# PJSC "IDGC of Centre"

# Consolidated Financial Statements for the year ended 31 December 2016 with Independent Auditor's Report

## Contents

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15.03.2017
№ ФСМ-1695

# INDEPENDENT AUDITOR'S REPORT

**To: the Shareholders of PJSC "IDGC of Centre"**

**Audited entity:**
**Interregional Distribution Grid Company of Centre, Public Joint Stock Company** (abbreviated name - **PJSC "IDGC of Centre"**);
Location: 4, 2nd Yamskaya street, Moscow, 127018, the Russian Federation;
Primary state registration number – 1046900099498.

**Auditor:**
**RSM RUS Ltd.**
Location: 4, Pudovkina Str., Moscow, 119285;
Tel.: (495) 363-28-48; Fax: (495) 981-41-21;
Primary state registration number – 1027700257540;
RSM RUS Ltd. is a member of Self-regulatory organization of auditors Association "Sodruzhestvo" (membership certificate # 6938, ORNZ 11306030308), location: 21, Michurinsky Ave., bldg. 4, Moscow, 119192.

***Opinion***

We have audited the consolidated financial statements of **PJSC IDGC of Center** and its subsidiaries (the Group), which comprise the Consolidated Statement of Financial Position as of 31 December 2016, and the Consolidated Statement of profit or loss and other comprehensive income , Consolidated Statement of Changes in Equity and Consolidated Statement of Cash Flows for the year then ended and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

### *Basis for Opinion*

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants` Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Russian Federation, and we have fulfilled our other ethical responsibilities in accordance with these requirements and IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### *Key Audit Matters*

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters

#### Impairment of non-current assets

In our opinion, this matter was one of most significance in our audit due to a significant share of property, plant and equipment in total assets of the Group, high level of subjectivity of assumptions used to determine a value in use of property, plant and equipment as well as materiality of judgments and estimates made by the management.

The majority of the Group's property, plant and equipment is specialized in nature and is rarely sold on the open market other than as part of a continuing business. The market for similar property, plant and equipment is not active in the Russian Federation and does not provide a sufficient number of sales transactions for use of a market-based approach for determination of the fair value of the property, plant and equipment.

Therefore, the value in use for property, plant and equipment as at 31 December 2016 was determined using projected cash flows method. This method considers the future net cash flows expected to be generated through the usage of property, plant and equipment during the operating activities and upon disposal, to determine the recoverable amount of these assets.

We have performed procedures of analysis and testing of the model used in making the estimates, assessment of adequacy of assumptions underlying the estimates, including assumptions in respect of projected revenue, tariffs solutions, discount rates etc.

We have also reviewed the relevant controls in respect of the estimates, consideration by management of estimation uncertainty and changes in approaches as compared to the previous period. We have reviewed the actual outcomes of the use of the model to obtain sufficient and appropriate audit evidence about whether the management in making the estimates complied with IFRS requirements, the methods used in estimates of tests are appropriate and are applied consistently and the changes in estimates are reasonable based on information available at the date of preparation of the accounts.

For testing the model of estimate and underlying assumptions, we have engaged an expert in accordance with the procedure established by ISA.

We have evaluated the accuracy and sufficiency of disclosures to the consolidated financial statements of information about determination of the value of property, plant and equipment, including information about uncertainties taken into consideration when making impairment test estimates.

Non-current assets are disclosed in Note 12 to the consolidated financial statements.

### Impairment of accounts receivable

In our opinion, this matter was one of most significance in our audit due to significant balances of the Group's accounts receivable as at 31 December 2016, and because the management estimate of collectability of the receivables is based on the assumptions, in particular, forecasting financial solvency of the Group's customers.

We have performed procedures of evaluation of the adequacy of the Group's policy on reviewing accounts receivable and determining if accounts receivables impairment allowance should be established, as well as procedures of confirming the reasonableness of the estimates made by the management of the Group, including review of accounts receivable payments, review of maturity dates and overdue debts, review of customers' financial solvency.

We performed audit procedures in respect of information used by the Group to determine the impairment of accounts receivable, accounts receivable ageing structure, tested the accuracy of accrued accounts receivables impairment allowance based on the estimates documented by the management.

Accrued accounts receivables impairment allowance is disclosed by the Group in Notes 18, 28 to the consolidated financial statements.

### Recognition and measurement of revenue

Recognition and measurement of revenue were matters of most significance in our audit due to certain imperfection of mechanisms of operation of retail electricity market and it leads to disagreements between electric grid companies and energy supply companies in respect of volume of electricity consumption and capacity. The assessment by the Group's management of favorable outcome of the dispute resolution is, to a large extent, subjective and is based on the assumptions of dispute resolution.

We evaluated the internal control over revenue recognition, reviewed the accuracy of determined revenue amounts based on concluded contracts for electricity transmission and other work (services), on a sample basis obtained confirmations of accounts receivable balances from the counterparties, reviewed and evaluated existing procedures for confirming the volume of electricity transmitted and outcomes of litigations in respect of disputed amounts for the provided services, and also performed other procedures to obtain sufficient and appropriate audit evidence, in order to confirm the accuracy, in all material respects, of the amounts of revenues recognized in the consolidated financial statements.

Revenue is disclosed in Note 7 to the consolidated financial statements.

### Service Concession Arrangement

In our opinion, this matter was one of most significance in our audit due to a significant share of the item in the form of the right to charge a fee from the users of electricity transmission services under "Service Concession Arrangement concerning the financing, establishment and operation of facilities for the transmission and distribution of electric energy on the territory of the Tambov region" in total intangible assets of the Group and high level of subjectivity of assumptions used to determine the asset value.

We made sure that the Group applies IFRIC 12 "Service Concession Arrangements".

We checked that the intangible asset was recognized at the fair value of remuneration that will be received by the Group for the construction of facilities under the concession agreement.

Information about the concession agreement is provided in Note 13 to the consolidated financial statements.

**Recognition, measurement and disclosure of provisions and contingent liabilities**

Recognition, measurement and disclosure of provisions and contingent liabilities in respect of litigations and claims of counterparties (including territorial electric grid companies and energy supply companies) were matters of most significance in our audit because they require a lot of management judgments in respect of significant amounts in dispute in the course of litigations and claim settlements.

The audit procedures included review of court rulings made by courts of different levels, review of adequacy of management judgments and documents confirming the assessment of possibility of outflow of economic resources following dispute resolutions, conformity of the prepared documentation with the existing contracts and compliance with the law.

Accrued provisions and contingent liabilities of the Group are disclosed in Notes 26, 31 to the consolidated financial statements.

***Responsibilities of Management and the Audit Committee of the Board of Directors for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the 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.

In preparing the consolidated financial statement, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

The Audit Committee of the Board of Directors is responsible for overseeing the Group's financial reporting process.

***Auditor's Responsibilities for the Audit of the Consolidated Financial Statements***

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee of the Board of Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee of the Board of Directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Audit Committee of the Board of Directors, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**Management Board Chairperson** — **N.A. Dantser**

Audit Certificate No. 05-000015. Issued following Resolution of self-regulatory organization Not-for-Profit Partnership "Russian Collegium of Auditors" dated 15 November 2011 No. 24. Permanent award.

ORNZ in the Register of auditors and audit organizations – 21706004215

"РСМ РУСЬ"

**Manager responsible for the audit** — **E.A. Gareeva**

Audit Certificate No. 05-000086. Issued following Resolution of self-regulatory organization Not-for-Profit Partnership "Russian Collegium of Auditors" dated 14 February 2012 No.4. Permanent award.

ORNZ in the Register of auditors and audit organizations – 21706002832

*Thousands of Russian Roubles, unless otherwise stated*

| | Note | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|---|
| Revenue | 7 | 86,294,863 | 80,830,287 |
| Operating expenses | 8 | (78,752,167) | (75,204,444) |
| Other income | 7 | 1,702,420 | 1,448,480 |
| **Results from operating activities** | | **9,245,116** | **7,074,323** |
| Finance income | 10 | 297,035 | 308,245 |
| Finance costs | 10 | (4,793,264) | (4,581,801) |
| **Net finance costs** | | **(4,496,229)** | **(4,273,556)** |
| **Profit before income tax** | | **4,748,887** | **2,800,767** |
| Income tax benefit / (expense) | 11 | 13,406 | (1,919,820) |
| **Profit for the year** | | **4,762,293** | **880,947** |
| **Other comprehensive income / (expense)** | | | |
| Net change in fair value of available-for-sale financial assets | 15 | (19,904) | 70,683 |
| Income tax on other comprehensive income | | 3,981 | (14,137) |
| *Total items that are or may be reclassified to profit or loss* | | **(15,923)** | **56,546** |
| Remeasurements of the net defined benefit liability | 24 | 71,659 | (181,439) |
| Income tax on other comprehensive income | | (2,603) | 27,476 |
| *Total items that will never be reclassified to profit or loss* | | **69,056** | **(153,963)** |
| **Other comprehensive income / (expense) for the year, net of income tax** | | **53,133** | **(97,417)** |
| **Total comprehensive income for the year** | | **4,815,426** | **783,530** |
| **Profit attributable to:** | | | |
| Owners of the Company | | 4,723,758 | 852,807 |
| Non-controlling interests | | 38,535 | 28,140 |
| | | **4,762,293** | **880,947** |
| **Total comprehensive income attributable to:** | | | |
| Owners of the Company | | 4,776,891 | 755,390 |
| Non-controlling interests | | 38,535 | 28,140 |
| | | **4,815,426** | **783,530** |
| **Earnings per share – basic and diluted (in Russian Roubles)** | 21 | 0.112 | 0.020 |

These consolidated financial statements were approved on 15.03.2017:

General Director
O.Y. Isaev

Chief Accountant
L.A. Sklyarova

The consolidated statement of profit or loss and other comprehensive income is to be read in conjunction with the Notes to, and forming part of, the consolidated financial statements 1 - 33.

*Thousands of Russian Roubles, unless otherwise stated*

| | Note | 31 December 2016 | 31 December 2015 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 12 | 83,790,818 | 77,639,154 |
| Intangible assets | 13 | 2,345,282 | 1,797,450 |
| Investments and financial assets | 15 | 713,486 | 673,062 |
| Other non-current assets | 16 | 166,251 | 65,768 |
| **Total non-current assets** | | **87,015,837** | **80,175,434** |
| **Current assets** | | | |
| Cash and cash equivalents | 17 | 2,567,305 | 123,220 |
| Trade and other receivables | 18 | 13,977,188 | 16,762,252 |
| Income tax prepayment | | 1,382,137 | 1,375,661 |
| Inventories | 19 | 2,099,699 | 2,012,403 |
| **Total current assets** | | **20,026,329** | **20,273,536** |
| **Total assets** | | **107,042,166** | **100,448,970** |
| **EQUITY AND LIABILITIES** | | | |
| **Equity** | 20 | | |
| Share capital | | 4,221,794 | 4,221,794 |
| Reserves | | (81,778) | (134,911) |
| Retained earnings | | 38,947,905 | 34,672,186 |
| **Total equity attributable to equity holders of the Company** | | **43,087,921** | **38,759,069** |
| Non-controlling interests | | 165,809 | 127,274 |
| **Total equity** | | **43,253,730** | **38,886,343** |
| **Non-current liabilities** | | | |
| Loans and borrowings | 22 | 39,282,692 | 40,435,180 |
| Employee benefits | 24 | 2,202,613 | 2,344,882 |
| Deferred tax liabilities | 14 | 4,420,822 | 5,177,990 |
| Trade and other payables | 26 | 1,035,516 | 380,688 |
| **Total non-current liabilities** | | **46,941,643** | **48,338,740** |
| **Current liabilities** | | | |
| Loans and borrowings | 22 | 3,995,795 | 1,676,505 |
| Finance lease liability | 23 | - | 1,503 |
| Trade and other payables | 26 | 8,174,734 | 8,311,537 |
| Provisions | 26 | 1,026,203 | 1,099,872 |
| Employee payables | 25 | 1,431,899 | 640,000 |
| Income tax payable | | 2,438 | 71 |
| Other taxes payable | 27 | 2,215,724 | 1,494,399 |
| **Total current liabilities** | | **16,846,793** | **13,223,887** |
| **Total liabilities** | | **63,788,436** | **61,562,627** |
| **Total equity and liabilities** | | **107,042,166** | **100,448,970** |

The consolidated statement of financial position is to be read in conjunction with the Notes to, and forming part of, the consolidated financial statements 1 - 33.

