

**JOINT STOCK COMPANY  
“DOROGOBUZH”**

**INTERNATIONAL FINANCIAL REPORTING STANDARDS  
CONSOLIDATED FINANCIAL STATEMENTS AND  
AUDITOR’S REPORT**

**31 DECEMBER 2007**

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## INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of Joint Stock Company "Dorogobuzh"

- 1 We have audited the accompanying consolidated financial statements of Joint Stock Company "Dorogobuzh" and its subsidiaries (the "Group") which comprise the consolidated balance sheet as at 31 December 2007 and the consolidated income statement, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory notes.

### **Management's Responsibility for the Financial Statements**

- 2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### **Auditor's Responsibility**

- 3 Our responsibility is to express an opinion on these consolidated financial statements based on our audit. Except as discussed below, we conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
- 4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- 5 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

- 6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group at 31 December 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.




Moscow, Russian Federation  
28 July 2008

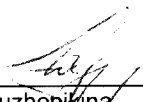
**Joint Stock Company "Dorogobuzh"**  
**Consolidated Balance Sheet at 31 December 2007**  
*(in thousands of Russian Roubles)*



	Note	2007	2006
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	13	3,355,216	3,085,532
Goodwill	14	52,068	52,068
Other non-current assets		163,389	216,551
Available-for-sale investments	15	5,266,912	2,790,118
Long-term loans receivable	11	55,000	5,500
<b>Total non-current assets</b>		<b>8,892,585</b>	<b>6,149,769</b>
<b>Current assets</b>			
Inventories	12	868,889	610,582
Other current assets		21,560	50,530
Short-term loans receivable	11	130,000	247,500
Accounts receivable	10	1,011,305	978,558
Dividends receivable		47,925	41,816
Cash and cash equivalents	9	350,760	458,855
<b>Total current assets</b>		<b>2,430,439</b>	<b>2,387,841</b>
<b>TOTAL ASSETS</b>		<b>11,323,024</b>	<b>8,537,610</b>
<b>EQUITY</b>			
Share capital	19	1,735,359	1,735,359
Share premium	19	93,794	93,794
Retained earnings		2,220,311	860,320
Revaluation reserve		3,970,103	2,092,624
<b>Share capital and reserves attributable to the Company's equity holders</b>		<b>8,019,567</b>	<b>4,782,097</b>
Minority interest		2,819	-
<b>TOTAL EQUITY</b>		<b>8,022,386</b>	<b>4,782,097</b>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Long-term borrowings	18	76,429	1,343,617
Other long-term liabilities		45,112	44,805
Deferred tax liability	23	1,479,120	902,113
<b>Total non-current liabilities</b>		<b>1,600,661</b>	<b>2,290,535</b>
<b>Current liabilities</b>			
Accounts payable	16	286,859	411,083
Current income tax payable		30,338	9,928
Other taxes payable	17	130,335	72,954
Short-term borrowings	18	932,480	600,000
Advances received	16	319,965	371,013
<b>Total current liabilities</b>		<b>1,699,977</b>	<b>1,464,978</b>
<b>TOTAL LIABILITIES</b>		<b>3,300,638</b>	<b>3,755,513</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>11,323,024</b>	<b>8,537,610</b>

Approved for issue and signed on behalf of the Board of Directors on 28 July 2008.

  
 I.N. Antonov  
 President

  
 N. I. Sluzhenikina  
 Chief Accountant

**Joint Stock Company "Dorogobuzh"**  
**Consolidated Income Statement for the year ended 31 December 2007**  
*(in thousands of Russian Roubles, except for per share amounts)*



	Note	2007	2006
Revenue	7	7,664,633	5,572,353
Cost of sales	20	(4,658,821)	(3,782,330)
<b>Gross profit</b>		<b>3,005,812</b>	<b>1,790,023</b>
Transportation services		(524,660)	(387,152)
Selling, general and administrative expenses	21	(644,671)	(703,151)
Loss on disposal of property, plant and equipment, net		(11,873)	(50,906)
Other operating expenses		(100,541)	(66,025)
<b>Operating profit</b>		<b>1,724,067</b>	<b>582,789</b>
Finance income	22	189,643	107,368
Interest expense		(117,502)	(128,706)
<b>Profit before taxation</b>		<b>1,796,208</b>	<b>561,451</b>
Income tax expense	23	(433,398)	(178,832)
<b>Net profit for the year</b>		<b>1,362,810</b>	<b>382,619</b>
<b>Net profit is attributable to:</b>			
Equity holders of the Company		1,359,991	382,619
Minority interest		2,819	-
<b>Net profit for the year</b>		<b>1,362,810</b>	<b>382,619</b>
Earnings per ordinary share for profit for the year attributable to the equity holders of the Company, basic and diluted (expressed in RR per share)	24	1.55	0.43
Earnings per preference share for profit for the year attributable to the equity holders of the Company, basic and diluted (expressed in RR per share)	24	1.55	0.47



	Note	2007	2006
<b>Cash flows from operating activities</b>			
Profit before taxation		1,796,208	561,451
<i>Adjustments for:</i>			
Depreciation and amortization	13	248,442	186,348
Reversal of impairment of accounts receivable		(46,435)	(5,894)
Decrease)/Increase in provision for write-down on inventory		(757)	2,614
Loss on disposal of property, plant and equipment		59,178	50,906
Interest expense		96,650	117,837
Interest income		(19,746)	(12,015)
Dividend income		(149,045)	(84,484)
Foreign exchange effect on non-operating balances		42,924	(25,089)
<b>Operating cash flows before working capital changes</b>		<b>2,027,419</b>	<b>791,674</b>
Decrease/(Increase) in gross trade receivables		315,345	(212,065)
Increase in advances to suppliers		(213,782)	(82,080)
Increase in other receivables		(93,984)	(30,510)
Increase in inventories		(204,387)	(71,052)
Increase / (decrease) in trade payables		(11,627)	78,378
Increase / (decrease) in advances from customers		(51,048)	103,558
Increase in other payables		12,038	51,869
(Decrease)/Increase in other current assets		28,969	(29,297)
Net change in other non-current assets and liabilities		307	(14,355)
<b>Cash provided from operations:</b>		<b>1,809,250</b>	<b>586,120</b>
Income taxes paid		(395,559)	(204,232)
Interest paid		(115,915)	(126,729)
<b>Net cash generated from operating activities:</b>		<b>1,297,776</b>	<b>255,159</b>
<b>Cash flows from investing activities:</b>			
Purchase of property, plant and equipment		(577,304)	(795,409)
Acquisition of subsidiary	26	(131,683)	-
Loans provided	11	(620,000)	(252,500)
Proceeds from loans repaid	11	688,000	82,000
Purchase of available-for-sale investments		(10,177)	-
Proceeds from sale of available-for-sale investments		3,750	-
Interest received		19,746	12,015
Dividends received		149,045	68,370
Proceeds from sale of property, plant and equipment		45,972	-
<b>Net cash used in investing activities:</b>		<b>(432,651)</b>	<b>(885,524)</b>
<b>Cash flows from financing activities:</b>			
Dividends paid		(80)	(221,524)
Proceeds from borrowings		616,080	1,486,877
Repayment of borrowings		(1,589,220)	(523,165)
<b>Net cash provided from (used in) financing activities</b>		<b>(973,220)</b>	<b>742,188</b>
<b>Net decrease in cash and cash equivalents</b>		<b>(108,095)</b>	<b>111,823</b>
<b>Cash and cash equivalents at the beginning of the year</b>	9	<b>458,855</b>	<b>347,032</b>
<b>Cash and cash equivalents at the end of the year</b>	9	<b>350,760</b>	<b>458,855</b>



Capital and reserves attributable to the Company's equity holders						
	Share capital (Note 19)	Share premium	Retained earnings	Revaluation reserve	Minority interest	Total equity
<b>Balance at 1 January 2006</b>	<b>1,735,359</b>	<b>93,794</b>	<b>623,942</b>	<b>1,910,257</b>	<b>-</b>	<b>4,363,352</b>
Fair value gains on available-for-sale investments (Note 15)	-	-	-	239,956	-	239,956
Income tax recorded in equity (Note 23)	-	-	-	(57,589)	-	(57,589)
Net income recognised directly in equity	-	-	-	182,367	-	182,367
Profit for the year	-	-	382,619	-	-	382,619
Total recognised income for 2006	-	-	382,619	182,367	-	564,986
Dividends	-	-	(146,241)	-	-	(146,241)
<b>Balance at 31 December 2006</b>	<b>1,735,359</b>	<b>93,794</b>	<b>860,320</b>	<b>2,092,624</b>	<b>-</b>	<b>4,782,097</b>
<b>Balance at 1 January 2007</b>	<b>1,735,359</b>	<b>93,794</b>	<b>860,320</b>	<b>2,092,624</b>	<b>-</b>	<b>4,782,097</b>
Fair value gains on available-for-sale investments (Note 15)	-	-	-	2,470,367	-	2,470,367
Income tax recorded in equity (Note 23)	-	-	-	(592,888)	-	(592,888)
Net income recognised directly in equity	-	-	-	1,877,479	-	1,877,479
Profit for the year	-	-	1,359,991	-	2,819	1,362,810
Total recognised income for 2007	-	-	1,359,991	1,877,479	2,819	3,240,289
Dividends	-	-	-	-	-	-
<b>Balance at 31 December 2007</b>	<b>1,735,359</b>	<b>93,794</b>	<b>2,220,331</b>	<b>3,970,103</b>	<b>2,819</b>	<b>8,022,386</b>

The accompanying notes on pages 7 to 37 are an integral part of the consolidated financial statements.



