

Bank “National Factoring Company” LLC
Financial statements

Year ended December 31, 2005

Together with independent auditors’ report

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REPORT OF INDEPENDENT AUDITORS

To the Participants and Board of Directors of Bank "National Factoring Company" (Limited Liability Company) -

We have audited the accompanying balance sheet of Bank "National Factoring Company" (Limited Liability Company) (the "Bank") as of December 31, 2005, and the related statements of income, changes in net assets attributable to participants, and cash flows for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements for the year ended December 31, 2004, were audited by other auditors whose report dated June 30, 2005, included an explanatory paragraph with respect to significant transactions with related parties.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of December 31, 2005, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Without qualifying our opinion, we draw attention to Note 19, which discloses significant transactions with related parties, in particular with respect to financing operations.

Ernst & Young Vneshaudit
by V. Dilanian

February 15, 2006

STATEMENTS OF INCOME*(Thousands of Russian Rubles)*

	<i>Notes</i>	<i>Years ended December 31,</i>	
		<i>2005</i>	<i>2004</i>
Interest income			
Factoring	5	878,138	129,564
Debt securities		1,801	–
Due from credit institutions		1,032	912
Loans		470	19,794
		881,441	150,270
Interest expense			
Due to credit institutions		69,572	6,559
Deposits		7,319	2,107
Other		12	9
		76,903	8,675
Net interest income		804,538	141,595
Impairment of interest earning assets	6	84,928	81,741
Net interest income after impairment		719,610	59,854
Fee and commission income less expense		(597)	(46)
Gains less losses from trading securities		404	–
Translation gains less losses from foreign currency		(280)	(5)
Foreign exchange gains less losses		(584)	(1)
Other income		384	73
Non interest income (loss)		(673)	21
Salaries and employment benefits	7	153,076	38,319
Administrative and operating expenses	7	83,866	18,006
Depreciation		967	213
Non interest expense		237,909	56,538
Income before income tax expense		481,028	3,337
Income tax expense	8	115,134	1,122
Net income		365,894	2,215

The accompanying notes on pages 5 to 21 are an integral part of these financial statements.

BALANCE SHEETS*(Thousands of Russian Rubles)*

	<i>Notes</i>	<i>December 31,</i>	
		<i>2005</i>	<i>2004</i>
Assets			
Cash and cash equivalents	9	875,243	844,652
Trading securities	10	20,694	–
Amounts due from credit institutions	11	287,690	55,251
Factoring advances	12	4,370,939	2,806,576
Tax assets	8	9,496	12,564
Other assets	13	32,867	4,861
Total assets		<u>5,596,929</u>	<u>3,723,904</u>
Liabilities			
Amounts due to credit institutions	14	3,621,521	1,487,167
Settlements with clients on factoring		77,886	43,510
Time deposits of clients		30,930	705,553
Tax liabilities	8	7,453	11,230
Other liabilities	13	34,931	18,130
Total liabilities excluding net assets attributable to participants		<u>3,772,721</u>	<u>2,265,590</u>
Net assets attributable to participants			
Statutory fund		1,456,000	1,456,000
Retained earnings		368,208	2,314
Total net assets attributable to participants	15	<u>1,824,208</u>	<u>1,458,314</u>
Total liabilities		<u>5,596,929</u>	<u>3,723,904</u>

Signed on behalf of the Board of Directors

Mikhail I. Treyvish

Chairman of Management Board

Dmitry A. Karpushin

Chief Accountant

February 15, 2006

The accompanying notes on pages 5 to 21 are an integral part of these financial statements.

STATEMENTS OF CHANGES IN NET ASSETS ATTRIBUTABLE TO PARTICIPANTS*(Thousands of Russian Rubles)*

	<i>Notes</i>	<i>Statutory fund</i>	<i>Retained earnings</i>	<i>Net assets attributable to participants</i>
December 31, 2003		456,000	99	456,099
Contribution from participants		1,000,000	–	1,000,000
Net income		–	2,215	2,215
December 31, 2004		1,456,000	2,314	1,458,314
Net income		–	365,894	365,894
December 31, 2005	15	1,456,000	368,208	1,824,208

The accompanying notes on pages 5 to 21 are an integral part of these financial statements.

