |
| Cash and cash equivalents | 9 | 653,068 | 2,948,801 |
| Accounts receivable | 10 | 1,493,998 | 1,332,425 |
| Inventories | 11 | 452,779 | 361,166 |
| Other current assets | 12 | 3,772,231 | 4,720,628 |
| Total current assets | | 6,372,076 | 9,363,020 |
| TOTAL ASSETS | | 93,382,344 | 88,325,285 |
| EQUITY AND LIABILITIES | | | |
| Equity attributable to equity holders of the parent | | | |
| Ordinary shares | 14 | 4,866,115 | 4,866,115 |
| Preference shares | 14 | 625,603 | 625,603 |
| Share premium | 14 | 5,548,880 | 5,548,880 |
| Other reserves | 14 | 28,659,394 | 29,003,426 |
| Retained earnings | | 10,237,449 | 5,769,857 |
| | | 49,937,441 | 45,813,881 |
| Non-controlling interest | | 23,542 | 19,812 |
| Total equity | | 49,960,983 | 45,833,693 |
| Non-current liabilities | | | |
| Long-term borrowings, net of current portion | 15 | 14,124,851 | 10,073,664 |
| Deferred tax liabilities | 23 | 5,331,912 | 5,283,093 |
| Post-employment benefits liabilities | 16 | 351,312 | 294,536 |
| Other non-current liabilities | 17 | 2,115,966 | 1,274,873 |
| Total non-current liabilities | | 21,924,041 | 16,926,166 |
| Current liabilities | | | |
| Current portion of long-term borrowings | 15 | 1,566,041 | 6,610,816 |
| Trade and other payables | 18 | 4,254,034 | 3,978,577 |
| Income tax payable | | 102,134 | 553,549 |
| Advances received from customers | | 15,575,111 | 14,422,484 |
| Total current liabilities | | 21,497,320 | 25,565,426 |
| Total liabilities | | 43,421,361 | 42,491,592 |
| TOTAL EQUITY AND LIABILITIES | | 93,382,344 | 88,325,285 |

General Director

A.V.Sorochinsky

Chief Accountant

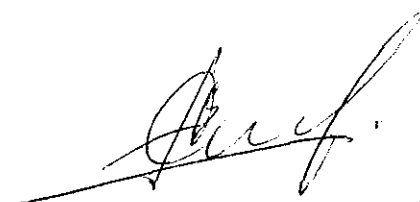
G.V.Kuznetsova

22 April 2011

OJSC LENENERGO
Consolidated income statement
for the year ended 31 December 2010
(in thousands of Russian Rubles, except per share amounts)

| | Note | Year ended 31 December 2010 | Year ended 31 December 2009 |
|---|------|-----------------------------------|-----------------------------------|
| Revenues | 19 | 28,573,575 | 22,800,390 |
| Operating expenses | 20 | <u>(21,440,791)</u> | <u>(18,489,176)</u> |
| Operating profit | | 7,132,784 | 4,311,214 |
| Finance income | 21 | 774,127 | 77,860 |
| Finance expenses | 22 | <u>(1,579,556)</u> | <u>(2,084,428)</u> |
| Foreign exchange loss | | <u>(70,141)</u> | <u>(172,760)</u> |
| Profit before tax | | 6,257,214 | 2,131,886 |
| Income tax (expense)/benefit | 23 | <u>(1,506,793)</u> | 455,486 |
| Net profit for the year | | <u>4,750,421</u> | <u>2,587,372</u> |
| Attributed to: | | | |
| Equity holders | | 4,746,691 | 2,578,481 |
| Non-controlling interest | | 3,730 | 8,891 |
| Earnings per ordinary share – basic and diluted (Russian Rubles) | 24 | 4.66 | 2.53 |
| Earnings per preference share – basic and diluted (Russian Rubles) | 24 | 4.66 | 2.53 |

General Director



A.V.Sorochinsky

Chief Accountant



G.V.Kuznetsova

22 April 2011

OJSC LENENERGO
Consolidated statement of comprehensive income
for the year ended 31 December 2010
(in thousands of Russian Rubles)

| | Note | Year ended 31 December 2010 | Year ended 31 December 2009 |
|--|------|-----------------------------------|-----------------------------------|
| Net profit | | <u>4,750,421</u> | <u>2,587,372</u> |
| Other comprehensive income | | | |
| Available-for-sale investments | | | |
| Unrealized gain | 7 | 161,207 | 221,380 |
| Income tax effect | | <u>(32,241)</u> | <u>(44,276)</u> |
| | | 128,966 | 177,104 |
| Reclassification of unrealized gain reserve on available-for-sale financial assets to income statement | 7 | (532,866) | - |
| Income tax effect | | <u>106,573</u> | <u>-</u> |
| | | (426,293) | - |
| Other comprehensive income, net of tax | | (297,327) | 177,104 |
| Total comprehensive income, net of tax | | <u>4,453,094</u> | <u>2,764,476</u> |
| Attributed to: | | | |
| Equity holders | | 4,449,364 | 2,755,585 |
| Non-controlling interest | | 3,730 | 8,891 |

General Director

A.V.Sorochinsky

Chief Accountant

G.V.Kuznetsova



22 April 2011

OJSC LENENERGO

Consolidated statement of changes in equity
for the year ended 31 December 2010

(in thousands of Russian Rubles)

| | Attributable to equity holders of the parent | | | | | | Non-controlling interest | Total equity |
|---|--|-------------------|------------------|--------------------------|-------------------|-------------------|--------------------------|-------------------|
| | Ordinary shares | Preference shares | Share premium | Other reserves (Note 14) | Retained earnings | Total | | |
| As at 1 January 2009 | 4,866,115 | 625,603 | 5,548,880 | 28,857,780 | 3,302,755 | 43,201,133 | 39,430 | 43,240,563 |
| Profit for the period | - | - | - | - | 2,578,481 | 2,578,481 | 8,891 | 2,587,372 |
| Other comprehensive income, net of tax | - | - | - | 177,104 | - | 177,104 | - | 177,104 |
| Total comprehensive income | - | - | - | 177,104 | 2,578,481 | 2,755,585 | 8,891 | 2,764,476 |
| Release of asset revaluation reserve on disposed property plant and equipment items, net of tax | - | - | - | (31,458) | 31,458 | - | - | - |
| Dividends for 2008 | - | - | - | - | (153,961) | (153,961) | - | (153,961) |
| Acquisition of non-controlling interest | - | - | - | - | 11,124 | 11,124 | (28,509) | (17,385) |
| As at 31 December 2009 | 4,866,115 | 625,603 | 5,548,880 | 29,003,426 | 5,769,857 | 45,813,881 | 19,812 | 45,833,693 |
| Profit for the period | - | - | - | - | 4,746,691 | 4,746,691 | 3,730 | 4,750,421 |
| Other comprehensive income, net of tax | - | - | - | (297,327) | - | (297,327) | - | (297,327) |
| Total comprehensive income | - | - | - | (297,327) | 4,746,691 | 4,449,364 | 3,730 | 4,453,094 |
| Release of asset revaluation reserve on disposed property plant and equipment items, net of tax | - | - | - | (46,705) | 46,705 | - | - | - |
| Dividends for 2009 | - | - | - | - | (325,804) | (325,804) | - | (325,804) |
| As at 31 December 2010 | 4,866,115 | 625,603 | 5,548,880 | 28,659,394 | 10,237,449 | 49,937,441 | 23,542 | 49,960,983 |

General Director

Chief Accountant

22 April 2011



A.V. Sorochinsky

G.V. Kuznetsova

OJSC LENENERGO
Consolidated statement of cash flows
for the year ended 31 December 2010
(in thousands of Russian Rubles)

| | Note | Year ended 31 December 2010 | Year ended 31 December 2009 |
|---|--------|-----------------------------------|-----------------------------------|
| Cash flows from operating activities | | | |
| Profit before tax | | 6,257,214 | 2,131,886 |
| Adjustments to reconcile profit before tax and net cash flow from operating activities: | | | |
| Loss on disposal of property, plant and equipment | | 204,429 | 53,306 |
| Finance income | 21 | (774,127) | (77,860) |
| Depreciation of property, plant and equipment | 5, 20 | 4,430,867 | 3,918,077 |
| Amortization of intangible assets | 4, 20 | 117,487 | 128,249 |
| Impairment of goodwill | 5 | — | 312,833 |
| Impairment of intangible asset | 4, 20 | 37,360 | 139,000 |
| Foreign exchange loss | | 70,141 | 172,760 |
| Finance expenses | 22 | 1,579,556 | 2,084,428 |
| Movements in the provision for impairment of receivables | 13, 20 | 260,548 | 226,052 |
| Impairment loss on finance leases | 20 | 94,242 | 490,894 |
| Non-cash settlement of technological connection revenue | 19 | (4,525,382) | (2,293,975) |
| (Reversal of) Provision for impairment of inventories | 15, 20 | (50,877) | 3,512 |
| Net expense for the defined benefit plan | 16 | 90,418 | 15,317 |
| Net change in provisions | 18 | (107,759) | 178,197 |
| Operating cash flows before changes in working capital | | 7,684,117 | 7,482,676 |
| Decrease in accounts payable and accrued expenses | | (2,253,422) | (2,308,916) |
| Increase in advances received | | 1,152,627 | 4,957,786 |
| Increase/ (decrease) in other non-current liabilities | | 660,468 | (3,517,671) |
| (Increase)/ decrease in trade and other receivables | | (137,332) | 67,965 |
| Increase in inventories | | (40,736) | (129,193) |
| Increase /(decrease) in taxes payable other than income tax | | 21,956 | (232,348) |
| (Increase)/ decrease in other current assets | | (275,750) | 561,835 |
| Cash generated from operations | | 6,811,928 | 6,882,134 |
| Interest paid | | (1,268,358) | (992,572) |
| Income tax paid | | (1,734,459) | (512,102) |
| Pension benefits paid | 16 | (33,642) | (29,094) |
| Net cash generated from operating activities | | 3,775,469 | 5,348,366 |

OJSC LENENERGO

Consolidated statement of cash flows
for the year ended 31 December 2010 (continued)

| | Note | Year ended 31 December 2010 | Year ended 31 December 2009 |
|---|------|-----------------------------------|-----------------------------------|
| Cash flow from investment activities | | | |
| Purchases of property, plant and equipment | | (5,825,998) | (6,335,270) |
| Purchases of intangible assets | | (99,018) | - |
| Proceeds from disposal of property, plant and equipment | | 43 | 3,289 |
| Proceeds from sale of available-for-sale investments | 7 | 657,087 | - |
| Dividends received | | 25,085 | 14,625 |
| Interest received | | 72,977 | 35,117 |
| Net cash used in investment activities | | (5,169,824) | (6,282,239) |
| Cash flow from financing activities | | | |
| Long-term borrowings received | | 8,561,000 | 3,000,000 |
| Settlement of swap agreement | | (4,900,000) | - |
| Repayment of long-term borrowings before maturity | | (3,000,000) | - |
| Acquisition of non-controlling interest | 3 | - | (17,385) |
| Dividends paid | 14 | (325,804) | (153,961) |
| Repayment of finance lease liabilities | | (1,236,574) | (1,444,830) |
| Total cash (used in)/ provided by financing activities | | (901,378) | 1,383,824 |
| Net (decrease)/ increase in cash and cash equivalents | | (2,295,733) | 449,951 |
| Cash and cash equivalents at the beginning of the year | 9 | 2,948,801 | 2,498,850 |
| Cash and cash equivalents at the end of the year | 9 | 653,068 | 2,948,801 |

General Director



A.V.Sorochinsky

Chief Accountant



G.V.Kuznetsova

22 April 2011

OJSC Lenenergo
Notes to the consolidated financial statements
for the year ended 31 December 2010
(in thousands of Russian Rubles)

1. Corporate information

Open joint stock company of Electricity and Electrification Lenenergo (hereinafter “the Company”) was established on 22 January 1993 as the successor of the rights and obligations of state-owned enterprise Electricity and Electrification Industrial Association Lenenergo to the extent specified in the privatization plan dated 22 December 1992. On 1 October 2005, as a result of corporate restructuring through the spin off of electricity generation and sales, heat generation, distribution and sales businesses, the Company retained the electricity transmission networks. Currently the Company provides electricity transmission and network connection services to the consumers.

As at 31 December 2010 and 2009 the Group comprised OJSC Lenenergo and its subsidiaries: CJSC Lenenergospetsremont (100%), CJSC Kurortenergo (98.13%) and CJSC Tsarskoselskaya Energeticheskaya Compania (96.95%) (hereinafter collectively referred to as “the Group”).

The Group currently operates in the city of St. Petersburg and Leningrad Region.

The registered office of the Company is at 1, Constitution Square, 196247, St. Petersburg.

At 31 December 2010 the total number of employees was 6,110 (31 December 2009: 6,285).

