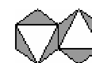
AK “ALROSA”

IFRS CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2008



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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Supervisory Council of Closed Joint Stock Company AK "ALROSA"

1 We have audited the accompanying consolidated financial statements of Closed Joint Stock Company AK "ALROSA" and its subsidiaries (the "Group") which comprise the consolidated balance sheet as at 31 December 2008 and the consolidated statement of income, 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. 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 as of 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

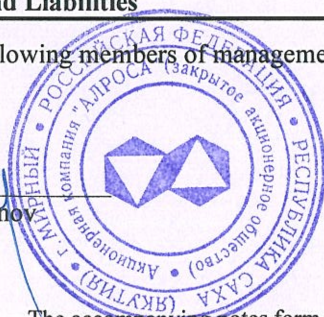
ZAO PricewaterhouseCoopers Audit

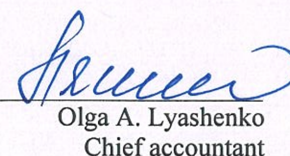
Moscow, Russian Federation
14 July 2009

Consolidated Balance Sheet

	Notes	31 December 2008	31 December 2007
Assets			
Non-current Assets			
Goodwill	5	1,439	1,439
Property, plant and equipment	8	178,074	155,696
Deferred tax assets	17	90	-
Investments in associates	5	1,813	1,613
Available-for-sale investments	5	512	786
Long-term accounts receivable	10	5,933	5,902
Restricted cash	7	31	133
Long-term deposits	7	11,285	-
Total Non-current Assets		**199,177**	**165,569**
Current Assets			
Inventories	9	32,307	22,208
Prepaid income tax		513	483
Current accounts receivable	10	25,509	12,564
Derivative financial instruments	6	-	5,106
Available-for-sale investments		-	12
Cash and cash equivalents	7	7,569	21,887
Total Current Assets		**65,898**	**62,260**
Total Assets		**265,075**	**227,829**
Equity			
Share capital	11	12,473	11,491
Share premium	11	10,431	-
Treasury shares	11	(24)	(16)
Deferred capital contribution	11	-	11,063
Retained earnings and other reserves		55,569	98,552
Equity attributable to shareholders of AK "ALROSA"		**78,449**	**121,090**
Non-Controlling Interest in Subsidiaries	11	**(431)**	**1,190**
Total Equity		**78,018**	**122,280**
Liabilities			
Non-current Liabilities			
Long-term debt	12	80,331	32,296
Provision for pension obligations	15	2,902	1,963
Other provisions	14	369	543
Deferred tax liabilities	17	-	6,265
Total Non-current Liabilities		**83,602**	**41,067**
Current Liabilities			
Short-term loans and current portion of long-term debt	13	54,068	49,452
Derivative financial instruments	6	22,444	-
Trade and other payables	16	19,942	11,876
Income tax payable		132	273
Other taxes payable	17	4,932	2,474
Dividends payable		1,937	407
Total Current Liabilities		**103,455**	**64,482**
Total Liabilities		**187,057**	**105,549**
Total Equity and Liabilities		**265,075**	**227,829**

Signed by the following members of management:



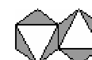


Sergey A. Vybornov
President

Olga A. Lyashenko
Chief accountant

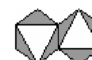
10 July 2009

The accompanying notes form an integral part of these consolidated financial statements



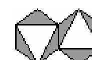
Consolidated Statement of Income

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Sales	18	91,082	90,734
Cost of sales	19	(52,555)	(51,441)
Royalty	17	(3,990)	(4,816)
Gross profit		**34,537**	**34,477**
General and administrative expenses	20	(6,379)	(5,266)
Selling and marketing expenses		(1,759)	(1,722)
Net (loss) / gain from foreign exchange forward contracts	6	(25,077)	5,149
Other operating income	21	573	3,912
Other operating expenses	22	(15,992)	(12,120)
Operating (loss) / profit		**(14,097)**	**24,430**
Finance income	23	5,056	6,093
Finance costs	24	(27,638)	(7,470)
Share of net profit of associates	5	676	936
(Loss) / profit before income tax		**(36,003)**	**23,989**
Income tax benefit / (expense)	17	3,236	(7,805)
(Loss) / profit for the year		**(32,767)**	**16,184**
Attributable to:			
Equity holders of AK “ALROSA”		(32,598)	15,981
Non-controlling interest		(169)	203
(Loss) / profit for the year		**(32,767)**	**16,184**



Consolidated Statement of Cash Flows

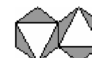
	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Net Cash Inflow from Operating Activities	25	**5,127**	**25,271**
Cash Flows from Investing Activities			
Purchase of property, plant and equipment		(27,333)	(24,153)
Proceeds from sales of fixed assets		402	562
Acquisition of available-for-sale investments		(42)	(93)
Proceeds from sale of available-for-sale investments		21	982
Acquisition of non-controlling interest in subsidiaries		(441)	(3,257)
Execution of the call option related to acquisition of “Rolant Investments Ltd.”		-	(8,217)
Proceeds from sale of gold mining operations		481	977
Net cash flow arising on disposal of subsidiary	5	-	257
Interest received		1,276	1,259
Transfer of cash on long-term deposit accounts		(11,285)	-
Dividends received from associates		660	632
Net Cash Used in Investing Activities		**(36,261)**	**(31,051)**
Cash Flows from Financing Activities			
Repayments of loans		(124,867)	(49,767)
Loans received		159,244	81,587
Distribution of retained earnings in favour of the Government of Russian Federation	11	(8,233)	-
Transaction costs relating to additional issue of shares	11	(170)	-
Interest paid		(9,010)	(6,123)
Purchase of treasury shares		(51)	(31)
Proceeds from sales of treasury shares		-	85
Dividends paid		(959)	(2,293)
Net Cash Inflow from Financing Activities		**15,954**	**23,458**
Net (Decrease) / Increase in Cash and Cash Equivalents		**(15,180)**	**17,678**
Cash and cash equivalents at the beginning of the year		21,887	4,209
Exchange gain on cash and cash equivalents		862	**-**
Cash and Cash Equivalents at the End of The Year		**7,569**	**21,887**



Consolidated Statement of Changes in Equity

	Attributable to shareholders of AK "ALROSA"									Non-controlling interest	Total equity
	Number of shares outstanding	Share capital	Share premium	Treasury shares	Deferred capital contribution	Other reserves	Retained earnings	Total			
Balance at 31 December 2006	**197,733**	**11,491**	**-**	**(130)**	**-**	**279**	**84,813**	**96,453**		**4,610**	**101,063**
Net gains arising from change in fair value of available-for-sale investments, net of income tax		-	-	-	-	329	-	329		-	**329**
Gain on disposal of available-for-sale investments recognised in the statement of income, net of income tax		-	-	-	-	(514)	-	(514)		-	**(514)**
Currency translation differences		-	-	-	-	(287)	-	(287)		-	**(287)**
Net loss recognised directly in equity		-	-	-	-	(472)	-	(472)		-	**(472)**
Profit for the year		-	-	-	-	-	15,981	15,981		203	**16,184**
Total recognised income for the year		-	-	-	-	(472)	15,981	15,509		203	**15,712**
Dividends (note 11)		-	-	-	-	-	(2,240)	(2,240)		-	**(2,240)**
Repayment of Grant		-	-	-	7,537	-	-	7,537		-	**7,537**
Reversal of provision for restoration liability		-	-	-	3,526	-	-	3,526		-	**3,526**
Disposal of treasury shares	1,987	-	-	114	-	-	191	305		-	**305**
Other changes in non-controlling interest (note 11)		-	-	-	-	-	-	-		(3,287)	**(3,287)**
Dividends paid by subsidiaries to minority shareholders (note 11)		-	-	-	-	-	-	-		(336)	**(336)**
Balance at 31 December 2007	**199,720**	**11,491**	**-**	**(16)**	**11,063**	**(193)**	**98,745**	**121,090**		**1,190**	**122,280**
Currency translation differences		-	-	-	-	440	-	440		-	**440**
Net income recognised directly in equity		-	-	-	-	440	-	440		-	**440**
Loss for the year		-	-	-	-	-	(32,598)	(32,598)		(169)	**(32,767)**
Total recognised loss for the year		-	-	-	-	440	(32,598)	(32,158)		(169)	**(32,327)**
Additional issue of shares (note 11)	72,726	982	10,431	-	(11,063)	-	-	350		-	**350**
Distribution of retained earnings in favor of the Government of Russian Federation (note 11)		-	-	-	-	-	(8,233)	(8,233)		-	**(8,233)**
Dividends (note 11)		-	-	-	-	-	(2,240)	(2,240)		-	**(2,240)**
Purchase of treasury shares	(140)	-	-	(8)	-	-	(43)	(51)		-	**(51)**
Purchase of non-controlling interest in OAO "Viluyskaya GES-3" (note 11)		-	-	-	-	(309)	-	(309)		(135)	**(444)**
Non-controlling interest in acquired net assets of OAO "NNGK Sakhaneftegaz" and OAO "Lenaneftegaz" (note 5)		-	-	-	-	-	-	-		(1,068)	**(1,068)**
Dividends paid by subsidiaries to minority shareholders (note 11)		-	-	-	-	-	-	-		(249)	**(249)**
Balance at 31 December 2008	**272,306**	**12,473**	**10,431**	**(24)**	**-**	**(62)**	**55,631**	**78,449**		**(431)**	**78,018**