STATEMENTS OF CASH FLOW*(Thousands of Russian Rubles)*

	<i>Years ended December 31,</i>		
	<i>Note</i>	<i>2005</i>	<i>2004</i>
Cash flows from operating activities			
Interest, fees and commissions received		853,980	115,81
Interest, fees and commissions paid		(68,536)	(4,976)
Gains less losses from trading securities		(126)	–
Realized gains less losses in foreign currencies		(584)	(1)
Other operating income		384	73
Salaries and employment benefits		(144,071)	(30,224)
Administrative and operating expenses		(84,868)	(16,914)
Cash flows from operating activities before changes in operating assets and liabilities		556,179	63,76
Net (increase) decrease in operating assets			
Trading securities		(19,956)	–
Amounts due from credit institutions		(231,891)	(55,251)
Factoring advances		(1,622,837)	(2,854,015)
Other assets		(25,083)	(3,020)
Net increase (decrease) in operating liabilities			
Settlements with clients on factoring		34,376	43,51
Time deposits of clients		(673,102)	703,69
Other liabilities		9,781	8,05
Net cash flows used in operating activities before income taxes		(1,972,533)	(2,093,258)
Corporate income tax paid		(115,843)	(2,456)
Net cash flows used in operating activities		(2,088,376)	(2,095,714)
Cash flows from investing activities			
Purchases of property and equipment		(3,891)	(2,055)
Net cash flows used in investing activities		(3,891)	(2,055)
Cash flows from financing activities			
Amounts due to credit institutions		2,123,869	1,485,27
Debt securities issued		(1,011)	1,01
Participants funds contributed		–	1,000,00
Net cash flows from financing activities		2,122,858	2,486,28
Net change in cash and cash equivalents		30,591	388,51
Cash and cash equivalents, beginning		844,652	456,13
Cash and cash equivalents, ending	9	875,243	844,65

The accompanying notes on pages 5 to 21 are an integral part of these financial statements.

(Thousands of Russian Rubles)

NOTE 1 – PRINCIPAL ACTIVITIES

Bank “National Factoring Company” (Limited Liability Company) (the “Bank”) was established in 2003 as a limited liability company under the laws of the Russian Federation. The Bank possesses a banking license from the Central Bank of Russia (the “CBR”) granted in March 2004. This license gives the Bank a right to perform operations with legal entities (including credit institutions). The Bank's core operations are factoring services, including financing transactions against cash cession and other transactions with trade receivables of business entities in the Russian Federation and abroad. The Bank acts as a factor for Russian and foreign legal entities and as an import factor for foreign factoring companies. The Bank is a member of Factors Chain International (FCI), International Factors Group (IFG) – special professional associations of the global factoring market. The Bank is the leader in the Russian factoring market.

The Bank is a member of a holding headed by Limited Liability Partnership “Limited Liability Company “Financial Corporation NIKoil” and Company” (the “Group”), involved in delivering financial and banking services in Russia and other CIS countries.

The bank's main office is located in Moscow and it has 18 operating outlets in the Russian Federation. The Bank's registered legal address is 56 Profsoyuznaya Street, Moscow 117420. The Bank had an average of 175 employees during 2005 (2004 – 45) and 210 employees as of December 31, 2005 (2004 – 85).

NOTE 2 – BASIS OF PREPARATION

General

These financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”).

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Russian Rubles in accordance with Russian accounting and banking legislation and related instructions (“RAL”). These financial statements are based on the Bank's RAL books and records, as adjusted and reclassified in order to comply with IFRS. The reconciliation between RAL and IFRS is presented later in this note.

The financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

These financial statements are presented in thousands of Russian Rubles (“RUB”), unless otherwise indicated.

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that the Bank has adopted those new/revised standards mandatory for financial years beginning on or after January 1, 2005.

The changes in accounting policies result from adoption of the following new or revised standards:

IAS 10 (revised) “Events after the Balance Sheet Date”;
IAS 16 (revised) “Property, Plant and Equipment”;
IAS 17 (revised) “Leases”;
IAS 24 (revised) “Related Party Disclosures”; and
IAS 39 (revised) “Financial Instruments: Recognition and Measurement”.

The principal effects of these changes in policies are discussed below.

IAS 39 “Financial Instruments: Recognition and Measurement” (amended 2004)

Financial Assets and Liabilities at Fair Value through Profit or Loss

A new category of financial instruments has been introduced, “Financial assets and liabilities at fair value through profit or loss”. This category includes trading financial assets and liabilities as well as any financial assets and liabilities designated into this category at initial recognition¹. These assets and liabilities are measured at fair value with recognition of gains or losses on re-measurement to fair value in net income or loss.