## 1 Dorogobuzh Group and Its Operations

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2007 for Joint Stock Company "Dorogobuzh" (the "Company" or "Dorogobuzh") and its subsidiaries (together referred to as the "Group" or "Dorogobuzh Group").

The Group's principal activities include the manufacture, distribution and sales of chemical fertilisers and related by-products. The Group's manufacturing facilities are primarily based in the Smolenskaya oblast of Russia. Dorogobuzh was incorporated as a joint stock company on 27 July 1994. On that date the majority of assets and liabilities previously managed by the state were transferred to the Company. The transfer of assets and liabilities was made in accordance with Decree No. 721 on the privatisation of state companies approved on 1 July 1992.

The Group's parent company is JSC "Acron" (Russian Federation). The Group's ultimate parent is Subero Associates Inc (British Virgin Islands) (2006: Subero Associates Inc). As at 31 December 2007 and 2006 the Group was ultimately controlled by Mr. Viatcheslav Kantor.

The Company's registered office is Verkhnedneprovsky, Smolenskaya oblast, 215753, Russia.

## 2 Basis of Preparation of the Financial Statements

**Basis of preparation.** These consolidated financial statements have been prepared in accordance with, and comply with, International Financial Reporting Standards ("IFRS") under the historical cost convention except as modified by the fair value revaluation of available-for-sale investments. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated (refer to Note 5, Adoption of New or Revised Standards and Interpretations).

**Presentation currency.** All amounts in these financial statements are presented in thousands of Russian Roubles ("RR thousands"), unless otherwise stated. The financial statements are based on the statutory records, with adjustments and reclassifications recorded for the purpose of fair presentation in accordance with IFRS.

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

## 3 Summary of Significant Accounting Policies

### 3.1 Group accounting

**Consolidated financial statements.** Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain economic benefits. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.





### 3 Summary of Significant Accounting Policies (continued)

#### 3.1 Group accounting (continued)

The excess of the cost of acquisition over the fair value of the net assets of the acquiree at each exchange transaction represents goodwill. The excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is recognised immediately in profit or loss. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

Minority interest is that part of the net results and of the net assets of a subsidiary, including the fair value adjustments, which is attributable to interests which are not owned, directly or indirectly, by the Company. Minority interest forms a separate component of the Group's equity.

**Purchases of minority interests.** Difference, if any, between the carrying amount of a minority interest and the amount paid to acquire it is recorded as goodwill.

**Pooling of interest.** Purchases of subsidiaries as the result of business combinations under common control are accounted for using the pooling of interest method. Under this method the financial statements of the combined entity are presented as if the businesses had been combined from the beginning of the earliest period presented. The assets and liabilities of the subsidiary transferred under common control are at the predecessor entity's carrying amounts. Related goodwill inherent in the predecessor entity's original acquisitions is also recorded in these financial statements. Any difference between the carrying amount of net assets, including the predecessor entity's goodwill, and the consideration paid is accounted for in these consolidated financial statements as an adjustment to equity.

**Investments in associates.** Associates are entities over which the Group has significant influence, but not control, generally accompanying a shareholding of between 20 and 50 percent of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group's share of the post-acquisition profits or losses of associates is recorded in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. When the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

#### 3.2 Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method. Bank overdrafts are shown within borrowings in the current liabilities on the balance sheet. Restricted balances are excluded from cash and cash equivalents for the purposes of the cashflow statement. Balances restricted from being exchanged or used to settle a liability for at least twelve months after the balance sheet date are included in other non-current assets.

#### 3.3 Trade and other receivables

Trade and other receivables are carried at amortised cost using the effective interest method. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of estimated future cash flows, discounted at the original effective rate of interest. The amount of the provision is recognised in the income statement. The primary factors that the Group considers whether a receivable is impaired is its overdue status. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:



### 3 Summary of Significant Accounting Policies (continued)

#### 3.3 Trade and other receivables (continued)

- Any portion of the receivable is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- The counterparty experiences a significant financial difficulty as evidenced by its financial information that the Group obtains;
- The counterparty considers bankruptcy or a financial reorganisation;
- There is adverse change in the payment status of the counterparty as a result of changes in the national or local economic conditions that impact the counterparty.

#### 3.4 Value added tax

Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognised in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, an impairment loss is recorded for the gross amount of the debtor, including VAT.

#### 3.5 Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overhead (based on normal operating capacity) but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

#### 3.6 Property, plant and equipment

Property, plant and equipment are recorded at cost, restated where applicable to the equivalent purchasing power of the Russian Rouble at 31 December 2002 for assets acquired prior to 1 January 2003, less accumulated depreciation and provision for impairment, where required.

At each reporting date the management assess whether there is any indication of impairment of property, plant and equipment. If any such indication exists, the management estimates the recoverable amount, which is determined as the higher of an asset's fair value less cost to sell and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the income statement. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the assets recoverable amount. Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in the profit or loss.

Land is not depreciated. Depreciation is calculated to allocate cost of property, plant and equipment to their residual values on a straight-line basis. The depreciation periods, which approximate the estimated useful economic lives of the respective assets, are as follows:

	<u>Number of years</u>
Buildings	40 to 50
Plant and machinery	10 to 20
Other equipment and motor vehicles	5 to 20

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.



### 3 Summary of Significant Accounting Policies (continued)

#### 3.6 Property, plant and equipment (continued)

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised and the assets replaced are retired. Gains and losses arising from the retirement or disposal of property, plant and equipment are included in the statement of income as incurred.

Borrowing costs on specific or general funds borrowed to finance the construction of qualifying asset are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

#### 3.7 Intangible assets

**Goodwill.** Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the net identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of exchange.

Goodwill on acquisitions of subsidiaries is presented separately in the consolidated balance sheet. Goodwill on acquisitions of associates is included in the investment in associates. Goodwill is carried at cost less accumulated impairment losses, if any.

The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired. Goodwill is allocated to the acquirer's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or group of units represent the lowest level at which the Group monitors goodwill and are not larger than a segment. Gains or losses on disposal of an operation within a cash generating unit to which goodwill has been allocated include the carrying amount of goodwill associated with the operation disposed of, generally measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit which is retained.

**Research and development.** Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technological feasibility, and costs can be measured reliably. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs with a finite useful life that have been capitalised are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of its expected benefit, on average over a period not exceeding 5 years.

**Other intangible assets.** All of the Group's other intangible assets have definite useful lives and primarily include capitalised computer software, patents, trademarks and licences. Acquired computer software licenses, patents and trademarks are capitalised on the basis of the costs incurred to acquire and bring them to use. Intangible assets are amortised using the straight-line method over their useful lives, but not exceeding 20 years.

#### 3.8 Borrowings

Borrowings are stated at amortised cost using the effective yield method; any difference between fair value of the proceeds (net of transaction costs) and the redemption amount is recognised as interest expense over the period of the borrowings. Borrowing costs on specific or general funds borrowed to finance the construction of qualifying asset are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

#### 3.9 Income taxes

Income taxes have been provided for in the consolidated financial statements in accordance with Russian legislation enacted or substantively enacted by the balance sheet date. The income tax charge/credit comprises current tax and deferred tax and is recognised in the consolidated income statement unless it relates to transactions that are recognised, in the same or a different period, directly in equity. Corporate profit tax rate is 24% (2006:24%) for Russia.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes, other than on income, are recorded within operating expenses.



### 3 Summary of Significant Accounting Policies (continued)

#### 3.9 Income taxes (continued)

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax liabilities are not recorded for temporary differences on initial recognition of goodwill and subsequently for goodwill which is not deductible for tax purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Deferred income tax is provided on post acquisition retained earnings of subsidiaries, except where the Group controls the subsidiary's dividend policy and it is probable that the difference will not reverse through dividends or otherwise in the foreseeable future.

#### 3.10 Foreign currency transactions

**Foreign currency translation.** Functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The Group's functional currency is the national currency of the Russian Federation, Russian Roubles ("RR").

For the Company and its subsidiaries monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the Central Bank at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into each entity's functional currency at year-end official exchange rates of the Central Bank are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

At 31 December 2007 the principal rate of exchange used for translating foreign currency balances was US\$ 1 = 24.5462 RR, EUR 1 = 35.9332 RR (2006: US\$ 1 = RR 26.3311, EUR 1 = 34.6965 RR). Exchange restrictions and controls exist relating to converting Russian Roubles into other currencies.

#### 3.11 Provisions for liabilities and charges

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Provisions are evaluated and re-estimated annually, and are included in the financial statements at their expected net present values using discount rates appropriate to the Company or its subsidiaries in applicable economic environment at each balance sheet date.

**Uncertain tax positions.** The Group's uncertain tax positions are reassessed by management at every balance sheet date. Liabilities are recorded for income tax positions that are determined by management as less likely than not to be sustained if challenged by tax authorities, based on the interpretation of tax laws that have been enacted or substantively enacted by the balance sheet date. Liabilities for penalties, interest and taxes other than on income are recognised based on management's best estimate of the expenditure required to settle the obligations at the balance sheet date.

#### 3.12 Shareholders' equity

**Share capital.** Ordinary and non-cumulative no redeemable preference shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction in equity from the proceeds, net of tax. Any excess of the fair value of consideration received over the par value of shares issued is recognised as a share premium.



### 3 Summary of Significant Accounting Policies (continued)

#### 3.12 Shareholders' equity (continued)

**Treasury shares.** Where any Group company purchases the Company's equity share capital, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

**Dividends.** Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

#### 3.13 Revenue recognition

Revenues from sales of chemical fertilisers and related by-products are recognised at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. If the Group agrees to transport goods to a specified location, revenue is recognised when the goods are passed to the customer at the destination point.