Relations with the state and current legislation

The Group is under control of OJSC MRSK Holding (hereinafter “MRSK-Holding”), which as at 31 December 2010 and 2009 owned 45.71% of the Group’s share capital, including 50.31% of voting ordinary shares, and which in turn is controlled by the Russian Federation. The Group provides services to a number of entities controlled by or closely related to the state. In addition, a number of the Group’s suppliers are state-controlled entities.

The government directly influences the Group’s operations through the regulation of wholesale electricity sales by the Federal Service on Tariffs (FST) and of retail electricity sales by Regional Electricity commissions for St. Petersburg and Leningrad Region. The Group sets electricity transmission tariffs for its customers based on regulated tariffs. The Russian Federation, St. Petersburg and Leningrad Region governments’ economic, social and other policies can have a material effect on the Group’s operations.

Financial position and liquidity

As at 31 December 2010 the Group’s current liabilities exceeded its current assets by 15,125,244 (31 December 2009: 16,202,406). The Group’s net profit for 2010 was 4,750,421 (2009: 2,587,372), including 4,746,691 attributed to equity holders of the parent (2009: 2,578,481). In 2010 the Group generated cash flow from operating activities of 3,775,469 (2009: 5,348,366).

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

1. Corporate information (continued)

Financial position and liquidity (continued)

In 2010 the Group experienced a decline in most of liquidity ratios. The current ratio, being current assets divided by current liabilities, decreased from 0.37 as at 31 December 2009 to 0.30 as at 31 December 2010; quick assets ratio, being current receivables and cash (including cash equivalents) divided by current liabilities, decreased from 0.17 as at 31 December 2009 to 0.10 as at 31 December 2010.

In the reporting period the change in the liquidity ratios was affected by the following:

- 1) repayment of the syndicated loan granted by Barclays Bank (Note 15);
- 2) increase in short-term obligations mainly due to the increase of advances received for technological connection to electricity grids which will be settled by the provision of respective services;
- 3) in 2010 tariffs for electricity transmission were established based on the application of 'cost plus' method and did not include economically reasonable rate of return on the investments.

The Group's management is taking the following measures to improve the Group's liquidity position:

- 1) Adjustment of the Group's investments into power lines and equipment:
 - the emphasis was shifted from the construction of new electric power supplies and other power equipment to completion of the previously launched projects having high stage of completion in order to ensure additional operating cash flows within relatively short period of time;
 - measures are being taken to decrease the construction period from 2-2.5 years to one year and thus to accelerate cash inflows from customers for technological connection to the electricity grids;
 - several engineering and construction works were suspended and some investment projects may be deferred or scaled down commensurate with the financing needed to support the Group's current operations.
- 2) Negotiating with federal and regional governments and regulators on increases in tariffs to support adequate long-term investments into electricity transmission and distribution assets of the Group. In 2010 the average increase in transmission regulated tariffs was 16%. In 2011 following the implementation of "Regulatory asset base" (RAB) system the transmission tariffs of the Group increased on average by 28%.
- 3) Improving operating efficiency of the Group through implementation of programs to reduce technological losses on transmission of electricity through the Group's own network and operating expenses.
- 4) Implementing improved financial budgeting procedures with a strong focus on timely collection of receivables; restructuring of liabilities to enable their repayment over a longer period.
- 5) Negotiating favorable terms for attracting additional borrowings. In 2010 the Group received long-term borrowings in the amount of 8,561,600 (Note 15).

The above measures are expected to ensure cash inflows sufficient to finance operations in 2011.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements

2.1 Basis of preparation

The consolidated financial statements comprise the financial statements of OJSC Lenenergo and its subsidiaries as at 31 December 2010. These financial statements are prepared based on the statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation, with adjustments and reclassifications recorded for the purpose of fair presentation of ending balances, results of operations and cash flows in accordance with IFRS.

The consolidated financial statements have been prepared on a historical cost basis, except for the following items that have been measured at fair value: property, plant and equipment and assets under construction, derivative financial instruments, available-for-sale investments and financial assets at fair value through profit and loss.

The consolidated financial statements are in Russian Rubles, with all amounts rounded to thousands, except where stated otherwise.

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

Basis of consolidation

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as at the parent company, using consistent accounting policies. All intra-group balances, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full.

Non-controlling interest (formally known as minority interests) represents the portion of profit or loss and net assets that is not held by the Group and is presented separately in the consolidated income statement and within equity in the consolidated statement of financial position, separately from parent shareholders' equity. Acquisitions of non-controlling interest are accounted for using the entity concept method, whereby, the difference between the consideration and the book value of the share of the net assets acquired is recognised in equity.

Losses within a subsidiary are attributed to the non-controlling interest even if that results in a deficit balance.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it:

- derecognises the assets (including goodwill) and liabilities of the subsidiary;
- derecognises the carrying amount of any non-controlling interest;
- derecognises the cumulative translation differences, recorded in equity;
- recognises the fair value of the consideration received;
- recognises the fair value of any investment retained;
- recognises any surplus or deficit in profit or loss;
- reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss or retained earnings, as appropriate.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.2 Changes in accounting policy and disclosures

The accounting policies adopted are consistent with those of the previous financial year except for the following new and amended IFRS and IFRIC interpretations effective as of 1 January 2010.

- IFRS 2 *Share-based Payment: Group Cash-settled Share-based Payment Transactions* effective 1 January 2010
- IFRS 3 *Business Combinations (Revised)* and IAS 27 *Consolidated and Separate Financial Statements (Amended)* effective 1 July 2009, including consequential amendments to IFRS 2, IFRS 5 IFRS 7, IAS 7, IAS 21, IAS 28, IAS 31 and IAS 39
- IAS 39 *Financial Instruments: Recognition and Measurement – Eligible Hedged Items* effective 1 July 2009
- IFRIC 17 *Distributions of Non-cash Assets to Owners* effective 1 July 2009
- Improvements to IFRSs (May 2008 and April 2009)

An impact of the adoption of the standard or interpretation on the financial statements of the Group is described below:

IFRS 2 Share-based Payment (Revised)

The IASB issued an amendment to IFRS 2 that clarified the scope and the accounting for group cash-settled share-based payment transactions. The Group adopted this amendment as of 1 January 2010. The adoption of this Standard did not have an impact on the financial position or performance of the Group.

IFRS 3 Business Combinations (Revised) and IAS 27 Consolidated and Separate Financial Statements (Amended)

IFRS 3 (Revised) introduces significant changes in the accounting for business combinations occurring after becoming effective. Changes affect the valuation of non-controlling interest, the accounting for transaction costs, the initial recognition and subsequent measurement of a contingent consideration and business combinations achieved in stages. These changes will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs and future reported results.

IAS 27 (Amended) requires that a change in the ownership interest of a subsidiary (without loss of control) is accounted for as a transaction with owners in their capacity as owners. Therefore, such transactions will no longer give rise to goodwill, nor will it give rise to a gain or loss. Furthermore, the amended standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary. The changes by IFRS 3 (revised) and IAS 27 (amended) affect acquisitions or loss of control of subsidiaries and transactions with non-controlling interests after 1 January 2010. The change in accounting policy was applied prospectively and had no material impact on earnings per share.

IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items

The amendment clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item. This also covers the designation of inflation as a hedged risk or portion in particular situations. The Group has concluded that the amendment will have no impact on the financial position or performance of the Group, as the Group has not entered into any such hedges.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.2 Changes in accounting policy and disclosures (continued)

IFRIC 17 Distribution of Non-cash Assets to Owners

This interpretation provides guidance on accounting for arrangements whereby an entity distributes non-cash assets to shareholders either as a distribution of reserves or as dividends. The interpretation has no effect on either financial position or performance of the Group.

Improvements to IFRSs

In May 2008 and April 2009 the IASB issued omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording. There are separate transitional provisions for each standard. The adoption of the following amendments resulted in changes to accounting policies but did not have any impact on the financial position or performance of the Group.

- ***IFRS 8 Operating Segment Information:*** Clarifies that segment assets and liabilities need only be reported when those assets and liabilities are included in measures that are used by the chief operating decision maker. As the Group's operations represent a single operating segment, the new disclosure requirements will not impact the presentation of financial information.
- ***IAS 7 Statement of Cash Flows:*** States that only expenditure that results in recognising an asset can be classified as a cash flow from investing activities. This amendment has an impact on the presentation in the statement of cash flows.
- ***IAS 17 Leases:*** The amendment removed the guidance that required a lease of land with an indefinite useful life to be classified as an operating lease and requires the entities to reassess the classification of the land elements of unexpired leases. Where reclassification is necessary, an entity will need to establish if it has the necessary information to apply the new classification retrospectively. If not, it is applied at the date when the entity applies the amendment, using the fair values of the asset and liability on that date, with the difference recognised in retained earnings. The Group analyzed its land lease agreements and concluded that no reassessment of land lease reclassification is required on 1 January 2010.
- ***IAS 36 Impairment of Assets:*** The amendment clarified that the largest unit permitted for allocating goodwill, acquired in a business combination, is the operating segment as defined in IFRS 8 before aggregation for reporting purposes. The amendment has no impact on the Group as it has a single operating segment.

Other amendments resulting from Improvements to IFRSs to the following standards did not have any significant impact on the accounting policies, financial position or performance of the Group:

- ***IFRS 2 Share-based Payment***
- ***IAS 1 Presentation of Financial Statements***
- ***IAS 34 Interim Financial Reporting***
- ***IAS 38 Intangible Assets***
- ***IAS 39 Financial Instruments: Recognition and Measurement***
- ***IFRIC 9 Reassessment of Embedded Derivatives***
- ***IFRIC 16 Hedge of a Net Investment in a Foreign Operation***

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.3 Future changes in accounting policies

Standards issued but not yet effective up to the date of issuance of the Group's financial statements are listed below. This listing is of standards and interpretations issued, which the Group reasonably expects to be applicable at a future date. The Group intends to adopt those standards when they become effective.

| Standard / Interpretation | Essence of amendments | Effective date |
|--|---|---|
| IFRS 9 <i>Financial Instruments</i> | Reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets as defined in IAS 39. In subsequent phases, the IASB will address classification and measurement of financial liabilities, hedge accounting and derecognition. The completion of this project is expected in early 2011. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets. The Group will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture. | Effective for annual reporting periods, starting on or after 1 January 2013. |
| Amendments to IAS 32 <i>Financial Instruments: Presentation – Classification of Right Issues</i> | Amended the definition of a financial liability in order to classify rights issues (and certain options or warrants) as equity instruments in cases where such rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, or to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. This amendment will have no impact on the Group after initial application. | Effective for annual reporting periods, starting on or after 1 February 2010. |
| Amendments to IFRIC 14 <i>Prepayments of a Minimum Funding Requirement</i> | The amendment provides guidance on assessing the recoverable amount of a net pension asset. The amendment permits an entity to treat the prepayment of a minimum funding requirement as an asset. The amendment is deemed to have no impact on the financial statements of the Group. | Effective for annual reporting periods, starting on or after 1 January 2011 with retrospective application. |
| IFRIC 19 <i>Extinguishing Financial Liabilities with Equity Instruments</i> | Clarifies that equity instruments issued to a creditor to extinguish a financial liability qualify as consideration paid. The equity instruments issued are measured at their fair value. In case that this cannot be reliably measured, the instruments are measured at the fair value of the liability extinguished. Any gain or loss is recognized immediately in profit or loss. The adoption of this interpretation will have no effect on the financial statements of the Group. | Effective for annual reporting periods, starting on or after 1 July 2010 with retrospective application. |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.3 Future changes in accounting policies (continued)

Improvements to IFRSs (issued in May 2010)

The IASB issued Improvements to IFRSs, an omnibus of amendments to its IFRS standards. The amendments have not been adopted as they become effective for annual periods on or after either 1 July 2010 or 1 January 2011:

- IFRS 3 *Business Combinations*
- IFRS 7 *Financial Instruments: Disclosures*
- IAS 1 *Presentation of Financial Statements*
- IAS 27 *Consolidated and Separate Financial Statements*
- IFRIC 13 *Customer Loyalty Programmes*

The Group, however, expects no impact from the adoption of the amendments on its financial position or performance.

2.4 Significant accounting judgments, estimates and assumptions

The preparation of the Group's consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date and for the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Judgments

In the process of applying the Group's accounting policies, management has made the following judgments which have the most significant effect on the amounts recognised in the consolidated financial statements:

Accounting for connection fee revenue

Management believes that connection fee revenue (one-time fee charged to clients when first connected to electricity grid) is a necessary prerequisite to the sale of electricity, and, as such, should be recognised immediately at the time when access to electrical power is provided (i.e. at the time of connection). The total connection fee revenue reported in the consolidated income statement for the year ended 31 December 2010 was 10,299,774 (31 December 2009: 6,638,230) (Note 19).