The accompanying notes form an integral part of these consolidated financial statements



1. ACTIVITIES

The core activities of Closed Joint Stock Company AK “ALROSA” (“the Company”) and its subsidiaries (“the Group”) are the exploration and extraction of diamond reserves and the marketing and distribution of raw and cut diamonds. The Company was registered on 13 August 1992 as a closed joint stock company in the Republic of Sakha (Yakutia), which is located within the Russian Federation. The Group operates mining facilities in Mirny, Udachny, Aikhal, Nyurba and Anabar (located in Eastern Siberia). Licenses for the Group’s major diamond deposits expire between 2015 and 2022. Management believes the Group will be able to extend the licenses’ terms after they expire.

As at 31 December 2008 the Company’s principal shareholders are the governments of the Russian Federation (50.9 percent of shares) and the Republic of Sakha (Yakutia) (32.0 percent of shares). Information about the additional issue of shares of the Company is presented in note 11.

The Company is registered and its principal operating office is situated at 6, Lenin Street, Mirny, 678170, Republic of Sakha (Yakutia), Russia.

As a result of a significant downturn at the world diamonds market in the fourth quarter 2008 and depreciation of the Russian Rouble against US Dollar, the financial and liquidity position of the Group deteriorated. As at 31 December 2008 the Group’s current liabilities exceeded its current assets by RR’mln 37,557 principally as a result of loans and borrowings due to be repaid during one year after the balance sheet date and decrease of fair value of foreign exchange forward contracts. In the year ended 31 December 2008 the Group incurred loss related to revaluation of foreign exchange forward contracts totalling RR’mln 25,077 (see note 6) and exchange loss totalling RR’mln 17,812 (see note 24). Also in the year ended 31 December 2008 the amount of the Group’s net cash inflows from operating activity decreased by RR’mln 20,144 as compared with the year ended 31 December 2007.

The Government of the Russian Federation, which is a controlling shareholder of the Group, considers it as a strategic enterprise; accordingly, in December 2008 the Group was included in the list of 295 strategic entities to which the Government is going to provide support during the economic downturn. The Group has access to short-term and medium-term financing provided by the banks controlled by the Government to repay the Group’s existing loans. In addition the State Depository for Precious Metals and Stones of the Russian Federation committed to purchase diamonds from the Group during 2009 for a total amount of up to US$’mln 1,000. Besides the measures of support undertaken by the Government, currently the Group is conducting negotiations and investigating opportunities to sell certain of its non-core assets; also in 2009 the Group implemented policy for reduction and optimisation of its expenses, which includes reduction of certain social expenses and short-term employee’s benefits, suspension of mining works at certain small diamond deposits with relatively low profitability, optimisation of procurement policy and construction plans. Management believes that the Group is able to continue its activity in the foreseeable future. Accordingly, management believes that a going concern basis for the preparation of these consolidated financial statements is appropriate. However, in the longer term the ability of the Group to continue as a going concern will depend on the recovery of the world diamonds market, ability to continue financing its capital investments program and refinance its debts.

2. ACCOUNTING POLICIES

(a) Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) under the historical cost convention as modified by the revaluation of available-for-sale investments and financial assets held-for-trading. The consolidated financial statements are based on the statutory accounting records, with adjustments and reclassifications for the purpose of fair presentation in accordance with International Financial Reporting Standards. 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, except for early adoption of the revised IAS 27 and IFRS 3 (refer to notes 2 (b) and (c)).

Group companies incorporated in Russia maintain their statutory accounting records and prepare statutory financial reports in accordance with the Regulations on Accounting and Reporting of the Russian Federation (“RAR”) and their functional currency is the Russian Rouble (“RR”). Group companies incorporated in other countries maintain their statutory accounting records in accordance with relevant legislation and in the appropriate functional currency.

The Russian Federation has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation has ceased, effective from 1 January 2003 the Group no longer applies the provisions of IAS

29. 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.

The official US dollar to RR exchange rates as determined by the Central Bank of the Russian Federation were 29.38 and 24.55 as at 31 December 2008 and 31 December 2007, respectively. The official Euro to RR exchange rates as determined by the Central bank of the Russian Federation were 41.44 and 35.93 as at 31 December 2008 and 31 December 2007, respectively.

(b) Recent accounting pronouncements

In 2008 the Group has adopted all standards, amendments and interpretations which were effective as at 1 January 2008 and which are relevant to its operations.

The adoption of new interpretations IFRIC 11 "IFRS 2 - Group and Treasury Share Transactions, IFRIC 12 "Service Concession Arrangements" and IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" did not have any impact on the consolidated financial statements of the Group.

In 2008 the Group adopted the amendment to IAS 39 "Financial instruments: Recognition and measurement", which is effective from 1 July 2008. The amendment allows the reclassification of certain financial assets previously classified as "held for trading" or "available for sale" to another category under limited circumstances. Various disclosures are required where a reclassification has been made. Derivatives and assets designated as "at fair value through profit or loss" under the fair value option are not eligible for this reclassification. Reclassification cannot be applied retrospectively before 1 July 2008. This amendment did not have any impact on the consolidated financial statements of the Group.

In 2008 the Group early adopted the revised IAS 27 "Consolidated and Separate Financial Statements" and the revised IFRS 3 "Business Combinations".

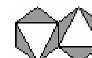
The revised IAS 27 requires an entity to attribute total recognised income and expense to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the previous version of the Standard required the excess losses to be allocated to the owners of the parent in most cases). The corresponding changes were made to the description of the "minority interest" category in these financial statements (see note 2 (c)). 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 revised IFRS 3 allows entities to choose to measure non-controlling interests using the method prescribed by the previous version of IFRS 3 (proportionate share of the acquiree's identifiable net assets) or 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 should be measured as the difference at the acquisition date between the fair value of any investment in the business held before acquisition, the consideration transferred and the net assets acquired. Accordingly, goodwill acquired in a business combination achieved in stages was determined in these consolidated financial statements at the date of acquisition rather than at the date of each exchange transaction. Acquisition-related costs should be accounted for separately from the business combination and therefore recognised as expenses rather than being included in goodwill. An acquirer shall 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 should be recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill.

The following new Standards and amendments to Standards are not yet effective and have not been applied in preparing these consolidated financial statements:

- IFRS 8 "Operating Segments", which is effective for annual periods beginning on or after 1 January 2009. The Standard replaces IAS 14 "Segment reporting". The Standard requires an entity to adopt the "management approach" to reporting of performance of its operating segments. Generally, the information to be reported would be what management uses internally for evaluating segment performance and deciding how to allocate resources to operating segments. Such information may be different from what is used to prepare the income statement and balance sheet. The IFRS therefore requires explanations of the basis on which the segment information is prepared and reconciliations to the amounts recognised in the income statement and balance sheet. The Group is currently assessing the impact of the application of IFRS 8 on its consolidated financial statements.

- Amendment to IAS 23 "Borrowing costs", which is effective for annual periods beginning on or after 1 January 2009. The main change to IAS 23 is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalise such borrowing costs as part of the cost of the asset. The revised standard applies prospectively to borrowing



costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. The Group is currently assessing what impact the amendment to IAS 23 will have on its consolidated financial statements.

- Amendment to IAS 1 “Presentation of Financial Statements”, which is 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.

- Amendment to IAS 32 and IAS 1 (“Puttable financial instruments and obligations arising on liquidation”), which is effective from 1 January 2009. The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability. Management does not expect the amendment to materially affect the Group’s consolidated financial statements.

- Amendment to IFRS 2 “Share-based Payment” (“Vesting Conditions and Cancellations”), which is 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. The application of the amended standard is not expected to materially affect the Group’s financial statements.