Sales of services are recognised in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. Sales are shown net of VAT, custom duties and discounts, and after eliminating sales within the Group. Revenues are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

#### 3.14 Mutual cancellations

A portion of sales and purchases are settled by mutual settlements or non-cash settlements. These transactions are generally in the form of direct settlements through cancellation of mutual trade receivables and payables balances within the operational contracts. Non-cash settlements include promissory notes or bills of exchange, which are negotiable debt obligations. Sales and purchases that are expected to be settled by mutual settlements or other non-cash settlements are recognised based on the estimate of the fair value to be received or given up in non-cash settlements. The fair value is determined with reference to various market information. Non-cash transactions have been excluded from the cash flow statement, so investing activities, financing activities and the total of operating activities represent actual cash transactions.

The Group also accepts bills of exchange from its customers (both issued by customers and third parties) as a settlement of receivables. A provision for impairment of bills of exchange is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

#### 3.15 Employee benefits

Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits (such as health services and kindergarten services) are accrued in the year in which the associated services are rendered by the employees of the Group and are included within labour costs in operating expenses.

**Social costs.** The Group incurs significant costs on social activities. These costs include the provision of health services, kindergartens, and the subsidy of worker holidays. These amounts represent an implicit cost of employing principally production workers and other staff and, accordingly, have been charged to operating expenses.

**Pension costs.** In the normal course of business the Group contributes to state pension schemes on behalf of its employees. Mandatory contributions to the governmental pension scheme are accrued in the year in which the associated services are rendered by the employees of the Group. The Group recognized contributions of RR 157,074 as part of labour costs in 2007 (2006: RR 150,865).



### 3 Summary of Significant Accounting Policies (continued)

#### 3.16 Financial assets and liabilities

**Classification of financial assets.** The Group classifies its financial assets into the following measurement categories: available-for-sale, held to maturity and loans and receivables.

Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Group intends to sell in the near term.

Held to maturity classification includes quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has both the intention and ability to hold to maturity. Management determines the classification of investment securities held to maturity at their initial recognition and reassesses the appropriateness of that classification at each balance sheet date.

**Initial recognition of financial instruments.** Financial assets and liabilities are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Group commits to deliver a financial asset. All other purchases and sales are recognised on the settlement date with the change in value between the commitment date and settlement date not recognised for assets carried at cost or amortised cost; and recognised in equity for assets classified as available for sale.

**Derecognition of financial assets.** The Group derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets have otherwise expired or (ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Group has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

**Available-for-sale investments.** Available-for-sale investments are carried at fair value. Interest income on available for sale debt securities is calculated using the effective interest method and recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Group's right to receive payment is established. All other elements of changes in the fair value are deferred in equity until the investment is derecognised or impaired at which time the cumulative gain or loss is removed from equity to profit or loss.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of available-for-sale investments. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through current period's profit or loss.

**Held to maturity investments.** Held to maturity investments are carried at amortised costs using the effective interest method, net of a provision for incurred impairment losses.

#### 3.17 Earnings per share

An earnings per share is determined by dividing the net profit attributable to shareholders by the weighted average number of shares outstanding during the reporting year. Preference shares are not redeemable and are considered to be participating shares. Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the period. Preference shares participate in the calculation because dividends attributable to preference shares cannot be less than dividends on ordinary shares.



### 3 Summary of Significant Accounting Policies (continued)

#### 3.18 Reclassifications

Certain amounts in previously issued financial statements have been reclassified to conform to the current year presentation (Note 7).

### 4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

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

**Estimated impairment of goodwill.** The Group tests goodwill for impairment at least annually. The recoverable amounts of cash-generating units have been determined based on the higher of the fair value less cost to sale or value-in-use calculations. These calculations require the use of estimates as further detailed in Note 14. At 31 December 2007 no impairment of goodwill was required, and none would be required even if the budgeted sales growth rate used in the value-in-use calculations for any CGU had been 5% lower than management estimates at 31 December 2007. If the estimated pre-tax discount rate applied to the discounted cash flows for any CGU had been 1% higher than management estimates, the goodwill would still have not been impaired.

**Impairment of available-for-sale equity investments.** The Group determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. The determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates, among other factors, the volatility in the share price. In addition, impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, in industry and sector performance, or in operating or financing cash flows, or when there are significant adverse consequences of changes in technology.

**Tax legislation.** Russian tax, currency and customs legislation is subject to varying interpretations. Refer to Note 23.

**Related party transactions.** In the normal course of business the Group enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analyses. Refer to Note 8.

**Useful lives of property, plants and equipment.** The estimation of the useful lives of items of property, plant and equipment is a matter of judgement based on the experience with similar assets. The future economic benefits embodied in the assets are consumed principally through use. However, other factors, such as technical or commercial obsolescence and wear and tear, often result in the diminution of the economic benefits embodied in the assets. Management assesses the remaining useful lives in accordance with the current technical conditions of the assets and estimated period during which the assets are expected to earn benefits for the Group. The following primary factors are considered: (a) expected usage of the assets; (b) expected physical wear and tear, which depends on operational factors and maintenance programme; and (c) technical or commercial obsolescence arising from changes in market conditions. The impact on depreciation for the period would be to increase it by RR 4,071 or decrease it by RR 3,974 were the estimated useful lives to differ by 10% from management's estimates.

**Valuation of available-for-sale investments.** As of 31 December 2006 the investments in JSC Acron had no active market in line with requirements of IAS 39. For these investments, fair value was estimated by using valuation techniques based on application guidance of IAS 39 (revised). As of 31 December 2007 the Group concluded that the investments in JSC Acron were traded in active market in line with requirements of IAS 39, and fair value was determined by reference to the current market value at the close of business on 31 December 2007. Although the free float and volume of trades of investments may be not significant, their quoted prices are readily and regularly available from exchange, and those prices represent actual and regularly occurring market transactions on an arm's length basis. Refer to Note 15.



## 5 Adoption of New or Revised Standards and Interpretations

Certain new IFRSs became effective for the Group from 1 January 2007. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Group's operations and the nature of their impact on the Group's accounting policies. All changes in accounting policies were applied retrospectively with adjustments made to retained earnings at 1 January 2006, unless otherwise described below.

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

**Other new standards or interpretations.** The Group has adopted the following interpretations which became effective from 1 January 2007:

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

These interpretations did not have a significant impact on these consolidated financial statements.

## 6 New Accounting Pronouncements

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

**IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009).** The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information.

**IAS 23, Borrowing Costs (revised March 2007; effective for annual periods beginning on or after 1 January 2009).** The revised IAS 23 was issued on March 2007. The main change in IAS 23 is the removal of the option of immediately recognizing as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. The revised standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009. The Group expects the revised IAS 23 has no impact on the financial statements as the Group's accounting policies historically complied with it.

**IAS 1, Presentation of Financial Statements (revised September 2007; effective for annual periods beginning on or after 1 January 2009).** The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances.





## 6 New Accounting Pronouncements (continued)

**IAS 27, Consolidated and Separate Financial Statements (revised January 2008; effective for annual periods beginning on or after 1 July 2009).** The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

**IFRS 3, Business Combinations (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009).** The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or on the same basis as US GAAP (at fair value). The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, goodwill will be measured as the difference at acquisition date between the fair value of any investment in the business held before the acquisition, the consideration transferred and the net assets acquired. Acquisition-related costs will be accounted for separately from the business combination and therefore recognised as expenses rather than included in goodwill. An acquirer will have to recognise at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

**Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment (issued in January 2008; effective for annual periods beginning on or after 1 January 2009).** The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. Amendment to IFRS 2, *Share-based Payment* is not currently applicable to the Group as it has no such payments.

**IFRIC 13, Customer Loyalty Programmes (issued in June 2007; effective for annual periods beginning on or after 1 July 2008).** IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. IFRIC 13 is not applicable to the Group as the Group companies do not currently operate any loyalty programmes.

**Improvements to International Financial Reporting Standards (issued in May 2008, effective for annual periods beginning on or after 1 January 2009).** In 2007, the International Accounting Standards Board decided to initiate an annual improvements project as a method of making necessary, but non-urgent, amendments to IFRS. The amendments issued in May 2008 consist of a mixture of substantive changes, clarifications, and changes in terminology in various standards. The substantive changes relate to the following areas: classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary; possibility of presentation of financial instruments held for trading as non-current under IAS 1; accounting for sale of IAS 16 assets which were previously held for rental and classification of the related cash flows under IAS 7 as cash flows from operating activities; clarification of definition of a curtailment under IAS 19; accounting for below market interest rate government loans in accordance with IAS 20; making the definition of borrowing costs in IAS 23 consistent with the effective interest method; clarification of accounting for subsidiaries held for sale under IAS 27 and IFRS 5; reduction in the disclosure requirements relating to associates and joint ventures under IAS 28 and IAS 31; enhancement of disclosures required by IAS 36; clarification of accounting for advertising costs under IAS 38; amending the definition of the fair value through profit or loss category to be consistent with hedge accounting under IAS 39; introduction of accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting. Most of the amendments are effective annual periods beginning on or after 1 January 2009. The Group is currently assessing what impact the amendments will have on its consolidated financial statements.



## 6 New Accounting Pronouncements (continued)

**Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate – IFRS 1 and IAS 27 Amendment (revised May 2008; effective for annual periods beginning on or after 1 January 2009).** The amendment allows first-time adopters of IFRS to measure investments in subsidiaries, jointly controlled entities or associates at fair value or at previous GAAP carrying value as deemed cost in the separate financial statements. The amendment also requires distributions from pre-acquisition net assets of investees to be recognised in profit or loss rather than as a recovery of the investment. The amendments will not have an impact on the Group's consolidated financial statements.