*PJSC "IDGC of Centre"*
***Consolidated Statement of Changes in Equity for the year ended 31 December 2016***
*Thousands of Russian Roubles, unless otherwise stated*

| | Equity attributable to shareholders of the Company | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Share capital (Note 20)** | **Fair value reserve for available-for-sale financial assets** | **Reserve for remeasurements of defined benefit plans** | **Retained earnings** | **Total** | **Non-controlling interests** | **Total equity** |
| **Balance at 1 January 2015** | **4,221,794** | **49,985** | **(87,479)** | **34,647,003** | **38,831,303** | **100,359** | **38,931,662** |
| Profit for the year | - | - | - | 852,807 | **852,807** | 28,140 | **880,947** |
| Net change in fair value of available-for-sale financial assets (Note 15) | - | 70,683 | - | - | **70,683** | - | **70,683** |
| Remeasurements of the net defined benefit liability (Note 24) | - | - | (181,439) | - | **(181,439)** | - | **(181,439)** |
| Income tax on other comprehensive income | | (14,137) | 27,476 | - | **13,339** | - | **13,339** |
| **Total comprehensive (expense) / income for the year** | **-** | **56,546** | **(153,963)** | **852,807** | **755,390** | **28,140** | **783,530** |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| Dividends (Note 20b) | - | - | - | (827,624) | **(827,624)** | (1,225) | **(828,849)** |
| **Total transactions with owners, recorded directly in equity** | **-** | **-** | **-** | **(827,624)** | **(827,624)** | **(1,225)** | **(828,849)** |
| **Balance at 31 December 2015** | **4,221,794** | **106,531** | **(241,442)** | **34,672,186** | **38,759,069** | **127,274** | **38,886,343** |
| **Balance at 1 January 2016** | **4,221,794** | **106,531** | **(241,442)** | **34,672,186** | **38,759,069** | **127,274** | **38,886,343** |
| Profit for the year | - | - | - | 4,723,758 | **4,723,758** | 38,535 | **4,762,293** |
| Net change in fair value of available-for-sale financial assets (Note 15) | - | (19,904) | - | - | **(19,904)** | - | **(19,904)** |
| Remeasurements of the net defined benefit liability (Note 24) | - | - | 71,659 | - | **71,659** | - | **71,659** |
| Income tax on other comprehensive income | | 3,981 | (2,603) | - | **1,378** | - | **1,378** |
| **Total comprehensive (expense) / income for the year** | **-** | **(15,923)** | **69,056** | **4,723,758** | **4,776,891** | **38,535** | **4,815,426** |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| Dividends (Note 20b) | - | - | - | (448,039) | **(448,039)** | - | **(448,039)** |
| **Total transactions with owners, recorded directly in equity** | **-** | **-** | **-** | **(448,039)** | **(448,039)** | **-** | **(448,039)** |
| **Balance at 31 December 2016** | **4,221,794** | **90,608** | **(172,386)** | **38,947,905** | **43,087,921** | **165,809** | **43,253,730** |

The consolidated statement of changes in equity is to be read in conjunction with the Notes to, and forming part of, the consolidated financial statements 1 - 33.

*Thousands of Russian Roubles, unless otherwise stated*

| CASH FLOWS FROM OPERATING ACTIVITIES | Note | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|---|
| **Profit for the year** | | 4,748,887 | 2,800,767 |
| *Adjustments for:* | | | |
| Depreciation of property, plant and equipment and amortisation of intangible assets | 8, 12, 13 | 8,696,131 | 7,812,923 |
| Impairment of property, plant and equipment and intangibles assets | 8, 12 | (564,140) | 728,846 |
| Allowance for impairment of accounts receivable | 8 | 2,044,849 | 1,504,937 |
| Net finance costs | 10 | 4,496,229 | 4,273,556 |
| Provision for inventory obsolescence | | (16) | (3,700) |
| Loss on disposal of property, plant and equipment and intangible assets | | 91,913 | 160,011 |
| Bad debts written-off | | 225,365 | 245,118 |
| Adjustment for other non-cash transactions | | (554,985) | (796,974) |
| **Cash flows from operating activities before changes in working capital** | | **19,184,233** | **16,725,484** |
| Change in trade and other receivables | | 72,314 | (2,375,811) |
| Change in inventories | | (71,773) | (123,830) |
| Change in investments, financial assets and other non-current and current assets | | (61,612) | (53,674) |
| Change in trade and other payables | | (212,239) | 68,722 |
| Change in employee payables | | 608,324 | (50,034) |
| Change in employee benefits | | (261,078) | (111,927) |
| Change in other liabilities | | 109,906 | (14,867) |
| Change in other taxes payable | | 721,325 | 501,205 |
| **Cash flows from operations before income taxes and interest paid** | | **20,089,400** | **14,565,268** |
| Interest paid | | (4,638,695) | (4,427,615) |
| Income tax paid | | (748,386) | (1,047,863) |
| **Cash flows from operating activities** | | **14,702,319** | **9,089,790** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Acquisition of property, plant and equipment and intangible assets | | (13,069,355) | (13,579,085) |
| Proceeds from disposal of property, plant and equipment and intangible assets | | 3,138 | 25,684 |
| Dividends received | 10 | 12,695 | 17,526 |
| Interest received | | 250,610 | 290,719 |
| Proceeds from sale of investments | | 1,439 | 1,934 |
| **Cash flows used in investing activities** | | **(12,801,473)** | **(13,243,222)** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Proceeds from loans and borrowings | | 20,784,487 | 26,099,722 |
| Repayment of loans and borrowings | | (19,793,050) | (21,311,491) |
| Dividends paid | | (446,695) | (824,930) |
| Repayment of finance lease liabilities | | (1,503) | (82,485) |
| **Cash flows from financing activities** | | **543,239** | **3,880,816** |
| **Net (decrease) / increase in cash and cash equivalents** | | **2,444,085** | **(272,616)** |
| Cash and cash equivalents at beginning of the year | | 123,220 | 395,836 |
| **Cash and cash equivalents at end of the year** | 17 | **2,567,305** | **123,220** |

The consolidated statement of Cash Flows is to be read in conjunction with the Notes to, and forming part of, the consolidated financial statements 1 - 33.

## 1 BACKGROUND

### (a) The Group and its operations

Public Joint-Stock Company "IDGC of Centre" (hereinafter - the "Company") and its subsidiaries (hereinafter together referred to as the "Group") comprise Russian public and joint stock companies as defined in the Civil Code of the Russian Federation. The Company was set up on 17 December 2004 based on Resolution no. 154p of 9 December 2004 and pursuant to the Board of Directors' decision (board of directors' meeting minutes no. 178 of 1 October 2004) and Management Board decision (Management Board minute no. 1102 of 15 November 2004) of Open Joint-Stock Company RAO "United Energy Systems of Russia" (hereinafter - "RAO UES"). From 07 July 2015, OJSC "IDGC of Centre" is renamed as PJSC "IDGC of Centre" based on the Decision of the Annual General Meeting of Shareholders of OJSC "IDGC of Centre" dated 25.06.2015 (minutes No. 01/15 of 26.06.2015), in order to bring it in line with the legal requirements.

The Company's registered office is 2nd, Yamskaya, 4, Moscow, 127018, Russia.

The Company's de facto address is 2nd, Yamskaya, 4, Moscow, 127018, Russia.

The Group's principal activity is the transmission of electricity and the connection of customers to the electricity grid. In 2013 and 2014 pursuant to orders of the Russian Ministry of Energy, "On the transfer of the functions of electricity supplier" the Group was performing power distribution services in several regions it operates. In 2016, the Group took over the functions of electricity guarantee supplier in the Tver Region again (Note 7).

The Group consists of PJSC "IDGC of Centre" and its subsidiaries, presented in Note 5.

As at 31 December 2016, the Government of the Russian Federation owned 87.90% (as at 31 December 2015 – 85.31%) of the shares of PJSC "Russian Grids" (formerly OJSC "IDGC Holding"), which in turn owned 50.23% of the shares of the Company. OJSC "IDGC Holding" was renamed OJSC "Russian Grids" following the decision made on 23 March 2013 at an Extraordinary General Meeting of Shareholders of OJSC "IDGC Holding". OJSC "Russian Grids" was renamed PJSC "Russian Grids" following the decision made on 30 June 2015 at an Extraordinary General Meeting of Shareholders of OJSC "Russian Grids", in order to bring it in line with the legal requirements.

The Government of the Russian Federation influences the Group's activities through setting electricity transmission tariffs.

### (b) Russian business environment

The Group's operations are located in the Russian Federation, consequently, the Group is exposed to the economic and financial markets of the Russian Federation. Russia continues economic reforms and development of its legal, tax and regulatory frameworks. 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.

In 2014 and 2015, the Russian economy was negatively impacted by macroeconomic factors, including devaluation of the Russian Rouble. In December 2014, the Rouble interest rates increased significantly after the Central Bank of Russia raised its key rate. The combination of the above resulted in reduced access to capital, a higher cost of capital, increased inflation and uncertainty regarding economic growth. In 2015, the situation has leveled off. The Central Bank of Russia has repeatedly reduced the key interest rate; exchange rate fluctuations and inflation have been smoothed. In 2016, there were signs of stabilization, the Central Bank of Russia continued to reduce the key interest rate, there were no significant exchange rate fluctuations, inflation is controlled by the government. However, risks remain that the combination of economic factors could negatively affect the Group's future financial position, results of operations and business prospects.

Management of the Group believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

## 2 BASIS OF PREPARATION

### (a) Statement of compliance

These consolidated financial statements (hereinafter "Financial Statements") have been prepared in accordance with International Financial Reporting Standards ("IFRSs", "IASs").

### (b) Basis of measurement

The Financial Statements are prepared on the historical cost basis except for available-for-sale financial assets measured at fair value; and property, plant and equipment which was revalued to determine deemed cost as part of the adoption of IFRS as at 1 January 2007.

### (c) Functional and presentation currency

The national currency of the Russian Federation is the Russian Rouble ("RUB"), which is the functional currency of the Company and all its subsidiaries, and the currency in which these Financial Statements are presented.

All financial information presented in RUB has been rounded to the nearest thousand.

### (d) Use of estimates and judgements

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the Financial Statements is included in the following notes:

- Note 28 – allowances for impairment of trade and other receivables;
- Note 29 – lease classification.

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year is included in the following note:

- Note 12 – determining the recoverable amount of property, plant and equipment;
- Note 24 – employee benefits
- Note 31 – contingencies.

### (e) Changes in accounting policies and data presentation

The Group has consistently applied the accounting policies set out in Note 3 to all periods presented in these consolidated financial statements.

The following new or amended standards are not expected to have a significant impact of the Group's consolidated financial statements.

The accounting policies adopted in the preparation of the Group's annual financial statements for the year ended 31 December 2016 are consistent with those followed in the preparation of the Group's annual financial statements for the year ended 31 December 2015, except for the adoption of new amendments of the following standards became effective for the Group's consolidated financial statements at 31 December 2016, noted below:

#### *(i) The amendments of the following standards became effective for the Group's consolidated financial statements as of 1 January 2016:*

- Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business, must apply the relevant IFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained.

## 2 BASIS OF PREPARATION (CONTINUED)

In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.

- The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are prospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. This amendment did not have any effect on the consolidated financial statements.

- Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture address the conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture, is recognised in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture. These amendments must be applied prospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. This amendment did not have any effect on the consolidated financial statements.

- IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Assets (or disposal groups) are generally disposed of either through sale or distribution to owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. This amendment must be applied prospectively. This amendment did not have any effect on the consolidated financial statements.

- IFRS 7 Financial Instruments: Disclosures
  - Servicing contracts. The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.
  - Applicability of the amendments to IFRS 7 to condensed interim financial statements. The amendment clarifies that the offsetting disclosure requirements do not apply to condensed interim financial statements, unless such disclosures provide a significant update to the information reported in the most recent annual report. This amendment must be applied retrospectively.

  This amendment did not have any effect on the consolidated financial statements.

- IAS 19 Employee Benefits. The amendment clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. This amendment must be applied prospectively. This amendment did not have any effect on the consolidated financial statements.

- IAS 34 Interim Financial Reporting. The amendment clarifies that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the interim financial report (e.g., in the management commentary or risk report). The other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time. This amendment must be applied retrospectively. This amendment did not have any effect on the consolidated financial statements.

- Amendments to IAS 1 Disclosure Initiative. The amendments to IAS 1 Presentation of Financial Statements clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

## 2 BASIS OF PREPARATION (CONTINUED)

- the materiality requirements in IAS 1;
- that specific line items in the statement(s) of profit or loss and other comprehensive income and the statement of financial position may be disaggregated;
- that entities have flexibility as to the order in which they present the notes to financial statements;
- that the share of other comprehensive income of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and other comprehensive income. These amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. This amendments did not have any effect on the consolidated financial statements.

The Group has not adopted earlier any other standard, interpretation and amendment that has been issued but is not yet effective.

***(ii) The following IFRSs and amendments to existing IFRSs that have been published are not yet effective:***

- The amendments to IAS 7 Statement of Cash Flows are part of the IASB's Disclosure Initiative and require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. These amendments are effective for annual periods beginning on or after 1 January 2017, with early application permitted.

- IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses – Amendments to IAS 12. The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognised in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact. These amendments are effective for annual periods beginning on or after 1 January 2017 with early application permitted. If an entity applies the amendments for an earlier period, it must disclose that fact.

- IFRS 2 Classification and Measurement of Share-based Payment Transactions – Amendments to IFRS 2. The IASB issued amendments to IFRS 2 Share-based Payment that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled. On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted.

- IFRS 16 Leases was issued in January 2016 and it replaces IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less).

*Thousands of Russian Roubles, unless otherwise stated*

**2 BASIS OF PREPARATION (CONTINUED)**

At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

- IFRS 9 Financial Instruments. In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

- IFRS 15 Revenue from Contracts with Customers was issued in May 2014 and establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018. Early adoption is permitted.

The Group is considering the implication of the new standards and the impact on the Group's consolidates financial statement and plans to adopt new standards when they become effective.

Certain amounts of the previous year have been adjusted to conform with the current year disclosures.

When necessary, comparative information for the prior periods has been reclassified due to the application of the extended data presentation. The quantitative impact of this reclassification on the comparative information specified in the statement for the 12 months of 2016 is set out below.