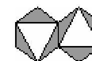
- Amendment to IFRS 1 and IAS 27 (“Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate”), which is effective for annual periods beginning on or after 1 January 2009. The amendment allows first-time adopters of IFRS to measure investments in subsidiaries, jointly controlled entities 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 recognized in profit or loss rather than as a recovery of the investment. The amendments will not have a material impact on the Group’s consolidated financial statements.

- Amendment to IAS 39 “Financial instruments: recognition and measurement” (“IAS 39”), which is effective for annual periods beginning on or after 1 July 2009. The amendment to IAS 39 clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The application of this amendment is not expected to materially affect the Group’s consolidated financial statements.

- Amendment to IFRS 7 “Financial Instruments: Disclosures” (“IFRS 7”), which is effective for annual periods beginning on or after 1 January 2009. The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity will be required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

- Amendments to IFRIC 9 and IAS 39 “Embedded Derivatives”, which are effective for annual periods ending on or after 30 June 2009. The amendments clarify that on reclassification of a financial asset out of the “at fair value through profit or loss” category, all embedded derivatives have to be assessed and, if necessary, separately accounted for.

- Improvements to International Financial Reporting Standards (issued in May 2008). 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

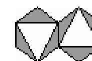


accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting. The Group does not expect the amendments to have any material effect on its consolidated financial statements except for reclassification of a portion of forward foreign exchange contracts, which is expected to be settled after 12 months from the balance sheet date, to non-current liabilities or assets.

- Improvements to International Financial Reporting Standards (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity's own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged. The Group does not expect the amendments to have any material effect on its consolidated financial statements.
- Amendments to IFRS 2 ("Share-based payment – Group cash-settled share-based payment transactions"), which are effective for annual periods beginning on or after 1 January 2010. The amendments provide a clear basis to determine the classification of share based payment awards in both consolidated and separate financial statements. They incorporate IFRIC 8 and IFRIC 11 into the standard and expand on the guidance given in IFRIC 11 to address plans that were previously not considered in the interpretation. The amendment also clarifies the defined terms in the Appendix to the standard.

The Group has not early adopted the following new interpretations:

- IFRIC 13 "Customer Loyalty Programmes" ("IFRIC 13"), which is effective for annual periods beginning on or after 1 July 2008. IFRIC 13 clarifies that where goods and services are sold with a customer loyalty incentive, the arrangement is a multi-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair value.
- IFRIC 15 "Agreements for the Construction of Real Estate" ("IFRIC 15"), which is effective for annual periods beginning on or after 1 January 2009. IFRIC 15 addresses diversity in accounting for real estate sales as some entities recognise revenue in accordance with IAS 18 "Revenue" (when the risks and rewards in the real estate are transferred) and others recognise revenue as the real estate is developed in accordance with IAS 11 "Construction Contracts". The interpretation clarifies which standard (IAS 18 or IAS 11) should be applied to particular transactions and is likely to mean that IAS 18 will be applied to a wider range of transactions. Entities that have previously recognised revenue from residential real estate sales under IAS 11 will be the most significantly affected and will probably be required to apply IAS 18.
- IFRIC 16 "Hedges of a Net Investment in a Foreign Operation" ("IFRIC 16") which is effective for annual periods beginning on or after 1 October 2008. This interpretation relates to the criteria required to apply hedge accounting in hedge of a net investment in a foreign operation in accordance with IAS 39.
- IFRIC 17 "Distributions of Non-cash assets to owners" ("IFRIC 17") which is effective for annual periods beginning on or after 1 July 2009. The interpretation provides guidance on accounting of distribution of assets other than cash (non-cash assets) as dividends to its owners acting in their capacity as owners. It also clarifies the situations, when entity gives its owners a choice of receiving either non-cash assets or a cash alternative.
- IFRIC 18 "Transfers of Assets from customers" ("IFRIC 18") which is effective for annual periods beginning on or after 1 July 2009. The interpretation clarifies the accounting for transfers of assets from customers, namely, the



circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers.

The Group is currently assessing what impact the new interpretations will have on its consolidated financial statements.

(c) Principles of consolidation

The Group comprises the Company and its subsidiaries. The effects of transactions between subsidiaries within the Group are eliminated and accounting policies of the subsidiaries and associates are conformed to those of the Company.

A subsidiary is an entity in which the Group has control through the holding of more than half of the voting rights or otherwise has the power to exercise control over the operations. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer 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 obtaining control. Costs directly attributable to the acquisition are recognised as expenses. The date of obtaining control is the acquisition date. The difference at the acquisition date between the fair value of any investment in the subsidiary held before acquisition, the consideration transferred and the net assets acquired represents goodwill. Any 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 non-controlling interest.

Non-controlling 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. Non-controlling interest forms a separate component of the Group’s equity.

The difference, if any, between the carrying amount of non-controlling interest and the amount paid to acquire it is recorded in equity.

Associates, over which the Group has a significant influence but not a control, are accounted for using the equity method. Significant influence is usually evidenced by the Group owning, directly or indirectly, between 20 percent and 50 percent of the voting share capital.

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, including any other unsecured receivables, 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.

(d) Property, plant and equipment

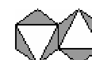
Property, plant and equipment comprises costs incurred in developing areas of interest as well as the costs related to the construction and acquisition of mining assets.

Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset’s carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the statement of income during the financial period in which they are incurred.

Expenditure related to geophysical analysis and exploration is expensed until it is determined to be probable that economically recoverable reserves exist. Exploration costs are classified as research and development expenses within operating expenses.

Gains and losses arising from the disposal of property, plant and equipment are included in the consolidated statement of income as incurred.

At each reporting date, management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher



of an asset's fair value less costs 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 statement of income. 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 asset's recoverable amount.

Depreciation and amortisation

Property, plant and equipment are depreciated from the date, when they are ready for the commencement of commercial mining activities at a specific area of interest.

Depreciation of buildings and land and improvements related to extraction of minerals is calculated on a units of production basis for each area of interest. For the purpose of this calculation at each reporting date management uses information with respect to volumes of diamonds containing ore reserves approved by the Ministry of Natural Resources of Russia. These quantities do not always correspond directly to generally accepted international categories of reserves but represent reserves for which geological and engineering data demonstrate with reasonable certainty to be recoverable in the future years from existing areas of interest under existing economic and operating conditions. Depreciation of assets not directly associated with production is calculated on a straight-line basis over their estimated useful life.

Summary of useful lives and alternative basis for depreciation:

	Assets related to extraction of minerals	**Other assets**
Buildings	Units of production	8-50 years
Land and improvements	Units of production	7-50 years
Plant and equipment	4-13 years	4-13 years
Transport	5-13 years	5-13 years
Other	4-17 years	4-17 years

The average depreciation rate for the property, plant and equipment depreciated on a units of production basis was 6.8 percent in the year ended 31 December 2008 (year ended 31 December 2007: 7.6 percent).

Local infrastructure assets

Local infrastructure assets constructed or purchased by the Group are included in the financial statements at historical cost and depreciated during their useful lives as set out above. These assets are an integral part of the Group's production activities.

Finance leases

Where the Group is a lessee in a lease which transferred substantially all the risks and rewards incidental to ownership to the Group, the assets leased are capitalised in property, plant and equipment at the commencement of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. The corresponding rental obligations, net of future finance charges, are included in debts. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The interest cost is charged to the statement of income over the lease period using the effective interest method. The assets acquired under finance leases are depreciated over their useful life or the shorter lease term if the Group is not reasonably certain that it will obtain ownership by the end of the lease term.

(e) ***Non-current assets classified as held for sale***

Non-current assets are classified in the balance sheet as "non-current assets held for sale" if their carrying amount will be recovered principally through a sale transaction within twelve months after the balance sheet date. Assets are reclassified when all of the following conditions are met: (a) the assets are available for immediate sale in their present condition; (b) the Group's management approved and initiated an active programme to locate a buyer; (c) the assets are actively marketed for a sale at a reasonable price; (d) the sale is expected within one year; and (e) it is unlikely that significant changes to the plan to sell will be made or that the plan will be withdrawn. Non-current assets classified as held for sale in the current period's balance sheet are not reclassified or re-presented in the comparative balance sheet to reflect the classification at the end of the current period.

Held for sale property, plant and equipment are measured at the lower of their carrying amount and fair value less costs to sell. Held for sale property, plant and equipment are not depreciated. Reclassified financial instruments are not subject to the write down to the lower of their carrying amount and fair value less costs to sell.

(f) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Provisions are reassessed at each reporting period, and are included

in the consolidated financial statements at their expected net present values using discount rates appropriate to the Group in the economic environment in the Russian Federation at each balance sheet date.