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

- IFRIC 11, IFRS 2 – *Group and Treasury Share Transactions* (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12, *Service Concession Arrangements* (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 14, IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective for annual periods beginning on or after 1 January 2008).
- IFRIC 15, IAS 11, IAS 18 – *Agreements for the Construction of Real Estate* (effective for annual periods beginning on or after 1 January 2009);
- IFRIC 16, IAS 39 – *Hedges of a Net Investment in a Foreign Operation* (effective for annual periods beginning on or after 1 October 2008).

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

## 7 Segment Information

The Group has one primary reportable segment, which is manufacturing and sale of chemical fertilizers which have similar risks and rewards. The Group evaluates performance and makes investment and strategic decisions based upon review of profitability for the Group as a whole.

Its secondary reporting format is determined to be the geographical segments: Russia and other countries.

In 2007 the Group's management changed the presentation of reportable geographical segments, to more appropriately report distinguishable components of an entity that are engaged in providing products or services within a particular economic environment and that are subject to risks and returns that are different from those of components operating in other economic environments. Sales in other countries represent export sales of Group's entities located in the Russian Federation including sales to CIS countries (previously reported within "Russia and CIS countries" in the amount of RR 885,066).

Sales are based on the geographical area in which the customer is located. There are no sales or other transactions between the segments. Production and assets of the Group are located in the Russian Federation.

	2007	2006
<u>Revenue</u>		
Russia	3,667,219	2,693,350
Other countries	3,997,414	2,879,003
	<b>7,664,633</b>	<b>5,572,353</b>

The Group sells to two international trading entities that account for the majority of segment "Other countries". In 2007 AgroNitrogen Logistics Ltd. and NPChemical Trading Inc. purchased 22% and 16% of the sales of segment "Other countries" respectively (2006: 30% and 21%). The sales to them are included in the segment "Other countries" as risks and returns on them are similar to other overseas sales. The rest of sales in segment "Other countries" is widely spread between a number of less significant customers.



## 8 Balances and Transactions with Related Parties

Related parties are defined in IAS 24, *Related Party Disclosures*. Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Company's ultimate controlling party is disclosed in Note 1.

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

### i Balances with related parties

Balance sheet caption	Notes	Relationship	2007	2006
Trade receivables, gross	10	Parent company	3,322	5,542
		Parties under common control	60,801	140,714
Provision for impairment of trade receivables	10	Parties under common control	(19,807)	(60,378)
Prepayments, gross		Parties under common control	156,844	42,811
Provision for impairment of prepayments		Parties under common control	(5,068)	(1,000)
Dividends receivable		Parent company	47,925	41,816
Loans provided	11	Parties under common control	55,000	103,000
		Parent company	130,000	150,000
Loans received	18	Parent company	36,995	-
Trade payables	16	Parties under common control	8,912	5,618
		Parent company	52,296	13,904
Advances from customers		Party under common control	77	44,319

### ii Transactions with related parties

Income statement caption	Notes	Relationship	2007	2006
Sales of chemical fertilizers	7	Parent company	52,753	37,054
		Parties under common control	1,999,044	1,263,193
Income from participation in other companies		Parent company	151,238	83,579
Purchases of raw materials	20	Parent company	(125,642)	(50,463)
		Parties under common control	(10,961)	(21,090)
Purchase of transportation services		Parties under common control	(153,510)	(106,985)
Security services	21	Parties under common control	(64,112)	(65,882)
<b>Statement of changes in equity caption</b>				
Dividends accrued		Parent company	-	(69,049)
		Parties under common control	-	(32,309)

### iii Loans issued to related parties

At 31 December 2007 and 2006 short-term loans to parent company and parties under common control denominated in RR totalled RR 130,000 and RR 247,500, respectively, at interest rates in the range of 8.5% to 10.0%. The loans are unsecured.

At 31 December 2007 long-term loans to parties under common control totalled RR 55,000 (2006: RR 5,500), at interest rates of 8,5%. The loans are unsecured.

In 2007 the Group accrued interest income of RR 19,746 (2006: RR 12,015).

### iv Key management personnel compensation

Compensation of key management personnel consists of remunerations paid to the members of the Management Boards of the Group's main subsidiaries and to members of Boards of Directors of the Company and its main subsidiaries. Compensation is made up of an annual remuneration and a performance bonus depending on operating results.



## 8 Balances and Transactions with Related Parties (continued)

Total key management personnel compensation included in general and administrative expenses in the income statement for the year ended 31 December 2007 amounted to RR 82,098 (31 December 2006: RR 61,514).

Related state pension and social security costs for the year ended 31 December 2007 amounted to RR 2,414 (31 December 2006: RR 1,955).

## 9 Cash and Cash Equivalents

	2007	2006
Cash on hand and bank balances denominated in RR	284,735	180,088
Bank balances denominated in US\$	65,342	278,109
Bank balances denominated in Euro	683	658
<b>Total cash and cash equivalents</b>	<b>350,760</b>	<b>458,855</b>

The fair value of cash and cash equivalents are equal to their carrying amount. All bank balances and term deposits are neither past due nor impaired. Analysis of the credit quality of bank balances and term deposits is as follows:

	2007	2006
A to AAA* rated	10,268	116,915
BB- to BBB+* rated	340,474	341,922
Unrated	18	18
<b>Total</b>	<b>350,760</b>	<b>458,855</b>

\* Based on the credit ratings of independent rating agency Standard & Poor's.

## 10 Accounts Receivable

	2007	2006
Trade accounts receivable	138,301	453,646
Notes receivable	-	23,910
Less: impairment provision	(54,596)	(101,023)
<b>Total financial assets</b>	<b>83,705</b>	<b>376,533</b>
Advances to suppliers	546,746	332,964
Value-added tax recoverable	374,629	259,891
Income tax prepayments	10,992	13,637
Other taxes receivable	2,896	2,203
Less: impairment provision	(7,663)	(6,670)
<b>Total accounts receivable</b>	<b>1,011,305</b>	<b>978,558</b>

The fair value of accounts receivable does not differ significantly from their carrying amounts.

As of 31 December 2007, trade and other accounts receivable of RR 62,259 (2006: RR 107,693) were individually impaired and an impairment provision was recognized. The individually impaired receivables mainly relate to customers that are in unexpectedly difficult economic situations.

The ageing of these receivables is as follows:

	2007	2006
Less than 3 months	-	-
From 3 to 9 months	(2,736)	(6,797)
From 9 to 12 months	(5,460)	(6,395)
Over 12 months	(54,063)	(94,501)
<b>Total gross amount of impaired accounts receivable</b>	<b>(62,259)</b>	<b>(107,693)</b>



## 10 Accounts Receivable (continued)

The movements in the provision for impairment of financial accounts receivable are as follows:

	2007		2006	
	Trade receivables	Other debtors	Trade receivables	Other debtors
<b>Provision for impairment at 1 January</b>	<b>(101,023)</b>	<b>(6,670)</b>	<b>(110,320)</b>	<b>(8,540)</b>
Provision for impairment	(9,736)	(5,674)	(15,999)	(4,862)
Provision used	50,743	4,208	15,665	6,633
Provision reversed	5,420	473	9,631	99
<b>Provision for impairment at 31 December</b>	<b>(54,596)</b>	<b>(7,663)</b>	<b>(101,023)</b>	<b>(6,670)</b>

The maximum exposure to credit risk on the reporting date is the fair value of each class of receivable mentioned above. The Group does not hold any collateral as security.

The other classes within accounts receivable do not contain impaired assets.

Financial assets which are potentially subject to credit risk, consist principally of trade receivables.

As of 31 December 2007, trade receivables of RR 23,404 thousand (2006: RR 30,403) were past due but not impaired. The ageing analysis of these trade receivables from past due date is as follows:

	2007	2006
Less than 3 months	-	-
From 3 to 9 months	21,980	30,403
From 9 to 12 months	510	-
Over 12 months	914	-
<b>Trade accounts receivable past due not impaired</b>	<b>23,404</b>	<b>30,403</b>

Analysis by credit quality of trade and notes receivables is as follows:

	2007		2006	
	Trade receivables	Notes receivable	Trade receivables	Notes receivable
<i>Current and not impaired – exposure to:</i>				
- Notes receivable from top Russian banks		-		23,910
- Foreign traders and customers	11,033		247,509	
- Small individual Russian companies and farms	72,672		105,113	
<b>Total current and not impaired</b>	<b>83,705</b>	<b>-</b>	<b>352,623</b>	<b>23,910</b>

## 11 Loans Receivable

	2007	2006
<b>Short-term loans receivable</b>		
Loans issued to related parties (refer to Note 8)	-	97,500
Loans issued to parent company	130,000	150,000
	<b>130,000</b>	<b>247,500</b>
<b>Long-term loans receivable</b>		
Loans issued to related parties (refer to Note 8)	55,000	5,500
	<b>55,000</b>	<b>5,500</b>

Loans receivable contain neither impaired nor overdue assets as of 31 December 2007 and 31 December 2006. No provision for impairment was created for loans receivable as of the respective dates.

At 31 December 2007 and 2006 short-term loans totalled RR 130,000 and RR 247,500, respectively, at interest rates in the range of 8.5 % to 10.0% (2006: 8.5% to 10.5%). The loans were unsecured.



## 11 Loans Receivable (continued)

At 31 December 2007 and 2006 long-term loans totalled RR 55,000 and RR 5,500, respectively, at interest rate 8.5% (2006: 8.5%). The loans were unsecured.

In 2007 the Group accrued interest income of RR 19,746 (2006: RR 12,015).