Estimates and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Group based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments however, may change due to market changes or circumstances arising beyond the control of the Group. Such changes are reflected in the assumptions when they occur.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.4 Significant accounting judgments, estimates and assumptions (continued)

Estimates and assumptions (continued)

Useful life of intangible assets

The Group assesses the remaining useful life of intangible assets at least at each financial year end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. These estimates may have a material impact on the amount of the carrying values of intangible assets and on amortization recognized in profit or loss.

Useful life of property, plant and equipment

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognized in profit or loss.

Revaluation of property, plant and equipment

The Group measures property, plant and equipment at revalued amounts with changes in fair value being recognised in other comprehensive income. The Group engaged independent valuation specialists to determine fair value as at 31 December 2008 (Note 5). The Group believes that there were no material changes in the fair value of property, plant and equipment as at 31 December 2010 and 2009, respectively (Note 5).

Impairment of non-financial assets

An impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or services or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash inflows from electricity transmission tariff growth rate used for a cash generating unit (Note 5).

Fair value of financial instruments

Where the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using valuation techniques including the discounted cash flows model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values as detailed in Note 7. Changes in assumptions about these factors could affect the reported fair values of financial instruments.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.4 Significant accounting judgments, estimates and assumptions (continued)

Estimates and assumptions (continued)

Impairment provision for accounts receivable and advances given

The Group estimates the amount of impairment provision for its receivables. Significant judgment is used to estimate accounts which are impaired. In estimating doubtful accounts historical and anticipated customer performance is considered. Changes in the economy, industry, or specific customer conditions may require adjustments to the impairment provision for accounts receivable and advances given recorded in the consolidated financial statements. As at 31 December 2010 impairment provision for accounts receivable and advances given was created in the amount of 956,336 (as at 31 December 2009: 703,060). Further details are disclosed in Note 13.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. Given the long-term nature and complexity of existing contractual agreements, differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expense already recorded. The Group establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences of interpretation may arise on a wide variety of issues. The contingent liability is recognised if the Group assesses the probability for litigation and subsequent cash outflow with respect to taxes as probable.

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

Pension and other post employment benefits

The cost of defined benefit pension plans and the present value of the pension obligation are determined using actuarial valuations. An actuarial valuation involves making various assumptions about the discount rate, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and its long-term nature, a defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date. In determining the appropriate discount rate, management of the Group uses a zero-coupon yield curve for government bonds for the term to maturity of 10 years. The net employee liability under the defined benefit pension plans as at 31 December 2010 was 351,312 (31 December 2009: 294,536). Further details are disclosed in Note 16.

Share-based payment transactions

The Group measures the cost of equity-settled transactions directly by reference to the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the Group measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability, will be recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it should not be remeasured until it is finally settled within equity.

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses, if any.

The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortised, but tested for impairment annually either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

In 2009 the Group acquired the right to connect end users to the electricity grid in Roschino, Leningrad Region for 624,000. In 2010 the Group recognized impairment of this asset of 37,360 (2009: 139,000) (Note 4).

The expected useful lives by asset groups, in years, are as follows:

| Asset group | Useful life |
|------------------------------|--------------------|
| Access right | 30 |
| Accounting software packages | 2-3 |
| Certificates | 3 |

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Property, plant and equipment

Property, plant and equipment is stated at a revalued amount, which is their fair value as at the revaluation date less accumulated depreciation and impairment losses recognised after the date of the revaluation. Valuations are performed frequently to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Any revaluation surplus is credited to the asset revaluation reserve in equity, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in the income statement, in which case the increase is recognised in the income statement. A revaluation deficit is recognised in the income statement, except to the extent that it offsets an existing surplus on the same asset recognised in the asset revaluation reserve.

The transfer from the asset revaluation reserve to retained earnings is made when the asset is derecognised. This involves transferring the whole of the surplus when the asset is retired or disposed of. Transfers from revaluation surplus to retained earnings are not made through profit or loss.

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement when the asset is derecognised.

Construction in progress reflects the net book value of property, plant and equipment items not yet put in operation, and as such, is not depreciated.

Expenditures related to the construction or acquisition of social assets are not capitalized as the Group does not expect to receive any future economic benefits from them.

Property, plant and equipment depreciation is calculated on a straight-line basis over the estimated useful life of the asset from the date it is put in operation. For revalued property, plant and equipment, depreciation rates are based on their estimated remaining useful lives as at the valuation date. The estimated useful lives by asset groups, in years, are as follows:

| Asset group | Useful life |
|--|--------------------|
| Production premises | 40-50 |
| Power lines | 30-40 |
| Equipment, power equipment, sub-stations | 25-40 |
| Other | 5-25 |

The assets' residual values, useful lives and methods of depreciation are reviewed at each financial year end, and adjusted prospectively, if appropriate.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Property, plant and equipment (continued)

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date, whether fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset, even if that right is not explicitly specified in an arrangement.

For arrangements entered into prior to 1 January 2005, the date of inception is deemed to be 1 January 2005 in accordance with the transitional requirements of IFRIC 4.

Group as a lessee

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are recognised in the income statement.

Leased assets are depreciated over the useful life of the asset. However, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the estimated useful life of the asset and the lease term.

Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

Group as a lessor

Leases where the Group does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same bases as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

Impairment of non-financial assets

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU) fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Impairment of non-financial assets (continued)

Impairment losses of continuing operations are recognised in the income statement in those expense categories consistent with the function of the impaired asset, except for property previously revalued where the revaluation was taken to other comprehensive income. In this case, the impairment is also recognised in other comprehensive income up to the amount of any previous revaluation.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Group estimates the asset's or cash-generating unit's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the income statement unless the asset is carried at a revalued amount, in which case the reversal is treated as a revaluation increase.

The following criteria are also applied in assessing impairment of specific assets:

Goodwill

Goodwill is tested for impairment annually as at 31 December and when circumstances indicate that the carrying value may be impaired.

Impairment is determined for goodwill by assessing the recoverable amount of each cash-generating unit (or group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than their carrying amount, an impairment loss is recognised. Impairment losses relating to goodwill cannot be reversed in future periods. In 2009 the Group recognized goodwill impairment of 312,833 (Note 5).

Intangible assets

Intangible assets with indefinite useful lives are tested for impairment annually as at 31 December either individually or at the cash generating unit level, as appropriate and when circumstances indicate that the carrying value may be impaired.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial assets

Initial recognition and measurement

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial assets at initial recognition.

Financial assets are recognised initially at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the marketplace (regular way trades) are recognised on the trade date, i.e., the date that the Group commits to purchase or sell the asset.

The Group's financial assets include cash and short-term deposits, trade and other receivables, quoted and unquoted financial instruments, and derivative financial instruments.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. This category includes derivative financial instruments entered into by the Group that do not meet the hedge accounting criteria as defined by IAS 39. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets at fair value through profit and loss are carried in the statement of financial position at fair value with changes in fair value recognised in finance income or finance cost in the income statement.

The Group evaluated its financial assets at fair value through profit and loss (held for trading) whether the intent to sell them in the near term is still appropriate. When the Group is unable to trade these financial assets due to inactive markets and management's intent to sell them in the foreseeable future significantly changes, the Group may elect to reclassify these financial assets in rare circumstances. The reclassification to loans and receivables, available-for-sale or held to maturity depends on the nature of the asset. This evaluation does not affect any financial assets designated at fair value through profit or loss using the fair value option at designation.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial assets (continued)

Subsequent measurement (continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortised cost using the effective interest rate method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the effective interest rate method. Amortisation is included in finance income in the income statement. The losses arising from impairment are recognised in the income statement in finance costs.

As at 31 December 2010 accounts receivable (Note 10) were classified as loans and receivables.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held-to-maturity when the Group has the positive intention and ability to hold it to maturity. After initial measurement held-to-maturity investments are measured at amortised cost using the effective interest method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the effective interest rate. The effective interest rate amortisation is included in finance income in the income statement. The losses arising from impairment are recognised in the income statement in finance costs. The Group did not have any held-to-maturity investments during the years ended 31 December 2010 and 2009.

Available-for-sale financial assets

Available-for-sale financial investments include equity securities. Equity investments classified as available-for sale are those, which are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale financial investments are subsequently measured at fair value with unrealised gains or losses recognised as other comprehensive income in other reserves until the investment is derecognised, at which time the cumulative gain or loss is recognised in other operating income, or determined to be impaired, at which time the cumulative loss is recognised in the consolidated income statement in finance costs and removed from the other reserves.

The Group evaluated its available-for-sale financial assets whether the ability and intention to sell them in the near term is still appropriate. When the Group is unable to trade these financial assets due to inactive markets and management intention significantly changes to do so in the foreseeable future, the Group may elect to reclassify these financial assets in rare circumstances. Reclassification to loans and receivables is permitted when the financial asset meets the definition of loans and receivables and has the intent and ability to hold these assets for the foreseeable future or maturity. The reclassification to held-to-maturity is permitted only when the entity has the ability and intent to hold until the financial asset accordingly.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial assets (continued)

Subsequent measurement (continued)

Available-for-sale financial assets (continued)

For a financial asset reclassified out of the available-for-sale category, any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the expected cash flows is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired then the amount recorded in equity is reclassified to the income statement.

As at 31 December 2010 the Group holds available-for-sale investments with the fair value of 30,000 (31 December 2009: 525,913) (Note 7).

Derecognition

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, a new asset is recognised to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained. Continuing involvement that takes the form of a guarantee over the transferred asset, is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial assets (continued)

Impairment of financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

For financial assets carried at amortised cost the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial assets original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income in the income statement. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to finance costs in the income statement.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial assets (continued)

Impairment of financial assets (continued)

Available-for-sale financial investments

For available-for-sale financial investments, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is to be evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the income statement – is removed from other comprehensive income and recognised in the income statement. Impairment losses on equity investments are not reversed through the income statement; increases in their fair value after impairment are recognised directly in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the income statement. Future interest income continues to be accrued based on the reduced carrying amount of the asset and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement.

Financial liabilities

Initial recognition and measurement

Financial liabilities within the scope of IAS 39 are classified as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial liabilities at initial recognition.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, directly attributable transaction costs.

As at 31 December 2010 the Group's financial liabilities include trade and other payables (Note 18) and borrowings (Note 15).

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Financial liabilities (continued)

Subsequent measurement

The measurement of financial liabilities depends on their classification as follows:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss includes financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are acquired for the purpose of selling in the near term. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognised in the income statement. The Group has not designated any financial liabilities upon initial recognition as at fair value through profit or loss.

Loans and borrowings

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the effective interest rate method amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the effective interest rate method and is included in finance cost in the income statement.

Financial guarantee contracts

Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognised initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the reporting date and the amount recognised less cumulative amortisation.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the income statement.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

Fair value of financial instruments

The fair value of financial instruments that are traded in active markets at each reporting date is determined by reference to quoted market prices or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs.

For financial instruments not traded in an active market, the fair value is determined using appropriate valuation techniques. Such techniques may include using recent arm's length market transactions; reference to the current fair value of another instrument that is substantially the same; discounted cash flow analysis or other valuation models.

An analysis of fair values of financial instruments and further details as to how they are measured are provided in Note 28.

Derivative financial instruments

Initial recognition and subsequent measurement

The Group uses derivative financial instruments such as currency and interest rate swaps to hedge its foreign currency and interest rate risks respectively. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

Any gains or losses arising from changes in fair value on derivatives are taken directly to the income statement.

For the years ended 31 December 2010 and 2009 the Group did not have any derivatives designated as hedging instruments. Gain of 143,179 (2009: loss of 816,018) (Notes 21, 22) related to the change in the fair value of the interest rate and currency swap contract was included into finance income and finance expense in the income statement for the year ended 31 December 2010 and 2009, respectively.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Inventories

Inventories are valued at the lower of net realisable value and cost determined using FIFO method. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs necessary to make the sale. As at 31 December 2010 and 2009 the Group recognized an impairment provision of 112,328 and 163,205 respectively (Note 11).

Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash at banks and on hand, short-term deposits and promissory notes issued by the banks with an original maturity of three months or less.

For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and short-term deposits and promissory notes as defined above.

Pensions and other post-employment benefit plans

In the normal course of business the Group contributes to the Russian Federation state pension scheme on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred. Discretionary pensions and other post-employment benefits are included in payroll expenses in the consolidated income statement. The Group also contributes to defined benefit and defined contribution pension plans. The defined benefit plan involves post-employment payments based upon one or more factors, such as age, years with the Group and salary. The defined benefit liability comprises the present value of the defined benefit obligation less past service costs and actuarial gains and losses not yet recognised and less the fair value of plan assets out of which the obligations are to be settled. Defined benefit obligation is determined using the projected unit credit actuarial valuation method.

Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses for each individual plan at the end of the previous reporting year exceed 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plans.