(g) Inventories

Inventories of diamonds, extracted ore and concentrates, mining and construction stores and consumable supplies are valued at the lower of cost or net realisable value. Cost of inventory is assigned using weighted average cost formula.

Cost of extracted ore and concentrates is calculated using the quantities determined based on surveyors' measurements of the volumes of ore and concentrates remaining at the period end. Cost of inventories include those directly attributable to mining the diamonds, extracting the ore and producing concentrates, and those directly attributable to bringing mining and construction stores and consumable supplies to their present location and condition. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

(h) Investments

The Group classifies its investments into the following categories: trading, held-to-maturity or available-for-sale. Investments that are acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as trading investments and included in current assets. Investments with a fixed maturity quoted in an active market that the management has the intent and ability to hold to maturity are classified as held-to-maturity and are included in non-current assets except for amounts maturing within twelve months from the reporting date. During the years ended 31 December 2008 and 31 December 2007, the Group did not hold any investments classified as held-to-maturity or trading (except for derivative financial instruments held for trading as described further below). Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; these are included in non-current assets unless management has expressed the intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets. Management determines the appropriate classification of its investments at the time of the purchase and reviews such designation on a regular basis.

Purchases of available-for-sale investments on public financial markets are recognised on the settlement date, which is the date that the investment is delivered to the Group. The available-for sale investments are initially recognised at fair value plus transaction costs. Available-for-sale investments are subsequently carried at fair value. Unrealised gains and losses arising from changes in the carrying value of these investments are included in the fair value reserve in equity in the period in which they arise. Realised gains and losses from the disposal of available-for-sale investments or impairment losses, if any, are included in the consolidated statement of income in the period in which they arise.

Available-for-sale investments principally comprise non-marketable securities, which are not publicly traded or listed on the Russian stock exchange. For these investments, fair value is estimated by reference to a variety of methods including those based on their earnings and those using the discounted value of estimated future cash flows. In assessing the fair value, management makes assumptions that are based on market conditions existing at each balance sheet date. Investments in equity securities that are not quoted on a stock exchange, and where fair value cannot be estimated on a reasonable basis by other means, are stated at cost less impairment losses.

Sale and repurchase agreements

Sale and repurchase agreements are treated as secured financing transactions. Investments sold under sale and repurchase agreements are not derecognised. The corresponding liability is presented within amounts due to banks or other borrowed funds.

(i) Derivative financial instruments

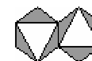
As part of trading activities the Group is also party to derivative financial instruments, primarily forward foreign exchange contracts. The Group's policy is to measure these instruments at fair value, with resultant gains or losses being reported within the consolidated statement of income. Derivatives are not accounted for as hedges.

(j) Components of cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks and instruments with maturity at the date of inception of less than three months, which are considered by the Group at the time of deposit to have minimal fair value and default risks.

(k) Income taxes

Income taxes have been provided for in the consolidated financial statements in accordance with legislation enacted or substantively enacted by the balance sheet date. The income tax charge (benefit) comprises current tax and deferred tax and is recognised in the income statement except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.



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.

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.

The Group controls reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains at their disposal. The Group does not recognise deferred tax liabilities on such temporary differences except to the extent that management expects the temporary differences to reverse in the foreseeable future.

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 more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the balance sheet date and any known court or other rulings on such issues. 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.

(l) Foreign currencies

Monetary assets and liabilities, which are held by the Group entities and denominated in foreign currencies at 31 December 2008 and 31 December 2007, are translated into Russian Roubles at the official exchange rate prevailing at that date. Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transaction. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currency are recognised in the consolidated statement of income.

The balance sheets of foreign subsidiaries are translated into Russian Roubles at the exchange rate prevailing at the respective reporting dates. Statements of operations of foreign entities are translated at the average exchange rate for the operating period. Exchange differences arising from the translation of the net assets of foreign subsidiaries are recognised as translation differences and included in the translation reserve in equity.

(m) Revenue recognition

Revenues are recognised when goods are shipped to the customer, as this is the date on which the risks and rewards of ownership are transferred to the customer. Sales are shown net of VAT and export duties, and after eliminating sales within the Group.

Revenue for "bill and hold" sales, in which delivery of goods is delayed at the buyer's request but the buyer takes title and accepts billing, is recognised, provided:

- it is probable that delivery will be made;
- the item is on hand, identified and ready for delivery to the buyer at the time the sale is recognised;
- the buyer specifically acknowledges the deferred delivery instructions; and
- the usual payment terms apply.

Revenue is not recognised when there is simply an intention to acquire the goods in time for delivery.

Revenue from rendering of transport services is recognised in financial statements in the period when the services are rendered.

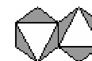
Interest income is recognised on accrual basis that takes into account the effective yield on the asset.

Dividend income is recognised when the shareholder's right to receive payment is established and inflow of economic benefits is probable.

(n) Measurement of trade and other receivables

Trade and other receivables are carried at amortised cost using the effective interest method.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. The primary factors that the Group



considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any portion or instalment 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; or
- the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

If the terms of an impaired financial asset held at amortised cost are renegotiated or otherwise modified because of financial difficulties of the counterparty, impairment is measured using the original effective interest rate before the modification of terms.

Impairment losses are always recognised through an allowance account to write down the asset’s carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. 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 foreclosure is probable.

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 (such as an improvement in the debtor’s credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss.

Uncollectible assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to impairment loss account in the statement of income.

(o) 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 a current asset and liability, except for VAT related to certain assets under construction included within non-current assets. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

(p) Borrowings

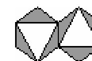
Borrowings are recognised initially at fair value, net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective yield method; any difference between the amount at initial recognition and the redemption amount is recognised as interest expense over the maturity period of the borrowings. Borrowing costs (the interest) are expensed as incurred.

(q) Pension and other post-retirement benefits

In the normal course of business the Group contributes to the Russian Federation State pension plan on behalf of its employees. Mandatory contributions to the State pension plan, which is a defined contribution plan, made on behalf of employees directly involved in production of diamonds, are included within wages, salaries and other staff costs in cost of production and apportioned between work-in-process (inventory of diamonds and ores and concentrates) and cost of sales. Mandatory contributions to the State pension plan made on behalf of other employees, are expensed as incurred and included within wages, salaries and other staff costs in general and administrative expenses.

The Group also operates a defined benefit pension plan. Pension costs are recognised using the projected unit credit method. The cost of providing pensions is charged to the relevant category in the consolidated statement of income so as to spread the regular cost over the service lives of employees. The pension obligation is measured at the present value of the estimated future cash outflows using the interest rates on governmental securities, which have the terms to maturity approximating the terms of the related liability. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of the greater of 10 percent of the value of plan assets or 10 percent of the defined benefit obligations are charged or credited to the statement of income over the employees’ expected average remaining working lives.

Pension Fund “Almaznaya Osen” administers the Group’s defined benefit plan. The amount of pension benefit that an employee will receive on retirement is usually dependent on one or more factors such as age, years of service and average salary for the year preceding the year of retirement. The liability recognised in the balance sheet in respect of the defined



benefit pension plan is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses. The Group contributes funds to the Pension Fund "Almaznaya Osen", which invests them in governmental securities and other financial instruments. These investments, which represent the majority of assets of Pension Fund "Almaznaya Osen", are considered the pension fund plan assets, as these assets are available to be used only to pay or fund employee benefits, are not available to the Group's own creditors (even in bankruptcy), and cannot be returned to the Group, unless either the remaining assets of the Pension Fund are sufficient to meet all the related employee benefit obligations of the pension plan, or the assets are returned to the Group to reimburse it for employee benefits already paid.

(r) Social costs

Discretionary and voluntary payments made to support social programs and related operations are expensed as incurred.

(s) Non-cash transactions

Non-cash transactions are measured at the fair value of the consideration received or receivable.

Non-cash transactions have been excluded from the operating, investing and financing activities components in the accompanying consolidated statement of cash flows.

(t) Equity

Share capital

Share capital consists of ordinary shares, which are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

Treasury shares

Where the Group companies purchase the Company's equity share capital, the consideration paid including any attributable transaction costs is deducted from total equity as treasury shares until they are re-sold. Where such shares are subsequently sold, any consideration received net of income taxes is included in equity. Treasury shares are recorded at weighted average cost. The gains (losses) arising from treasury share transactions are recognised as a movement in the consolidated statement of changes in equity, net of associated costs including taxation.

Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are approved at the General Meeting of Shareholders before or on the balance sheet date.

(u) Segment reporting

Business segments (primary segments) provide products or services that are subject to risks and returns that are different from those of other business segments. Geographical segments (secondary segments) provide products or services within a particular economic environment that is subject to risks and returns that are different from those of components operating in other economic environments.