## 12 Inventory

	2007	2006
Raw materials and spare parts	571,373	458,625
Work in progress	99,219	28,117
Finished products	198,317	123,840
	<b>868,889</b>	<b>610,582</b>

Raw materials are shown net of impairment provision of RR 39,123 (2006: 39,880). No inventory was pledged as security at 31 December 2007 and 2006.

## 13 Property, Plant and Equipment

Property, plant and equipment and related accumulated depreciation consist of the following:

	Buildings and constructions	Plant and equipment	Other	Assets under construction	Total
<b>Cost</b>					
<b>Balance at 1 January 2006</b>	<b>5,679,277</b>	<b>4,227,978</b>	<b>63,267</b>	<b>179,592</b>	<b>10,150,114</b>
Additions	-	-	-	797,239	797,239
Acquisitions through business combinations (Note 26)	53,078	26,097	-	405	79,580
Transfers	14,329	141,852	38,931	(195,112)	-
Disposals	(123,013)	(88,271)	(19,487)	-	(230,771)
<b>Balance at 31 December 2006</b>	<b>5,863,035</b>	<b>4,342,302</b>	<b>82,711</b>	<b>782,124</b>	<b>11,070,172</b>
<b>Accumulated Depreciation</b>					
Balance at 1 January 2006	3,580,757	4,073,783	41,751	-	7,696,291
Depreciation charge	103,790	65,700	16,858	-	186,348
Disposals	(69,002)	(86,965)	(16,042)	-	(172,009)
<b>Balance at 31 December 2006</b>	<b>3,854,909</b>	<b>4,087,164</b>	<b>42,567</b>	<b>-</b>	<b>7,984,640</b>
<b>Net Book Value</b>					
<b>Balance at 1 January 2006</b>	<b>2,098,520</b>	<b>154,195</b>	<b>21,516</b>	<b>179,592</b>	<b>2,453,823</b>
<b>Balance at 31 December 2006</b>	<b>2,008,126</b>	<b>255,138</b>	<b>40,144</b>	<b>782,124</b>	<b>3,085,532</b>



### 13 Property, Plant and Equipment (continued)

	Buildings and constructions	Plant and equipment	Other	Assets under construction	Total
<b>Cost</b>					
Balance at 1 January 2007	5,863,035	4,342,302	82,711	782,124	11,070,172
Additions	-	-	-	577,304	577,304
Transfers	59,135	251,171	54,977	(365,283)	-
Disposals	(121,959)	(88,263)	(13,118)	-	(223,340)
<b>Balance at 31 December 2007</b>	<b>5,800,211</b>	<b>4,505,210</b>	<b>124,570</b>	<b>994,145</b>	<b>11,424,136</b>
<b>Accumulated Depreciation</b>					
Balance at 1 January 2007	3,854,909	4,087,164	42,567	-	7,984,640
Depreciation charge	139,071	89,283	20,088	-	248,442
Disposals	(65,484)	(87,093)	(11,585)	-	(164,162)
<b>Balance at 31 December 2007</b>	<b>3,928,496</b>	<b>4,089,354</b>	<b>51,070</b>	<b>-</b>	<b>8,068,920</b>
<b>Net Book Value</b>					
Balance at 1 January 2007	2,008,126	255,138	40,144	782,124	3,085,532
<b>Balance at 31 December 2007</b>	<b>1,871,715</b>	<b>415,856</b>	<b>73,500</b>	<b>994,145</b>	<b>3,355,216</b>

The assets transferred to the Group upon privatisation did not include the land on which the Group's factories and buildings, comprising the Group's principal manufacturing facilities, are situated. As a result of changes in legislation in 2001, all companies located in the Russian Federation have been granted the option to purchase this land upon application to the state registration body or to continue occupying this land under a rental agreement. The purchase price of the land is calculated by reference to the cadastral value applied for property taxes and certain coefficients which are determined by local state authorities. This purchase price may significantly differ from its market value. In accordance with Russian legislation the expiry date for this option is the end of 2008. At 31 December 2007 major subsidiaries of the Group exercised the option and purchased the land under production plants.

At 31 December 2007, buildings, machinery and equipment with a net book value of RR 21,790 had been pledged as security for long-term loans (Note 18).

### 14 Goodwill

Movements in goodwill arising on the acquisition of new subsidiaries are:

	Note	2007	2006
Carrying amount at 1 January		52,068	-
Acquisition of subsidiary	27	-	52,068
<b>Carrying amount at 31 December</b>		<b>52,068</b>	<b>52,068</b>
Gross book value at 31 December		-	52,068
<b>Carrying amount at 31 December</b>		<b>52,068</b>	<b>52,068</b>



## 14 Goodwill (continued)

In December 2006 the Group acquired 100% of the share capital of LLC Andrex for a cash consideration of RR 131,683. The Group concluded that there are no separately identifiable intangible assets in the acquired company, which could qualify for separate accounting in accordance with IFRS 3, *Business Combinations*. The goodwill of RR 52,068 is primarily attributable to the profitability of the acquired business, cost of new market entry and the significant synergies and combined costs savings expected to arise due to unique geographical location of assets of the acquired company for the Group.

**Goodwill Impairment Test.** Goodwill is allocated to cash-generating units (CGUs) which represent the lowest level within the Group at which the goodwill is monitored by management and which are not larger than a segment as follows:

	2007	2006
LLC Andrex	52,068	52,068
<b>Total carrying amount of goodwill</b>	<b>52,068</b>	<b>52,068</b>

The recoverable amount of each CGU was determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a five year period. The growth rates do not exceed the long-term average growth rate for the business sector of the economy in which the CGU operates.

Based on the results of these calculations the Group concluded that no impairment charge was required.

The key assumptions used for value-in-use at 31 December 2007 are as follows:

	LLC Andrex
Growth rate beyond five years	0%
Discount rate	8%

Management determined budgeted gross margin based on past performance and its expectations of market development. The weighted average growth rates used are consistent with the forecasts included in industry reports. The discount rates used are pre-tax and reflect specific risks relating to the relevant segments.

## 15 Available-for-sale investments

	2007	2006
<b>Balance at 1 January</b>	<b>2,790,118</b>	<b>2,548,887</b>
Additions	50,000	17,901
Fair value gain recognized directly in equity	2,470,367	239,956
Disposals	(43,573)	(16,626)
<b>Balance at 31 December</b>	<b>5,266,912</b>	<b>2,790,118</b>

The Group has investments in the following companies:

Name	Activity	Country of registration	2007	2006
JSC Acron	Fertilizers manufacture	Russia	4,981,767	2,538,591
JSC Sberbank	Banking	Russia	254,405	227,213
Other			30,740	24,314
			<b>5,266,912</b>	<b>2,790,118</b>

Investments previously classified as at fair value through profit or loss were retrospectively designated by the Group as available-for-sale in line with requirements of IAS 39 (Amendment) "The Fair Value Option" effective from 1 January 2006. Respective fair value gains were recognized directly in equity. These investments comprise principally equity securities, which are listed on the Russian Trading System and Moscow International Currency Exchange. As of 31 December 2006 the investments in JSC Acron had no active market in line with requirements of IAS 39. For these investments, fair value was estimated by using valuation techniques based on application guidance of IAS 39 (revised). Applied multiples of enterprise value to sales and EBITDA were 1.3 and 4.96 for JSC Acron. Applied discounts for lack of control and lack of marketability were 15% and 35% respectively. For other investments traded in active markets, fair value was determined by reference to the current market value at the close of business on 31 December 2006.





## 15 Available-for-sale investments (continued)

As at 31 December 2007 the Group concluded that the investments in JSC Acron were traded in active market in line with the requirements of IAS 39, and fair value was determined by reference to the current market value at the close of business on 31 December 2007. The share price quoted by MICEX for JSC Acron amounted to 1,223.54 Roubles for 1 share at 31 December 2007.

## 16 Accounts Payable and Advances Received

	2007	2006
Trade accounts payable (refer to Note 8)	132,250	143,877
Deferred purchase consideration for acquisition of subsidiary (refer to Notes 14 and 26)	-	131,683
Dividends payable	1,929	2,076
<b>Total financial payables</b>	<b>134,179</b>	<b>277,636</b>
Payables to employees	137,618	111,426
Accrued liabilities and other creditors	15,062	22,021
<b>Total accounts payable and accrued expenses</b>	<b>286,859</b>	<b>411,083</b>

## 17 Other Taxes Payable

	2007	2006
Value-added tax payable	85,929	42,308
Payroll taxes	36,396	24,154
Property and other taxes payable	8,010	6,492
	<b>130,335</b>	<b>72,954</b>

## 18 Short-Term and Long-Term Borrowings

Borrowings consist of the following:

	2007	2006
Bonds issued	882,823	882,823
Credit lines	68,729	460,794
Term loans	57,357	600,000
	<b>1,008,909</b>	<b>1,943,617</b>

In June 2005 the Group issued 900 thousand non-convertible three year Russian Rouble denominated bonds (at par value 1,000 roubles each) for RR 900,000 with quarterly coupon payments of 9.9% per annum with an early redemption option. In June 2005 Board of Directors approved the decision to grant to the holders of the bonds a one off option to redeem the bonds in December 2006. Bonds for RR 17,177 were redeemed and not placed as at 31 December 2007 (2006: RR 17,177). In December 2006 Board of Directors of JSC Dorogobuzh approved the decision to reduce quarterly coupon payments to 8.6% per annum. The bonds are guaranteed by a parent company.

The Group's borrowings mature as follows:

	2007	2006
Borrowings due:		
- within 1 year	932,480	600,000
- between 2 and 5 years	76,429	1,343,617
	<b>1,008,909</b>	<b>1,943,617</b>



## 18 Short-Term and Long-Term Borrowings (continued)

The Group's borrowings are denominated in currencies as follows:

	2007	2006
Borrowings denominated in:		
- Russian Roubles	940,180	1,482,823
- US Dollars	68,729	460,794
	<b>1,008,909</b>	<b>1,943,617</b>

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

At 31 December 2007 and 31 December 2006 the fair value of borrowings was not materially different from their carrying amounts.