(Thousands of Russian Rubles)

NOTE 2 – BASIS OF PREPARATION (CONTINUED)

Reconciliation of RAL and IFRS Net Assets Attributable to Participants and Net Income

Net assets attributable to participants and net income are reconciled between RAL and IFRS as follows:

	2005		2004	
	<i>Net assets attributable to participants</i>	<i>Net income</i>	<i>Net assets attributable to participants</i>	<i>Net income</i>
Russian Accounting Legislation	1,737,394	261,339	1,476,199	20,100
Impairment of financial assets and other provisions	62,171	114,076	(51,905)	(51,905)
Deferred taxation	(7,453)	(20,017)	12,564	12,564
Effect of accrued interest	49,213	18,499	30,714	30,714
Accrual of additional compensation benefits	(17,100)	(9,005)	(8,095)	(8,095)
Other	(17)	1,002	(1,163)	(1,163)
International Financial Reporting Standards	1,824,208	365,894	1,458,314	2,215

IFRSs and IFRIC interpretations not yet effective

The Bank has not applied the following IFRSs and Interpretations of the International Financial Reporting Interpretations Committee (IFRIC) that have been issued but are not yet effective:

IAS 19 (amended 2004) "Employee Benefits";
IAS 21 (amended 2005) "The Effects of Changes in Foreign Exchange Rates";
IAS 39 (amended 2005) "Financial Instruments: Recognition and Measurement";
IFRS 7 "Financial Instruments: Disclosures";
IFRIC 4 "Determining whether an Arrangement contains a Lease";

The Bank expects that the adoption of the pronouncements listed above will have no significant impact on the Bank's financial statements in the period of initial application.

NOTE 3 – SUMMARY OF ACCOUNTING POLICIES

Financial Assets

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Bank determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year-end.

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Bank commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial Assets at Fair Value through Profit or Loss

Financial assets classified as held for trading are included in the category 'financial assets at fair value through profit or loss'. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated and effective hedging instruments. Gains or losses on investments held for trading are recognised in income.

(Thousands of Russian Rubles)

NOTE 3 – SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

Loans, Factoring Advances and Receivables

Loans, factoring advances and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in income when the loans, factoring advances and receivables are derecognised or impaired, as well as through the amortisation process.

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the CBR, excluding obligatory reserves, and due from credit institutions that mature within three months of the date of origination and are free from contractual encumbrances.

Borrowings

All borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in net income or loss when the liabilities are derecognised as well as through the amortisation process.

Leases

Operating - Bank as Lessee

The Bank presents assets subject to operating leases in the balance sheets according to the nature of the asset. Lease income from operating leases is recognized in statement of income on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognized as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

Allowances for Impairment of Financial Assets

The Bank assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets Carried at Amortised Cost

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced through use of an allowance account. The amount of the loss shall be recognised in the statement of income.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not the foreclosure is probable.

(Thousands of Russian Rubles)

NOTE 3 – SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the statement of income, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

When a loan is uncollectible, it is written off against the related allowance for loan impairment. Such loans are written off after all necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of allowance for loan impairment in the statement of income.

Derecognition of Financial Assets and Liabilities

Financial Assets

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

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

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial Liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

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

Taxation

The current income tax expense is calculated in accordance with the regulations of the Russian Federation.

(Thousands of Russian Rubles)

NOTE 3 – SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Russia also has various operating taxes, that are assessed on the Bank's activities. These taxes are included as a component of other operating expenses.

Property and Equipment

Property and equipment are carried at cost less accumulated depreciation and any accumulated impairment for diminution in value. Depreciation of assets under construction and those not placed in service commences from the date the assets are placed into service. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Computers and office equipment	3-7
Motor vehicles	3-5

Leasehold improvements are amortized over the life of the related leased asset. The carrying amounts of property and equipment are reviewed at each balance sheet date to assess whether they are recorded in excess of their recoverable amounts, and where carrying values exceed this estimated recoverable amount, assets are written down. Impairment is recognized in the respective period and is included in administrative and operating expenses.

Costs related to repairs and renewals are charged when incurred and included in administrative and operating expenses, unless they qualify for capitalization.

Provisions

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made.

Retirement and Other Benefit Obligations

The Bank does not have any pension arrangements separate from the State pension system of the Russian Federation, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such expense is charged in the period the related salaries are earned. In addition, the Bank has no post-retirement benefits or significant other compensated benefits requiring accrual.

Statutory Fund

Statutory fund is recognized at cost. Distributions are recognized in net assets attributable to participants as a reduction in the period in which they are declared. Distributions that are declared after the balance sheet date are treated as a subsequent event under IAS 10 "Events After the Balance Sheet Date" and disclosed accordingly.

(Thousands of Russian Rubles)

NOTE 3 – SUMMARY OF ACCOUNTING POLICIES (CONTINUED)

Contingencies

Contingent liabilities are not recognised in the balance sheet but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the balance sheet but disclosed when an inflow of economic benefits is probable.