Other long-term benefits include:

- funeral benefit
- jubilee benefit

The Group applies a simplified accounting treatment to other long-term benefits. Under simplified method the actuarial gains and losses are recognized immediately, and so is the cost of past services.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Equity-settled share-based payment transactions

The Group treats the transfers of an entity's equity instruments by its shareholders to parties that have supplied goods or services to the entity (including employees) as share-based payment transactions, unless the transfer is clearly for a purpose other than payment for goods or services supplied to the entity or remuneration for the service. The Group recognizes the goods or services received or acquired in a share-based payment transaction when it obtains the goods or as the services are received. In situations where equity instruments are issued and some or all of the goods or services received by the entity as consideration cannot be specifically identified, the unidentified goods or services received (or to be received) are measured as the difference between the fair value of the share-based payment transaction and the fair value of any identifiable goods or services received at the grant date. This is then capitalised or expensed as appropriate. The Group recognizes a corresponding increase in equity if the goods or services were received in an equity-settled share-based payment transaction or a liability if the goods or services were acquired in a cash-settled share-based payment transaction.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement.

Borrowing costs

The Group qualifies for the exemption from borrowing cost capitalization according to IAS 23 (4) since its qualified assets are measured at fair value. Borrowing costs are recognised as an expense when incurred.

Foreign currency translation

The Group's consolidated financial statements are presented in rubles, which is the Group's functional currency, being the currency of the primary economic environment in which the Group operates. Transactions in foreign currencies are initially recorded at the functional currency rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when fair value is determined.

The official spot exchange rates prevailing at 31 December 2010 were 30.4769 Rubles for 1 USD and 40.3331 Rubles for 1 Euro (31 December 2009: 30.2442 Rubles for 1 USD and 43.3883 Rubles for 1 Euro).

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and sales taxes or duty. The Group assesses its revenue arrangements against specific criteria in order to determine if it is acting as principal or agent. The Group has concluded that it is acting as a principal in all of its revenue arrangements. The following specific recognition criteria must also be met before revenue is recognised:

Rendering of services

Revenue is recognized by type of activity:

- Network transmission of electricity, and
- Technological connection to electricity grids

The Group charges all its customers (wholesale or retail sellers of electricity) for actual electricity network transmission traffic based on pre-set per kW tariffs regulated by the St.-Petersburg Tariffs Committee and Leningrad Region Tariffs and Pricing Policy Committee. Technological losses of electricity in transmission through the Group's network include losses at the normal expected level (Note 19). Revenue from network transmission of electricity is presented net of technological losses at the normal expected level. Technological losses in excess of the normal expected level are included into operating expenses.

Technological connection fees are recognised as revenues immediately at the time when access to electrical power is provided (i.e. at the time of connection) as they do not result in the Group's obligation to provide further services to the customers that are consumers of electricity and are separate from network transmission services provided to the sellers of electricity.

Sales of other assets

Revenue from the sale of other assets (materials, property, plant and equipment) is recognised when the significant risks and rewards of ownership of these assets have passed to the buyer, usually on delivery of the goods.

Interest income

For all financial instruments measured at amortised cost and interest bearing financial assets classified as available-for-sale, interest income or expense is recorded using the effective interest rate, which is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability. Interest income is included into finance income in the income statement (Note 21).

Dividends

Revenue is recognised when the Group's right to receive the payment is established.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Taxes

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, by the reporting date, in the country where the Group operates and generates taxable income. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate. Income tax rate enacted in the Russian Federation is 20%.

Deferred income tax

Deferred tax is provided using the liability method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss;
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss;
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred income tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

2. Basis of presentation of the financial statements (continued)

2.5 Summary of significant accounting policies (continued)

Taxes (continued)

Deferred tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in other comprehensive income or directly in equity.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Value-added tax

Revenues, expenses and assets are recognised net of the amount of value-added tax.

The net amount of value-added tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Dividends

Dividends are recognized as a liability and deducted from equity at the reporting date only if they are declared (approved by shareholders) before or on the reporting date. Dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the financial statements are authorised for issue.

Earnings per share

IAS 33, as revised, requires the application of the “two-class method” to determine earnings applicable to ordinary shareholders, the amount of which is used as a nominator to calculate earnings per ordinary share. The application of the “two-class method” requires that the profit or loss after deducting preferred dividends declared in the period is allocated to ordinary shares and other participating equity instruments to the extent that each instrument shares in earnings as if all of the profit or loss for the period had been distributed. The total profit or loss allocated to each class of equity instrument is determined by adding together the amount allocated for dividends and the amount allocated for a participation feature.

Preference shares are treated as voting shares (Note 14). Earnings per share are calculated by dividing profit attributable to ordinary and preference shareholders by the weighted average number of ordinary and preference shares outstanding during the period less weighted average number of treasury shares held by the Group.

2.6 Reclassifications

Certain prior year amounts and disclosures have been reclassified to conform to the current year presentation. The reclassifications and other presentation changes made by the Group are as follows:

- Non-cash settlement for technological connection in 2009 of 2,293,975 is presented separately in the Consolidated Statement of Cash Flows as adjustment to reconcile profit before tax and net cash flow from operating activities while previously was partially reported within Increase/(decrease) in accounts payable and accrued expenses.

Such reclassification had no impact on net cash generated from operating activities of the Group.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

3. Acquisition of non-controlling interests

Acquisition of additional interest in CJSC Kurortenergo

In October 2009, the Group acquired an additional 5.562% of the voting shares of CJSC Kurortenergo, increasing its ownership to 98.127%. A cash consideration of 17,385 was paid to the non-controlling interest shareholders.

The carrying value of the net assets of CJSC Kurortenergo (excluding goodwill on the original acquisition) at this date was 512,559, and the carrying value of the additional interest acquired was 28,509. The difference of 11,124 between the consideration paid and carrying value of the interest acquired has been recognised in 2009 directly in retained earnings within equity.

4. Intangible assets

| | Accounting software | Certificates | Access right | Goodwill | Total |
|------------------------------------|------------------------|--------------|-----------------|-----------|-----------|
| Cost | | | | | |
| As at 1 January 2009 | 269,440 | 88,641 | – | 312,833 | 670,914 |
| Additions for the period | 67,567 | 14,636 | 624,000 | – | 706,203 |
| As at 31 December 2009 | 337,007 | 103,277 | 624,000 | 312,833 | 1,377,117 |
| Additions for the period | 40,793 | 18,963 | – | – | 59,756 |
| Disposal for the period | (137,151) | (74,614) | – | – | (211,765) |
| As at 31 December 2010 | 240,649 | 47,626 | 624,000 | 312,833 | 1,225,108 |
| Amortization and impairment | | | | | |
| As at 1 January 2009 | (65,131) | (35,629) | – | – | (100,760) |
| Charge for the period | (87,069) | (27,180) | (14,000) | – | (128,249) |
| Impairment | – | – | (139,000) | (312,833) | (451,833) |
| As at 31 December 2009 | (152,200) | (62,809) | (153,000) | (312,833) | (680,842) |
| Charge for the period | (73,528) | (27,899) | (16,060) | – | (117,487) |
| Disposal for the period | 137,151 | 74,614 | – | – | 211,765 |
| Impairment | – | – | (37,360) | – | (37,360) |
| As at 31 December 2010 | (88,577) | (16,094) | (206,420) | (312,833) | (623,924) |
| Net book value | | | | | |
| as at 31 December 2009 | 184,807 | 40,468 | 471,000 | – | 696,275 |
| Net book value | | | | | |
| as at 31 December 2010 | 152,072 | 31,532 | 417,580 | – | 601,184 |

Certificates are acquired for the purposes of conformity with the electricity quality standards. The new certificates are valid until 2013. The Group believes that it will be able to renew the certificates upon expiration without incurring substantial costs.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

5. Property, plant and equipment

| | Production premises | Power lines | Equipment, power equipment, substations | Other | Assets under construction | Total |
|--|------------------------|---------------------|--|--------------------|---------------------------------|---------------------|
| Cost | | | | | | |
| As at 1 January 2009 | 12,395,759 | 57,406,179 | 19,738,420 | 8,820,729 | 14,511,774 | 112,872,861 |
| Additions | – | 1,325 | 1,360,218 | – | 10,197,174 | 11,558,717 |
| Disposals | (8,843) | (27,367) | (16,569) | (66,089) | (7,784) | (126,652) |
| Transfer | 2,705,083 | 1,555,624 | 4,079,660 | 1,161,190 | (9,501,557) | – |
| As at 31 December 2009 | 15,091,999 | 58,935,761 | 25,161,729 | 9,915,830 | 15,199,607 | 124,304,926 |
| As at 1 January 2010 | 15,091,999 | 58,935,761 | 25,161,729 | 9,915,830 | 15,199,607 | 124,304,926 |
| Additions | – | – | 357,807 | 3,591 | 14,657,527 | 15,018,925 |
| Disposals | (22,509) | (4,316) | (50,181) | (110,330) | (137,870) | (325,206) |
| Transfer | 6,781,267 | 1,608,965 | 5,304,555 | 995,145 | (14,689,932) | – |
| As at 31 December 2010 | 21,850,757 | 60,540,410 | 30,773,910 | 10,804,236 | 15,029,332 | 138,998,645 |
| Accumulated depreciation and impairment | | | | | | |
| As at 1 January 2009 | (2,038,102) | (30,306,847) | (5,417,947) | (6,982,034) | (1,892,139) | (46,637,069) |
| Charge for the year | (428,276) | (2,286,802) | (936,861) | (266,138) | – | (3,918,077) |
| Impairment loss on initial recognition of finance leases (Note 15) | – | – | (490,894) | – | – | (490,894) |
| Disposals | 941 | 12,122 | 6,322 | 53,960 | – | 73,345 |
| As at 31 December 2009 | (2,465,437) | (32,581,527) | (6,839,380) | (7,194,212) | (1,892,139) | (50,972,695) |
| As at 1 January 2010 | (2,465,437) | (32,581,527) | (6,839,380) | (7,194,212) | (1,892,139) | (50,972,695) |
| Charge for the year | (515,235) | (2,274,640) | (1,227,624) | (413,368) | – | (4,430,867) |
| Impairment loss on initial recognition of finance leases (Note 15) | – | – | (94,242) | – | – | (94,242) |
| Disposals | 4,037 | 4,316 | 20,750 | 91,631 | – | 120,734 |
| As at 31 December 2010 | (2,976,635) | (34,851,851) | (8,140,496) | (7,515,949) | (1,892,139) | (55,377,070) |
| Net book value as at 31 December 2009 | 12,626,562 | 26,354,234 | 18,322,349 | 2,721,618 | 13,307,468 | 73,332,231 |
| Net book value as at 31 December 2010 | 18,874,122 | 25,688,559 | 22,633,414 | 3,288,287 | 13,137,193 | 83,621,575 |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

5. Property, plant and equipment (continued)

Impairment analysis

Impairment analysis on property, plant and equipment was carried as at 31 December 2010. The analysis was performed based on the reports of a qualified independent appraiser.

The recoverable amount of the CGU has been determined based on a value in use calculated using cash-flow projections from financial budgets approved by the management of the Group covering a 4-year period. The selected forecast period is stipulated by fluctuations of the expected cash flows during 4 years after RAB tariff system implemented in 2011. After 2015 average cash flows are forecasted as stable.

Key assumptions used in value-in-use calculations

The calculation of value-in-use for a cash-generating unit is the most sensitive to the following assumptions:

| | 2011 | 2012-2013 | 2014-2015 | 2016-2020 |
|---|-------------|-------------|--------------|-------------|
| Transmission revenue tariff increase, % | 34.0%-59.0% | 18.0%-29.0% | (1.1%)-13.1% | 1.1%-7.5% |
| Transmission volume increase, % | 1.3% | 0.5%-1.0% | 0.5%-1.0% | 0.5%-1.0% |
| Normal network technological losses, % | 12.3%-12.4% | 12.3%-12.4% | 12.3%-12.4% | 12.3%-12.4% |
| Weighted average cost of capital (WACC) | 17.2% | 14.2%-15.4% | 13.2%-13.4% | 11.6%-12.9% |

Transmission revenue tariff increase – The Group considered the change in tariffication system from the cost-plus model applied in 2010 to a reasonable rate on return (ROR) model from 2011 and onwards, which is expected to cause future increase in transmission tariffs in the next four years. A reduction of revenue tariff growth by 1% would result in the recoverable amount of CGU decrease by 15%.

Transmission volume increase – The Group has considered transmission volume trends during prior periods as well as management plans and analytic forecasts on future electricity consumption in Saint-Petersburg and Leningrad region. Should the Group be unable to achieve any growth in transmission volume the recoverable amount of CGU will decrease by 17%.

Normal network technological losses – The Group accounted for future decline in technological losses normal level as result of taken measures on losses prevention and installation of more accurate electricity metering equipment. Increase in normal network technological losses by 1% would affect the reduction of CGU recoverable amount by 3%.

Weighted average cost of capital (WACC) – The Group considered future decrease in cost of capital mainly caused by the expected decline in inflation rate. If WACC increases by 1%, the recoverable amount of CGU reduces by 2%.