The details of the significant short-term loan balances are summarized below:

	2007	2006
<b>Short-term borrowings</b>		
<b>Russian rubles</b>		
Loans with fixed interest rates of 7% to 14% per annum	49,657	600,000
Bonds with coupon payments of 8.6% per annum	882,823	-
<b>Total short-term borrowings</b>	<b>932,480</b>	<b>600,000</b>

The details of the significant long-term loan balances are summarized below:

	2007	2006
<b>Long-term borrowings</b>		
<b>Russian rubles</b>		
Bonds with coupon payments of 8.6% to 9.9% per annum	-	882,823
<b>US\$</b>		
Loans with fixed interest rates of 14% per annum	7,700	-
Loans with floating interest rates of LIBOR + 2.75% to LIBOR + 4% per annum	68,729	460,794
<b>Total long-term borrowings</b>	<b>76,429</b>	<b>1,343,617</b>

The loan agreements for a total of RR 68,729 (2006: RR 460,794) contain certain covenants including those which require the Parent company to maintain a minimum level of net assets of at least USD 190 million, and impose restrictions on total debt which should not exceed 60% of the net assets, and EBITDA/net interest expense ratio which should be no less than 4 to 1. The loan agreements also provide for the borrower's obligation to maintain the required level of foreign currency inflows through the accounts opened with the lending banks. The loan agreements also provide for subjective acceleration clauses in case of the borrower's failure to fulfill or appropriately fulfill his obligations to the bank.

The loan agreements for a total of RR 20,363 (2006: RR 600,000) contain a covenant to maintain the required level of cash flows through the accounts opened with the lender. Also, they allow the bank to directly debit the borrower's accounts with the lending banks to ensure repayment of his debt. These loan agreements are collateralized by property for a total of RR 21,790 (see Note 13).



## 19 Shareholders' Equity

Total number of outstanding shares comprises (par value is expressed in roubles per one share):

	Ordinary shares		Share premium	Preferred shares	
	Number of shares authorised issued and paid	Share Capital		Number of shares authorised issued and paid	Share Capital
At 31 December 2006	721,182,860	1,379,569	93,794	154,256,400	355,790
At 31 December 2007	721,182,860	1,379,569	93,794	154,256,400	355,790

The Shareholders' of the Company has two classes of shares, Class A preferred and ordinary. The nominal value for both classes of share capital is RR 0.25 per share.

Class A preferred shares carry no voting rights and are entitled to a minimum annual dividend of 10% of the Company's net statutory profit after taxes. Preferred shares have priority over ordinary shares in the event of liquidation but carry no voting rights except on resolutions regarding liquidation or reorganisation of the Company, changes to dividend levels of preferred shares, or the issuance of additional preferred shares. Such resolutions require approval by two thirds of preferred shareholders. The preferred shares have no rights of redemption or conversion. The share capital is shown in the amount of the historical contribution adjusted for inflation since the date of privatisation until 31 December 2002.

In accordance with Russian legislation, the Company distributes profits as dividends or transfers them to reserves (fund accounts) on the basis of financial statements prepared in accordance with Russian Accounting Rules. The statutory accounting reports of the Company are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit. For 2007, the current year net statutory profit for the Company as reported in the published annual statutory reporting forms was RR 2,891,764 (2006: RR 2,962,865) and the closing balance of the accumulated profit including the current year net statutory profit totalled RR 6,496,195 (2006: RR 3,588,001). However, this legislation and other statutory laws and regulations are open to legal interpretation and accordingly management believes at present that it would not be appropriate to disclose an amount for the distributable reserves in these consolidated financial statements.

No dividends were declared for financial year 2007 (2006: RR 0.69 per ordinary share and RR 0.55 per preferred share in respect of 2005). No interim 2007 dividends were declared during the year.

## 20 Cost of Sales

The components of cost of sales were as follows:

	2007	2006
Change in inventories of finished goods and work in progress	(65,806)	10,725
Staff costs	529,787	481,357
Materials and components used	1,726,897	1,106,527
Fuel and energy	504,537	484,708
Natural gas	1,308,270	986,690
Depreciation and amortization	248,442	186,348
Production overheads	16,477	25,172
Repairs and maintenance	322,503	420,039
Social expenditure	67,714	80,764
	<b>4,658,821</b>	<b>3,782,330</b>



## 21 Selling, General and Administrative Expenses

	2007	2006
Staff costs	402,154	381,474
Reversal of provision for bad debts	(30,942)	(1,314)
Business trips expenses	15,145	20,338
Audit, legal and consulting services	4,538	76,818
Taxes other than income tax	36,592	35,387
Bank services	22,101	19,164
Insurance	6,168	4,394
Buildings maintenance and rent	70,166	58,326
Security	86,544	80,640
Telecommunication costs	9,600	9,441
Representation expenses	5,136	4,918
Other expenses	17,469	13,565
	<b>644,671</b>	<b>703,151</b>

## 22 Finance Income

	2007	2006
Interest income from loans provided	19,746	12,015
Dividend income	149,045	84,484
Foreign exchange gains	20,852	10,869
	<b>189,643</b>	<b>107,368</b>

## 23 Income Taxes

	2007	2006
Income tax expense – current	449,279	195,196
Deferred tax credit – origination and reversal of temporary differences	(15,881)	(16,364)
<b>Income tax charge</b>	<b>433,398</b>	<b>178,832</b>

Profit before taxation for financial reporting purposes is reconciled to tax expense/(credit) as follows:

	2007	2006
<b>Profit before taxation</b>	1,796,208	561,451
Theoretical tax charge at statutory rate of 24% thereon (2006: 24%)	431,090	134,748
Tax effect of items which are not deductible or assessable for taxation purposes:		
Income not taxable	(35,771)	(20,276)
Other non-deductible expenses	38,079	64,360
<b>Income tax charge</b>	<b>433,398</b>	<b>178,832</b>

In the context of the Group's current structure, tax losses and current tax assets of different group companies may not be offset against current tax liabilities and taxable profits of other group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity. Differences between IFRS and Russian statutory taxation regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 24% (2006: 24%).



23 Income Taxes (continued)

	31 December 2005	Differences recognition and reversal in income statement	Differences recognition and reversal directly in equity	31 December 2006
<b>Tax effects of taxable temporary differences:</b>				
Property, plant and equipment	331,922	(22,761)	-	309,161
Investments available for sale	594,786	6,836	57,589	659,211
Inventories	6,866	(2,471)	-	4,395
Other temporary differences	2,477	(360)	-	2,117
<b>Tax effects of deductible temporary differences:</b>				
Accounts receivable	(44,381)	2,680	-	(41,701)
Accounts payable	(16,584)	(3,733)	-	(20,317)
Other liabilities	(14,198)	3,445	-	(10,753)
<b>Total net deferred tax liability</b>	<b>860,888</b>	<b>(16,364)</b>	<b>57,589</b>	<b>902,113</b>
<b>Including:</b>				
<b>Deferred tax liability, long-term</b>	<b>912,510</b>			<b>957,618</b>
<b>Deferred tax asset, short-term</b>	<b>(51,622)</b>			<b>(55,505)</b>

	31 December 2006	Differences recognition and reversal in income statement	Differences recognition and reversal directly in equity	31 December 2007
<b>Tax effects of taxable temporary differences:</b>				
Property, plant and equipment	309,161	(24,531)	-	284,630
Investments available for sale	659,211	(10,523)	592,888	1,241,576
Inventories	4,395	9,638	-	14,033
Other temporary differences	2,177	(893)	-	1,224
<b>Tax effects of deductible temporary differences:</b>				
Accounts receivable	(41,701)	10,905	-	(30,796)
Accounts payable	(20,317)	(402)	-	(20,719)
Other liabilities	(10,753)	(75)	-	(10,828)
<b>Total net deferred tax liability</b>	<b>902,113</b>	<b>(15,881)</b>	<b>592,888</b>	<b>1,479,120</b>
<b>Including:</b>				
<b>Deferred tax liability, long-term</b>	<b>957,618</b>			<b>1,515,379</b>
<b>Deferred tax asset, short-term</b>	<b>(55,505)</b>			<b>(36,259)</b>

Substantially all deferred tax liabilities presented in the balance sheet are expected to be realised within a period exceeding 12 months from the balance sheet date.

Substantially all deferred tax assets presented in the balance sheet are expected to be realised within a period of 12 months from the balance sheet date.



## 24 Earnings per Share

Earnings per share is calculated by dividing the net income attributable to participating shareholders by the weighted average number of ordinary and preference shares in issue during the period, excluding the average number of ordinary shares purchased by the Company or its subsidiary and held as treasury shares (see Note 19).

	2007	2006
Weighted average number of ordinary shares outstanding	721,182,860	721,182,860
Weighted average number of preference shares outstanding	154,256,400	154,256,400
Dividends to ordinary shareholders	-	115,390
Dividends to preference shareholders	-	30,851
<b>Total dividends for the year</b>	<b>-</b>	<b>146,241</b>
Profit attributable to ordinary shareholders	1,120,355	310,117
Profit attributable to preference shareholders	239,636	72,502
<b>Profit for the year</b>	<b>1,359,991</b>	<b>382,619</b>
<b>Basic and diluted earnings per ordinary share (in Russian roubles)</b>	<b>1.55</b>	<b>0.43</b>
<b>Basic and diluted earnings per preference share (in Russian roubles)</b>	<b>1.55</b>	<b>0.47</b>

## 25 Contingencies, Commitments and Operating Risks

### i Contractual commitments and guarantees

As at 31 December 2007 the Group had outstanding capital commitments in relation to property, plant and equipment for amount of RR 327,726 (2006: RR 27,852).