Income and Expense Recognition

Interest income and expense are recognized on an accrual basis calculated using the effective interest method. Loan origination and other fees for loans issued or received and factoring advances are deferred or accrued (together with related direct costs) and recognized as an adjustment to the effective yield of the instruments. Fees, commissions and other income and expense items are generally recorded on an accrual basis when the service has been provided.

Foreign Currency Translation

The financial statements are presented in Russian Rubles, which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. Gains and losses resulting from the translation of foreign currency transactions are recognized in the statement of income as gains less losses from foreign currencies - translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a certain transaction and the Central Bank exchange rate on the date of the transaction are included in foreign exchange gains less losses. The official CBR exchange rates at December 31, 2005 and 2004, were 28.78 Rubles and 27.75 Rubles to 1 USD, respectively.

NOTE 4 – SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

Estimation Uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Allowance for Impairment of Loans, Factoring Advances and Receivables

The Bank regularly reviews its advances, loans and receivables to assess impairment. The Bank uses its experienced judgement to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are few available historical data relating to similar borrowers. Similarly, the Bank estimates changes in future cash flows based on the observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of advances, loans and receivables. The Bank uses its experienced judgement to adjust observable data for a group of loans, advances or receivables to reflect current circumstances.

Taxation

Russian tax, currency 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 Bank may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and, as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, 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.

As at 31 December 2005 management believes that its interpretation of the relevant legislation is appropriate and that the Bank's tax, currency and customs positions will be sustained.

*(Thousands of Russian Rubles)***NOTE 5 – INTEREST INCOME FROM FACTORING OPERATIONS**

Interest income from factoring operations comprise the following types:

	<u>2005</u>	<u>2004</u>
Financing	563,474	78,670
Service premium	312,607	50,894
Risk premium	2,057	–
Interest income from factoring operations	<u>878,138</u>	<u>129,564</u>

NOTE 6 – ALLOWANCES FOR IMPAIRMENT

The movements in the allowances for impairment of interest earning assets were as follows:

	<u>Factoring advances</u>
December 31, 2003	–
Charge	81,741
December 31, 2004	<u>81,741</u>
Charge	84,928
December 31, 2005	<u>166,669</u>

Allowances for impairment of assets are deducted from the related assets. In accordance with Russian legislation, advances and loans may only be written off with the approval of the Board of Directors and, in certain cases, with the respective decision of the Court.

NOTE 7 – SALARIES AND ADMINISTRATIVE AND OPERATING EXPENSES

Salaries and benefits, administrative and operating expenses comprise:

	<u>2005</u>	<u>2004</u>
Salaries and additional compensation payments	134,909	33,168
Social security costs	18,167	5,151
Salaries and employment benefits	<u>153,076</u>	<u>38,319</u>
Occupancy and rent	33,704	3,905
Equipment support and maintenance	20,002	2,282
Business development	12,479	2,432
Marketing and advertising	10,012	3,992
Communications	2,515	72
Professional services	2,129	60
Operating taxes	226	2,547
Other	2,799	2,716
Administrative and operating expenses	<u>83,866</u>	<u>18,006</u>

*(Thousands of Russian Rubles)***NOTE 8 – TAXATION**

The corporate income tax expense comprises:

	<u>2005</u>	<u>2004</u>
Current tax expense	95,117	13,686
Deferred tax expense (benefit)	20,017	(12,564)
Income tax expense	<u>115,134</u>	<u>1,122</u>

Russian legal entities must file individual tax declarations. The tax rate on income other than on state securities was 24% for 2005 and 2004. The tax rate for interest income on state securities was 15% for Federal taxes.

Tax assets and liabilities consist of the following:

	<u>2005</u>	<u>2004</u>
Current tax assets	9,496	–
Deferred tax assets	–	12,564
Current tax liabilities	–	11,230
Deferred tax liabilities	7,453	–

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	<u>2005</u>	<u>2004</u>
Income before taxation	481,028	3,337
Statutory tax rate	24%	24%
Theoretical income tax expense at statutory rate	115,447	801
State securities income taxed at difference rate	(56)	–
Non-deductible expenditures and other non-temporary differences	(257)	321
Income tax expense	<u>115,134</u>	<u>1,122</u>

Deferred tax assets and liabilities comprise:

	<u>2005</u>	<u>2004</u>
Tax effect of deductible temporary differences		
Factoring advances	–	12,457
Other	–	280
Deferred tax assets	<u>–</u>	<u>12,737</u>
Tax effect of taxable temporary differences		
Factoring advances	6,484	–
Accruals	969	173
Deferred tax liabilities	<u>7,453</u>	<u>173</u>
Deferred tax liability (asset)	<u>7,453</u>	<u>(12,564)</u>