Cash flows beyond the ten-year period are projected using the 5% long-term average *inflation rate* in Russia. Decrease in inflation rate by 1% would result in the reduction of CGU recoverable amount by 0.5%.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

5. Property, plant and equipment (continued)

Impairment analysis (continued)

As a result of the analysis the Group didn't identify any impairment of property, plant and equipment as at 31 December 2010.

As at 31 December 2010 and 2009 the carrying value of property, plant and equipment received under finance lease contracts was as follows:

| | Power equipment | Vehicles | Total |
|--|------------------------|-----------------|------------------|
| Cost | | | |
| As at 31 December 2009 | 3,674,878 | 11,784 | 3,686,662 |
| Additions | 357,003 | – | 357,003 |
| As at 31 December 2010 | 4,031,881 | 11,784 | 4,043,665 |
| Accumulated depreciation and impairment | | | |
| As at 31 December 2009 | (607,879) | (9,178) | (617,057) |
| Charge for the year | (131,405) | (2,606) | (134,011) |
| Impairment loss on finance leases | (94,242) | – | (94,242) |
| As at 31 December 2010 | (833,526) | (11,784) | (845,310) |
| Net book value as at 31 December 2009 | 3,066,999 | 2,606 | 3,069,605 |
| Net book value as at 31 December 2010 | 3,198,355 | – | 3,198,355 |

Property, plant and equipment under finance lease were pledged as security for the respective finance lease agreements.

Acquisitions under finance leases of 357,003 (2009: 1,359,604) have been excluded from the consolidated statement of cash flows, so investing activities in the consolidated statement of cash flows represent actual cash transactions.

6. Advances for construction of property, plant and equipment

Advances of 2,317,079 paid to construction contractors (31 December 2009: 4,135,536) are stated net of an impairment provision of 420,436 (31 December 2009: 176,502). Movements in the provision for impairment of advances to construction are disclosed in Note 13.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

7. Available-for-sale investments

| | % | 31 December 2010 | 31 December 2009 |
|--|---------------------|---------------------|---------------------|
| | Shareholding | | |
| OJSC Petersburg Sales Company (OJSC PSK) | 12.5% | – | 303,000 |
| OJSC FSK UES | 0.051% | – | 189,480 |
| OJSC North-West Energy Management Company (OJSC NW EMK) | 12.5% | 29,900 | 33,300 |
| Other | | 100 | 133 |
| Total | | 30,000 | 525,913 |

In 2010 the Group sold its equity interests in OJSC FSK UES and OJSC PSK for a cash consideration of 657,087, representing the fair value of investments as of the date of transaction. The increase in fair values of the investments from 31 December 2009 till the date of sale (OJSC FSK UES and OJSC PSK) and till the reporting date (OJSC NW EMK) in the amount of 161,207 is recognized within other comprehensive income.

On disposal of OJSC FSK UES and OJSC PSK unrealized gains related to these available-for-sale investments of 532,866 before tax were reclassified from other reserves and recognized within finance income (Note 21).

The fair value of the unquoted ordinary and preference shares of OJSC NW EMK was estimated using income method by applying the weighted-average cost of capital of 18.8% for 2010 and 13.4%-16.8% for the period from 2011 to 2021.

8. Other non-current assets

| | 31 December 2010 | 31 December 2009 |
|---|---------------------|---------------------|
| VAT recoverable after more than 12 months | 314,639 | 197,800 |
| Other non-current assets | 125,791 | 74,510 |
| Total | 440,430 | 272,310 |

9. Cash and cash equivalents

| | 31 December 2010 | 31 December 2009 |
|--|---------------------|---------------------|
| Bank deposits reclaimable on demand – Rubles | 520,620 | 2,057,208 |
| Bank accounts and cash in hand – Rubles | 132,448 | 791,593 |
| Promissory notes | – | 100,000 |
| Total | 653,068 | 2,948,801 |

As at 31 December 2010 the Group had open deposit agreements with original maturity of less than 3 months placed with a number of banks bearing an interest of 1.2-7.4 % p.a. if the Group maintains minimum cash balances. Interest receivable for the year ended 31 December 2010 included in finance income (Note 21) comprised 72,977 (2009: 50,467).

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

10. Accounts receivable

| | 31 December 2010 | 31 December 2009 |
|---|---------------------|---------------------|
| Trade receivables net of impairment provision of 383,336 (2009: 410,130) | 1,357,726 | 1,114,615 |
| Other accounts receivable net of impairment provision of 35,834 (2009: 39,889) | 136,272 | 217,810 |
| Total | 1,493,998 | 1,332,425 |

Management determined the provision for impairment of receivables based on specific customer solvency, industry-specific payment trends, subsequent receipts and settlements and analysis of expected future cash flows. The Group analyses the ability of debtors to fulfill the payment obligation on a regular basis and creates provision for impairment that represents the estimate of potential losses in respect of trade and other receivables (Note 13). The components of this provision are a specific provision for individual losses. Management believes that the Group will be able to realise the net receivable amount through direct collections and non-cash settlements, and therefore the recorded value approximates their fair value. Movements in the provision for impairment of accounts receivable are disclosed in Note 13.

For trade and other receivables which are neither past due nor impaired at the reporting date, no information is available to indicate that the debtors may default on their obligations, as the Group monitors debtors on an ongoing basis and periodically reconciles receivable balances. Trade and other receivables bear no interest and are generally repaid within a calendar year.

As at 31 December 2010 and 2009, the analysis of trade receivables is as follows:

| | 31 December 2010 | | | 31 December 2009 | | |
|---|------------------|-------------------------------------|-----------------------------|------------------|-------------------------------------|-----------------------------|
| | Total | Neither past due nor impaired | Past due not impaired | Total | Neither past due nor impaired | Past due not impaired |
| Trade receivables (electricity transmission services) | 913,348 | 888,062 | 25,286 | 836,123 | 375,022 | 461,101 |
| Trade receivables (technological connection services) | 444,378 | 82,025 | 362,353 | 278,492 | 45,163 | 233,329 |
| Total trade accounts receivable | 1,357,726 | 970,087 | 387,639 | 1,114,615 | 420,185 | 694,430 |
| Other accounts receivable | 136,272 | 136,272 | – | 217,810 | 217,810 | – |

As at 31 December 2010 the amounts which are past due but not impaired mainly represent receivables from technological connection customers who have failed to make a payment when contractually due.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

11. Inventories, net of impairment

| | 31 December 2010 | 31 December 2009 |
|-------------------|---------------------|---------------------|
| Materials | 328,818 | 254,304 |
| Spare parts | 72,295 | 62,351 |
| Uniform | 20,405 | 11,194 |
| Tools | 13,605 | 7,787 |
| Other inventories | 17,656 | 25,530 |
| Total | 452,779 | 361,166 |

As at 31 December 2010 inventories are stated at cost net of impairment of 112,328 (as at 31 December 2009: 163,205).

12. Other current assets

| | 31 December 2010 | 31 December 2009 |
|---|---------------------|---------------------|
| VAT receivable net of impairment provision of 89,535 (2009: 53,924) | 3,415,153 | 3,218,752 |
| Prepayments and advances given to suppliers net of impairment provision of 27,195 (2009: 22,615) | 335,743 | 372,231 |
| Other taxes receivable | 19,144 | 1,275 |
| Fair value of derivative instrument | – | 1,075,836 |
| Promissory notes | – | 51,458 |
| Other current assets | 2,191 | 1,076 |
| Total | 3,772,231 | 4,720,628 |

In 2010 the Group fully met its obligations under the swap contract. Change in fair value of the swap contract for the year ended 31 December 2010 is included in finance income (Note 21).

Movements in the provision for impairment of VAT receivable, prepayments and advances to suppliers are disclosed in Note 13.

13. Impairment provision for accounts receivable and advances given

Movements in the provision for impairment of receivables were as follows:

| | Trade receivables | VAT receivable | Advances to suppliers | Advances for construction | Other receivables | Total |
|-------------------------------|----------------------|-------------------|--------------------------|------------------------------|----------------------|----------------|
| As at 1 January 2009 | 631,427 | 65,154 | 21,710 | 110,805 | 63,533 | 892,629 |
| Charge for the year | 221,763 | 16,823 | 11,220 | 107,857 | 1,467 | 359,130 |
| Released | (98,175) | (11,287) | (8,725) | (4,594) | (10,297) | (133,078) |
| Utilized | (344,885) | (16,766) | (1,590) | (37,566) | (14,814) | (415,621) |
| As at 31 December 2009 | 410,130 | 53,924 | 22,615 | 176,502 | 39,889 | 703,060 |
| Charge for the year | 95,049 | 43,963 | 16,428 | 361,213 | – | 516,653 |
| Released | (114,827) | (8,352) | (11,770) | (117,279) | (3,877) | (256,105) |
| Utilized | (7,016) | – | (78) | – | (178) | (7,272) |
| As at 31 December 2010 | 383,336 | 89,535 | 27,195 | 420,436 | 35,834 | 956,336 |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

14. Equity

| | Number of shares issued and fully paid | | Share capital | |
|-------------------|---|----------------------|---------------------|---------------------|
| | 31 December 2010 | 31 December 2009 | 31 December 2010 | 31 December 2009 |
| Ordinary shares | 926,021,679 | 926,021,679 | 4,866,115 | 4,866,115 |
| Preference shares | 93,264,311 | 93,264,311 | 625,603 | 625,603 |
| Total | 1,019,285,990 | 1,019,285,990 | 5,491,718 | 5,491,718 |

Share capital

The par value of both ordinary and preference shares is 1 Ruble per share.

Ordinary shares carry voting rights with no guarantee of dividends.

Preference shares

Preference shares have priority over ordinary shares in the event of liquidation but carry no voting rights except on resolutions regarding liquidation or reorganization of the Group, changes or amendments to the Articles of Association limiting rights of preference shareholders, changes to dividend levels of preference shares, or the issuance of additional preference stock. Such resolutions require 75% approval of both preference and ordinary shareholders.

Preference shareholders have the right to participate in general shareholders' meetings and vote on all issues within the competence of general shareholders' meetings following the annual general meeting at which, for whatever reason, a decision not to pay (or not to pay the full amount of) dividends on preference shares was taken. The right of preference shareholders to vote at general shareholders' meetings ceases from the date of the first full payment of dividend on such shares.

Preference shares carry no rights of redemption or conversion.

Preference shares carry dividends amounting to the higher of 10% of the net income after taxation of the Group as reported in the Russian statutory accounts divided by the number of preference shares and the dividends paid on one ordinary share. Dividends on the preference shares are non-cumulative. In case of liquidation, the assets remaining after settlement with creditors, payment of preference dividends and redemption of the par value of preference shares are distributed among preference and ordinary shareholders proportionally to the number of shares owned.

Accordingly, the Group's preference shares are considered participating equity instruments for the purpose of earnings per share calculations (Note 24).

Distributable earnings

Distributable earnings of all entities included in the Group are limited to their respective retained earnings, as mandated by statutory accounting rules. Statutory net profit of the Company as at 31 December 2010 amounted to 3,805,591 (as at 31 December 2009: 3,258,036).

Dividend declared and paid

In 2010 dividends for the year ended 31 December 2009 were declared in the amount of 3.4933 Rubles per preference share (nil per ordinary share). The total amount of dividends accrued in 2010 for the year ended 31 December 2009 was 325,804 (31 December 2008: 153,961). In 2011 dividends for the year ended 31 December 2010 were not declared by the date of report issue.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

14. Equity (continued)

Other reserves

| | Asset revaluation reserve | Net unrealised gains on available-for-sale investments | Total |
|--|---------------------------------|--|------------|
| As at 1 January 2009 | 28,753,090 | 104,690 | 28,857,780 |
| Unrealised gain on available-for-sale investments, net of tax effect of 44,276 | - | 177,104 | 177,104 |
| Release of asset revaluation reserve on disposed property, plant and equipment items, net of tax effect of 7,863 | (31,458) | - | (31,458) |
| As at 31 December 2009 | 28,721,632 | 281,794 | 29,003,426 |
| Unrealised gain on available-for-sale investments, net of tax effect of 32,241 | - | 128,966 | 128,966 |
| Reclassification of unrealized gain reserve on available-for-sale financial assets to income statement, net of tax effect of 106,573 | - | (426,293) | (426,293) |
| Release of asset revaluation reserve on disposed property, plant and equipment items, net of tax effect of 11,676 | (46,705) | - | (46,705) |
| As at 31 December 2010 | 28,674,927 | (15,533) | 28,659,394 |

Asset revaluation reserve is used to record increases in the fair value of property, plant and equipment and assets under construction and decreases to the extent that such decrease relates to an increase on the same asset previously recognised in equity.

Net unrealized gains reserve accumulates changes in the fair value of available-for-sale investments.