The Group has already allocated the necessary resources in respect of these commitments. The Group believes that future net income and funding will be sufficient to cover this and any similar such commitments.

As at December 31, 2007 and 2006, the Group has not issued any financial guarantees to third parties in respect of borrowings from non-group companies.

### ii Legal proceedings

From time to time and in the normal course of business, claims against the Group are received. On the basis of its own estimates and both internal and external professional advice the Management is of the opinion that no material losses will be incurred in respect of claims in excess of provisions that have been made in these consolidated financial statements.

### iii Compliance with covenants

The Group is subject to certain covenants related primarily to its borrowings. Non-compliance with such covenants may result in negative consequences for the Group including growth in the cost of borrowings and declaration of default.

### iv Recent volatility in global financial markets

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



## **25 Contingencies, Commitments and Operating Risks (continued)**

### **v Taxation**

Russian tax and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant authorities.

The Russian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. In October 2006, the Supreme Arbitration Court issued guidance to lower courts on reviewing tax cases providing a systemic roadmap for anti-avoidance claims, and it is possible that this will significantly increase the level and frequency of tax authorities scrutiny.

As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Russian transfer pricing legislation introduced 1 January 1999 provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controllable transactions, provided that the transaction price differs from the market price by more than 20%.

Controllable transactions include transactions with interdependent parties, as determined under the Russian Tax Code, all cross-border transactions (irrespective whether performed between related or unrelated parties), transactions where the price applied by a taxpayer differs by more than 20% from the price applied in similar transactions by the same taxpayer within a short period of time, and barter transactions. There is no formal guidance as to how these rules should be applied in practice. In the past, the arbitration court practice with this respect has been contradictory.

Tax liabilities arising from intercompany transactions are determined using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Russian Federation and the changes in the approach of the Russian tax authorities, that such transfer prices could potentially be challenged in the future. Given the brief nature of the current Russian transfer pricing rules, the impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial condition and/or the overall operations of the entity.

The Group's management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency legislation and customs positions will be sustained. Accordingly, at 31 December 2007 no provision for potential tax liabilities had been recorded (2006: no provision).

### **vi Environmental matters**

The environmental regulation in the Russian Federation is at evolving stage. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

### **vii Operating environment**

The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation and strong economic growth. Management is unable to predict all developments in the economic environment which could have an impact on the Group's operations and consequently what effect, if any, they could have on the financial position of the Group.

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes, and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the government, together with tax, legal, regulatory, and political developments.



## 26 Business combinations

### Acquisition of subsidiaries

On 27 December 2006 the Group acquired 100% of the share capital of LLC Andrex for a cash consideration of RR 131,683. The acquired company holds title for facilities for transshipment, mixing, packaging and storing of bulk fertilizers located in Kaliningrad seaport. This acquisition was made consistent with Group's strategy, aiming for optimisation of fertilizer exports logistics. The acquired company is consolidated by the Group for the first time as at the effective date of obtaining control which is December 2006.

The acquired company contributed revenue of RR 0 thousand and profit of RR 0 to the Group for the period from the date of acquisition to 31 December 2006. If the acquisition had occurred on 1 January 2006, effect on Group revenue for 2006 would have been RR 0, and effect on profit for 2006 would have been RR 0. Prior to acquisition LLC Andrex leased out its primary assets to JSC Kaliningrad Seaport on a free of charge basis under non-cancellable lease agreements. Starting from date of acquisition the Group concluded new lease contracts at current market rates.

The Group has completed the process of the purchase price allocation and the following table summarizes the fair values of the assets acquired and liabilities assumed in this business combination, determined in accordance with IFRS 3, *Business combinations*. The fair values of property, plant and equipment were based on estimates of independent professional appraiser.

Details of the assets acquired and liabilities assumed and goodwill arising on acquisition are as follows:

	Note	IFRS carrying amount immediately before business combination	Attributed fair value
Cash and cash equivalents		11	11
Property, plant and equipment		12,826	79,580
Other assets		274	275
Other liabilities		(251)	(251)
<b>Fair value of net assets of subsidiary</b>			<b>79,615</b>
Goodwill arising from the acquisition	14		52,068
<b>Total purchase consideration</b>			<b>131,683</b>
Less: deferred purchase consideration	16		(131,683)
Less: cash and cash equivalents of subsidiary acquired			(11)
<b>Inflow of cash and cash equivalents on acquisition</b>			<b>11</b>

## 27 Significant Non-Cash Transactions

Included in sales are non-cash transactions amounting to RR 8,310 (2006: RR 100,235) were settled via non-cash transactions during the years ended 31 December 2007 and 2006, respectively. The transactions primarily represent cancellation of mutual balances with customers and suppliers within the operating cycle.

## 28 Financial Risk Management

### 28.1 Financial risk management

The Group's activities expose it to a variety of financial risks: market risk (including foreign currency exchange risk, interest rate risk and price risk), credit risk and liquidity risk. The overall risk management programme seeks to minimize potential adverse effects on the financial performance of the Group.





## 28 Financial Risk Management (continued)

### 28.1 Financial risk management (continued)

#### (a) Market risk

##### (i) Foreign currency risk

Foreign currency risk is the risk of losses resulting from adverse movements in different currency exchange rates against the Group functional currency. Foreign currency risk arises from the international operations of the Group, future commercial transactions in foreign currencies, including repayment of foreign currency denominated borrowings and recognition of assets and liabilities denominated in a currency which is not a functional currency of the Group.

The objective of the Group's foreign exchange risk management activities is to minimise the volatility of the Group's financial results by matching the same foreign currency denominated assets and liabilities. The Group does not currently hedge foreign exchange exposure using financial instruments. Group entities are prohibited from borrowing and investing in foreign currencies on a speculative basis.

Group's policies for attracting foreign exchange denominated borrowings depend on current and forward rates of foreign currencies to Russian rouble. Credit lines denominated in various currencies allow the Group to be flexible in reaction to foreign currency rate shocks and minimize foreign currency exposure.

The tables below summarise the Group's exposure to foreign currency exchange rate risk at the balance sheet date:

At 31 December 2007	US Dollar	EURO
<b>Monetary financial assets:</b>		
Cash and cash equivalents	65,342	683
Accounts receivable	11,193	20,985
	76,535	21,668
<b>Monetary financial liabilities:</b>		
Accounts payable and other liabilities	(1,178)	(7,187)
Borrowings and notes payable	(68,729)	-
	(69,907)	(7,187)
<b>Net balance sheet position</b>	<b>6,628</b>	<b>14,481</b>

At 31 December 2006	US Dollar	EURO
<b>Monetary financial assets:</b>		
Cash and cash equivalents	278,109	658
Accounts receivable	247,512	-
	525,621	658
<b>Monetary financial liabilities:</b>		
Accounts payable and other liabilities	(843)	(3,539)
Borrowings and notes payable	(460,794)	-
	(461,637)	(3,539)
<b>Net balance sheet position</b>	<b>63,984</b>	<b>(2,881)</b>

The above analysis includes only monetary assets and liabilities.

The foreign exchange rate sensitivity is calculated by aggregation of the net foreign exchange risk exposure and primarily arises from US dollar denominated trade receivables, cash and cash equivalents, borrowings and accounts payable.

	2007	2006
<i>Impact on post-tax profit and on equity of:</i>		
US Dollar strengthening by 10%	663	6,398
US Dollar weakening by 10%	(663)	(6,398)
Euro strengthening by 10%	1,448	(288)
Euro weakening by 10%	(1,448)	288



## **28 Financial Risk Management (continued)**

### **28.1 Financial risk management (continued)**

#### **(a) Market risk (continued)**

##### **(i) Foreign currency risk (continued)**

The Group relies on export sales to generate foreign currency earnings. As the Group sales outside the Russian Federation a significant portion of its production, it is exposed to foreign currency risk arising primarily on volatility of US dollar rate, in which major export sales are denominated.

Since the Group does not hold any foreign currency denominated equity securities and other financial instruments revalued through equity, the effect of a change in the exchange rate on equity would be the same as that on the post-tax profit.

##### **(ii) Interest rate risk**

Interest rate risk arises from movements in interest rates which could affect the Group's financial results or the value of the Group's equity. A change in interest rates may cause variations in interest income and expense. The primary objective of the Group's interest rate management is to protect the net interest result. Interest risk management is carried out by the corporate finance and corporate treasury functions of the Group.

All entities of the Group obtain any required financing through the corporate treasury function of the Group in the form of loans. Generally, the same concept is adopted for deposits of cash generated by the units.

Monitoring of current market interest rates and analysis of the Group's interest-bearing position is performed by the corporate treasury and corporate finance functions as a part of interest rate risk management procedures. Monitoring is performed taking into consideration refinancing, renewal of existing positions and alternative financing.

The Group has no interest-bearing assets at floating rates, and the Group's operating cash flows are substantially independent of changes in market interest rates.

The Group interest rate risk arises from various long-term debt facilities. Borrowings at variable rates expose the Group's cash flow to an interest rate risk. At 31 December 2007 and 2006 borrowings at variable rates amounted to RR 68,729 and RR 460,794, respectively (Note 18).

At 31 December 2007, if interest rates at that date had been 1% higher with all other variables held constant, profit for the year would have been RR 189 (2006: RR 83) lower, mainly as a result of higher interest expense on variable interest liabilities.

The effect of a change for the year in the interest rate on equity would be the same as that on post-tax profit.