(Thousands of Russian Rubles)

NOTE 9 – CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise:

	<u>2005</u>	<u>2004</u>
Current account with the Central Bank	445,369	12,435
Current accounts with other credit institutions	199,788	832,217
Time deposits with credit institutions up to 90 days	230,086	–
Cash and cash equivalents	<u>875,243</u>	<u>844,652</u>

As of December 31, 2005, the Bank placed RUB 30,000 (2004 - nil) as a deposit in RUB with a Russian bank and received RUB 30,000 (2004 – nil) as a RUB deposit from the same bank (see Note 14).

NOTE 10 – TRADING SECURITIES

Trading securities owned comprise Russian State bonds (OFZ) with coupon rate of 6.3% and maturity in 2008.

NOTE 11 – AMOUNTS DUE FROM CREDIT INSTITUTIONS

Amounts due from credit institutions comprise:

	<u>2005</u>	<u>2004</u>
Obligatory reserve with the Central Bank	170,557	55,251
Time deposits for more than 90 days or overdue	117,133	–
Amounts due from credit institutions	<u>287,690</u>	<u>55,251</u>

Credit institutions are required to maintain a non-interest earning cash deposit (obligatory reserve) with the CBR, the amount of which depends on the level of funds attracted by the credit institution. The Bank's ability to withdraw such deposit is significantly restricted by the statutory legislation.

NOTE 12 – FACTORING ADVANCES

Factoring advances comprise:

	<u>2005</u>	<u>2004</u>
Factoring advances with recourse	4,484,757	2,841,182
Factoring advances without recourse	55,709	56,861
	<u>4,540,466</u>	<u>2,898,043</u>
Less – Clients counter-claims	(2,858)	(9,726)
Less – Allowance for impairment	(166,669)	(81,741)
Factoring advances	<u>4,370,939</u>	<u>2,806,576</u>

As of December 31, 2005, the Bank's advances to its 10 largest third party borrowers comprised RUB 1,302,417, or 29% of gross factoring portfolio (2004 – RUB 862,991, or 30%). As of December 31, 2005, an allowance of RUB 3,904 (2004 – RUB 22,739) was made against these advances.

*(Thousands of Russian Rubles)***NOTE 12 – FACTORING ADVANCES (CONTINUED)**

The majority of advances have been extended to private companies. Advances are made principally within Russia in the following industry sectors:

	<i>2005</i>	<i>2004</i>
Production and wholesale of food and beverages	2,196,199	869,451
Production and wholesale of computers and consumer electronics	991,119	670,881
Other trading enterprises	524,773	761,804
Construction and finishing materials	397,890	279,021
Metallurgy and manufacturing	159,374	225,757
Other	271,111	91,129
	4,540,466	2,898,043

NOTE 13 – OTHER ASSETS AND LIABILITIES

Other assets comprise:

	<i>2005</i>	<i>2004</i>
Prepayments	26,015	2,652
Property and equipment, net	4,759	1,835
Prepaid operating taxes	2,088	368
Intangible assets, net	5	6
Other assets	32,867	4,861

Other liabilities comprise:

	<i>2005</i>	<i>2004</i>
Operating taxes payable	17,825	8,061
Accrued additional compensation and other employee benefits	17,106	8,095
Debt securities issued	–	1,000
Other	–	974
Other liabilities	34,931	18,130

NOTE 14 – AMOUNTS DUE TO CREDIT INSTITUTIONS

Amounts due to credit institutions comprise:

	<i>2005</i>	<i>2004</i>
Current accounts	1,267	–
Time deposits and loans	3,620,254	1,487,167
Amounts due to credit institutions	3,621,521	1,487,167

As discussed in Note 19, the Bank had a significant concentration of time deposits and loans due to a related party bank.

(Thousands of Russian Rubles)

NOTE 15 – NET ASSETS ATTRIBUTABLE TO PARTICIPANTS

As of December 31, 2005, the authorized nominal statutory fund equals 1,456,000 RUB and is contributed by:

728,000 RUB	50%	LLC "Salerna"
728,000 RUB	50%	LLC "Centerryboproduct"

As of December 31, 2005, the statutory fund was registered and fully paid. The statutory fund of the Bank was contributed by the participants in Russian Rubles. Participants are entitled to vote at general meetings of participants in proportion to their share in the statutory fund.