In Note 6 "Operating segments" information of expenditure items was updated;

| *31 December 2015* | *As previously reported* | *Effect of change* | *As restated* |
|---|---|---|---|
| Recognition of employee benefit obligations | 111,927 | (223,879) | (111,952) |
| Other adjustments | 302,070 | (173,706) | 128,364 |
| **Consolidated earnings before interest, tax and depreciation and amortization (EBITDA)** | **15,195,491** | **(397,585)** | **14,797,906** |
| Interest expense | (4,352,520) | 173,706 | (4,178,814) |
| Interest expense on employee benefit obligations | (223,879) | 223,879 | - |

*Thousands of Russian Roubles, unless otherwise stated*

## 2 BASIS OF PREPARATION (CONTINUED)

In Note 8 "Operating expenses" information of expenditure items was updated:

| *31 December 2015* | *As previously reported* | *Effect of change* | *As restated* |
|---|---|---|---|
| Losses of previous years | 630,319 | (630,319) | - |
| Bad debt written-off | 245,118 | (245,118) | - |
| Target contributions and membership fee | 3,106 | (3,106) | - |
| Other works and production services | - | 80,851 | 80,851 |
| Other services | - | 821,739 | 821,739 |
| Debt settlement for electricity transmission, electricity for resale, purchased electricity to compensate for losses. non-contracted consumption | - | 693,840 | 693,840 |
| Other expenses | 2,020,869 | (717,887) | 1,302,982 |

## 3 SIGNIFICANT ACCOUNTING POLICIES

### (a) Basis of consolidation

#### *(i) Subsidiaries*

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

#### *(ii) Transactions eliminated on consolidation*

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

#### *(iii) Business combinations*

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that currently are exercisable.

The Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus,
- if the business combination is achieved in stages, the fair value of the existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination, are expensed as incurred.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

#### *(iv) Non-controlling interests*

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the acquisition date.

Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

#### *(v) Business combinations involving entities under common control*

Business combinations arising from transfers of interests in entities that are under the control of the shareholder that controls the Group are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date that common control was established; for this purpose comparatives are revised. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the acquired entity's IFRS consolidated financial statements. The components of equity of the acquired entities are added to the same components within Group equity except that any share capital of the acquired entities is recognised as part of retained earnings. Any cash paid for the acquisition is recognised directly in equity.

### (b) Financial instruments

#### *(i) Non-derivative financial assets*

Non-derivative financial assets comprise investments in equity, trade and other receivables, cash and cash equivalents.

The Group initially recognises loans and receivables and deposits on the date that they are originated. All other financial assets are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group classifies non-derivative financial assets into the following categories: loans and receivables and available-for-sale financial assets.

*Loans and receivables*

Loans and receivables are a category of financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables category comprise the following classes of financial assets: trade and other receivables as presented in Note 16 and Note 18, and cash and cash equivalents as presented in Note 17.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

*Cash and cash equivalents*

Cash and cash equivalents comprise cash balances and highly liquid investments with maturities at initial recognition of three months or less from the acquisition date that are subject to insignificant risk of changes in their fair value.

*Available-for-sale financial assets*

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale and that are not classified in any of the above categories of financial assets. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see note 3(f)(i)), are recognised in other comprehensive income and presented within equity in the fair value reserve. When an investment is derecognised or impaired, the cumulative gain or loss in other comprehensive income is transferred to profit or loss.

Investments in equity securities that are not quoted on a stock exchange and where fair value cannot be reliably measured are stated at cost less impairment losses.

Available-for-sale financial assets comprise equity securities.

***(ii) Non-derivative financial liabilities***

All financial liabilities are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group classifies non-derivative financial liabilities into the other financial liability category.

Such financial liabilities are recognised initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortised cost using the effective interest method. Other financial liabilities comprise loans and borrowings, and trade and other payables.

### (c) Property, plant and equipment

***(i) Recognition and measurement***

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses.

The cost of property, plant and equipment at 1 January 2007, the date of transition to IFRSs, was determined by reference to its fair value at that date.

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

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

Any gain or loss on disposal of an item of property, plant and equipment is determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and is recognised net within other income/other expenses in profit or loss.

***(ii) Subsequent expenditure***

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

***(iii) Depreciation***

Depreciation is based on the cost of an asset less its residual value.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

The estimated useful lives of property, plant and equipment by type of facility are as follows:

- Buildings 7 – 50 years;
- Transmission networks 5 – 40 years;
- Equipment for electricity transformation 3 – 20 years;
- Other 1 – 25 years.

Depreciation methods, useful lives and residual values are reviewed at each financial year end and adjusted if appropriate.

### *(iv) Leased assets*

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

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are operating leases and the leased assets are not recognised in the Group's statement of financial position. Operating lease payments (net of benefits granted by the lessor) are recognised in profit or loss on a straight line basis over the lease term.

### *(v) Borrowing costs*

Borrowing costs directly attributable to the acquisition, construction or production of an asset that takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the asset. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that the Group incurs in connection with the borrowing of funds.

### (d) Intangible assets

### *(i) Intangible assets other than Goodwill*

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

### *(ii) Subsequent expenditure*

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as incurred.

### *(iii) Amortisation*

Amortisation is calculated over the cost of the asset, or other amount substituted for cost, less its residual value.

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use since this most closely reflects the expected pattern of consumption of future economic benefits embodied in the asset.

The estimated useful lives for the current and comparative periods are as follows:

- Computer software 1 – 10 years;
- Other intangible assets 1 – 20 years.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Amortisation methods, useful lives and residual values are reviewed at each financial year end and adjusted if appropriate.

### (e) Inventories

Inventories are measured at the lower of cost and net realisable value.

The cost of inventories includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. The cost of inventories is determined using the weighted average cost method.

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

### (f) Impairment

#### *(i) Non-derivative financial assets*

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Group on terms that the Group would not consider otherwise, indications that a debtor or issuer will enter bankruptcy, adverse changes in the payment status of borrowers, economic conditions that correlate with defaults or the disappearance of an active market for a security. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account. When the Group considers that there are no realistic prospects of recovery of the asset, the relevant amounts are written off. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale equity securities are recognised by reclassifying the losses accumulated in the fair value reserve in equity, to profit or loss. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost, and the current fair value, less any impairment loss previously recognised in profit or loss. Any subsequent recovery in fair value of an impaired available-for-sale equity securities is recognised in other comprehensive income.

#### *(ii) Non-financial assets*

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs.

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated to reduce the carrying amount of the assets in the CGU (group of CGUs) on a pro rata basis.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

### (g) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

### (h) Revenue

Revenue from electricity transmission is recognised based on acts of services rendered. The act is prepared in respect of each counterparty in accordance with the concluded contract on the provision of services based on the meter readings and the "boiler" tariffs approved by the Regional Energy Commission of each region of the Group's operations.

Revenue from the sale of electricity is recognized based on:

- monthly acts of acceptance of electricity under the electricity supply agreements (electricity sale agreements) of legal entities based on the meter readings and unregulated prices formed on the retail market in the settlement period;
- monthly documents (receipts) on the consumption of utilities services by individuals based on the meter readings and tariffs approved by the Regional Energy Commission.

Revenue from connection services represents a non-refundable fee for connecting the customer to the electricity grid network. The tariffs for connection services are approved by the Federal Tariff Agency and Regional Energy Commission of each region of the Group's operations. The terms, conditions and amounts of these fees are negotiated separately and are independent from fees generated by electricity transmission services. Revenue is recognised when electricity is activated and the customer is connected to the grid network or, for contracts where connection services are performed in stages, revenue is recognised in proportion to the stage of completion when an act of acceptance is signed by the customer.

Revenue from installation, repair and maintenance services and other sales is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer or when the services are provided.

### (i) Finance income and costs

Finance income comprises interest income on cash balances and bank deposits and dividend income. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group's right to receive payment is established.

Finance costs comprise interest expense on borrowings, employee benefits and finance leases. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualified asset are recognised in profit or loss using the effective interest method.

### (j) Income tax

Income tax expense comprises current and deferred tax. It is recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

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

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

**3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- temporary differences relating to investments in subsidiaries to the extent that the Group is able to control the timing of the reversal of the temporary differences and it is probable that they will not reverse in the foreseeable future;
- taxable temporary differences arising on the initial recognition of goodwill.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

In determining the amount of current and deferred tax the Group takes into account the impact of uncertain tax positions and whether additional taxes, penalties and late-payment interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretations of tax law and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Group to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact the tax expense in the period that such a determination is made.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

In accordance with the tax legislation of the Russian Federation, tax losses and current tax assets of a company in the Group may not be set off against taxable profits and current tax liabilities of other Group companies. In addition, the tax base is determined separately for each of the Group's main activities and, therefore, tax losses and taxable profits related to different activities cannot be offset.

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

### (k) Employee benefits

#### *(i) Defined contribution plans*

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, including Russia's State pension fund, are recognised as an employee benefit expense in profit or loss in the periods during which services are rendered by employees. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

#### *(ii) Defined benefits plan*

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and any unrecognised past service costs and the fair value of plan assets are deducted. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations and that are denominated in the same currency in which the benefits are expected to be paid. The calculation is performed annually by a qualified actuary using the projected unit credit method.

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in OCI. The Group determines the net interest expense on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability, taking into account any changes in the net defined benefit liability during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognised in profit or loss.

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognised immediately in profit or loss. The Group recognises gains and losses on the settlement of a defined benefit plan when the settlement occurs.

### *(iii) Other long-term employee benefits*

The Group's net obligation in respect of long-term employee benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any related assets is deducted.

The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations as at reporting date and that are denominated in the same currency in which the benefits are expected to be paid.

The Group calculates obligation in respect of other long-term employee benefits using the projected unit credit method. Remeasurements are recognised in profit or loss in the period in which they arise.

### *(iv) Short-term employee benefits*

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and if the obligation can be estimated reliably.

### (l) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

### (m) Earnings per share

The Group presents basic earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period, adjusted for own shares held.

### (n) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are reviewed regularly by the Management Board, the Group's operating decision making body, to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the Management Board, the Group's operating decision making body, include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

### (o) Service Concession Arrangements

The Group applies IFRIC Interpretation 12 "Service Concession Arrangements" (IFRIC 12) to public-to-private service concession arrangements if:

- the grantor controls or regulates what services the Group must provide with the infrastructure, to whom it must provide them, and at what price; and

## 3 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- the grantor controls—through ownership, beneficial entitlement or otherwise—any significant residual interest in the infrastructure at the end of the term of the arrangement.

The Group accounts for revenue and costs relating to construction services in accordance with IAS 11 and accounts for revenue and costs relating to electricity transmission in accordance with IAS 18.

The consideration for construction or upgrade services received or receivable by the Group is recognised at its fair value.

The Group recognizes a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law.

The Group recognizes an intangible asset to the extent that it receives a right to charge users of the public service.

As to the financial asset - the amount receivable from the grantor or by his orders, is accounted for in accordance with IAS 39:

- a loan or account receivable;
- financial asset, available-for-sale; or
- financial asset measured at fair value through profit or loss if on initial recognition the criteria for such classification are met.

The Group recognizes an intangible asset in accordance with IAS 38. Paragraphs 45–47 of IAS 38 provide guidance on measuring intangible assets acquired in exchange for a non-monetary asset or assets or a combination of monetary and non-monetary assets. Amortization period is defined as a duration of the Service Concession Arrangements. The Group tests the intangible asset for impairment in accordance with IAS 36.

The Group capitalizes the borrowing costs attributable to the construction stage of the Service Concession Agreement as part of an intangible asset, in accordance with IAS 23. The Group recognizes other borrowing costs attributable to the Service Concession Agreement as an expense in the period in which they are incurred.

## 4 MEASUREMENT OF FAIR VALUES

A number of the Group's accounting policies and disclosures require the measurement of fair value, for both financial and non-financial assets and liabilities.

When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values is included in Note 28.

*Thousands of Russian Roubles, unless otherwise stated*

## 5 SUBSIDIARIES

**List of subsidiaries**

| | Country of incorporation | 31 December 2016 Ownership/voting, % | 31 December 2015 Ownership/voting, % |
|---|---|---|---|
| JSC "Sanatorium "Energetic" | Russian Federation | 100 | 100 |
| JSC "Yaroslavl Electric Grid Company" | Russian Federation | 51 | 51 |
| CJSC "Innovation and energy efficiency center" | Russian Federation | 51 | 51 |

## 6 OPERATING SEGMENTS

The Group has eleven reportable segments representing branches of the Company, as described below. These are the Group's strategic business units and are the Company's branches. The strategic business units offer similar services representing transmission of electric power and connection services and are managed separately. In addition in 2013 and 2014 five divisions (Bryanskenergo, Kurskenergo, Oryolenergo, Tverenergo and Smolenskenergo) were performing electricity guarantee supplier functions. In 2016, the division of Company Tverenergo performs the electricity guarantee supplier functions again (see Note 7). For each of the strategic business units, the Management Board, the Group's operating decision making body, reviews internal management reports on at least a quarterly basis.

"Others" include operations of subsidiaries and the head office branch. None of them meets any of the quantitative thresholds for determining reportable segments in 2016 or 2015.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment earnings before interest expense, income tax and depreciation and amortisation – EBITDA, as included in the internal management reports that are reviewed by the Management Board.

Segment reports are based on the information reported in statutory accounts, which differ significantly from the consolidated financial statements prepared under IFRS. The reconciliation of items measured as reported to the Management Board with similar items in these Financial Statements includes those reclassifications and adjustments that are necessary for financial statements to be presented in accordance with IFRS.

Segment capital expenditure is the total cost incurred during the period to acquire property, plant and equipment.