15. Borrowings

| | Effective Currency interest rate | Maturity date | 31 December 2010 | 31 December 2009 | |
|---|-------------------------------------|------------------------------|---------------------|---------------------|-------------|
| Bonds issued by the Group | | | | | |
| series 02 | Rubles | 8.54% | 2012 | 2,993,647 | 2,988,301 |
| series 03 | Rubles | 8.02% | 2012 | 2,992,469 | 2,987,237 |
| Bank loans (local currency denominated) | Rubles | 6.95% - 10.5% | 2011-2015 | 8,561,600 | 3,000,000 |
| Bank loans (foreign currency denominated) | USD | Libor + 1.25% - 16.92% | 2010 | - | 6,026,914 |
| Finance lease liabilities | Rubles | 57.44% | 2011-2015 | 1,143,176 | 1,682,028 |
| Total borrowings | | | | 15,690,892 | 16,684,480 |
| Less: current portion of finance lease liabilities | | | | (566,041) | (583,902) |
| Less: current portion of bank loans | | | | (1,000,000) | (6,026,914) |
| Current portion of long-term borrowings | | | | (1,566,041) | (6,610,816) |
| Long-term borrowings, net of current portion | | | | 14,124,851 | 10,073,664 |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

15. Borrowings (continued)

Bonds

As at 31 December 2010 the Group had outstanding 2nd and 3rd issue bonds.

In February 2007 the Group registered the 2nd issue of 3,000,000 certified coupon bonds with a par value of 1,000 Rubles each carrying 10 interest-bearing coupons. Payments under the 1st coupon were due on the 181st day from the date of bond placement, and other coupon payments are payable every 184th day. The interest rate under coupons is set at 8.54% p.a. The bonds mature in January 2012, in 1820 days from the date of placement with no option for early redemption. In 2010 the Group fully met its coupon obligations under the 6th and 7th coupons at 8.54% p.a. in the total amount of 255,480 (2009: under the 4th and 5th coupons - 255,480). Coupon payment per bond was 42.58 Rubles. As at 31 December 2010 the outstanding 2nd issue bonds of 2,993,647 were classified as long-term debt (31 December 2009: 2,988,301).

In April 2007 the Group registered the 3rd issue of 3,000,000 certified coupon bonds with a par value of 1,000 Rubles each carrying 10 interest-bearing coupons. Payments under the 1st coupon are due on the 181st day from the date of bond placement, and other coupon payments are effected every 184 day. The interest rate under coupons is set at 8.02% p.a. The bonds mature in April 2012, in 1820 days from the date of placement with no option for early redemption. In 2010 the Group fully met its coupon obligations under the 6th and 7th coupons at 8.02% p.a. in the total amount of 239,940 (2009: under the 4th and 5th coupons - 239,940). Coupon payment per bond was 39.99 Rubles. As at 31 December 2010 the outstanding 3rd issue bonds of 2,992,469 were classified as long-term debt (31 December 2009: 2,987,237).

Loans

Bank loans (denominated in local currency)

On 31 May 2010 the Group entered into two non-renewable credit line agreements with OJSC Bank VTB Severo-Zapad for a total amount of 2,225,000 maturing on 30 May 2012 and bearing interest of 6.95% - 6.97%. In 2010 the Group repaid 1,000,000 under these agreements before maturity. Also the Group repaid 2,000,000 under agreements with OJSC Bank VTB Severo-Zapad concluded in 2009 before maturity.

On 31 May 2010 the Group entered into a non-renewable credit line agreement with OJSC Bank Russia for a total amount of 800,000 maturing on 31 May 2012 and bearing interest of 7.1%.

In July 2010 the Group borrowed 1,100,000 and 44,000 under credit lines granted by OJSC AKB Svyaz-bank bearing interest of 8.00% and 8.06% and maturing on 29 July 2014 and 29 July 2015 respectively.

In July-August 2010 the Group received several tranches in the total amount of 1,521,500 from OJSC Bank VTB Severo-Zapad bearing interest of 7.83% - 8.19% and maturing in July 2014-July 2015.

In August-November 2010 the Group entered into agreements with OJSC Sberbank for non-renewable credit lines in the total amount of 2,871,100 bearing interest of 7.29% - 7.91% and maturing in August 2013-November 2014.

Bank loans (denominated in foreign currency)

In 2010 the Group fully met its payment obligations under the loan agreement with Barclays Bank at a fixed swap exchange rate.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

15. Borrowings (continued)

Finance lease liabilities

As at 31 December 2010 the Group entered into lease agreements for electricity transmission equipment and transport vehicles which have been delivered to the Group by the reporting date and, therefore, are recognized in these consolidated financial statements. Future minimum lease payments under finance lease are as follows:

| | During the next year | During 2-5 years | Over 5 years | Total |
|---|---------------------------------|-----------------------------|---------------------|------------------|
| As at 31 December 2010 | | | | |
| Future minimum lease payments | 767,450 | 664,021 | – | 1,431,471 |
| Less: future interest expenses | (201,409) | (86,886) | – | (288,295) |
| Present value of future minimum lease payments | 566,041 | 577,135 | – | 1,143,176 |
| As at 31 December 2009 | | | | |
| Future minimum lease payments | 915,129 | 1,348,503 | – | 2,263,632 |
| Less: future interest expenses | (331,227) | (250,377) | – | (581,604) |
| Present value of future minimum lease payments | 583,902 | 1,098,126 | – | 1,682,028 |

All lease agreements are fully secured against the Group's leased assets (Note 5).

In 2010 and 2009 the Group's primary lessors were LLC Goldline and LLC Sevzapleasing.

Certain finance lease agreements provide for inception and commencement dates which are substantially different in time and the Group is required to prepay a substantial amount of the fair value of the leased assets before commencement date. As of the commencement dates the present value of future minimum lease payments together with the amounts already prepaid exceeded the fair value of the leased assets, and the Group had to recognize an impairment loss on initial recognition of the leased assets. As a result, the difference of 94,242 (2009: 490,894) was immediately recognized within operating expenses in the income statement for 2010 (Note 20).

The Group had entered into a number of finance leases under which equipment was not received as at 31 December 2010. Accordingly, the liabilities arising from the above financial leases are not reported in these financial statements. The present value of future minimum lease payments under these agreements as at 31 December 2010 is 765,663 (31 December 2009: 1,878,475). Future interest expense is 194,034 (31 December 2009: 1,007,011). As at 31 December 2010 the Group paid advances of 932,851 under these leases (31 December 2009: 1,058,499).

16. Post-employment benefit liabilities

The Group makes obligatory contributions to the Government pension fund for its employees which are charged to expense when incurred during the employee's service period. Total contributions to Government pension fund amounted to 396,607 during the year ended 31 December 2010 (2009: 326,451).

In addition to mandatory payments to the Russian Federation state pension scheme, the Group provides non-government pensions to its employees through post-employment benefits unfunded plan.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

16. Post-employment benefit liabilities (continued)

The majority of employees are eligible for defined benefit plans which provide an old age retirement pension. The plans provide for payments of retirement benefits starting from statutory retirement age which is currently 55 for women and 60 for men. The amount of payments is calculated using the formula according to which the amount of benefit depends on a number of parameters, including an employee's salary at the retirement date and a number of years with the Group.

Non-government pension fund Electroenergetiki, which is related to the Group (Note 26), maintains the above defined benefit pension plan.

The Group further provides other long-term employee benefits of a defined benefit nature such as lump-sum payments upon retirement, lump-sum payments upon death, jubilees benefits.

As at 31 December 2010 there were 6,044 working employees participating to the defined benefit plan of the Group and 1,342 pensioners (31 December 2009: 5,923 and 1,389, respectively).

For the purpose of presentation, lump-sum benefits at retirement, pension benefits and funeral compensations are classified as 'post-employment benefits'; jubilee benefits and funeral compensations in the case of a relative's death are classified as 'long-term employee benefits'.

As at 31 December 2010 and 2009 net liabilities under defined benefit and other post-employment benefit plans comprised the following:

| | 2010 | | | 2009 | | |
|---|------------------|--------------------------------|-----------------------------------|------------------|--------------------------------|-----------------------------------|
| | Total | Post employment benefits | Long-term employee benefits | Total | Post employment benefits | Long-term employee benefits |
| Present value of defined benefit obligation | (438,280) | (348,778) | (89,502) | (374,822) | (314,621) | (60,201) |
| Unrecognized net actuarial gains | (12,360) | (12,360) | – | (29,208) | (29,208) | – |
| Unrecognized past service cost | 99,328 | 99,328 | – | 109,494 | 109,494 | – |
| Net pension liability in the statement of financial position | (351,312) | (261,810) | (89,502) | (294,536) | (234,335) | (60,201) |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

16. Post-employment benefit liabilities (continued)

Changes in the present value of defined benefit obligations in 2010 and 2009 were as follows:

| | 2010 | | | 2009 | | |
|---|----------------|--------------------------|-----------------------------|----------------|--------------------------|-----------------------------|
| | Total | Post employment benefits | Long-term employee benefits | Total | Post employment benefits | Long-term employee benefits |
| Net defined benefit obligation as at 1 January | 374,822 | 314,621 | 60,201 | 421,168 | 339,936 | 81,232 |
| Interest cost on benefit obligation | 36,473 | 29,319 | 7,154 | 33,148 | 27,797 | 5,351 |
| Current service cost | 19,532 | 12,816 | 6,716 | 17,653 | 12,511 | 5,142 |
| Past service cost (recognized and unrecognized) | 16,153 | – | 16,153 | (27,676) | (19,146) | (8,530) |
| Benefits paid | (33,642) | (24,826) | (8,816) | (29,094) | (22,121) | (6,973) |
| Actuarial losses/(gains) on obligation | 24,942 | 16,848 | 8,094 | (20,914) | (17,232) | (3,682) |
| Curtailement gain | – | – | – | (19,463) | (7,124) | (12,339) |
| Net defined benefit obligation as at 31 December | 438,280 | 348,778 | 89,502 | 374,822 | 314,621 | 60,201 |

The movements in the net pension liability in 2010 and 2009 were as follows:

| | 2010 | | | 2009 | | |
|--|----------------|--------------------------|-----------------------------|----------------|--------------------------|-----------------------------|
| | Total | Post employment benefits | Long-term employee benefits | Total | Post employment benefits | Long-term employee benefits |
| Net pension liability as at 1 January | 294,536 | 234,335 | 60,201 | 308,313 | 227,081 | 81,232 |
| Net expense/(income) | 90,418 | 52,301 | 38,117 | 15,317 | 29,375 | (14,058) |
| Benefits paid | (33,642) | (24,826) | (8,816) | (29,094) | (22,121) | (6,973) |
| Net pension liability as at 31 December | 351,312 | 261,810 | 89,502 | 294,536 | 234,335 | 60,201 |

Net expense/(income) under the defined benefit plans in 2010 and 2009 was as follows:

| | 2010 | | | 2009 | | |
|--|---------------|--------------------------|-----------------------------|---------------|--------------------------|-----------------------------|
| | Total | Post employment benefits | Long-term employee benefits | Total | Post employment benefits | Long-term employee benefits |
| Current service cost | 19,532 | 12,816 | 6,716 | 17,653 | 12,511 | 5,142 |
| Interest cost | 36,473 | 29,319 | 7,154 | 33,148 | 27,797 | 5,351 |
| Net actuarial loss/(gain) recognized in the period | 8,094 | – | 8,094 | (3,682) | – | (3,682) |
| Recognized past service cost | 26,319 | 10,166 | 16,153 | (12,585) | (4,055) | (8,530) |
| Curtailement gain | – | – | – | (19,217) | (6,878) | (12,339) |
| Net expense/(income) for the defined benefit plan | 90,418 | 52,301 | 38,117 | 15,317 | 29,375 | (14,058) |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

16. Post-employment benefit liabilities (continued)

Net expenses/(income) on the defined benefit plans were included in Payroll and payroll taxes in the consolidated income statement.

As at 31 December the principal actuarial assumptions of defined benefit pension plan were as follows:

| | <u>2010</u> | <u>2009</u> |
|---|-------------|-------------|
| Discount rate (actuarial rate of return), % | 8.0 | 9.5 |
| Estimated future salary increases, % | 7.5 | 8.0 |
| Estimated future rate of inflation, % | 6.0 | 6.5 |

Present value of defined benefit obligation and experience adjustments for the current and previous three periods are as follows:

| | <u>2010</u> | <u>2009</u> | <u>2008</u> | <u>2007</u> |
|--|-------------|-------------|-------------|-------------|
| Defined benefit obligation | (438,280) | (374,822) | (421,168) | (296,924) |
| Experience adjustments on plan liabilities | 14,714 | 5,715 | 56,625 | (32,967) |

The Group expects to contribute 34,869 to its defined benefit pension plans in 2011.