In accordance with the Russian legislation, participants in limited liability companies may unilaterally withdraw from the company. In such cases the company will be obliged to pay the withdrawing participant's share of net assets of the company, determined on the basis of statutory accounting reports for the year of withdrawal, in cash or, subject to consent of the participant, by an in kind transfer of assets. The payment should be made no later than six months after the end of the year of the withdrawal. According to article 11 of the Federal law "On banks and banking activity", participants can not withdraw from banks formed as a limited liability company for three years from the bank registration date. The Bank was registered on June 17, 2003.

NOTE 16 – FINANCIAL COMMITMENTS AND CONTINGENCIES

Operating Environment

The Russian economy while deemed to be of market status continues to display certain characteristics consistent with that of a market in transition. These characteristics include, but are not limited to, relatively high inflation and the existence of currency controls which cause the national currency to be illiquid outside of Russia. The stability of the Russian economy will be significantly impacted by the government's policies and actions with regards to supervisory, legal, and economic reforms.

Legal

In the ordinary course of business, the Bank may be subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of the Bank's future operations.

Financial Commitments and Contingencies

As of December 31, 2005 and December 31, 2004 the Bank's financial commitments and contingencies comprised the following:

	<u>2005</u>	<u>2004</u>
Non-cancellable operating lease commitments		
Not later than 1 year	39,605	24,435
Later than 1 year	34,176	–
	<u>73,781</u>	<u>24,435</u>
Financial commitments and contingencies	<u>73,781</u>	<u>24,435</u>

(Thousands of Russian Rubles)

NOTE 17 – FINANCIAL RISK MANAGEMENT POLICIES

Management of risk is fundamental to the banking business and is an essential element of the Bank's operations. The main risks inherent in the Bank's operations are those related to credit exposures, liquidity, and market movements in interest rates and foreign exchange rates. A description of the Bank's risk management policies in relation to those risks follows.

Credit Risk

The Bank is exposed to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry and geographical segments. Such risks are monitored on a continuing basis and are subject to an annual or more frequent review.

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on and off-balance sheet exposures which are set by the Risk Management Committee and Management Board that meet at least once a week. Actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations and by changing these lending limits when appropriate. Exposure to credit risk is additionally mitigated in part by obtaining collateral and corporate and personal guarantees.

Credit-related commitments ensure that funds are available to a customer as required. Guarantees, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the credit risk as well.

Concentration

The geographical concentration of banking assets and liabilities follows.

	2005				2004			
	Russia	OECD	CIS and other foreign countries	Total	Russia	OECD	CIS and other foreign countries	Total
Assets								
Cash and cash equivalents	875,243	–	–	875,243	844,652	–	–	844,652
Trading securities	20,694	–	–	20,694	–	–	–	–
Amounts due from credit institution	287,690	–	–	287,690	55,251	–	–	55,251
Factoring advances	4,264,063	14,111	92,765	4,370,939	2,784,247	–	22,329	2,806,576
All other assets	42,363	–	–	42,363	17,425	–	–	17,425
	5,490,053	14,111	92,765	5,596,929	3,701,575	–	22,329	3,723,904
Liabilities								
Due to credit institutions	3,551,188	70,333	–	3,621,521	1,487,167	–	–	1,487,167
Settlements with clients on factoring	77,886	–	–	77,886	43,510	–	–	43,510
Time deposits of clients	30,930	–	–	30,930	705,553	–	–	705,553
All other liabilities	42,384	–	–	42,384	29,360	–	–	29,360
	3,702,388	70,333	–	3,772,721	2,265,590	–	–	2,265,590
Net balance sheet position	1,787,665	(56,222)	92,765	1,824,208	1,435,985	–	22,329	1,458,314

(Thousands of Russian Rubles)

NOTE 17 – FINANCIAL RISK MANAGEMENT POLICIES (CONTINUED)

Currency Risk

Currency risk is a risk that a financial instrument will change its value due to changes in currency exchange rates. Bank's financial position and cash flows are affected by fluctuations of foreign currency exchange rates.

The Risk Management Committee executes general control over the currency risks and sets limits on currency transactions performed by departments of the Bank. The Treasury and Electronic Settlement Department projects and analyzes open balance sheet and off-balance currency positions of the Bank.

The Bank's exposure to foreign currency exchange rate risk follows.