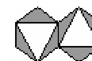
(v) Critical accounting estimates and judgements in applying accounting policies

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements preparation and the reported amounts of revenues and expenses during the reporting year. Actual results may differ from such estimates. In particular, information about significant areas of estimation and critical judgments in applying accounting policies made by management in preparing these financial statements include:

Impairment provision for receivables. The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, amount receivable is written off against associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of



current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Impairment of property, plant and equipment. The estimation of forecast cash flows involves the application of a number of significant judgements and estimates to certain variables including volumes of production, prices on diamonds, operating costs, capital investments, diamonds reserves estimates and macroeconomic factors such as inflation and discount rates. In addition, judgement is applied in determining the cash generating units assessed for impairment.

The information about impairment test of its property, plant and equipment conducted by the Group as at 31 December 2008 and the sensitivity of its results to assumptions used are disclosed in note 8.

Tax legislation. Russian tax, currency and customs legislation is subject to varying interpretations (see note 26).

Useful lives of property, plant and equipment. Items of property, plant and equipment are stated at cost less accumulated depreciation. The estimation of the useful life of an item of property, plant and equipment is a matter of management judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustments to future depreciation rates.

Management believes diamond production licenses will be extended past their current expiration dates at insignificant additional costs. Because of the extensions, the assets are depreciated over their useful lives beyond the end of the current license term.

In the year ended 31 December 2008, if the estimated useful lives of property, plant and equipment had been 10 percent longer / shorter with all other variables held constant, depreciation charge for the year would have been RR’mln 670 (year ended 31 December 2007 – RR’mln 955) lower / higher.

Classification of production licenses. Management treats cost of production licenses as an integral part of acquisition cost of tangible mining properties, i.e. land where the respective area of interest is located; accordingly, production licenses are included in property, plant and equipment in these consolidated financial statements.

Pension benefits. The present value of the pension obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost (income) for pensions include the discount rate. Any changes in these assumptions will impact the carrying amount of pension obligations. The Group determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the pension obligations. In determining the appropriate discount rate, the Group considers the yield to maturity on federal loan bonds denominated in the currency in which the benefits will be paid, and with terms to maturity approximating the terms of the related pension liability. Other key assumptions for pension obligations are based in part on current market conditions (see note 15).

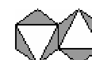
3. FINANCIAL RISK MANAGEMENT

The Group’s activities expose it to a variety of financial risks, including market risk (currency risk, fair value interest rate risk and cash flow interest rate risk), credit risk and liquidity risk. The Group’s overall risk management focuses on minimising potential adverse effects on the financial performance of the Group. The Group uses derivative financial instruments to manage its risk exposures (primarily foreign exchange risk).

Cash flow and fair value interest rate risk. The Group’s principal interest rate risk arises from interest-bearing long-term cash and cash equivalents and long-term and short-term borrowings. Borrowings issued at variable rates and cash deposits at the refinancing rate of the Central Bank of the Russian Federation expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. During 2008 and 2007, the Group’s borrowings at variable rates were denominated in US dollars and Russian Roubles (see notes 12 and 13).

To mitigate this risk, the Group’s treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms. Management does not have a formal policy of determining how much of the Group’s exposure should be to fixed or variable rates. However, at the time of raising new debts management uses its judgment to decide whether it believes that a fixed or variable rate would be more favorable over the expected period until maturity. In order to reduce the Group’s cash flow interest rate risk exposure associated with the RR denominated floating rate loans, in 2008 the Group entered into US$ / RR cross currency interest rate swap transactions (see note 6). The Group currently does not use derivative instruments to hedge its fair value interest rate risk.

At 31 December 2008, if the refinancing rate of the Central Bank of the Russian Federation had been 30 percent



higher/lower with all other variables held constant, post-tax profit for the year would have been RR’mln 276 (at 31 December 2007 - nil) higher/lower, as result of higher/lower interest income on long-term deposits.

At 31 December 2008, if interest rates on US dollar-denominated borrowings had been 20 percent higher/lower with all other variables held constant, post-tax profit for the year would have been RR’mln 41 (at 31 December 2007 - RR’mln 36) lower/higher, mainly as result of higher/lower interest expense on floating rate borrowings.

At 31 December 2008, if interest rates on Russian Roubles-denominated borrowings had been 30 percent higher/lower with all other variables held constant, post-tax profit for the year would have been RR’mln 266 (at 31 December 2007 - RR’mln 14) lower/higher, mainly as result of higher/lower interest expense on floating rate borrowings.

Foreign exchange risk. The Group exports production to European and other countries and attracts a substantial amount of foreign currency denominated borrowings and is, thus, exposed to foreign exchange risk arising from various contracts, primarily with respect to the US dollar and to a lesser extent the Euro. The Group manages its foreign exchange risk arising from future sale transactions adjusted for other transactions (foreign currency denominated borrowings and purchases) primarily using forward contracts (see note 6). The Group does not account for these derivative financial instruments as hedges.

The table below summarised the Group’s exposure to foreign currency exchange rate risk at the balance sheet date:

	US Dollar		**Euro**		**Other foreign currency**	
	31 December		**31 December**		**31 December**	
	2008	**2007**	**2008**	**2007**	**2008**	**2007**
Assets						
Cash and cash equivalents	1,029	8,456	29	21	167	83
Trade and other receivables	5,325	4,692	367	386	1	-
Derivative financial instruments	-	5,106	-	-		-
	6,354	**18,254**	**396**	**407**	**168**	**83**
Liabilities						
Trade and other payables	870	510	32	95	-	-
Borrowings	63,055	72,568	181	287	-	-
Derivative financial instruments	22,444	**-**	**-**	**-**	**-**	**-**
	86,369	**73,078**	**213**	**382**	**-**	**-**

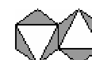
At 31 December 2008, if the Russian Rouble had weakened / strengthened by 20 percent against the US dollar with all other variables held constant, post-tax profit for the year would had been RR’mln 19,138 (at 31 December 2007 – RR’mln 19,964) lower / higher, mainly as a result of losses / gains from revaluation of derivative financial instruments and foreign exchange losses / gains on translation of US dollar-denominated borrowings and accounts payable partially offset by foreign exchange gains / losses on translation of US dollar-denominated cash and cash equivalents and accounts receivable.

At 31 December 2008, if the Russian Rouble had weakened/strengthened by 20 percent against the Euro with all other variables held constant, post-tax profit for the year would had been RR’mln 56 (at 31 December 2007 – RR’mln 4) higher/lower, mainly as a result of foreign exchange gains/losses on translation of Euro-denominated trade and other receivables.

Equity investments price risk. The Group is exposed to movements in the equity securities prices because of available-for-sale investments held by the Group. The major part of available-for-sale investments held by the Group has no active market. To manage price risk arising from available-for-sale investments, the Group diversifies its investment portfolio.

At 31 December 2008, if the prices of available-for-sale investments held by the Group had been 20 percent higher/lower with all other variables held constant, its equity would have been RR’mln 102 (at 31 December 2007 – RR’mln 157) higher/lower and there would have been no impact on post-tax profit.

Credit risk. Credit risk arises from cash and cash equivalents, as well as credit exposures to customers, including outstanding trade receivables, loans issued, derivative financial instruments and other financial assets. Cash and cash equivalents are deposited only with banks that are considered by the Group at the time of deposit to have minimal risk of default. Due to the fact that most of the counterparties do not have individual external credit rating, the Group has policies in place to ensure that sales of products and services and loans issuing are made to counterparties with positive credit history. These procedures include assessment of financial position, past experience and other factors. To support certain receivables from customers of diamonds the Group may require either collateral, or bank or any other third party’s guarantee. Although collections of accounts receivable could be influenced by economic factors affecting these customers, management believes there is no significant risk of loss to the Group beyond the provisions already recorded.



The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

Liquidity risk. Liquidity risk management includes maintaining sufficient cash balances, the availability of funding from an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, Group management maintains flexibility in funding by ensuring availability under committed credit lines and expected cash flows from operating activities. Management monitors a rolling forecast of the Group's liquidity reserve (comprises undrawn borrowing facility and cash and equivalents) on the basis of expected cash flow. This is carried out at Group level monthly and annually. In addition, the Group's liquidity management policy involves projecting cash flows in major currencies and considering the level of liquid assets necessary to meet any net cash outflows and maintaining debt financing plans.

The table below analyses the Group's liabilities for financial instruments into relevant maturity grouping based on the remaining period at the balance sheet to contractual maturity date.