*Thousands of Russian Roubles, unless otherwise stated*

## 6 OPERATING SEGMENTS (CONTINUED)

### *(i) Information about reportable segments*

As at and for the year ended 31 December 2016:

| | Belgorod-energo | Bryansk-energo | Voronezh-energo | Kostroma-energo | Kurskenergo | Lipetsk-energo | Orelenergo | Smolensk-energo | Tambov-energo | Tverenergo | Yarenergo | Others | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Revenue from electricity transmission | 13,173,503 | 4,522,996 | 11,918,157 | 4,440,142 | 6,709,599 | 8,894,089 | 4,070,102 | 6,487,408 | 5,296,027 | 9,489,906 | 8,611,113 | - | **83,613,042** |
| Inter-segment revenue | - | - | - | - | - | - | - | - | - | - | - | 335,832 | **335,832** |
| Revenue from connection services | 225,321 | 13,640 | 292,753 | 59,191 | 131,405 | 89,524 | 22,576 | 182,165 | 30,389 | 116,109 | 248,165 | 4,636 | **1,415,874** |
| Inter-segment revenue | - | - | - | - | - | - | - | - | - | - | 40 | - | **40** |
| Other revenue | 347,300 | 39,308 | 134,972 | 40,288 | 45,615 | 53,577 | 46,189 | 115,064 | 41,361 | 82,325 | 138,131 | 52,820 | **1,136,950** |
| Inter-segment revenue | - | - | - | - | - | - | - | - | - | - | 1,809 | 6,454 | **8,263** |
| **Total revenues** | **13,746,124** | **4,575,944** | **12,345,882** | **4,539,621** | **6,886,619** | **9,037,190** | **4,138,867** | **6,784,637** | **5,367,777** | **9,688,340** | **8,999,258** | **399,742** | **86,510,001** |
| **Results from operating activities *** | **1,472,466** | **260,386** | **1,335,824** | **514,393** | **226,991** | **116,567** | **302,577** | **516,060** | **693,668** | **60,461** | **1,266,799** | **95,232** | **6,861,424** |
| Finance income | 51,699 | 16,995 | 34,556 | 10,703 | 24,024 | 30,005 | 9,367 | 15,097 | 12,453 | 19,540 | 26,274 | 497 | **251,210** |
| Finance costs | (549,796) | (194,764) | (418,292) | (154,069) | (250,892) | (300,153) | (216,040) | (562,397) | (457,434) | (948,153) | (455,715) | (1,057) | **(4,508,762)** |
| **Reportable segment profit/(loss) before income tax** | **974,369** | **82,617** | **952,088** | **371,027** | **123** | **(153,581)** | **95,904** | **(31,240)** | **248,687** | **(868,152)** | **837,358** | **94,672** | **2,603,872** |
| Depreciation and amortisation | 2,524,766 | 437,301 | 949,337 | 550,346 | 763,558 | 1,152,142 | 366,064 | 908,912 | 448,200 | 751,144 | 1,015,860 | 29,924 | **9,897,554** |
| EBITDA | 4,048,931 | 714,682 | 2,319,717 | 1,075,442 | 1,014,573 | 1,298,714 | 678,008 | 1,440,069 | 1,154,321 | 831,145 | 2,308,933 | 125,653 | **17,010,188** |
| **Reportable segment assets** | **26,155,875** | **5,519,381** | **12,636,968** | **6,393,904** | **7,786,579** | **16,758,333** | **4,128,838** | **7,803,461** | **6,078,509** | **11,525,320** | **13,551,514** | **4,750,030** | **123,088,712** |
| Property, plant and equipment | 24,221,682 | 4,451,274 | 11,137,522 | 5,744,243 | 6,773,060 | 14,180,321 | 3,519,369 | 6,827,473 | 5,052,950 | 9,012,344 | 11,024,592 | 638,454 | **102,583,284** |
| **Reportable segment liabilities** | **3,832,499** | **869,938** | **2,142,016** | **996,511** | **1,332,931** | **1,598,925** | **633,036** | **1,155,076** | **1,006,587** | **2,904,316** | **2,126,087** | **46,455,992** | **65,053,914** |
| Capital expenditure | 3,562,793 | 467,520 | 1,148,179 | 999,581 | 440,910 | 1,606,184 | 423,370 | 1,167,265 | 541,763 | 677,884 | 2,295,056 | 89,838 | **13,420,343** |

* Results from operating activities include other income and expense of reportable segment

*Thousands of Russian Roubles, unless otherwise stated*

## 6 OPERATING SEGMENTS (CONTINUED)

As at and for the year ended 31 December 2015:

| | Belgorod-energo | Bryansk-energo | Voronezh-energo | Kostroma-energo | Kurskenergo | Lipetsk-energo | Orelenergo | Smolensk-energo | Tambov-energo | Tverenergo | Yarenergo | Others | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Revenue from electricity transmission | 12,607,530 | 4,360,490 | 10,916,421 | 4,038,658 | 6,463,925 | 8,690,451 | 3,713,089 | 5,895,553 | 4,682,304 | 8,655,622 | 7,709,567 | - | **77,733,610** |
| Inter-segment revenue | - | - | - | - | - | - | - | - | - | - | - | 271,907 | **271,907** |
| Revenue from connection services | 220,818 | 6,775 | 166,922 | 88,265 | 47,168 | 73,751 | 15,431 | 121,330 | 27,497 | 146,805 | 244,940 | 9,877 | **1,169,579** |
| Other revenue | 283,677 | 63,267 | 125,515 | 39,146 | 44,464 | 49,889 | 26,810 | 97,658 | 32,803 | 47,042 | 111,736 | 57,494 | **979,501** |
| Inter-segment revenue | - | - | - | - | - | - | - | - | 7 | - | 1,879 | 1,080 | **2,966** |
| **Total revenues** | **13,112,025** | **4,430,532** | **11,208,858** | **4,166,069** | **6,555,557** | **8,814,091** | **3,755,330** | **6,114,541** | **4,742,611** | **8,849,469** | **8,068,122** | **340,358** | **80,157,563** |
| **Results from operating activities *** | **1,508,592** | **(104,771)** | **1,218,138** | **531,302** | **(70,983)** | **494,331** | **25,831** | **543,789** | **527,365** | **12,360** | **1,206,497** | **68,569** | **5,961,020** |
| Finance income | 55,003 | 18,061 | 36,767 | 11,431 | 25,664 | 31,921 | 10,089 | 16,114 | 13,413 | 20,869 | 27,955 | 383 | **267,670** |
| Finance costs | (548,929) | (261,246) | (425,134) | (160,177) | (213,442) | (244,505) | (183,424) | (546,161) | (339,300) | (872,337) | (400,781) | (617) | **(4,196,053)** |
| **Reportable segment profit/(loss) before income tax** | **1,014,666** | **(347,956)** | **829,771** | **382,556** | **(258,761)** | **281,747** | **(147,504)** | **13,742** | **201,478** | **(839,108)** | **833,671** | **68,335** | **2,032,637** |
| Depreciation and amortisation | 2,328,771 | 433,077 | 888,751 | 519,230 | 736,880 | 1,090,534 | 354,751 | 819,981 | 375,267 | 641,162 | 871,070 | 23,590 | **9,083,064** |
| EBITDA | 3,892,366 | 346,367 | 2,143,656 | 1,061,963 | 691,561 | 1,616,786 | 390,671 | 1,379,884 | 916,045 | 674,391 | 2,105,522 | 92,542 | **15,311,754** |
| **Reportable segment assets** | **25,217,202** | **5,775,222** | **12,107,095** | **5,803,309** | **7,956,006** | **15,828,331** | **3,963,374** | **8,408,157** | **5,856,921** | **13,353,323** | **11,784,898** | **2,162,169** | **118,216,007** |
| Property, plant and equipment | 22,822,085 | 4,216,036 | 10,547,947 | 5,109,597 | 6,812,465 | 13,413,772 | 3,332,402 | 6,373,143 | 4,840,169 | 8,421,744 | 9,393,616 | 266,383 | **95,549,359** |
| **Reportable segment liabilities** | **3,178,274** | **778,149** | **1,810,589** | **640,100** | **1,280,912** | **1,295,351** | **501,086** | **1,050,065** | **718,218** | **3,452,364** | **1,488,808** | **45,480,069** | **61,673,985** |
| Capital expenditure | 3,485,441 | 247,608 | 1,264,008 | 667,243 | 498,737 | 1,055,919 | 376,231 | 1,113,232 | 1,268,320 | 1,586,389 | 1,371,434 | 56,725 | **12,991,287** |

* Results from operating activities include other income and expense of reportable segment

*Thousands of Russian Roubles, unless otherwise stated*

## 6 OPERATING SEGMENTS (CONTINUED)

### *(ii) Major customer*

In 2016 revenue from one customer of the Group's reportable segment (Belgorodenergo) represented approximately 10% (RUB 8,728,257 thousand) of the Group's total revenue (in 2015 – RUB 6,991,523 thousand or 9% of the Group's total revenue).

### *(iii) Reconciliations of reportable segment revenues, profit or loss and assets and liabilities*

Reconciliation of key segment items measured as reported to the Management Board with similar items in these Consolidated Financial Statements is presented in the tables below.

| **Revenues** | **Year ended 31 December 2016** | **Year ended 31 December 2015** |
|---|---|---|
| Total revenue for reportable segments | 86,510,001 | 80,157,563 |
| Elimination of inter-segment revenue | (344,135) | (274,873) |
| Reclassification | 128,997 | 947,597 |
| **Consolidated revenue** | **86,294,863** | **80,830,287** |

| | **Year ended 31 December 2016** | **Year ended 31 December 2015** |
|---|---|---|
| EBITDA for the reportable segments | 17,010,188 | 15,311,754 |
| Impairment of property, plant and equipment and intangibles assets | 564,140 | (728,846) |
| Adjustments for property, plant and equipment | 3,478 | (109,966) |
| Recognition of assets related to employee benefit fund | 61,612 | 53,674 |
| Recognition of employee benefit obligations | 70,610 | (111,952) |
| Adjustment for finance lease | 1,543 | 82,858 |
| Adjustment for allowance for impairment of account receivables | (2) | (29,880) |
| Provision for inventory obsolescence | 63 | (165) |
| Amortisation of intangible assets | 273,480 | 202,065 |
| Other adjustments | (36,906) | 128,364 |
| **Consolidated earnings before interest, tax and depreciation and amortization (EBITDA)** | **17,948,206** | **14,797,906** |
| Depreciation and amortization | (8,696,131) | (7,812,923) |
| Interest expense | (4,503,062) | (4,178,814) |
| Interest on finance lease liabilities | (126) | (5,402) |
| Income tax expense | 13,406 | (1,919,820) |
| **Profit for the year per Consolidated Statement of Profit or Loss and Other Comprehensive Income** | **4,762,293** | **880,947** |

*Thousands of Russian Roubles, unless otherwise stated*

## 6 OPERATING SEGMENTS (CONTINUED)

| **Assets** | **31 December 2016** | **31 December 2015** |
|---|---|---|
| Total assets for reportable segments | 123,088,712 | 118,216,007 |
| Impairment of property, plant and equipment and intangibles assets | 564,140 | (728,846) |
| Elimination of cost of investments in subsidiaries | (17,295) | (17,295) |
| Elimination of other inter-segment assets | (41,002) | (33,025) |
| Adjustments for net book value of property, plant and equipment | (15,531,552) | (17,181,359) |
| Recognition of assets related to employee benefit fund | 500,305 | 438,693 |
| Provision for inventory obsolescence | (1,654) | (1,717) |
| Adjustment for deferred tax | (1,514,164) | (1,203,808) |
| Other adjustments | (5,324) | 960,320 |
| **Consolidated total assets** | **107,042,166** | **100,448,970** |

| **Liabilities** | **31 December 2016** | **31 December 2015** |
|---|---|---|
| Total liabilities for reportable segments | 65,053,914 | 61,673,985 |
| Elimination of inter-segment liabilities | (41,002) | (34,852) |
| Adjustment for finance lease | - | 1,503 |
| Recognition of employee benefit obligations | 2,202,613 | 2,344,882 |
| Adjustment for deferred tax | (3,328,217) | (2,346,030) |
| Other adjustments | (98,872) | (76,861) |
| **Consolidated total liabilities** | **63,788,436** | **61,562,627** |

## 7 REVENUE AND OTHER INCOME

For the years ended 31 December, revenue includes:

| | **Year ended 31 December 2016** | **Year ended 31 December 2015** |
|---|---|---|
| Electricity transmission | 83,590,448 | 77,733,610 |
| Connection services | 1,415,874 | 1,169,579 |
| Repairs and maintenance | 328,971 | 311,300 |
| Service Concession Arrangements | 123,889 | 972,341 |
| Revenue from the resale of electricity and capacity | 51,628 | - |
| Rent | 50,634 | 55,313 |
| Other | 733,419 | 588,144 |
| | **86,294,863** | **80,830,287** |

Revenue from connection services represents a non-refundable fee for connecting the customer to the electricity grid network.

*Thousands of Russian Roubles, unless otherwise stated*

## 7 REVENUE AND OTHER INCOME (CONTINUED)

In 2013 pursuant to orders of the Russian Ministry of Energy, "On the transfer of the functions of electricity supplier" the Company started to perform the functions of electricity supplier in Bryansk, Oryol, Kursk, Tver and Smolensk regions. In 2016, the Company started to perform the functions of guarantee electricity supplier in the Tver Region again. Hence, in addition to performing power transmission services, Tverenergo division of the Company commenced performing power distribution services, including purchasing electricity on the wholesale market and selling it on the retail market, and entering into power purchase agreements with all customers, including householders. The period within which the functions of electricity supplier are to be performed was established prior to the effective date of the decision to provide the tender winner with the electricity supplier status in the abovementioned operating area of the Company, but not more than 12 months.

In 2016, revenue from the resale of electricity and capacity was RUB 51,628 thousand (there was no revenue from the resale of electricity and capacity in 2015). Tariff for sale of electricity under power supply contracts is calculated taking into account the transmission fee.

Revenue under the Service Concession Arrangement is the consideration for the services related to the construction of objects of the Service Concession Arrangement, subject to receipt by the Group, and represented the rights to the intangible asset. The consideration payable is recognised at its fair value (Note 13).