	2005					2004			
	Rubles	USD	EUR	Other	Total	Rubles	USD	EUR	Total
Assets:									
Cash and cash equivalents	874,116	893	185	49	875,243	841,638	64	2,950	844,652
Trading securities	20,694	–	–	–	20,694	–	–	–	–
Amounts due from credit institutions	200,912	86,778	–	–	287,690	55,251	–	–	55,251
Factoring advances	4,270,961	96,132	3,846	–	4,370,939	2,783,552	23,024	–	2,806,576
All other assets	42,186	177	–	–	42,363	17,369	–	56	17,425
	5,408,869	183,980	4,031	49	5,596,929	3,697,810	23,088	3,006	3,723,904
Liabilities:									
Amounts due to credit institutions	3,403,082	216,730	1,709	–	3,621,521	1,461,885	21,312	3,970	1,487,167
Settlements with clients on factoring	77,568	318	–	–	77,886	43,510	–	–	43,510
Time deposits of clients	30,930	–	–	–	30,930	705,553	–	–	705,553
All other liabilities	42,384	–	–	–	42,384	29,360	–	–	29,360
	3,553,964	217,048	1,709	–	3,772,721	2,240,308	21,312	3,970	2,265,590
Net balance sheet position	1,854,905	(33,068)	2,322	49	1,824,208	1,457,502	1,776	(964)	1,458,314

Liquidity Risk

Liquidity risk is a risk of encountering difficulties regarding receipt of funds required to return deposits and settle liabilities related to financial instruments when they mature.

The Bank's Risk Management Committee executes general control over the liquidity risks. The Treasury and Electronic Settlement Department is responsible for the day-to-day control. The respective liquidity risk management actions of the Bank include the following activities:

- daily liquidity projections;
- placement of funds in relation to terms of raised funds balances;
- on an ongoing basis, analysis of clients' cash flows in order to identify seasonal and other trends;
- stress-testing to analyze potential implications in case of adverse events.

(Thousands of Russian Rubles)

NOTE 17 – FINANCIAL RISK MANAGEMENT POLICIES (CONTINUED)

The contractual maturities of monetary assets and liabilities:

	2005							Total
	On demand	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Overdue	No defined maturity	
Assets								
Cash and cash equivalents	645,15	200,07	30,01	–	–	–	–	875,24
Trading securities	20,69	–	–	–	–	–	–	20,69
Amount due from credit institutions	–	15,03	185,66	85,22	1,76	–	–	287,69
Factoring advances	–	377,06	3,422,49	527,10	–	44,27	–	4,370,93
All other assets	–	10,53	9,49	3,86	13,70	–	4,764	42,363
	665,85	602,70	3,647,66	616,19	15,47	44,27	4,764	5,596,929
Liabilities								
Amounts due to credit institutions	1,26	632,79	1,778,96	1,208,48	–	–	–	3,621,52
Settlements with clients on factoring	–	15,14	62,74	–	–	–	–	77,88
Time deposits of clients	–	30,93	–	–	–	–	–	30,93
All other liabilities	–	34,93	–	–	7,45	–	–	42,62
	1,26	713,80	1,841,71	1,208,48	7,45	–	–	3,772,72
Net position	664,58	(111,10)	1,805,95	(592,29)	8,01	44,27	4,76	1,824,20
Accumulated gap	664,58	553,48	2,359,44	1,767,14	1,775,16	1,819,44	1,824,20	
	2004							
	On demand	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Overdue	No defined maturity	Total
Assets								
Cash and cash equivalents	844,65	–	–	–	–	–	–	844,65
Amounts due from credit institutions	–	54,97	–	273	–	–	–	55,251
Factoring advances	–	164,68	2,406,348	231,18	131	4,22	–	2,806,57
All other assets	–	3,02	–	–	12,56	–	1,841	17,425
	844,65	222,68	2,406,348	231,45	12,69	4,22	1,841	3,723,904
Liabilities								
Amounts due to credit institutions	–	614,33	772,733	100,09	–	–	–	1,487,167
Settlements with clients on factoring	–	43,51	–	–	–	–	–	43,51
Time deposits of clients	–	701,84	–	3,70	–	–	–	705,55
All other liabilities	–	1,00	–	–	–	–	28,360	29,360
	–	1,360,69	772,733	103,80	–	–	28,360	2,265,590
Net position	844,652	(1,138,009)	1,633,615	127,653	12,695	4,227	(26,519)	1,458,314
Accumulated gap	844,652	(293,357)	1,340,258	1,467,91	1,480,606	1,484,833	1,458,314	

Long-term credits and overdraft facilities are generally not available in Russia except for programs set up by international financial institutions. However, in the Russian marketplace, many short-term credits are granted with the expectation of renewing the loans at maturity. As such, the ultimate maturity of assets may be different from the analysis presented above. The maturity of obligatory reserve with the CBR was presented based on contractual maturity of related liabilities.