	Within 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 years and thereafter
31 December 2008					
Borrowings	66,985	54,344	9,157	15,083	18,205
Derivative financial instruments	6,872	10,782	10,969	-	-
Trade payables	6,749	-	-	-	-
Accounts payable of OAO "NNGK Sakhaneftegaz" to the companies of former "YUKOS" Group	3,688	-	-	-	-
Current accounts of third parties in OOO "MAK-Bank"	1,090	-	-	-	-
Interest payable	790	-	-	-	-
Payables to associates	91	-	-	-	-
Other payables and accruals	570	-	-	-	-
	86,835	**65,126**	**20,126**	**15,083**	**18,205**
31 December 2007					
Borrowings	52,273	13,713	2,499	2,679	22,148
Trade payables	3,728	-	-	-	-
Current accounts of third parties in OOO "MAK-Bank"	658	-	-	-	-
Interest payable	565	-	-	-	-
Payables to associates	89	-	-	-	-
Other payables and accruals	508	-	-	-	-
	57,821	**13,713**	**2,499**	**2,679**	**22,148**

As the amounts included in the table are contractual undiscounted cash flows which include future interest payments, these amounts will not reconcile to the amounts disclosed on the balance sheet for borrowings and derivative financial instruments.

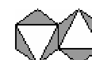
In order to meet the liquidity requirements of the Group increased as a result of the recent downturn at the world diamonds market, management relies on the ability of the Group to raise funds from the institution controlled by the Russian Government. Besides that management is also investigating opportunities to sell certain non-core assets of the Group and implementing policy for optimisation of its expenses (see note 1).

Capital risk management. The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group is subject to external capital requirements imposed by banks on certain loans, which require mostly maintaining the net debt / EBITDA, gearing and EBITDA / interest expense ratios at the specified levels. At 31 December 2008 the Group breached requirements relating to certain financial ratios of the long-term loan of RR'mln 3,966 (see note 12). During 2008 the Group complied with external capital requirements imposed by banks on all other loans and borrowings.

The Group monitors capital mostly on the basis of the gearing ratio for the purpose of maintaining major debt parameters at the optimal level. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings, as shown in the consolidated balance sheet, less cash and cash equivalents and long-term deposits. Total capital is calculated as equity, as shown in the consolidated balance sheet, plus net debt.



The gearing ratios at 31 December 2008 and 31 December 2007 were as follows:

	31 December 2008	31 December 2007
Total borrowings	134,399	81,748
Less: cash and cash equivalents and long-term deposits	(18,854)	(21,887)
Net debt	115,545	59,861
Total equity	78,018	122,280
Total capital	193,563	182,141
Gearing ratio	60%	33%

4. FINANCIAL INSTRUMENTS BY CATEGORY

ASSETS	Loans and receivables		Available for sale		Assets at fair value through the profit and loss-held for trading		Total	
	31 December		31 December		31 December		31 December	
	2008	2007	2008	2007	2008	2007	2008	2007
Non-current assets								
Restricted cash	31	133	-	-	-	-	31	133
Long-term deposits	11,285	-	-	-	-	-	11,285	-
Available-for-sale investments	-	-	512	786	-	-	512	786
Receivables from associates	2,990	2,734	-	-	-	-	2,990	2,734
Loans issued	1,616	1,303	-	-	-	-	1,616	1,303
Notes receivable	636	654	-	-	-	-	636	654
Other long-term receivables	8	24	-	-	-	-	8	24
	16,566	4,848	512	786	-	-	17,078	5,634
Current assets								
Trade receivables for supplied diamonds	12,787	65	-	-	-	-	12,787	65
Loans issued	4,508	4,063	-	-	-	-	4,508	4,063
Receivables from associates	1,108	486	-	-	-	-	1,108	486
Notes receivable	168	922	-	-	-	-	168	922
Receivables for sale of gold mining operations	-	555	-	-	-	-	-	555
Receivables for sale of treasury shares	251	251	-	-	-	-	251	251
Other receivables	3,355	2,289	-	-	-	-	3,355	2,289
Derivative financial instruments	-	-	-	-	-	5,106	-	5,106
Available-for-sale investments	-	-	-	12	-	-	-	12
Cash and cash equivalents	7,569	21,887	-	-	-	-	7,569	21,887
	29,746	30,518	-	12	-	5,106	29,746	35,636
	46,312	**35,366**	**512**	**798**	**-**	**5,106**	**46,824**	**41,270**

LIABILITIES	Liabilities at fair value through the profit and loss-held for trading		Liabilities at amortised cost		Total	
	31 December		31 December		31 December	
	2008	2007	2008	2007	2008	2007
Non-current liabilities						
Long-term debt	-	-	80,331	32,296	80,331	32,296
	-	-	80,331	32,296	80,331	32,296
Current liabilities						
Short-term loans and current portion of long-term debt	-	-	54,068	49,452	54,068	49,452
Derivative financial instruments	22,444	-	-	-	22,444	-
Trade payables	-	-	6,749	3,728	6,749	3,728
Accounts payable of OAO “NNGK Sakhaneftegaz” to the companies of former “YUKOS” Group	-	-	3,688	-	3,688	-
Current accounts of third parties in OOO “MAK-Bank”	-	-	1,090	658	1,090	658
Interest payable	-	-	790	565	790	565
Payables to associates	-	-	91	89	91	89
Other payables and accruals	-	-	570	508	570	508
	22,444	-	67,046	55,000	89,490	55,000
	22,444	**-**	**147,377**	**87,296**	**169,821**	**87,296**

5. GROUP STRUCTURE AND INVESTMENTS

The Company's significant consolidated subsidiaries are as follows:

Name	Principal activity	Country of Incorporation	Percentage of ownership interest held	
			31 December 2008	**31 December 2007**
"ALROSA Finance" S.A.	Financial services	Luxembourg	100	100
"Sunland Trading" S.A.	Diamonds trading	Switzerland	100	100
"Arcos Belgium" N.V.	Diamonds trading	Belgium	100	100
ZAO "Irelyakhneft"	Oil production	Russia	100	100
OAO "ALROSA-Gaz"	Gas production	Russia	100	100
OOO "ALROSA-VGS"	Capital construction	Russia	100	100
OAO "Almazy Anabara"	Diamonds production	Russia	100	100
OAO "Investment Group ALROSA"	Investing activity	Russia	100	100
OAO "Viluyskaya GES-3"	Electricity production	Russia	98	93
OAO "Severalmaz"	Diamonds production	Russia	95	95
ZAO "Geotransgaz"	Gas production	Russia	90	90
ZAO "Urengoyskaya Gazovaya Company"	Gas production	Russia	90	90
OOO "MAK Bank"	Banking activity	Russia	88	88
OAO "ALROSA-Nyurba"	Diamonds production	Russia	88	88
OAO "NNGK Sakhaneftegaz"	Oil & gas industry	Russia	50	50

As at 31 December 2008 and 31 December 2007 the percentage of ownership interest of the Group in subsidiaries is equal to the percentage of voting interest.

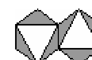
Consolidation of OAO "NNGK Sakhaneftegaz"

In February 2006 the Company acquired 50.4 percent of the voting shares of OAO "NNGK Sakhaneftegaz", a holding oil and gas company operating in the Republic of Sakha (Yakutia), for a total purchase consideration of RR'mln 493 (the cost of this investment represented a single payment in cash). The major asset of OAO "NNGK Sakhaneftegaz" is 85 percent interest in OAO "Lenaneftegaz", a company providing drilling services and services of operator at Talakan oil deposit located in the Republic of Sakha (Yakutia). After this acquisition, minority shareholders of OAO "NNGK Sakhaneftegaz" initiated claims against the Company and, as a result, the Arbitration Court of the Republic of Sakha (Yakutia) prohibited the Company to participate in the election of the Board of Directors of OAO "NNGK Sakhaneftegaz". Due to this court decision, the Company was not able to exercise control or significant influence over the financial and operating activity of OAO "NNGK Sakhaneftegaz". Accordingly OAO "NNGK Sakhaneftegaz" was not consolidated in the financial statements of the Group for the years ended 31 December 2006 and 31 December 2007. The investment of the Company in OAO "NNGK Sakhaneftegaz" was recognised at 31 December 2006 and 31 December 2007 within available-for-sale investments at cost. Management believed that the fair value of this investment could not be estimated on a reasonable basis because there was no active market for these shares; also management did not have the full information in respect to the legal status and physical conditions of assets controlled by OAO "NNGK Sakhaneftegaz" and was not able to reliably estimate its liabilities and contingent liabilities.