For the years ended 31 December, other income includes:

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| Income from gratuitously received property, plant and equipment (including excess inventory) | 581,117 | 714,565 |
| Income in the form of fines and penalties | 489,721 | 292,346 |
| Write-off of accounts payable | 220,588 | 20,871 |
| Income in the form of the cost of inventories obtained by disposal of property, plant and equipment | 100,443 | 126,071 |
| Income from the identified non-contractual electricity consumption | 100,395 | 72,959 |
| Income from reimbursement of costs and damages | 85,494 | 82,240 |
| Compensation of insurance claims | 43,846 | 52,980 |
| Revenues from gratuitously received inventories (including excess inventory) | 6,966 | 127 |
| Other income | 73,850 | 86,321 |
| | **1,702,420** | **1,448,480** |

*Thousands of Russian Roubles, unless otherwise stated*

## 8 OPERATING EXPENSES

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| Personnel costs (Note 9) | 18,376,802 | 17,798,496 |
| Depreciation and amortisation | 8,696,131 | 7,812,923 |
| Allowance for impairment of accounts receivable | 2,044,849 | 1,504,937 |
| Taxes other than income tax | 1,347,906 | 1,074,812 |
| *Material expenses, inc.* | | |
| Electricity to compensate for losses | 11,914,634 | 10,640,307 |
| Purchased electricity and thermal energy for own needs | 360,650 | 323,364 |
| Electricity for resale | 27,005 | - |
| Other raw material expenses | 2,777,079 | 2,666,635 |
| *Works and production services, inc.* | | |
| Electricity transmission | 27,901,259 | 26,435,032 |
| Repairs, maintenance and installation services | 514,215 | 510,017 |
| Other works and production services | 81,321 | 80,851 |
| *Other services of outside organizations, inc.* | | |
| Information services | 326,794 | 338,715 |
| Security | 303,236 | 298,700 |
| Communication services | 272,669 | 274,352 |
| Consulting, legal and audit services | 46,210 | 41,734 |
| Transportation services | 22,884 | 8,184 |
| Other services | 864,871 | 821,739 |
| Debt settlement for electricity transmission, electricity for resale, purchased electricity to compensate for losses. Non-contracted consumption | 712,228 | 693,840 |
| Rent | 565,576 | 549,588 |
| Provisions recognized | 327,831 | 277,947 |
| Insurance | 145,792 | 144,460 |
| Costs of Service Concession Arrangements | 111,612 | 875,983 |
| Impairment of property, plant and equipment and intangible assets | (564,140) | 728,846 |
| Other expenses | 1,574,753 | 1,302,982 |
| | **78,752,167** | **75,204,444** |

Allowance for impairment of accounts receivable recognized in the reporting period relates to impairment of trade receivables from the companies with which there is disagreement on electricity transmission, as well as companies with outstanding resale of electricity and capacity.

Costs under Service Concession Arrangements represent the Group's construction costs of objects of the Service Concession Arrangement (Note 13).

Loss on impairment of property, plant and equipment and intangible assets recognized during the period is determined as a result of testing of the Group's assets for economic impairment (Note 12).

*Thousands of Russian Roubles, unless otherwise stated*

## 9 PERSONNEL COSTS

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| Salaries and wages | 11,809,306 | 11,544,584 |
| Compulsory social security contributions | 4,040,058 | 3,832,542 |
| Unused vacation provision | 1,165,029 | 997,806 |
| Finance aid | 633,024 | 615,511 |
| Remuneration to management provision | 292,332 | 247,672 |
| Current service cost (Note 24) | 85,104 | 73,905 |
| Past service cost (Note 24) | (135,540) | 6,680 |
| Other personnel costs | 487,489 | 479,796 |
| | **18,376,802** | **17,798,496** |

The average number of employees (including production and non-production staff) in 2016 was 29,775 (in 2015: 29,677 employees).

## 10 FINANCE INCOME AND COSTS

| **Finance income** | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| Interest income | 277,837 | 290,719 |
| Dividends | 12,695 | 17,526 |
| Other finance income | 6,503 | - |
| | **297,035** | **308,245** |
| **Finance costs** | | |
| Interest expense | 4,503,062 | 4,178,814 |
| Interest expense on employee benefits obligation (Note 24 b) | 190,468 | 223,879 |
| Interest on finance lease liabilities | 126 | 5,402 |
| Other finance expense | 99,608 | 173,706 |
| | **4,793,264** | **4,581,801** |

*Thousands of Russian Roubles, unless otherwise stated*

## 11 INCOME TAX BENEFIT / (EXPENSE)

The Group's applicable tax rate is the income tax rate of 20%. For the years ended 31 December income tax benefit / (expense) is as follows:

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| **Current tax expense** | | |
| Current year | (1,177,708) | (943,326) |
| Adjustment for prior years | 435,324 | 194,838 |
| | **(742,384)** | **(748,488)** |
| **Deferred tax expense** | | |
| Origination and reversal of temporary differences | 755,790 | (1,171,424) |
| Change in tax base of property, plant and equipment | - | 92 |
| | **755,790** | **(1,171,332)** |
| | **13,406** | **(1,919,820)** |

In 2016, the Group recalculated the profit tax for prior periods (2012-2015), as a result of resolving differences with contractors in the trial and the pre-trial order. As a result, income tax overprovided in prior periods, in accordance with the adjusted tax declarations submitted to the tax authorities, amounted to RUB 435,324 thousand.

### Income tax recognised in other comprehensive income

| | Year ended 31 December 2016 | | | Year ended 31 December 2015 | | |
|---|---|---|---|---|---|---|
| | Before tax | Tax | Net of tax | Before tax | Tax | Net of tax |
| Net change in fair value of available-for-sale financial assets | (19,904) | 3,981 | **(15,923)** | 70,683 | (14,137) | **56,546** |
| Remeasurements of the net defined benefit liability | 71,659 | (2,603) | **69,056** | (181,439) | 27,476 | **(153,963)** |
| | **51,755** | **1,378** | **53,133** | **(110,756)** | **13,339** | **(97,417)** |

*Reconciliation of profit before income tax is as follows:*

| | Year ended 31 December 2016 | % | Year ended 31 December 2015 | % |
|---|---|---|---|---|
| Profit before income tax | 4,748,887 | 100 | 2,800,767 | 100 |
| Income tax expense at applicable tax rate | (949,777) | (20) | (560,153) | (20) |
| Adjustment for prior periods | 435,324 | 9 | 194,838 | 7 |
| Change in the tax base of property, plant and equipment | - | - | 92 | - |
| Net tax effect of expenses not deductible/not taxable for taxation purposes | 527,859 | 11 | (1,554,597) | (56) |
| | 13,406 | - | **(1,919,820)** | **(69)** |

*Thousands of Russian Roubles, unless otherwise stated*

## 12 PROPERTY, PLANT AND EQUIPMENT

| | Land and buildings | Transmission networks | Equipment for electricity transformation | Other | Construction in progress | Total |
|---|---|---|---|---|---|---|
| ***Deemed cost*** | | | | | | |
| Balance at 1 January 2015 | 27,530,532 | 50,581,383 | 28,030,259 | 15,665,756 | 3,579,210 | 125,387,140 |
| Reclassification between groups | 1,093,197 | (1,120,604) | 30,133 | (2,726) | - | - |
| Additions | 83,849 | 526,143 | 151,900 | 179 | 12,343,409 | 13,105,480 |
| Transfers | 2,890,902 | 4,808,431 | 3,503,354 | 1,088,507 | (12,291,194) | - |
| Disposals | (9,096) | (35,932) | (25,340) | (214,672) | (152,644) | (437,684) |
| **Balance at 31 December 2015** | **31,589,384** | **54,759,421** | **31,690,306** | **16,537,044** | **3,478,781** | **138,054,936** |
| Balance at 1 January 2016 | 31,589,384 | 54,759,421 | 31,690,306 | 16,537,044 | 3,478,781 | 138,054,936 |
| Reclassification between groups | 2 | (1) | 978 | (979) | - | - |
| Additions | 127,794 | 293,276 | 77,575 | 62,214 | 13,445,115 | 14,005,974 |
| Transfers | 2,463,011 | 5,015,140 | 3,617,959 | 1,930,955 | (13,027,065) | - |
| Disposals | (6,587) | (28,557) | (55,358) | (193,024) | (30,514) | (314,040) |
| **Balance at 31 December 2016** | **34,173,604** | **60,039,279** | **35,331,460** | **18,336,210** | **3,866,317** | **151,746,870** |
| ***Accumulated depreciation and impairment*** | | | | | | |
| Balance at 1 January 2015 | (8,583,549) | (23,663,816) | (10,376,198) | (9,101,302) | (575,833) | (52,300,698) |
| Reclassification between groups | (316,050) | 147,860 | (165,737) | 108,575 | 225,352 | - |
| Depreciation for the period | (1,302,092) | (2,923,034) | (1,599,690) | (1,764,112) | - | (7,588,928) |
| Disposals | 3,538 | 30,694 | 18,459 | 123,038 | 26,961 | 202,690 |
| Impairment | (12,210) | (364,282) | (217,028) | 10,780 | (146,106) | (728,846) |
| **Balance at 31 December 2015** | **(10,210,363)** | **(26,772,578)** | **(12,340,194)** | **(10,623,021)** | **(469,626)** | **(60,415,782)** |
| Balance at 1 January 2016 | (10,210,363) | (26,772,578) | (12,340,194) | (10,623,021) | (469,626) | (60,415,782) |
| Reclassification between groups | (47,044) | (113,236) | (40,098) | (3,990) | 204,368 | - |
| Depreciation for the period | (1,438,464) | (3,338,849) | (1,822,013) | (1,756,947) | - | (8,356,273) |
| Disposals | 4,283 | 26,234 | 35,358 | 177,136 | 8,852 | 251,863 |
| Impairment | 95,397 | 259,931 | 122,714 | 15,184 | 70,914 | 564,140 |
| **Balance at 31 December 2016** | **(11,596,191)** | **(29,938,498)** | **(14,044,233)** | **(12,191,638)** | **(185,492)** | **(67,956,052)** |
| ***Net book value*** | | | | | | |
| **At 1 January 2015** | **18,946,983** | **26,917,567** | **17,654,061** | **6,564,454** | **3,003,377** | **73,086,442** |
| **At 31 December 2015** | **21,379,021** | **27,986,843** | **19,350,112** | **5,914,023** | **3,009,155** | **77,639,154** |
| **At 31 December 2016** | **22,577,413** | **30,100,781** | **21,287,227** | **6,144,572** | **3,680,825** | **83,790,818** |

*Thousands of Russian Roubles, unless otherwise stated*

## 12 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

As at 31 December 2016 construction in progress includes prepayments for property, plant and equipment of RUB 847 thousand (as at 31 December 2015: RUB 2,782 thousand) and inventories for the construction of property, plant and equipment of RUB 481,548 thousand (as at 31 December 2015: RUB 334,349 thousand). In 2016, the reserve of prepayments for property, plant and equipment of RUB 6,218 thousand was restored.

Borrowing costs totalling RUB 295,524 thousand with a capitalisation rate of 8.75-16% during 2016 (2015: RUB 274,810 thousand with a capitalization rate of 8.75-18%) were included in the cost of property, plant and equipment and represent interest on loans.

### Leased property, plant and equipment

As at 31 December 2016, the Group has no leased facilities (as at 31 December 2015 the Group leases transportation vehicles under a finance lease agreements). Title to the leased assets transfers to the Group at the end of lease.

As at 31 December 2015 the net book value of leased property, plant and equipment, accounted for as part of the Group's property, plant and equipment, was as follows:

| | Other | Total |
|---|---|---|
| Cost | 32,663 | 32,663 |
| Accumulated depreciation | (14,247) | (14,247) |
| **Net book value at 31 December 2015** | **18,416** | **18,416** |

### Impairment of property, plant and equipment

Due to the negative impact of macroeconomic factors on Russian economy the Group performed a test for impairment of property, plant and equipment as at 31 December.

As a result of the impairment test as at 31 December 2016 loss on impairment of property, plant and equipment was recognized in the amount of RUB 294,230 thousand for "Yarenergo" and reversal of loss on impairment was recognized in the amount of RUB 852,152 thousand for "Lipetskenergo".

| Division | Impairment at 31 December 2015 | Depreciation and disposals during 2016 | Recognized impairment at 31 December 2016 | Reversal of impairment at 31 December 2016 | Impairment at 31 December 2016 |
|---|---|---|---|---|---|
| Lipetskenergo | 9,003,102 | (764,276) | - | (852,152) | 7,386,674 |
| Yarenergo | - | - | 294,230 | - | 294,230 |
| **Total** | **9,003,102** | **(764,276)** | **294,230** | **(852,152)** | **7,680,904** |

The majority of the Group's property, plant and equipment is specialized in nature and is rarely sold on the open market other than as part of a continuing business. The market for similar property, plant and equipment is not active in the Russian Federation and does not provide a sufficient number of sales transactions for use of a market-based approach for determination of the fair value.

Therefore, the values in use for property, plant and equipment as at 31 December 2016 and as at 31 December 2015 were determined using projected cash flows method. This method considers the future net cash flows expected to be generated through the usage of property, plant and equipment in the process of operating activities up to its ultimate disposal to determine the recoverable amount of the assets of the Group.

## 12 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Each cash-generating unit (CGU) is determined by the Group based on the geographical location of the Company's branches and subsidiaries which is the smallest identifiable group of assets that generates cash inflows that are independent of the cash inflows from other groups of assets.

The following key assumptions were used in determining the recoverable amounts of each of the cash-generating units:

- cash flows were predicted on the basis of the provisions of the guidelines for the testing of power grid assets for impairment and recognition/reversal of losses on their impairment (approved by the Order of PJSC "IDGC of Centre" No. 432-CA of 26.12.2016 and forecast data for the period up to 2021);
- forecast cash flows were prepared for the period 2017-2021 for all the CGUs and were based on the best estimate of the Group's Management in respect of the transmission volumes, operating and capital expenditures and tariffs approved by regulatory bodies for 2017;
- tariffs for electricity transmission services for forecasted period were estimated using business plans, amended and approved by PJSC "Russian Grids"which were based on the tariff models prepared taking into account annual average growth of tariffs for electricity transmission services (in accordance with "The socio-economic development of the Russian Federation for 2017 and the planning period of 2018-2019"). Tariffs growth rates in 2017-2022 are restricted by inflation rates according to Ministry of Economic Development of the Russian Federation (till 2030);
- forecasted electricity transmission volumes for all CGUs were determined based on the Company's business plans for 2017-2021;
- the cash flow forecasts were discounted to their present value at the nominal weighted average cost of capital of 10.91% (2015: 11,31%);
- growth rate of the net cash flows amounted to 3.3% for all CGUs in the post-forecasted period.