##### **(iii) Price risk**

The Group is exposed to an equity securities price risk, since it has an investment in equity stakes of JSC Acron and JSC Sberbank, which are classified on the consolidated balance sheet as available-for-sale as of 31 December 2007 and 31 December 2006, respectively. Monitoring of the fair value of the stakes is performed on a regular basis to assess risk of impairment of the stakes. No impairment of these investments was recognized as of 31 December 2007 and 31 December 2006.

From time to time the Group makes investments in entities with high upside market potential. Investments are assessed by corporate treasury department and accepted provided that internal rate of return for investment exceeds current weighted average cost of capital.

The Group does not enter into any transactions with financial instruments whose value is exposed to the value of any commodities traded on a public market.



## 28 Financial Risk Management (continued)

### 28.1 Financial risk management (continued)

#### **(b) Credit risk**

Credit risk arises from the possibility that counterparties to transactions may default on their obligations, causing financial losses for the Group. Financial assets, which potentially subject Group entities to credit risk, consist principally of trade receivables, cash and bank deposits and loans receivable. The objective of managing credit risk is to prevent losses of liquid funds deposited with or invested in financial institutions or the loss in value of receivables.

The maximum exposure to credit risk resulting from financial assets is equal to the carrying amount of the Group's financial assets, including loans receivable, not including equity investments. The Group has no significant concentrations of credit risk.

**Cash and cash equivalents.** Cash and short-term deposits are placed in major multinational and Russian banks with independent credit ratings. All bank balances and term deposits are neither past due nor impaired. See analysis by credit quality of bank balances and term deposits in Note 9.

**Trade receivables and loans receivable.** Trade receivables and loans receivable are subject to a policy of active credit risk management which focuses on an assessment of ongoing credit evaluation and account monitoring procedures. The objective of the management of receivables is to sustain the growth and profitability of the Group by optimising asset utilisation whilst maintaining risk at an acceptable level.

The monitoring and controlling of credit risk is performed by the corporate treasury function of the Group. The credit policy requires the performance of credit evaluations and ratings of customers or borrowers. The credit quality of each new customer is analyzed before the Group provides it with the standard terms of goods supply and payments. The credit quality of new borrowers is analyzed before the Group provides it with the loan. The Group gives preference to customers with an independent credit rating. The credit quality of customers and borrowers is assessed taking into account their financial position, past experience and other factors. Customers which do not meet the credit quality requirements are supplied on a prepayment basis only.

Management monitors and discloses concentrations of credit risk by obtaining reports listing exposures to counterparties with aggregated balances in excess of 10% of the Group's gross accounts receivable balances. At 31 December 2007 and 31 December 2006 the Group had no counterparties with aggregated receivables balances of in excess of 10% of the Group's gross accounts receivable balances, except for trade receivables from NPKchemical Trading Inc. as of 31 December 2006 in the amount of RR 247,205.

Although the collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded (Note 10).

#### **(c) Liquidity risk**

Liquidity risk results from the Group's potential inability to meet its financial liabilities, such as settlements of financial debt and payments to suppliers. The Group's approach to liquidity risk management is to maintain sufficient readily available reserves in order to meet its liquidity requirements at any point in time.

Weekly liquidity planning is performed by the corporate treasury function and reported to the management of the Group. Beyond cash management, the Group mitigates liquidity risk by keeping committed credit lines available.

The table below analyses the Group's financial liabilities into the relevant maturity groupings based on the time remaining from the balance sheet date to the contractual maturity date.



## 28 Financial Risk Management (continued)

### 28.1 Financial risk management (continued)

#### (c) Liquidity risk

	Demand and less than 3 months	From 3 to 12 months	From 12 months to 2 years	From 2 years to 5 years	Over 5 years	Total
<b>As of 31 December 2007</b>						
Bonds issued * (Note 18)	18,876	897,759	-	-	-	916,635
Credit lines * (Note 18)	1,324	4,002	2,422	68,729	-	76,477
Term loans * (Note 18)	1,667	2,053	57,400	-	-	61,120
Trade payables (Note 16)	119,079	13,171	-	-	-	132,250
Dividends and other distributions to shareholders (Note 16)	1,929	-	-	-	-	1,929
<b>Total future payments, including future principal and interest payments</b>	<b>142,875</b>	<b>916,985</b>	<b>59,822</b>	<b>68,729</b>	<b>-</b>	<b>1,188,411</b>
<b>As of 31 December 2006</b>						
Bonds issued * (Note 18)	18,721	57,202	917,199	-	-	993,122
Credit lines * (Note 18)	4,642	14,183	5,327	463,339	-	487,491
Term loans * (Note 18)	4,284	613,091	-	-	-	617,375
Trade payables (Note 16)	96,041	43,547	4,289	-	-	143,877
Deferred purchase consideration for acquisition of new subsidiaries (Notes 16 and 26)	-	131,683	-	-	-	131,683
Dividends and other distributions to shareholders (Note 16)	2,076	-	-	-	-	2,076
<b>Total future payments, including future principal and interest payments</b>	<b>125,764</b>	<b>859,706</b>	<b>926,815</b>	<b>463,339</b>	<b>-</b>	<b>2,375,624</b>

\* The table above shows undiscounted cash outflows for financial liabilities (including interest together with the borrowings) based on conditions existing as of 31 December 2007 and 31 December 2006, respectively.

The Group controls the minimum required level of cash balances available for short-term payments in accordance with the financial policy of the Group. Such cash balances are represented by current cash balances on bank accounts and bank deposits. Group's policy for financing its working capital is aimed at maximum reliance on own operating cash flows, availability of short-term bank and other external financing to maintain sufficient liquidity.

### 28.2 Capital risk management

The Group's objectives when managing capital are to safeguard its ability to continue as a going concern, to provide returns for shareholders and benefits for other stakeholders, to have available the necessary financial resources for investing activities and to maintain an optimal capital structure in order to reduce the cost of capital.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as total debt divided by total capital under management. The Group considers total capital under management to be equity as shown in the IFRS consolidated balance sheet. This is considered more appropriate than alternative methods available, such as the value of equity shown in the Company's statutory financial (accounting) reports. In 2007, the Group's strategy, which was unchanged from 2006, was to maintain the gearing ratio at the level not exceeding 80%.



## 28 Financial Risk Management (continued)

### 28.2 Capital risk management (continued)

The gearing ratio as of 31 December 2007 and 31 December 2006 is shown in the table below:

	2007	2006
Long-term borrowings	76,429	1,343,617
Short-term borrowings	932,480	600,000
<b>Total debt</b>	<b>1,008,909</b>	<b>1,943,617</b>
<b>Shareholders' equity</b>	<b>8,022,386</b>	<b>4,782,097</b>
<b>Gearing ratio, %</b>	<b>12.6%</b>	<b>40.6%</b>

The Group also maintains an optimal capital structure by tracing certain capital requirements based on the minimum level of EBITDA/net interest expense ratio. In 2007, the Group's strategy, which was unchanged from 2006, was to maintain EBITDA/net interest expense ratio at the level not be lower than 4:1. For this purpose EBITDA is defined as earnings before tax, interest, depreciation and amortization. Net interest expense is defined as interest expense less interest income. This ratio is included as a covenant in the loan agreements (see Note 18).

The ratio of EBITDA/net interest expense as of 31 December 2007 and 31 December 2006 is shown in the table below:

	2007	2006
Operating profit	1,724,067	582,789
Add: depreciation and amortization (Note 13)	248,442	186,348
<b>EBITDA</b>	<b>1,972,509</b>	<b>769,137</b>
Net interest expense	97,756	116,691
<b>EBITDA/Net interest expense</b>	<b>20:1</b>	<b>7:1</b>

## 29 Fair Value of Financial Instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Russian Federation continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

**Financial instruments carried at fair value.** Available-for-sale investments are carried on the consolidated balance sheet at their fair value. Cash and cash equivalents are carried at amortised cost, which approximates current fair value.

Fair values for available-for-sale investments carried at fair value were determined by reference to the current market value at active markets (refer to Note 15).

**Financial assets carried at amortised cost.** The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on credit risk of the counterparty. Carrying amounts of trade receivables approximate fair values.



## **29 Fair Value of Financial Instruments (continued)**

**Liabilities carried at amortised cost.** The fair value is based on quoted market prices, if available. The estimated fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. At 31 December 2006 and 2005 the fair value of the current and non-current borrowings is not materially different from their carrying amounts.

## **30 Subsequent Events**

### **Export duties**

In March 2008 the Government of the Russian Federation introduced duties, effective from April 2008, on exports of nitrogen fertilizers, complex fertilizers and apatite to countries outside the CIS Customs Union. The duties applicable to the Group's products are 8.5% and 6% of the declared customs value of nitrogen and complex fertilizers and apatite, respectively. Management is currently assessing the impact of these duties on the Group's future financial results. Currently, export sales represent 52% (2006: 52%) of Group's revenues.

### **Dividends declared by the Company**

In May 2008 the annual shareholders meeting approved an annual dividends distribution for the year ended 31 December 2007 in the amount of 1.88 Russian roubles per each ordinary and preferred share.

### **Bonds repayment**

Subsequent to 31 December 2007 and prior to the date of these consolidated financial statements, the Group has repaid existing bonds of RR 882,823.

### **Sale of JSC Acron's shares**

In connection with the proposed secondary public offering of shares of JSC Acron, a parent company, in July 2008 the Board of Directors approved a decision to sale JSC Acron's shares in a quantity of not more than 1,907,504, which is 4% of total share capital of JSC Acron, with nominal value of 5 roubles at a price, which is to be determined per results of offers received from potential investors in accordance with the market rules and will correspond their market value.