In March 2008 the Company resolved its conflict with minority shareholders of OAO "NNGK Sakhaneftegaz" and appointed new management to this company. Accordingly, as at that date the Company obtained control over the financial and operating activity of OAO "NNGK Sakhaneftegaz".

Details of fair values of the assets and liabilities of OAO "NNGK Sakhaneftegaz" as at the date when the Company obtained control over its financial and operating activity are as follows:

Property, plant and equipment	1,351
Available-for-sale investments	195
Inventories	702
Trade and other receivables	430
Cash and cash equivalents	8
Trade and other payables	(4,792)
Net assets	**(2,106)**
Non-controlling interest in fair value of the acquired net assets	**(1,068)**
Goodwill arising from the acquisition	**1,531**
Investment in OAO "NNGK Sakhaneftegaz"	**493**



Management believes that the fair value of investment in OAO “NNGK Sakhaneftegaz” at the date when the Company obtained control over its financial and operating activity approximates its cost.

The acquired entity was not preparing financial statements in accordance with IFRS. Therefore, it was impracticable to disclose IFRS carrying amounts of the assets and liabilities immediately before acquisition.

OAO “NNGK Sakhaneftegaz” contributed revenue of RR’mln 971 and net loss of RR’mln 237 to the Group for the period from the date of acquisition to 31 December 2008. If the Group would have obtained control over financial and operating activity of OAO “NNGK Sakhaneftegaz” on 1 January 2008, the acquired entity would have contributed revenue of RR’mln 1,015 and net loss of RR’mln 274 to the Group for the year ended 31 December 2008.

As at the date when the Company obtained control over financial and operating activity of OAO “NNGK Sakhaneftegaz” the gross contractual amounts receivable in OAO “NNGK Sakhaneftegaz” totalled RR’mln 1,560, including loans issued totalling RR’mln 193 and trade and other receivables totalling RR’mln 1,367. Receivables in the amount of RR’mln 1,130 were not expected to be collected.

Before 2006 OAO “NNGK Sakhaneftegaz” was controlled by OAO “NK YUKOS”, since then the entity has significant amount of overdue accounts payable to the companies of “YUKOS” Group, most of which are now controlled by OAO “NK Rosneft”, totalling RR’mln 3,688 (payable on demand). In November 2008 the state authorities initiated the bankruptcy procedures in relation to OAO “NNGK Sakhaneftegaz” in accordance with the legal claim of OAO “NK Rosneft”. At the date of these consolidated financial statements the supervision procedure (the first stage of bankruptcy procedure) is conducted in OAO “NNGK Sakhaneftegaz”. At this stage management of OAO “NNGK Sakhaneftegaz” continues to control the financial and operating activity of the entity. Currently management of OAO “NNGK Sakhaneftegaz” performs analysis of the entity’s debts and started negotiations with creditors in respect of their restructuring. The future financial position and performance of OAO “NNGK Sakhaneftegaz” depend significantly on the result of these negotiations.

The recoverable amount of goodwill arising from the acquisition was determined on the basis of the management’s estimation of future cash flows of OAO “NNGK Sakhaneftegas” and OAO “Lenaneftegaz”. The pre-tax discount rate used in the analysis was 20.1 percent, which presented the weighted average cost of capital for the Group as at 31 December 2008. Based on results of the analysis impairment loss totalling RR’mln 1,531 was recognised within other operating expenses (see note 22).

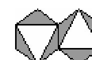
Disposal of OAO “Yakutskgeofizika”

In October 2007 the Group sold 75 percent of the voting shares of OAO “Yakutskgeofizika” for a total cash consideration of RR’mln 264. Net assets of OAO “Yakutskgeofizika” at the date of disposal were as follows:

Property, plant and equipment	335
Trade and other receivables and other assets	120
Cash and cash equivalents	7
Trade and other payables and other liabilities	(252)
Minority interest in subsidiary of “Yakutskgeofizika”	(50)
Net assets	**160**
Gain on disposal	104
Total consideration	**264**
Net cash flow arising on disposal:	
Cash consideration received	264
Cash and cash equivalents disposed of	(7)
	257

Associates

Name		Country of incorporation	Percentage of ownership interest held as at 31 December		Carrying value of investment as at 31 December		Group’s share of net profit (loss) for the year ended 31 December	
			2008	**2007**	**2008**	**2007**	**2008**	**2007**
“Catoca Mining Company Ltd”	(1)	Angola	33	33	1,558	1,382	670	934
“Escom-ALROSA Ltd”	(2)	United Kingdom	44	44	-	-	-	-
OAO “Almazny Mir”		Russia	47	47	173	174	3	3
Other		Russia			82	57	3	(1)
					1,813	1,613	676	936



As at 31 December 2008 and 31 December 2007 the percentage ownership interest of the Group in its associates is equal to the percentage of voting interest.

(1) "Catoca Mining Company Ltd" is a diamond-mining venture located in Angola. In April 2008 "Catoca Mining Company Ltd" declared dividends for the year ended 31 December 2007; the Group's share of these dividends amounted to RR'mln 773. Currency translation income recognised in the consolidated statement of changes in equity for the year ended 31 December 2008 in respect of investment in "Catoca Mining Company Ltd" totalled RR'mln 279. In May 2007 "Catoca Mining Company Ltd" declared dividends for the year ended 31 December 2006; the Group's share of these dividends amounted to RR'mln 796. Currency translation loss recognised in the consolidated statement of changes in equity for the year ended 31 December 2007 in respect of investment in "Catoca Mining Company Ltd" totalled RR'mln 111.

(2) "Escom-ALROSA Ltd" is a holding company, the only purpose of which is to own a 45 percent voting interest in "Camachia-Camagico", a development stage diamond-mining venture located in Angola, which is in the pilot stage of mining of the Luo diamond deposit. In October 2005 the Company issued a US$ denominated loan to "Escom-ALROSA Ltd"; the repayment period of this loan is June 2006 – June 2014 and it bears interest at LIBOR+2.5% per annum. "Escom-ALROSA Ltd", which acts as a holding company, in its turn lent the funds to "Camachia-Camagico" to finance construction of the main processing plant at the Luo deposit. The amount of loan outstanding at 31 December 2008 is RR'mln 3,582, including current portion of RR'mln 592 (31 December 2007: RR'mln 2,809, including current portion of RR'mln 75). The Group has not recognised its share of net loss of "Camachia-Camagico" for the year ended 31 December 2008 in the amount of RR'mln 216 (year ended 31 December 2007: RR'mln 320). The accumulated losses of "Camachia-Camagico" not recognised by the Group in its consolidated financial statements as at 31 December 2008 were RR'mln 641 (31 December 2006: RR'mln 425).

Summarised IFRS financial information of the Group's associates is as follows:

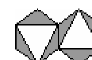
	Assets as at 31 December		Liabilities as at 31 December		Revenues for the year ended 31 December		Profit (loss) for the year ended 31 December	
	2008	**2007**	**2008**	**2007**	**2008**	**2007**	**2008**	**2007**
"Catoca Mining Company Ltd"	11,302	9,192	6,553	4,986	14,524	11,080	2,043	2,847
"Camachia-Camagico"	6,139	6,323	9,278	8,260	695	858	(1,146)	(1,616)
OAO "Almazny Mir"	404	395	39	35	186	254	7	6
Other	157	156	45	37	102	70	1	(3)
	18,002	16,066	15,915	13,318	15,507	12,262	905	1,234

Non-current available-for-sale investments

	Year ended 31 December 2008	Year ended 31 December 2007
Available-for-sale investments at the beginning of the year	786	1,285
Additions	47	103
Additions through consolidation of OAO "NNGK Sakhaneftegaz"	195	-
Net changes in fair value	-	433
Derecognition of investment in OAO "NNGK Sakhaneftegaz"	(493)	-
Disposals	(23)	(1,035)
Available-for-sale investments at the end of the year	512	786

Acquisition of a 45 percent interest in OOO "KIT Finance Holding Company"

In order to support the process of normalisation of financial position of OAO "KIT Finance Investment bank", on 30 December 2008 the Group as part of syndicate of investors, which besides it included companies of "Russian Railroads" group, acquired a 45 percent interest in share capital of OOO "KIT Finance Holding Company", which at the date of transaction owned 87 percent of shares of OAO "KIT Finance Investment bank". The amount of cash consideration paid under this transaction totalled RR 45. In accordance with the intention of the Group's management formed at the date of transaction and the plan of financial rehabilitation of OAO "KIT Finance Investment bank", developed by Deposit Insurance Agency of the Russian Federation and approved by Central Bank of the Russian Federation, it is anticipated that the share of the Group in OOO "KIT Finance Holding Company" will be transferred to "Russian Railroads" group during 2009 for a cash consideration also not exceeding RR 45. Consequently, in accordance with IFRS 5 "Non-current assets held for sale and discontinued operations" the Group classified its investment in share capital of OOO "KIT Finance Holding Company" as at 31 December 2008 as an asset held for sale at fair value totalling RR 45.