Quantitative information on significant unobservable inputs used in assessing value in use, are disclosed below:

| | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|
| Growth rate of necessary gross revenue to the previous year | 2.39% | 0.75% | 4.16% | 4.33% | 4.40% |
| Productive supply ("boiler"), million KWh | 51,908 | 47,572 | 47,829 | 48,122 | 48,424 |
| Inflation forecast of the MED | 5.43% | 4.00% | 4.00% | 4.10% | 4.10% |
| The level of capital investment, millions of Russian Roubles | 9,738 | 9,656 | 10,066 | 10,983 | 11,798 |

Sensitivity analysis for key assumptions for PJSC "IDGC of Centre" is presented below:

- increase of discount rate to 12% increases impairment loss by RUB 363,830 thousand for "Yarenergo";
- reduction of necessary gross revenue to the base value in each period by 3% increases impairment loss by RUB 733,437 thousand for "Yarenergo";
- increase of operating expenses level to the base value in each period by 5% increases impairment loss by RUB 1,048,546 thousand for "Yarenergo";
- increase of capital investment level in the forecasted and post-forecasted period by 10% increases impairment loss by RUB 114,338 thousand for "Yarenergo";
- increase in annual revenue by 3% would result in no impairment of "Yarenergo".

*Thousands of Russian Roubles, unless otherwise stated*

## 13 INTANGIBLE ASSETS

| | Software | Research and development | Other intangible assets | Total |
|---|---|---|---|---|
| ***Cost*** | | | | |
| Balance at 1 January 2015 | 414,496 | 19,320 | 659,906 | 1,093,722 |
| Reclassification between groups | 513,937 | - | (513,937) | - |
| Additions | 433,264 | 24,591 | 972,592 | 1,430,447 |
| Disposals | (400,545) | - | - | (400,545) |
| **Balance at 31 December 2015** | **961,152** | **43,911** | **1,118,561** | **2,123,624** |
| Balance at 1 January 2016 | 961,152 | 43,911 | 1,118,561 | 2,123,624 |
| Reclassification between groups | - | (22,645) | 22,645 | - |
| Additions | 778,495 | 32,596 | 124,245 | 935,336 |
| Disposals | (274,135) | (23,915) | (47,200) | (345,250) |
| **Balance at 31 December 2016** | **1,465,512** | **29,947** | **1,218,251** | **2,713,710** |
| ***Accumulated amortisation*** | | | | |
| Balance at 1 January 2015 | (170,248) | - | (332,476) | (502,724) |
| Reclassification between groups | (287,650) | - | 287,650 | - |
| Amortisation for the period | (202,065) | - | (21,930) | (223,995) |
| Disposals | 400,545 | - | - | 400,545 |
| **Balance at 31 December 2015** | **(259,418)** | **-** | **(66,756)** | **(326,174)** |
| Balance at 1 January 2016 | (259,418) | - | (66,756) | (326,174) |
| Amortisation for the period | (273,480) | - | (72,609) | (346,089) |
| Disposals | 258,310 | - | 45,525 | 303,835 |
| **Balance at 31 December 2016** | **(274,588)** | **-** | **(93,840)** | **(368,428)** |
| ***Net book value*** | | | | |
| **At 1 January 2015** | **244,248** | **19,320** | **327,430** | **590,998** |
| **At 31 December 2015** | **701,734** | **43,911** | **1,051,805** | **1,797,450** |
| **At 31 December 2016** | **1,190,924** | **29,947** | **1,124,411** | **2,345,282** |

In 2015 and in 2016, the intangible assets of the Group (subgroup "Other intangible assets") include a right to charge fee from users of services on electricity transmission in accordance with "Service Concession Arrangement concerning the financing, establishment and operation of facilities for the transmission and distribution of electric energy on the territory of the Tambov region". This agreement provides for the construction by a Group of objects for the purposes of transmission and distribution of electricity in the Tambov region and the provision of transmission services, electricity distribution and connection services with the use of objects of the Service Concession Arrangement. Ownership of the constructed objects belongs to the Tambov region, and the Group receives the right of possession and use of objects for the Group activities. The Service Concession Arrangement is concluded for 20 years. The calculation of long-term gross revenue from transmission of electricity produced by the parties taking into account the planned change of tariffs provided by the Forecast "The socio-economic development of the Russian Federation for 2016 and the planning period of 2017-2018" and should be reviewed annually. Thus during the term of the Service Concession Arrangement the administration of Tambov region can provide the Group with subsidies in terms of payment of the consideration for construction of objects, and in part compensation for lost revenue from electricity

*Thousands of Russian Roubles, unless otherwise stated*

## 13 INTANGIBLE ASSETS (CONTINUED)

transmission. The group is obliged to support the objects of the agreement in good condition, produce for own account current and capital repairs, to cover the costs for facility maintenance. At the end of the term of the agreement the Group has the right to redeem the objects of the agreement pursuant to the Federal Law of 21 December 2001 № 178-FZ "On privatization of state and municipal property".

In 2016, the intangible asset is recognized at fair value of the consideration receivable by the Group for the construction of objects of the Service Concession Arrangement in the amount of RUB 123,889 thousand (2015: in the amount of RUB 972,341 thousand) (Note 7). The construction costs in 2016 amounted to RUB 111,612 thousand (2015: RUB 875,983 thousand) (Note 8). Profit from construction of objects of the Service Concession Arrangement was recognized by the Group in 2016 in the amount of RUB 12,277 thousand (2015: in the amount of RUB 96,358 thousand).

## 14 DEFERRED TAX ASSETS AND LIABILITIES

### a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following items:

| | Assets | | Liabilities | | Net | |
|---|---|---|---|---|---|---|
| | **31 December 2016** | **31 December 2015** | **31 December 2016** | **31 December 2015** | **31 December 2016** | **31 December 2015** |
| Property, plant and equipment | - | - | (6,260,811) | (6,669,266) | (6,260,811) | (6,669,266) |
| Intangible assets | - | - | (27,088) | (19,271) | (27,088) | (19,271) |
| Investments and financial assets | - | - | (100,061) | (87,739) | (100,061) | (87,739) |
| Inventories | 597 | 600 | - | - | 597 | 600 |
| Trade and other receivables | 1,129,249 | 833,035 | - | - | 1,129,249 | 833,035 |
| Finance lease liabilities | - | 301 | - | - | - | 301 |
| Loans and borrowings | - | - | (4,462) | (3,964) | (4,462) | (3,964) |
| Employee benefits | 221,449 | 247,613 | - | - | 221,449 | 247,613 |
| Provision for employee payables | 162,931 | 126,216 | - | - | 162,931 | 126,216 |
| Trade and other payables | 456,478 | 393,352 | - | - | 456,478 | 393,352 |
| Other | 896 | 1,272 | - | (139) | 896 | 1,133 |
| **Deferred tax assets / (liabilities)** | **1,971,600** | **1,602,389** | **(6,392,383)** | **(6,780,379)** | **(4,420,822)** | **(5,177,990)** |

*Thousands of Russian Roubles, unless otherwise stated*

## 14 DEFERRED TAX ASSETS AND LIABILITIES (CONTINUED)

### b) Movements in temporary differences during the period

| | 1 January 2016 | Recognised in profit or loss | Recognised in other comprehensive income | 31 December 2016 |
|---|---|---|---|---|
| Property, plant and equipment | (6,669,266) | 408,455 | - | (6,260,811) |
| Intangible assets | (19,271) | (7,817) | - | (27,088) |
| Investments and financial assets | (87,739) | (16,303) | 3,981 | (100,061) |
| Inventories | 600 | (3) | - | 597 |
| Trade and other receivables | 833,035 | 296,214 | - | 1,129,249 |
| Finance lease liabilities | 301 | (301) | - | - |
| Loans and borrowings | (3,964) | (498) | - | (4,462) |
| Employee benefits | 247,613 | (23,561) | (2,603) | 221,449 |
| Provision for employee payables | 126,216 | 36,715 | - | 162,931 |
| Trade and other payables | 393,352 | 63,126 | - | 456,478 |
| Other | 1,133 | (237) | - | 896 |
| **Net deferred tax assets / (liabilities)** | **(5,177,990)** | **755,790** | **1,378** | **(4,420,822)** |

| | 1 January 2015 | Recognised in profit or loss | Recognised in other comprehensive income | 31 December 2015 |
|---|---|---|---|---|
| Property, plant and equipment | (5,221,541) | (1,447,725) | - | (6,669,266) |
| Intangible assets | - | (19,271) | - | (19,271) |
| Investments and financial assets | (77,004) | 3,402 | (14,137) | (87,739) |
| Inventories | 1,340 | (740) | - | 600 |
| Trade and other receivables | 604,998 | 228,037 | - | 833,035 |
| Finance lease liabilities | 16,798 | (16,497) | - | 301 |
| Loans and borrowings | (758) | (3,206) | - | (3,964) |
| Employee benefits | 210,119 | 10,018 | 27,476 | 247,613 |
| Provision for employee payables | 116,578 | 9,638 | - | 126,216 |
| Trade and other payables | 329,034 | 64,318 | - | 393,352 |
| Other | 439 | 694 | - | 1,133 |
| **Net deferred tax assets / (liabilities)** | **(4,019,997)** | **(1,171,332)** | **13,339** | **(5,177,990)** |

*Thousands of Russian Roubles, unless otherwise stated*

## 15 INVESTMENTS AND FINANCIAL ASSETS

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Assets related to the employee benefit fund | 500,305 | 438,693 |
| Available-for-sale financial assets | 213,181 | 234,369 |
| | **713,486** | **673,062** |

Financial assets related to the employee benefit fund relate to the Group's contributions accumulated in the solidary and employees' individual pension accounts with the Non-State Pension Fund of Electric Power Industry (employee benefit fund). These assets are not assets of the plan, because under the terms of existing agreements with the Fund the Group is able to use the above contributions to reduce future contributions, or for compensation though the funding of other plans, or transfer to another fund on its own initiative.

Available-for-sale financial assets represent investments in shares of JSC E.ON Russia and other securities, which are listed on CJSC "MICEX Stock Exchange", recorded at fair market value (belong to Level 1 in the fair value hierarchy). In 2016, the Group recognized impairment loss on revaluation of available-for-sale financial assets in the amount of RUB (19,904) thousand as a component of other comprehensive income (2015: gain in the amount of RUB 70,683 thousand).

The Group's exposure related to credit risks and impairment losses related to financial assets is disclosed in Note 28

## 16 OTHER NON-CURRENT ASSETS

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Trade accounts receivable | 29,376 | 21,825 |
| Trade accounts receivable impairment allowance | (789) | (489) |
| Non-current prepayments | 3,493 | 3,250 |
| Other accounts receivable | 134,171 | 41,182 |
| | **166,251** | **65,768** |

## 17 CASH AND CASH EQUIVALENTS

Cash and cash equivalents represent cash in bank accounts and short-term deposits placed in banks in the amount of RUB 2,567,305 thousand (as at 31 December 2015: RUB 123,220 thousand).

As at 31 December 2016 cash on accounts in banks with controlling interest of the Government is in the amount of RUB 213,286 thousand (as at 31 December 2015: RUB 53,930 thousand), in banks with non-controlling interests or without participation of the Government RUB 14,493 thousand (2015: RUB 31,035 thousand).

As at 31 December 2016 short-term deposits placed in banks with controlling interest of the Government, are in the amount of RUB 1,180,000 thousand (as at 31 December 2015: nil), in banks with non-controlling interests or without participation of the Government RUB 1,139,500 thousand (2015: nil).

*Thousands of Russian Roubles, unless otherwise stated*

## 18 TRADE AND OTHER RECEIVABLES

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Trade accounts receivables | 25,646,470 | 26,718,559 |
| Trade accounts receivables impairment allowance | (12,986,991) | (11,335,201) |
| Other accounts receivables | 1,316,587 | 1,299,127 |
| Other receivables impairment allowance | (562,203) | (501,482) |
| **Total financial assets** | **13,413,863** | **16,181,003** |
| Prepayments | 221,181 | 212,160 |
| Prepayments impairment allowance | (106,446) | (93,886) |
| VAT recoverable | 433,035 | 405,315 |
| Prepaid taxes other than income tax | 15,555 | 57,660 |
| **Total** | **13,977,188** | **16,762,252** |

For more detailed information concerning the Group's exposure to credit risks and impairment losses related to trade and other receivables refer to Note 28.

## 19 INVENTORIES

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Materials and supplies | 1,192,462 | 1,182,517 |
| Other inventories | 910,222 | 832,887 |
| **Total inventories** | **2,102,684** | **2,015,404** |
| Less: provision for inventory obsolescence | (2,985) | (3,001) |
| **Total** | **2,099,699** | **2,012,403** |

## 20 EQUITY

### (a) Share capital

| | Ordinary shares | |
|---|---|---|
| | 31 December 2016 | 31 December 2015 |
| Issued shares, fully paid, number | 42,217,941,468 | 42,217,941,468 |
| Par value of one share (in RUB) | 0.10 | 0.10 |

### (b) Dividends

In accordance with Russian legislation the Company's distributable reserves are limited to the balance of accumulated retained earnings as recorded in the Company's statutory financial statements prepared in accordance with Russian Accounting Principles.