(Thousands of Russian Rubles)

NOTE 17 – FINANCIAL RISK MANAGEMENT POLICIES (CONTINUED)

Interest Rate Risk

The interest rate risk is related to changes in value of financial instruments driven by changes of interest rates. Asset and liability maturities, as well as the potential for replacement of interest liabilities at acceptable cost at maturity are important factors for assessment of the Bank's liquidity and level of dependence on changes in interest rates.

Risk Management Committee and Credit Committee within their authorities control interest rate risk by setting allowed ranges of interest rates and tariffs in respect to raised and placed funds.

Most of Bank's interest-bearing financial assets and liabilities have fixed interest rates. Furthermore, as specified above in the maturity analysis section, most of the Bank's assets and liabilities are relatively short-term. The Bank's management monitors interest margin of the Bank and believes that the Bank is not exposed to significant interest rate risks.

The Bank's average effective interest rates for monetary financial instruments follow.

	2005			2004		
	Rubles	USD	Other foreign currencies	Rubles	USD	Other foreign currencies
Cash and cash equivalents, time deposits	6.8%		–	–	–	–
Trading securities	6.3%	–	–	–	–	–
Amounts due from credit institutions, time deposits	9.0%	4.0%	–	–	–	–
Factoring advances	21.0%	15.8%	15.2%	21.2%	17.9%	–
Due to credit institutions, time deposits	4.8%	3.8%	3.5%	3.7%	1.6%	1.0%
Time deposits of clients	10.0%	–	–	7.6%	–	–

NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of IAS 32 "Financial Instruments: Disclosure and Presentation". Fair value is defined as the amount at which the instrument could be exchanged in a current transaction between knowledgeable willing parties on arm's length conditions, other than in forced sale or liquidation. As no readily available market exists for a large part of the Bank's financial instruments, judgment is necessary in arriving at fair value, based on current economic conditions and the specific risks attributable to the instrument. The estimates presented herein are not necessarily indicative of the amounts the Bank could realize in a market exchange from the sale of its full holdings of a particular instrument.

The following methods and assumptions are used by the Bank to estimate the fair value of these financial instruments:

Amounts Due from Credit Institutions and Factoring Advances

For assets maturing within three months, the carrying amount approximates fair value due to the relatively short-term maturity of these financial instruments. For longer-term assets, the interest rates applicable reflect market rates and, consequently, the fair value approximates the carrying amounts.

(Thousands of Russian Rubles)

NOTE 18 – FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Amounts Due to Customers and Credit Institutions

For balances maturing within three months the carrying amount approximates fair value due to the relatively short term maturity of these financial instruments. For longer term fixed interest bearing deposits and other borrowings the estimated fair value is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

The Bank's assets and operations are concentrated primarily in the Russian Federation. Management believes that, based upon its best estimates, as of December 31, 2005, and December 31, 2004, the fair value of substantially all Bank's assets and liabilities approximates their carrying values.

NOTE 19 – RELATED PARTIES

In accordance with IAS 24 "Related Party Disclosures", parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The Bank is a member of a holding headed by Limited Liability Partnership "Limited Liability Company "Financial Corporation NIKoil" and Company". The Bank is ultimately controlled by Mr. Nickolai A. Tsvetkov.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for the year are as follows:

	2005		2004	
	<i>Entities of holding headed by Limited Liability Partnership "Limited Liability Company "Financial Corporation NIKoil" and Company"</i>	<i>Key management personnel</i>	<i>Entities of holding headed by Limited Liability Partnership "Limited Liability Company "Financial Corporation NIKoil" and Company"</i>	<i>Key management personnel</i>
Cash and cash equivalents	133,220	–	831,363	–
Factoring advances outstanding at January 1	–	–	–	–
Factoring advances issued during the year	36,036	–	–	–
Factoring advances repayments during the year	–	–	–	–
Factoring advances outstanding at December 31, gross	36,036	–	–	–
Less: allowance for impairment at December 31	461	–	–	–
Factoring advances outstanding at December 31, net	35,575	–	–	–
Interest income on loans	36	–	–	–
Impairment of loans	461	–	–	–
Amounts due to credit institutions at December 31	2,774,051	–	1,457,106	–
Time deposits of clients at December 31	–	–	705,553	–
Interest expense	59,955	–	8,611	–
Salaries and employment benefits	–	8,831	–	4,756

(Thousands of Russian Rubles)

NOTE 19 – RELATED PARTIES (CONTINUED)**Terms and Conditions of Transactions with Related Parties**

Transactions with related parties are provided on market conditions in accordance with the set tariff schedule. Outstanding balances at year-end are unsecured and settlement occurs in cash. There have been no guarantees provided or received for any related party receivables.