17. Other non-current liabilities

| | <u>31 December 2010</u> | <u>31 December 2009</u> |
|-----------------------------|-----------------------------|-----------------------------|
| Long-term advances received | 2,053,831 | 1,223,292 |
| Trade accounts payable | 62,135 | 51,581 |
| Total | <u>2,115,966</u> | <u>1,274,873</u> |

18. Trade and other payables

| | <u>31 December 2010</u> | <u>31 December 2009</u> |
|---|-----------------------------|-----------------------------|
| Trade accounts payable | 3,298,985 | 2,914,569 |
| Provisions | 202,514 | 310,273 |
| Interest accrued on bank loans and coupon bonds | 171,790 | 246,430 |
| Salaries payable | 147,940 | 163,893 |
| Other taxes payable | 89,735 | 67,916 |
| Other | 343,070 | 275,496 |
| Total | <u>4,254,034</u> | <u>3,978,577</u> |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

18. Trade and other payables (continued)

Movements in provisions during the reporting period were as follows:

| | Litigations | Employee related | Total |
|-------------------------------|---------------|---------------------|----------------|
| As at 1 January 2009 | 67,400 | 64,676 | 132,076 |
| Arising during the period | 120,091 | 358,993 | 479,084 |
| Utilised | (54,634) | (233,950) | (288,584) |
| Reversed | (12,303) | – | (12,303) |
| As at 31 December 2009 | 120,554 | 189,719 | 310,273 |
| Arising during the period | 16,516 | 125,263 | 141,779 |
| Utilised | (51,352) | (149,664) | (201,016) |
| Reversed | (48,522) | – | (48,522) |
| As at 31 December 2010 | 37,196 | 165,318 | 202,514 |

Provision for litigations relates to the claims brought against the Group in the ordinary course of business. The balance of the provision as at 31 December 2010 is expected to be utilised in 2011. The management of the Group believes that the outcome of current legal claims will not give rise to any significant loss beyond the accrued amounts.

Employee-related provisions relates to annual bonus and unused vacation.

19. Revenue

| | 2010 | 2009 |
|---|-------------------|-------------------|
| Network transmission of electricity | 23,872,903 | 19,335,492 |
| Technological losses at the normal (expected) level | (6,181,027) | (3,919,789) |
| Network transmission of electricity, net of normal (expected) losses | 17,691,876 | 15,415,703 |
| Technological connection to electricity grids | 10,299,774 | 6,638,230 |
| Other revenue | 581,925 | 746,457 |
| Total | 28,573,575 | 22,800,390 |

In 2010 electricity transmission revenue before technological losses at the normal (expected) level from OJSC PSK and LLC Energia-Holding, amounted to 16,269,034 (2009: 13,406,763) and 5,557,066 (2009: 2,878,569), respectively, comprising 91% (2009: 83%) of the total revenue from transmission of electricity before the technological losses at the normal (expected) level. Technological connection fees of 4,525,382 (2009: 2,293,975) were settled by contribution of property, plant and equipment items from the customers.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

20. Operating expenses

| | 2010 | 2009 |
|---|-------------------|-------------------|
| Transmission fee | 9,773,797 | 6,824,717 |
| Depreciation (Note 5) | 4,430,867 | 3,918,077 |
| Payroll and payroll taxes | 3,224,912 | 2,819,333 |
| Repairs and maintenance | 936,824 | 831,428 |
| Rent | 504,015 | 503,256 |
| Telecommunication and information services | 265,783 | 244,672 |
| Provision for impairment of receivables (Note 13) | 260,548 | 226,052 |
| Raw materials and supplies | 231,235 | 210,149 |
| Social expenses | 172,853 | 161,626 |
| Taxes other than income tax | 154,512 | 185,303 |
| Consulting, legal and audit services | 146,121 | 216,913 |
| Electric metering services | 131,964 | 242,584 |
| Amortisation of intangible assets (Note 4) | 117,487 | 128,249 |
| Internal security expenses | 110,770 | 110,469 |
| Utilities | 108,019 | 78,076 |
| Impairment loss on finance leases (Note 15) | 94,242 | 490,894 |
| Impairment of intangible asset (Note 4) | 37,360 | 139,000 |
| Agency services | 23,549 | 41,933 |
| (Reversal of) provision for impairment of inventories | (50,877) | 3,512 |
| Impairment of goodwill | – | 312,833 |
| Other operating expenses | 766,810 | 800,100 |
| Total | 21,440,791 | 18,489,176 |

21. Finance income

| | 2010 | 2009 |
|---|----------------|---------------|
| Gain on disposal of available-for-sale investments (Note 7) | 532,866 | – |
| Gain on swap settlement | 143,179 | – |
| Interest receivable | 72,977 | 50,467 |
| Dividends received | 25,085 | 16,072 |
| Other finance income | 20 | 11,321 |
| Total | 774,127 | 77,860 |

Gain on swap contract settlement in the amount of 1,219,015 is presented net of change in fair value of swap asset of 1,075,836 (Note 12).

22. Finance expenses

| | 2010 | 2009 |
|------------------------------------|------------------|------------------|
| Interest expense on loans | 719,078 | 524,561 |
| Interest expense on bonds | 507,359 | 511,734 |
| Interest expense on finance leases | 332,846 | 185,943 |
| Change in fair value of swap | – | 816,018 |
| Other finance expenses | 20,273 | 46,172 |
| Total | 1,579,556 | 2,084,428 |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

23. Income tax

| Consolidated income statement | 2010 | 2009 |
|---|------------------|------------------|
| Current income tax: | | |
| Current income tax charge | 1,383,642 | 1,396,247 |
| Reverse of tax accruals under favourable court resolutions (Note 25) | – | (1,226,564) |
| Deferred income tax: | | |
| Relating to origination/(reversal) of temporary differences | 123,151 | (625,169) |
| Income tax expense /(benefit) reported in the income statement | 1,506,793 | (455,486) |

| Consolidated statement of comprehensive income | 2010 | 2009 |
|--|---------------|---------------|
| Deferred tax related to items charged or credited directly to equity during the year: | | |
| Unrealised (gain)/loss on available-for-sale investments | (32,241) | 44,276 |
| Reclassification of unrealized gain reserve on available-for-sale financial assets to income statement | 106,573 | – |
| Income tax charged directly to equity | 74,332 | 44,276 |

Reconciliation between tax expense and accounting profit multiplied by tax rate for the years ended 31 December is as follows:

| | 2010 | 2009 |
|---|------------------|------------------|
| Accounting profit before tax | 6,257,214 | 2,131,886 |
| Theoretical tax expense at statutory income tax rate of 20% | 1,251,443 | 426,377 |
| Non-deductible expenses | 255,350 | 282,134 |
| Reverse of tax accruals under favourable court resolutions (Note 25) | – | (1,226,564) |
| Impairment of goodwill | – | 62,567 |
| Income tax expense /(benefit) reported in the consolidated income statement at the effective income tax rate of 24% (2009: -21%) | 1,506,793 | (455,486) |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

23. Income tax (continued)

Deferred income tax as at 31 December 2010 relates to the following:

| | 31 December 2009 | Movement during 2010 recognized in | | 31 December 2010 |
|---|---------------------|---------------------------------------|----------------------------------|---------------------|
| | | Equity | Profit or loss for the period | |
| <i>Tax effect of deferred tax assets:</i> | | | | |
| Impairment provision for accounts receivable | 139,127 | – | 50,924 | 190,051 |
| Inventory impairment provision | 29,773 | – | (11,145) | 18,628 |
| Foreign exchange differences on swapped loan | 229,771 | – | (229,771) | – |
| Post-employee benefits liability | 58,907 | – | 11,355 | 70,262 |
| Employee-related accruals | 31,549 | – | 1,514 | 33,063 |
| Impairment of intangible assets | 27,800 | – | 7,472 | 35,272 |
| Others | 78,847 | – | 22,335 | 101,182 |
| Deferred tax assets, total | 595,774 | – | (147,316) | 448,458 |
| <i>Tax effect of deferred tax liabilities:</i> | | | | |
| Property, plant and equipment | (5,616,540) | – | (134,564) | (5,751,104) |
| Revaluation of available-for-sale investments | (28,257) | 74,332 | (42,191) | 3,884 |
| Discounting of long-term trade accounts payable | (4,353) | – | (4,780) | (9,133) |
| Revaluation of swap to fair value | (215,167) | – | 215,167 | – |
| Discounting of bonds issued | (4,892) | – | 2,115 | (2,777) |
| Deferred expenses | (9,658) | – | (11,582) | (21,240) |
| Deferred tax liabilities, total | (5,878,867) | 74,332 | 24,165 | (5,780,370) |
| Total deferred tax liabilities, net | (5,283,093) | 74,332 | (123,151) | (5,331,912) |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

23. Income tax (continued)

| | 31 December 2008 | Movement during 2009 recognized in | | 31 December 2009 |
|---|---------------------|---------------------------------------|----------------------------------|---------------------|
| | | Equity | Profit or loss for the period | |
| <i>Tax effect of deferred tax assets:</i> | | | | |
| Impairment provision for accounts receivable | 178,526 | – | (39,399) | 139,127 |
| Inventory impairment provision | 31,523 | – | (1,750) | 29,773 |
| Foreign exchange differences on swapped loan | 189,813 | – | 39,958 | 229,771 |
| Post-employee benefits liability | 61,662 | – | (2,755) | 58,907 |
| Employee-related accruals | 7,370 | – | 24,179 | 31,549 |
| Impairment of intangible assets | – | – | 27,800 | 27,800 |
| Others | 34,886 | – | 43,961 | 78,847 |
| Deferred tax assets, total | 503,780 | – | 91,994 | 595,774 |
| <i>Tax effect of deferred tax liabilities:</i> | | | | |
| Property, plant and equipment | (6,002,880) | – | 386,340 | (5,616,540) |
| Revaluation of available-for-sale investments | 16,019 | (44,276) | – | (28,257) |
| Discounting of long-term trade accounts payable | (11,472) | – | 7,119 | (4,353) |
| Revaluation of swap to fair value | (381,227) | – | 166,060 | (215,167) |
| Discounting of bonds issued | (7,399) | – | 2,507 | (4,892) |
| Deferred expenses | 19,193 | – | (28,851) | (9,658) |
| Deferred tax liabilities, total | (6,367,766) | (44,276) | 533,175 | (5,878,867) |
| Total deferred tax liabilities, net | (5,863,986) | (44,276) | 625,169 | (5,283,093) |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

24. Earnings per share

| | 31 December 2010 | 31 December 2009 |
|--|-----------------------------|-----------------------------|
| Weighted average number of outstanding ordinary shares (thousands) | 926,022 | 926,022 |
| Weighted average number of outstanding preference shares (thousands) | 93,264 | 93,264 |
| Net profit attributable to equity holders | 4,746,691 | 2,578,481 |
| - attributable to holders of ordinary shares | 4,312,372 | 2,342,552 |
| - attributable to holders of preference shares | 434,312 | 235,929 |
| Earnings per ordinary share – basic and diluted (Rubles) | 4.66 | 2.53 |
| Earnings per preference share – basic and diluted (Rubles) | 4.66 | 2.53 |

25. Commitments and contingencies

Operating lease commitments

Operating lease commitments mainly relate to contractual obligations under long-term lease agreements for office premises and land plots under Group's power lines and equipment. These non-cancellable leases have terms between 5 and 49 years and contain renewal option. Rent expenses for 2010 in the amount of 504,015 (2009: 503,256) were recognized within income statement (Note 20).

Future minimum rentals payable under non-cancellable operating leases as at 31 December are as follows:

| | 2010 | 2009 |
|---|------------------|------------------|
| Within one year | 373,423 | 373,328 |
| After one year but not more than five years | 1,181,298 | 1,501,873 |
| More than five years | 396,106 | 401,977 |
| Total | 1,950,827 | 2,277,178 |

Commitments to purchase property, plant and equipment

Future capital expenditures under the signed contracts amount to 13,657,959 as at 31 December 2010 (31 December 2009: 18,865,916).

As at 31 December 2010 the Group provided the following guarantees for the loan granted by OJSC Bank VTB Severo-Zapad to the Group's lessor (CJSC Rosgazleasing):

| Guarantee | Underlying loan agreement | Maturity date | Amount of loan guaranteed |
|--------------------|----------------------------------|----------------------|----------------------------------|
| CJSC Rosgazleasing | №107/07 dated 22 August 2007 | 22 August 2012 | 26,780 |

Social commitments

The Group contributes to the maintenance and upkeep of the local infrastructure and the welfare of its employees involved in production. In particular, the Group participates in the development and maintenance of housing, recreation and other social needs in the geographical areas in which it operates. All expenditures in connection with social commitments are expensed when incurred.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

25. Commitments and contingencies (continued)

Political environment

The operations and earnings of the Group are affected by political, legislative, fiscal and regulatory developments in Russia.

Operating environment of the Group

Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. In 2010 the Russian Government continued to take measures to support the economy in order to overcome the consequences of the global financial crisis. Despite some indications of recovery there continues to be uncertainty regarding further economic growth, access to capital and cost of capital, which could negatively affect the Group's future financial position, results of operations and business prospects.