At the Company's annual shareholders meeting held on 26 June 2015 the decision was made to distribute the Company's profit for the year 2014 to dividends in the amount of RUB 831,693 thousand and to pay dividends for the year 2014 in the amount of RUB 0.0197 per ordinary share of the Company in cash.

*Thousands of Russian Roubles, unless otherwise stated*

## 20 EQUITY (CONTINUED)

At the Company's annual shareholders meeting held on 8 June 2016 the decision was made to distribute the Company's profit for the year 2015 to dividends in the amount of RUB 455,954 thousand and to pay dividends for the year 2015 in the amount of RUB 0.0108 per ordinary share of the Company in cash.

In 2016, the Company recovered unclaimed dividends for 2012 in the amount of RUB 2,253 thousand (in 2015 – in the amount of RUB 4,069 thousand for 2011).

## 21 EARNINGS PER SHARE: BASED AND DILUTED

The calculation of earnings per share was based on the profit attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding during the period. The Company has no dilutive potential ordinary shares.

| | **Ordinary shares** | **Ordinary shares** |
|---|---|---|
| | **31 December 2016** | **31 December 2015** |
| Authorised (ordinary) shares (number) | 42,217,941,468 | 42,217,941,468 |
| Par value of one share (in RUB) | 0.10 | 0.10 |
| Weighted average number of shares | 42,217,941,468 | 42,217,941,468 |
| **Profit for the year attributable to shareholders** | **4,723,758** | **852,807** |
| **Earning per share (in RUB): basic and diluted** | **0.112** | **0.020** |

*Thousands of Russian Roubles, unless otherwise stated*

## 22 LOANS AND BORROWINGS

This note provides information about the contractual terms of the Group's loans and borrowings. For more information about the Group's exposure to interest rate risk, refer to Note 28.

*Long-term loans and borrowings*

| | | | | | Par value | | Carrying value | |
|---|---|---|---|---|---|---|---|---|
| **Name of lender** | | **Effective interest rate 31 December 2016** | **Effective interest rate 31 December 2015** | **Maturity** | **31 December 2016** | **31 December 2015** | **31 December 2016** | **31 December 2015** |
| PJSC "Bank VTB" | Unsecured | 8,75-10,40% | 8,75-13,98% | 2017-2019 | 9,260,000 | 10,670,000 | 9,260,000 | 10,670,000 |
| PJSC "Rosbank" | Unsecured | - | 12,90% | 2016 | - | 1,500,000 | - | 1,500,000 |
| PJSC "Sberbank" | Unsecured | 9,90-10,10% | 10,524-14,06% | 2018-2019 | 13,696,185 | 12,797,055 | 13,696,185 | 12,797,055 |
| Unsecured bond issues | Unsecured | 9,32-12,42% | 11,58-12,42% | 2018-2020 | 20,336,400 | 15,475,454 | 20,314,092 | 15,144,630 |
| PJSC "Promsvyasbank" | Unsecured | 14,55% | - | 2017 | 8,200 | - | 8,200 | - |
| PJSC "Bank SGB" | Unsecured | 13,00% | - | 2017 | 10 | - | 10 | - |
| PJSC "Sovkombank" | Unsecured | - | 11,90% | 2018-2022 | - | 2,000,000 | - | 2,000,000 |
| | | | | | **43,300,795** | **42,442,509** | **43,278,487** | **42,111,685** |
| Less: current portion | | | | | | | | |
| PJSC "Bank VTB" | Unsecured | 8,75-10,40% | 8,75-13,98% | 2017-2019 | 3,640,000 | - | 3,640,000 | - |
| PJSC "Sberbank" | Unsecured | 9,90-10,10% | 10,524-14,06% | 2018-2019 | 11,185 | 1,512,055 | 11,185 | 1,512,055 |
| PJSC "Promsvyasbank" | Unsecured | 14,55% | - | 2017 | 8,200 | - | 8,200 | - |
| PJSC "Bank SGB" | Unsecured | 13,00% | - | 2017 | 10 | - | 10 | - |
| Unsecured bond issues | Unsecured | 9,32-12,42% | 11,58-12,42% | 2018-2020 | 336,400 | 475,454 | 336,400 | 164,450 |
| | | | | | **3,995,795** | **1,987,509** | **3,995,795** | **1,676,505** |
| **Total long-term loans and borrowings** | | | | | **39,305,000** | **40,455,000** | **39,282,692** | **40,435,180** |

*Thousands of Russian Roubles, unless otherwise stated*

## 22 LOANS AND BORROWINGS (CONTINUED)

*Current loans and borrowings and current portion of long-term loans and borrowings*

| | | Effective | Effective | Par value | | Carrying value | |
|---|---|---|---|---|---|---|---|
| Name of lender | | interest rate 31 December 2016 | interest rate 31 December 2015 | 31 December 2016 | 31 December 2015 | 31 December 2016 | 31 December 2015 |
| PJSC "Bank VTB" | Unsecured | 8,75-10,40% | 8,75-13,98% | 3,640,000 | - | 3,640,000 | - |
| PJSC "Sberbank" | Unsecured | 9,90-10,10% | 10,524-14,06% | 11,185 | 1,512,055 | 11,185 | 1,512,055 |
| PJSC "Promsvyasbank" | Unsecured | 14,55% | - | 8,200 | - | 8,200 | - |
| PJSC "Bank SGB" | Unsecured | 13,00% | - | 10 | - | 10 | - |
| Unsecured bond issues | Unsecured | 9,32-12,42% | 11,58-12,42% | 336,400 | 475,454 | 336,400 | 164,450 |
| | | | | **3,995,795** | **1,987,509** | **3,995,795** | **1,676,505** |

All the Group's loans and borrowings are denominated in RUB and bear a fixed interest rate. The effective interest rate is the market interest rate applicable to the loan on the date of its receipt.

The carrying value of loans and borrowings approximates their fair value.

As at 31 December 2016 and 31 December 2015 no bank loans are secured over bank guarantees received.

During 2015, the Group made three issues of non-convertible documentary interest - bearing bonds with a total nominal value of RUB 15,000,000 thousand with a nominal interest rate of 11.58-12.42% per annum. The maturity of the bonds is 3-7 years. Two issues of the interest - bearing bonds have been purchased by PJSC "Russian Grids". During 2016, the Group made the issue of non-convertible documentary interest - bearing bonds with a nominal value of RUB 5,000,000 thousand with a nominal interest rate of 9.32% per annum. The maturity of the bonds is 10 years. The issue of the interest - bearing bonds have been purchased by PJSC "Russian Grids" (Note 32d).

*Thousands of Russian Roubles, unless otherwise stated*

## 23 FINANCE LEASE LIABILITIES

The finance lease liabilities are secured by the leased assets.

As at 31 December 2016, the Group has no finance lease liabilities because of the termination of finance lease agreements. In 2016 the Group leased transportation vehicles (in 2015 - transportation vehicles) under finance lease agreements. Finance lease liabilities are payable as follows:

| | At 31 December 2015 | | |
|---|---|---|---|
| | Future minimum lease payments | Present value of minimum lease payments | Interest |
| Less than one year | 1,629 | 1,503 | 126 |
| | **1,629** | **1,503** | **126** |

## 24 EMPLOYEE BENEFITS

The tables below provide information about the employee benefit obligations and actuarial assumptions used for the years ended 31 December 2016 and 31 December 2015.

### (a) Net liability in Consolidated Statement of Financial Position

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Recognised post-employment benefit | 2,202,613 | 2,344,882 |
| Total recognised liability | **2,202,613** | **2,344,882** |

### (b) Movements in the defined benefit liability

| | Post-employment benefit | | Other long-term liability | | Total liability | |
|---|---|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| Balance at 1 January | 2,344,882 | 2,051,491 | - | - | 2,344,882 | 2,051,491 |
| Included in profit or loss | | | | | | |
| Current service cost | 85,104 | 73,905 | - | - | 85,104 | 73,905 |
| Past service cost | (135,540) | 6,680 | - | - | (135,540) | 6,680 |
| Interest cost | 190,468 | 223,879 | - | - | 190,468 | 223,879 |
| | **140,032** | **304,464** | **-** | **-** | **140,032** | **304,464** |
| Included in OCI | | | | | | |
| Remeasurements loss (gain): | | | | | | |
| - Actuarial loss (gain) arising from: | | | | | | |
| - demographic assumptions | (18,063) | (46,392) | - | - | (18,063) | (46,392) |
| - financial assumptions | (59,432) | 230,324 | - | - | (59,432) | 230,324 |
| - experience adjustment | 5,836 | (2,493) | - | - | 5,836 | (2,493) |
| | **(71,659)** | **181,439** | **-** | **-** | **(71,659)** | **181,439** |
| Other | | | | | | |
| Benefits paid | (210,642) | (192,512) | - | - | (210,642) | (192,512) |
| **Balance at 31 December** | **2,202,613** | **2,344,882** | **-** | **-** | **2,202,613** | **2,344,882** |

*Thousands of Russian Roubles, unless otherwise stated*

## 24 EMPLOYEE BENEFITS (CONTINUED)

### (c) Actuarial assumptions

Principal actuarial assumptions used are as follows:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Discount rate, annual | 8.50% | 9.50% |
| Future salary increase, per year | 4.70% | 6.00% |
| Inflation rate, per year | 4.70% | 6.00% |

Assumptions regarding future mortality have been based on published statistics and mortality tables. The current longevities underlying the values of the defined benefit obligation at the reporting date were as follows.

| | 2016 | 2015 |
|---|---|---|
| **Longevity at age 60 for current pensioners** | | |
| Males | 19 | 19 |
| Females | 25 | 25 |
| **Longevity at age 60 for current members aged 45** | | |
| Males | 22 | 22 |
| Females | 26 | 27 |

At 31 December 2016, the weighted-average duration of the defined benefit obligation was 7.5 years (2015: 7.1 years).

The amount of expected payments under defined benefit plans for 2017 is RUB 236,860 thousand.

### (d) Sensitivity analysis

Reasonably possible changes at the reporting date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit obligation by the amounts shown below.

| 31 December 2016 | **Impact of movement in actuarial assumptions on Defined benefit plan obligation** | |
|---|---|---|
| **Actuarial assumptions** | Increase | Decrease |
| Discount rate (0.5% movement) | -3.67% | 3.67% |
| Future salary growth (0.5% movement) | 0.79% | -0.79% |
| Future pension growth (0.5% movement) | 3.01% | -3.01% |
| Staff turnover (10% movement) | -0.85% | 0.85% |
| Future mortality (10% movement) | -1.25% | 1.25% |

Although the analysis does not take account of the full distribution of cash flows expected under the plan, it does provide an approximation of the sensitivity of the assumptions shown.

*Thousands of Russian Roubles, unless otherwise stated*

## 25 EMPLOYEE PAYABLES

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Salaries and wages payable | 617,246 | 8,922 |
| Unused vacation provision | 466,146 | 344,827 |
| Annual bonus provision | 348,507 | 286,061 |
| Provision for termination benefits | - | 190 |
| | **1,431,899** | **640,000** |

Provision for annual bonuses includes bonuses and other similar payments accrued (including compulsory social security contributions) based on employees' performance.

## 26 TRADE AND OTHER PAYABLES, PROVISIONS

Current trade and other payables include:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Trade accounts payable | 5,696,074 | 4,907,108 |
| Other payables | 701,138 | 1,355,955 |
| Advances from customers | 1,777,522 | 2,048,474 |
| | **8,174,734** | **8,311,537** |

As a part of current liabilities, there is litigation provision, which includes:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **Balance at 1 January** | **1,099,872** | **1,162,928** |
| Provision increase during the year | 684,782 | 1,074,233 |
| Decrease due to the use of provision | (401,501) | (348,168) |
| Decrease due to reversal | (356,950) | (789,121) |
| **Balance at 31 December** | **1,026,203** | **1,099,872** |

Non-current trade and other payables include:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Advances from customers | 169,521 | 365,804 |
| Other trade payables | 865,995 | 14,884 |
| | **1,035,516** | **380,688** |

Advances from customers are mainly represented by prepayments received from customers under contracts of technical connection to the power grid.

*Thousands of Russian Roubles, unless otherwise stated*

## 27 OTHER TAXES PAYABLE

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Value added tax | 1,319,583 | 910,038 |
| Compulsory social security contributions | 446,336 | 421,964 |
| Property tax | 300,464 | 145,911 |
| Other taxes | 149,341 | 16,486 |
| | **2,215,724** | **1,494,399** |

## 28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### (a) Overview

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

- credit risk;
- liquidity risk;
- market risk.

The Group does not have any significant exposure to currency risk on sales, purchases and borrowings, because no significant sales, purchases, or borrowings are denominated in a currency other than the functional currency of the Company, which is the Russian Rouble.

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital.

The Group's principal objective when managing capital risk is to sustain its creditworthiness and a normal level of capital adequacy for doing business as a going concern, in order to ensure returns for shareholders and benefits to other stakeholders and to maintain an optimal capital structure to reduce the cost of borrowed capital.

In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders or issue new shares.

### (b) Credit risk

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

#### *(i) Trade and other receivables*

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

To manage credit risk the Group attempts, to the fullest extent possible, to demand prepayments from customers. As a rule, prepayment for connection services is set in a contract and depends on the amount of capacity to be connected.

The customer base for electricity transmission services is limited to several distribution companies and a small number of large manufacturing/extraction enterprises. Payments are tracked regularly and electricity transmission customers are advised of any failures to submit timely payments. For quick collection and complete control of accounts receivable collection activities are performed to reduce the Company's finance losses, caused by non-fulfilment or insufficient fulfilment by some contractors of their contractual obligations.

The Group does not require collateral in respect of trade and other receivables.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables that relate to individually significant exposures.