While the management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

Tax legislation

The existing Russian tax, currency and customs legislation allows for various interpretations and is prone to frequent changes. Interpretation by the Group's management of the legislation in place when applicable to the Group's transactions and activities may be challenged by the appropriate regional or federal authorities. Recent events that occurred in the Russian Federation are indicative of the fact that tax authorities may assume a tougher stance with regard to interpretation of legislation and review of tax returns. Consequently, tax authorities may challenge transactions and accounting methods that they had never challenged before. As a result, significant additional taxes, penalties and fines may be accrued. It is not possible to determine amounts of constructive claims or evaluate probability of their negative outcome. Tax audits may cover a period of three calendar years immediately preceding the reporting one. Under certain circumstances, tax authorities may review earlier accounting periods.

As at 31 December 2010 management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained.

Since the tax and other legislation does not fully cover all aspects of the Group restructuring, certain legal and tax risks might still arise.

In 2010 the tax authorities performed a tax field audit of the Group covering the period from 1 January 2007 to 31 December 2008. As a result no significant incompliances with tax legislation were identified.

As at 31 December 2009 under favourable resolution of the Supreme Arbitration Court the Group reversed 1,226,564 (Note 23) of taxes accrued as a result of field tax audit in 2008.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

25. Commitments and contingencies (continued)

Environmental matters

Group entities and their predecessor entities have operated in the electric power industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group entities periodically evaluate their obligations under environmental regulations. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, 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.

Insurance

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

Legal proceedings

Sometimes, the Group is a 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, may have a material adverse effect on the financial position of the Group.

26. Related party transactions

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

The Group had balances outstanding as at 31 December 2010 and 2009 with the following related parties.

Transactions with MRSK-Holding and entities under MRSK-Holding control

| | 31 December 2010 | 31 December 2009 |
|--|---------------------|---------------------|
| <i>Accounts receivable, including:</i> | | |
| Advances given | 516 | 916 |
| OJSC NW EMK | 516 | 674 |
| OJSC EnergoUchet | – | 242 |
| <i>Accounts payable, including</i> | | |
| Trade accounts payable | 5,987 | 6,210 |
| MRSK-Holding | 5,664 | 5,664 |
| OJSC EnergoUchet | 323 | – |
| OJSC NW EMK | – | 546 |
| Other accounts payable | 1,633 | 44,198 |
| MRSK-Holding | – | 44,198 |
| OJSC NW EMK | 1,633 | – |

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

26. Related party transactions (continued)

| | 2010 | 2009 |
|---------------------------|-------|------|
| Dividends received | | |
| OJSC NW EMK | 4,134 | – |

Transactions with other related parties

Non-government pension fund Electroenergetiki

The outstanding balances with NPF Electroenergetiki were as follows:

| | 31 December 2010 | 31 December 2009 |
|---------------------------|---------------------|---------------------|
| Other accounts receivable | 118,482 | 112,967 |

Compensation to key management personnel

Key management personnel comprise general director of the Company and his deputies, including finance director and chief accountant, as well as members of the Board of Directors. Total compensation to key management personnel, which is represented by short-term and termination employee benefits (monthly payroll, annual bonuses and pensions), included in payroll and payroll taxes in the income statement, was as follows:

| | 2010 | 2009 |
|------------------------------|----------------|---------------|
| Short-term employee benefits | 59,751 | 66,551 |
| Termination benefits | 47,123 | 9,276 |
| Total | 106,874 | 75,827 |

Transactions with state-controlled entities

In the course of its operating activities the Group is also engaged in significant transactions with state-controlled entities. Revenues and purchases from state-controlled entities are measured at regulated tariffs where applicable, in other cases revenues and purchases are measured at normal market prices.

27. Segment information

The Group operates in one industry segment, being the provision of electricity transmission services and technological connection to the electricity grids to domestic customers in one geographic area, i.e. St. Petersburg and Leningrad region. The results of this segment and assets and liabilities as at 31 December 2010 and 2009 are presented in the consolidated income statement and the consolidated statement of financial position, respectively.

An analysis of revenue by service type is disclosed in Note 19.

All of the Group's assets are located within the territory of St. Petersburg and Leningrad Region.

The Group had no individual customers, other than disclosed in Note 19 that accounted for greater than 10% of its revenue during the years ended 31 December 2010 and 2009.

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

28. Financial risk management

As at 31 December 2010 the Group's major financial liabilities comprise bank loans, bonds, finance leases and trade payables. The main purpose of these instruments is to raise finance for the Group's operations. The Group has various financial assets such as trade receivables, cash and short term deposits which arise directly from its operations.

In addition, during 2010 the Group fully settled its payment obligations in a transaction involving a derivative instrument, namely, a currency/interest rate swap agreement concluded in 2007 with a view to manage interest rate and foreign exchange risks arising from the changes in floating interest rates and foreign exchange rates which affect its currency denominated borrowings. It is, and has been throughout 2010 and 2009, the Group's policy that no trading in derivatives shall be undertaken.

The main risks arising from the Group's financial instruments are credit risk and liquidity risk. The exposure of the Group to these and other financial risks is disclosed below.

Credit risk

The Group trades only with recognised, creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant. The maximum exposure is the carrying amount as disclosed in Note 10.

The Group's revenue from two largest customers OJSC PSK and LLC Energia-Holding is disclosed in Note 19.

With respect to credit risk arising from other financial assets of the Group, which comprise cash and cash equivalents, available-for-sale financial investments, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Liquidity risk

The Group monitors its risk of a shortage of funds using a recurring liquidity planning tool. With the help of this tool, the Group considers the maturity of both its financial assets and liabilities and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans, bonds, preference shares and finance leases.

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

28. Financial risk management (continued)

Fair value hierarchy (continued)

Reconciliation of fair value measurements of Level 1 and Level 3 financial instruments

| | Level 1 | | Level 3 | | Total |
|--|-----------|-----------|---------------|------------|------------------|
| | OJSC FSK | OJSC PSK | OJSC NW | EMK Other | |
| 1 January 2009 | 71,700 | 196,000 | 36,700 | 133 | 232,833 |
| Unrealised gains (losses) recognised in other comprehensive income | 117,780 | 107,000 | (3,400) | – | 221,380 |
| 31 December 2009 | 189,480 | 303,000 | 33,300 | 133 | 336,433 |
| Unrealised gains (losses) recognised in other comprehensive income | (393) | 165,000 | (3,400) | – | 161,207 |
| Sales (Note 7) | (189,087) | (468,000) | – | (33) | (657,120) |
| 31 December 2010 | – | – | 29,900 | 100 | 30,000 |

Capital risk management

Capital includes ordinary and preference shares attributable to the equity holders of the parent.

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise shareholder value. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares.

No changes were made in the objectives, policies or processes during the years ending 31 December 2010 and 31 December 2009.

The Group monitors capital using a gearing ratio, which is net debt divided by total capital plus net debt. The Group's policy is to keep the gearing ratio up to 80%. The Group includes within net debt, interest bearing loans and borrowings, trade and other payables, less cash and cash equivalents.

| | 31 December 2010 | 31 December 2009 |
|---|---------------------|---------------------|
| Interest-bearing borrowings (Note 15) | 14,547,716 | 15,002,452 |
| Trade and other payables (Note 18) | 4,254,034 | 3,978,577 |
| Less cash and cash equivalents (Note 9) | (653,068) | (2,948,801) |
| Net debt | 18,148,682 | 16,032,228 |
| Ordinary shares (Note 14) | 4,866,115 | 4,866,115 |
| Preference shares (Note 14) | 625,603 | 625,603 |
| Total capital | 5,491,718 | 5,491,718 |
| Capital and net debt | 23,640,400 | 21,523,946 |
| Gearing ratio | 77% | 74% |

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

28. Financial risk management (continued)

Liquidity risk (continued)

The table below summarises the maturity profile of the Group's financial liabilities as at 31 December 2010 and 2009 based on contractual undiscounted payments:

| As at 31 December 2010 | 1 year | 2 years | 3-5 years | Over 5 years |
|----------------------------------|------------------|------------------|------------------|--------------|
| Bonds issued | 652,348 | 6,247,719 | - | - |
| Interest-bearing loans | 1,663,929 | 2,513,425 | 6,116,531 | - |
| Trade and other accounts payable | 3,642,055 | 1,800 | 106,001 | - |
| Other financial obligations | 767,450 | 509,029 | 154,992 | - |
| Total | 6,725,782 | 9,271,973 | 6,377,524 | - |

| As at 31 December 2009 | 1 year | 2 years | 3-5 years | Over 5 years |
|----------------------------------|-------------------|------------------|------------------|--------------|
| Bonds issued | 651,703 | 495,439 | 6,247,719 | - |
| Interest-bearing loans | 5,765,327 | 3,324,038 | - | - |
| Trade and other accounts payable | 3,190,065 | 1,800 | 107,801 | - |
| Other financial obligations | 915,129 | 796,961 | 551,542 | - |
| Total | 10,522,224 | 4,618,238 | 6,907,062 | - |

Fair values

Set out below is a comparison by category of carrying amount and fair value of the Group's financial instruments that are carried in the consolidated financial statements:

| | 2010 | | 2009 | |
|----------------------------------|-----------------|--------------|-----------------|-------------|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| Financial assets | | | | |
| Cash | 653,068 | 653,068 | 2,948,801 | 2,948,801 |
| Available-for-sale investments | 30,000 | 30,000 | 525,913 | 525,913 |
| Loans and receivables | 1,493,998 | 1,493,998 | 1,383,883 | 1,383,883 |
| Derivative financial instruments | - | - | 1,075,836 | 1,075,836 |
| Financial liabilities | | | | |
| Obligations under finance leases | (1,143,176) | (1,143,176) | (1,682,028) | (1,682,028) |
| Floating rate borrowings | - | - | (6,026,914) | (6,026,914) |
| Short-term fixed rate borrowings | (1,000,000) | (1,000,000) | - | - |
| Long-term fixed rate borrowings | (13,663,600) | (13,547,716) | (8,975,538) | (8,692,200) |
| Interest payable on borrowings | (171,790) | (171,790) | (246,430) | (246,430) |

OJSC Lenenergo

Notes to the consolidated financial statements (continued)

28. Financial risk management (continued)

Fair values (continued)

The following methods and assumptions were used to estimate the fair values:

Cash, loans and receivables, interest payable and short-term borrowings approximate their carrying amounts largely due to the short-term maturities of these instruments.

The fair value of available-for-sale investments was determined using valuation techniques disclosed in Note 7.

The fair value of obligations under finance leases is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

The fair value of borrowings is calculated by discounting the expected future cash flows at interest rates determined with regard to the Group's creditworthiness. As at 31 December 2010, the carrying amounts of borrowings are not materially different from their calculated fair values.

Fair value hierarchy

As at 31 December 2010 and 2009 the Group held the following financial instruments measured at fair value:

| | 31 December 2010 | Level 1 | Level 2 | Level 3 |
|----------------------------------|-------------------------|----------------|----------------|----------------|
| Available-for-sale investments | 30,000 | – | – | 30,000 |
| | 31 December 2009 | Level 1 | Level 2 | Level 3 |
| Available-for-sale investments | 525,913 | 189,480 | – | 336,433 |
| Derivative financial instruments | 1,075,836 | – | 1,075,836 | – |

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

For financial instruments for which quoted prices in an active market are available, the fair value is determined directly from those quoted market prices (Level 1).

For financial instruments which do not have quoted market prices directly available from an active market, fair values are estimated using valuation techniques or models, based wherever possible on assumption supported by observable market prices or rate prevailing at the reporting date (Level 2).

For other financial instruments the fair value cannot be obtained directly from quoted market prices, or indirectly using valuation techniques based on observable market data (Level 3). For these instruments the fair value is estimated using income approach.

During the year ended 31 December 2010 and 2009 there were no transfer within Level 1 and Level 2 of the fair value measurements.

The transfer out of Level 1 and Level 3 in the amount of 189,480 and 303,000 resulted from the sale of investment in OJSC FSK UES and OJSC PSK (Note 7).

The transfer out of Level 2 in the amount of 1,075,836 occurred due to the settlement of swap contract (Note 15).

OJSC Lenenergo
Notes to the consolidated financial statements (continued)

28. Financial risk management (continued)

Capital risk management (continued)

As at 31 December 2010 the Group has been in compliance with share capital requirements established by the legislation of Russian Federation.

Foreign exchange and interest rate risks

The Group operates in the Russian Federation. The majority of the Group's purchases and borrowings are denominated in Russian Rubles. In 2010 interest rate and foreign exchange risks were solely attributable to a syndicated foreign currency denominated loan fully settled in 2010 (Note 15).

29. Events after the reporting period

In January 2011 the Group fully met its coupon obligations on the 2nd bond issue under the 8th coupon at 8.54% p.a. in the total amount of 127,740.

In January and February 2011 the Group borrowed 1,853,900, 713,630 and 96,662 under credit lines granted by OJSC Sberbank, OJSC Bank VTB Severo-Zapad and OJSC AKB Svyaz-bank, respectively bearing interest of 7.11% and 8.06% respectively.