ИД

*Thousands of Russian Roubles, unless otherwise stated*

## 28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

### *(ii) Exposure to credit risk*

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

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Trade and other receivables | 13,576,621 | 16,243,521 |
| Cash and cash equivalents | 2,567,305 | 123,220 |
| | **16,143,926** | **16,366,741** |

The Group's two most significant customers, regional distribution entities, account for RUB 3,465,552 thousand of the trade receivables carrying amount at 31 December 2016 (at 31 December 2015: RUB 5,239,024 thousand).

The maximum exposure to credit risk for trade receivables (excluding other receivables) at the reporting date by type of customer was:

| | Carrying amount at 31 December 2016 | Carrying amount at 31 December 2015 |
|---|---|---|
| Electricity transmission customers | 11,932,488 | 13,210,035 |
| Consumers of electricity and capacity | 455,815 | 1,837,013 |
| Connection services customers | 134,091 | 176,016 |
| Other customers | 165,672 | 181,630 |
| | **12,688,066** | **15,404,694** |

*Impairment losses*

The tables below analyse the Group's trade and other receivables into relevant groups based on the past due periods:

| | At 31 December 2016 | | At 31 December 2015 | |
|---|---|---|---|---|
| | Carrying amount | Allowance | Carrying amount | Allowance |
| Not past due | 9,687,712 | (173,167) | 7,602,048 | (39,217) |
| Past due 0-3 months | 2,217,142 | (809,813) | 3,472,186 | (155,276) |
| Past due 3-6 months | 429,072 | (211,695) | 713,945 | (100,480) |
| Past due 6-12 months | 883,411 | (380,174) | 2,216,021 | (424,166) |
| Past due more than 12 months | 13,909,267 | (11,975,134) | 14,076,493 | (11,118,033) |
| | **27,126,604** | **(13,549,983)** | **28,080,693** | **(11,837,172)** |

The movements in the allowance for impairment in respect of trade and other receivables were as follows:

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| **Balance at 1 January** | **11,837,172** | **10,505,153** |
| Increase during the period | 3,149,514 | 2,214,226 |
| Amounts written-off against trade and other receivables | (318,608) | (74,803) |
| Decrease due to reversal of amounts written off | (1,118,095) | (807,404) |
| **Balance at 31 December** | **13,549,983** | **11,837,172** |

**28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)**

**(c) Liquidity risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group monitors the risk of cash shortfalls by means of current liquidity planning. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. This approach is used to analyse payment dates associated with financial assets, and also to forecast cash flows from operating activities.

To manage the liquidity risk, the Group has negotiated long-term and short-term credit lines with a pool of banks.

As at 31 December 2016 the Group's unused portion of long-term and short-term credit line facilities amounted to RUB 18,915,779 thousand (as at 31 December 2015: RUB 12,419,291 thousand). Among them, credit line facilities related to the banks with controlling interest of the Government amounted to RUB 8,815,779 thousand (as at 31 December 2015: RUB 5,319,291 thousand).

*Thousands of Russian Roubles, unless otherwise stated*

## 28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements:

| | Carrying amount | Contractual cash flows | 12 months or less | Between 1 and 2 years | Between 2 and 3 years | Between 3 and 4 years | Between 4 and 5 years | More than 5 years |
|---|---|---|---|---|---|---|---|---|
| **Liabilities as at 31 December 2016** | | | | | | | | |
| Short-term and long-term bank loans including current portion | 22,964,395 | 27,102,489 | 5,828,997 | 14,194,360 | 7,079,132 | - | - | - |
| Unsecured bond issues | 20,314,092 | 26,408,850 | 2,249,800 | 6,940,150 | 11,630,500 | 5,588,400 | - | - |
| Trade and other payables | 6,524,409 | 6,524,409 | 6,397,212 | 42,867 | 45,873 | 2,273 | 2,273 | 33,911 |
| | **49,802,896** | **60,035,748** | **14,476,009** | **21,177,377** | **18,755,505** | **5,590,673** | **2,273** | **33,911** |

| | Carrying amount | Contractual cash flows | 12 months or less | Between 1 and 2 years | Between 2 and 3 years | Between 3 and 4 years | Between 4 and 5 years | More than 5 years |
|---|---|---|---|---|---|---|---|---|
| **Liabilities as at 31 December 2015** | | | | | | | | |
| Short-term and long-term bank loans including current portion | 26,967,055 | 34,993,800 | 4,528,331 | 7,874,198 | 19,408,394 | 3,182,877 | - | - |
| Unsecured bond issues | 15,144,630 | 23,532,050 | 1,785,100 | 1,785,100 | 6,475,450 | 1,165,800 | 6,165,800 | 6,154,800 |
| Finance lease liabilities | 1,503 | 1,629 | 1,629 | - | - | - | - | - |
| Trade and other payables | 6,277,947 | 6,277,947 | 6,263,063 | 859 | 1,035 | 1,035 | 1,035 | 10,920 |
| | **48,391,135** | **64,805,426** | **12,578,123** | **9,660,157** | **25,884,879** | **4,349,712** | **6,166,835** | **6,165,720** |

*Thousands of Russian Roubles, unless otherwise stated*

## 28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

### (d) Market risk

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

### (e) Interest rate risk

Substantially all the operations of the Group are denominated in Russian Roubles, hence the Group is not exposed to significant currency risk.

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group is exposed to interest rate risk only through market value fluctuations of loans and borrowings. The interest rates on most long- and short-term loans and borrowings are fixed. Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt).

The Group Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

*Profile*

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

| **Fixed rate instruments** | **Carrying amount 31 December 2016** | **Carrying amount 31 December 2015** |
|---|---|---|
| Loans and borrowings, finance lease liability | 43,278,487 | 42,113,188 |

*Fair value sensitivity analysis for fixed rate instruments*

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit and loss, and the Group does not designate derivatives (interest rate swaps) as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

### (f) Accounting classifications and fair values

The fair values of the Group's financial assets and liabilities approximate their carrying amounts as at 31 December 2016.

The Group measures at fair value available-for-sale financial assets represented by equity securities (Note 15).

### (g) Capital management

Management's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. Management monitors the return on capital, which the Group defines as result from operating activities divided by total shareholders' equity.

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

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

The Company and its subsidiaries are subject to external capital requirements that require that their net assets as determined in accordance with Russian Accounting Principles must exceed their charter capital at all times.

*Thousands of Russian Roubles, unless otherwise stated*

## 28 FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

As at the end of the reporting year the debt-to-equity ratio for the Group was as follows:

| | Carrying value | |
|---|---|---|
| | **31 December 2016** | **31 December 2015** |
| Aggregate liabilities | 63,788,436 | 61,562,627 |
| Less: cash and cash equivalents | (2,567,305) | (123,220) |
| **Net debt** | **61,221,131** | **61,439,407** |
| Shareholders' equity | 43,253,730 | 38,886,343 |
| **Gearing ratio** | 142% | 158% |

## 29 OPERATING LEASES

The Group leases a number of land plots owned by local governments under operating leases. In addition, the Group leases non-residential premises and vehicles.

Land leases were entered in prior periods and represented land plots on which power lines, equipment for electricity transformation and other assets are located. The land leases typically run for an initial period of 1 to 49 years, with an option to renew the lease after that date. Lease payments are reviewed regularly to reflect market rentals.

The land title does not pass and the landlord retains control over land usage. The Group determined that substantially all the risks and rewards of the land plots are with the landlord, therefore the leases are considered as operating leases.

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

| | **31 December 2016** | **31 December 2015** |
|---|---|---|
| Less than one year | 519,922 | 535,471 |
| Between one year and five years | 1,406,331 | 663,997 |
| More than five years | 3,000,333 | 4,320,503 |
| | **4,926,586** | **5,519,971** |

The amount of lease expense under operating leases recognised in profit or loss in 2016 was RUB 565,576 thousand (in 2015: RUB 549,588 thousand).

## 30 COMMITMENTS

The Group has outstanding commitments under the contracts for the purchase and construction of the items of property, plant and equipment for RUB 4,766,748 thousand as at 31 December 2016 (as at 31 December 2015: RUB 6,462,396 thousand).

## 31 CONTINGENCIES

### (a) Insurance

The insurance industry in the Russian Federation is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group has reliable insurance coverage for its property: industrial buildings, structures and premises, air and cable transmission lines, energy (power) machines and others. In addition, insurance covers risks that could lead to losses in the event of damage to third parties (health, property) arising from operation of dangerous production units. The Group has no insurance coverage against losses caused by business interruption.

## 31 CONTINGENCIES (CONTINUED)

### (b) Litigation

The Group is a party to certain legal proceedings arising in the ordinary course of business. Management does not believe than these matters will have a material adverse effect on the Group's financial position and operating results. Changes in litigation provisions are presented in Note 26.

### (c) Taxation contingencies

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

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

### (d) Environmental matters

The Company and its predecessors have operated in the electric transmission industry in the Russian Federation for many years. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement posture of Government authorities is continually being reconsidered. Management periodically evaluates its obligations under environmental regulations.

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

### (e) Other contingencies

The Group believes that the electricity services provided are in compliance with the Russian legislation regulating electric power transmission. Other contingencies to disclose as at 31 December 2016 and 31 December 2015 are absent.

### (f) Guarantees

As at 31 December 2016, the Group has no issued financial guarantees for loans and borrowings.

## 32 RELATED PARTY TRANSACTIONS

### (a) Control relationships

The Company's parent as at 31 December 2016 and 31 December 2015 was PJSC "Russian Grids". The party with the ultimate control over the Company is the Government of the Russian Federation, which held the majority of the voting rights of PJSC "Russian Grids". The economic, social and other policies of the Government of the Russian Federation could have a significant impact on the Group's activities.

*Thousands of Russian Roubles, unless otherwise stated*

## 32 RELATED PARTY TRANSACTIONS (CONTINUED)

### (b) Transactions with parent company and entities under control of parent company

| | Transaction value for the year ended 31 December | | Balance as at 31 December | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| **Sale of goods and services:** | **22,804** | **313,050** | **21,567** | **55,745** |
| Fellow subsidiaries | 22,804 | 313,050 | 21,567 | 55,745 |
| **Purchase of goods and services:** | **16,675,567** | **17,368,367** | **1,232,264** | **2,144,793** |
| Parent company | 384,647 | 384,647 | 22,617 | 22,617 |
| Fellow subsidiaries | 16,290,920 | 16,983,720 | 1,209,647 | 2,122,176 |
| **Advances given:** | **-** | **-** | **30,335** | **33,881** |
| Fellow subsidiaries | - | - | 30,335 | 33,881 |
| **Advances received:** | **-** | **-** | **173,440** | **167,040** |
| Fellow subsidiaries | - | - | 173,440 | 167,040 |

### (c) Management compensation

There are no transactions or balances with key management and their close family members except for remuneration in the form of salary and bonuses.

Total remuneration to key management, Board of Directors and Management Board members for the reporting year, included into personnel costs (Note 9) was:

| | Year ended 31 December 2016 | Year ended 31 December 2015 |
|---|---|---|
| Salary and bonuses (including contributions to state insurance funds) | 259,684 | 258,442 |
| Pensions and post-employment benefits | 508 | 397 |

The amount of commitments to key management personnel included in employee benefit obligations (Note 25) was as follows:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Present value of defined benefit and defined contribution plans, as well as other payments for post-employment benefits | 4,541 | 3,994 |

### (d) Transactions with government-related entities

The Group applies the exemption in IAS 24 Related party disclosures that allows to present reduced related party disclosures regarding transactions with government-related entities.

In the course of business, the Group makes a significant number of transactions with companies that are government-related. These operations are carried out under the regulated tariffs, or in accordance with market prices.

Revenue from government-related entities accounts for 23% of the Group's total revenue for the year ended 31 December 2016, (for the year ended 31 December 2015: 20%) including 23% of the proceeds from the transmission of electricity (for the year ended 31 December 2015: 21%).

*Thousands of Russian Roubles, unless otherwise stated*

## 32 RELATED PARTY TRANSACTIONS (CONTINUED)

Costs of electricity transmission for government-related entities account for 76% of the total cost of the electricity transmission for the year ended 31 December 2016 (for the year ended 31 December 2015: 44%).

Interest income for government-related entities account for 82% of the total interest income for the year ended 31 December 2016 (for the year ended 31 December 2015: 90%).

Interest expense for government-related entities account for 55% of the total interest expenses for the year ended 31 December 2016 (for the year ended 31 December 2015: 59%).

During 2015, the Group made three issues of non-convertible documentary interest - bearing bonds with a total nominal value of RUB 15,000,000 thousand with a nominal interest rate of 11.58-12.42% per annum. The maturity of the bonds is 3-7 years. Two issues of the interest - bearing bonds with a total nominal value of RUB 10,000,000 thousand with a nominal interest rate of 11.58-12.42% per annum have been fully purchased by PJSC "Russian Grids". During 2016, the Group made the issue of non-convertible documentary interest - bearing bonds with a nominal value of RUB 5,000,000 thousand with a nominal interest rate of 9.32% per annum. The maturity of the bonds is 10 years. The issue of the interest - bearing bonds have been purchased by PJSC "Russian Grids".

### (e) Loans and borrowings received from government-related entities

| | Addition of loans and borrowings | The balance of transactions | Addition of loans and borrowings | The balance of transactions |
|---|---|---|---|---|
| | 2016 | 31 December 2016 | 2015 | 31 December 2015 |
| Loans and borrowings received | 12,203,276 | 22,956,185 | 5,792,342 | 23,467,055 |
| | **12,203,276** | **22,956,185** | **5,792,342** | **23,467,055** |

Loans and borrowings are drawn at the market interest rate (Note 28).

Other disclosures related to transactions with government-related entities, are provided in Notes 17 and 28(c).

### (f) Pricing policy

Transactions with related parties for the transmission of electricity are carried out at the tariffs set by the state.

## 33 EVENTS AFTER THE REPORTING PERIOD

Events after the balance sheet date, which should be reflected in the consolidated financial statements for the reporting period, have not been identified.