Goodwill

The amount of goodwill totalling RR'mln 1,439 relates to acquisition of a 49 percent minority interest in OAO "Almazy Anabara" in December 2007. The goodwill is attributable to the operational synergies expected to arise after this acquisition as a result of more effective integration of operational activity of this subsidiary into the Group's one. As at 31 December 2008 the recoverable amount of goodwill was determined on the basis of the recent management's forecast of future cash flows of OAO "Almazy Anabara" for the years 2009-2019. The pre-tax discount rate used in the analysis was 20.1 percent, which presents the weighted average cost of capital for the Group. Based on results of the analysis management concluded that there is no impairment for goodwill as at 31 December 2008. The impairment test involves making judgment about several key future business indicators. Management believes that their judgements are reasonable and supportable in the current economic environment. However, as compared to the estimates used in the impairment test, if diamond prices fall by 10 percent or US$ depreciates against Russian Rouble by 16 percent or discount rate increases by 13 percent, there will be no excess of value in use over carrying value of assets allocated to the respective cash generating unit.

6. DERIVATIVE FINANCIAL INSTRUMENTS

To reduce the Group's US$ / RR foreign exchange risk exposure, in 2006 the Group entered into US$ / RR forward sale transactions with five foreign banks having an investment grade rating within the range Aa2-Aa3 as assessed by Moody's rating agency under which it agreed to sell US$ for RR during a five-year period starting in September 2006 and ending in September 2011, at a strike price fixed at the exchange rates ranging from RR 26.56 to RR 26.84 per US$ 1, averaged on a quarterly basis. The transactions have varying maturities and amounts spread evenly over the five-year period in the aggregate amount of US$'mln 215 per quarter (US$'mln 4,300 in total over the five-year period). At 31 December 2008 the fair value of the forward foreign exchange contracts totalled RR'mln 21,348 (liability), at 31 December 2007 - RR'mln 5,106 (asset). It represents the net present value of the differences between the cash flows related to these contracts calculated at forward exchange rates prevailing at the market as at the reporting dates and forward exchange rates fixed by the forward sales contracts concluded by the Company over the five-years period.

	Year ended 31 December 2008	Year ended 31 December 2007
Fair value of foreign exchange forward contracts at the beginning of the year	5,106	902
Net proceeds from exercising of foreign exchange forward contracts	(1,377)	(945)
Net (loss) / gain from change of fair value of foreign exchange forward contracts	(25,077)	5,149
Fair value of foreign exchange forward contracts at the end of the year	(21,348)	5,106

Additionally, to reduce the Group's interest rate risk exposure associated with the RR denominated floating rate loans from "Bank VTB", in 2008 the Group entered into US$ / RR cross currency interest rate swap transactions with "VTB Bank Europe Plc" having an investment grade rating Baa1 as assessed by Moody's rating agency. Under the swap transactions the Group agreed to convert into US$ the amount due to "Bank VTB" totalling RR'mln 4,518 at the exchange rate of RR 26.62 and pay fixed interest rates ranging from 9.55 to 9.88 percent in exchange of RR floating interest rates based on three months MosPrime interest rate. The transactions have varying maturities and amounts spread evenly from October 2008 to May 2011. At 31 December 2008 the fair value of the cross currency interest rate swap transactions totalled RR'mln 1,096 (liability).

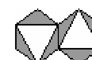
The discount rate used to calculate the fair value of the forward foreign exchange contracts and cross currency interest rate swap transactions as at 31 December 2008 was 15 percent, which represents the incremental interest rate on RR denominated borrowings applicable to the Group as at that date. The discount rate used to calculate the fair value of the forward foreign exchange contracts as at 31 December 2007 was 7 percent, which represented the average cost of borrowing by the counterparty banks.

As at 31 December 2008 and 31 December 2007 derivative financial instruments are not past due. Derivative financial instruments are classified as current assets and current liabilities in these consolidated financial statements as they present financial instruments held for trading, but a portion of derivative financial instruments totalling RR'mln 16,174 (liability) as at 31 December 2008 and totalling RR'mln 3,037 (asset) as at 31 December 2007 is expected to be settled after 12 months from the balance sheet date.

7. CASH AND CASH EQUIVALENTS

Restricted cash

Restricted cash included within non-current assets in the balance sheet of RR'mln 31 and RR'mln 133 as at 31 December 2008 and 31 December 2007, respectively, is represented by mandatory reserve deposits held with the Central Bank of the



Russian Federation by OOO "MAK Bank", a subsidiary of the Group; these balances are not available for use in the Group's day to day operations. Payments to this restricted cash account are included in cash flows from operating activity in consolidated statement of cash flows (see note 25).

At 31 December 2008 and 31 December 2007 the weighted average interest rate on the restricted cash balances is approximately nil percent.

Long-term deposits

As at 31 December 2008 the Group held RR'mln 11,285 on deposit accounts in OAO "KIT Finance Investment Bank" (credit rating of this bank is Caa 2 as assessed by Moody's rating agency). The maturity of these deposits is on 29 November 2010. The Group has the right for early refund of these deposits in case of the liquidity requirements. Annual interest rate is floating and equals to the refinancing rate of the Central Bank of the Russian Federation (as at 31 December 2008 – 13 percent). In order to guarantee the refund of these deposits the bank pledged certain assets to the Group.

Since September 2008 due to significant decline in financial markets the liquidity position and quality of assets of OAO "KIT Finance Investment Bank" significantly deteriorated. In order to improve the financial position of the bank the Russian Government undertook certain measures, including its acquisition by a syndicate of the companies controlled by the Government, which included the Group and companies of "Russian Railroads" group (see note 5), and provision of financial support by the banks controlled by the Government. In June 2009 the Central Bank of the Russian Federation approved the plan of financial rehabilitation of OAO "KIT Finance Investment Bank", which was developed by Deposit Insurance Agency of the Russian Federation. This plan includes transfer of control over the bank's operating and financial activity to "Russian Railroads" group, further provision of financial support, refinancing of certain liabilities and buyout of certain assets. Management of the Group believes that these measures will be sufficient for improvement of financial position and liquidity of OAO "KIT Finance Investment Bank", accordingly, it believes that the amounts held by the Group on deposit accounts in OAO "KIT Finance Investment Bank" are not impaired and will be withdrawn not later than on the contractual date of maturity of the respective deposit agreements.

Cash and cash equivalents

	31 December 2008	31 December 2007
Current accounts	3,952	14,235
Deposit accounts	2,102	288
Notes receivable	1,515	-
Special accounts	-	7,364
	7,569	21,887

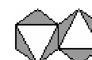
As at 31 December 2008 cash and cash equivalents included non-interest bearing notes of OAO "Bank VTB" totalling RR'mln 1,515 with maturity at the date of inception less than three months.

At 31 December 2008 the weighted average interest rate on the cash balances of the Group was 1.96 percent (31 December 2007: 4.81 percent).

The table below analyses the credit quality of banks at which the Group holds cash and cash equivalents as at 31 December 2008:

	External credit rating	Rating agency	31 December 2008	31 December 2007
OAO "Bank VTB"	Baa 1	Moody's	4,286	10,386
Current accounts of OOO "MAK Bank" in the Central Bank of the Russian Federation	Not applicable	Not applicable	1,044	1,032
Cash of OOO "MAK Bank" on hand and in cash machines	Not applicable	Not applicable	441	479
OAO "AKB Bank of Moscow"	Baa 1	Moody's	323	235
OAO "KIT Finance Investment Bank"	Caa 2	Moody's	230	8,296
OAO "Sberbank"	Baa 1	Moody's	141	11
ZAO "UniCredit Bank"	BBB+	Fitch Ratings	137	200
ZAO "Bank Societe Generale Vostok"	Aa 2	Moody's	97	-
Other banks	Aa 2–Baa 2	Moody's	870	1,248
			7,569	21,887

As at 31 December 2008 and 31 December 2007 all balances of cash and cash equivalents of the Group are neither past due nor impaired.



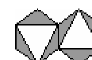
8. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Land and Improvements	Plant and Equipment	Transport	Production Licenses	Assets under Construction	Other	TOTAL
Cost at 31 December 2006	**53,582**	**47,138**	**36,477**	**16,334**	**10,626**	**39,663**	**1,449**	**205,269**
Additions	284	1,027	2,873	1,374	549	22,355	425	28,887
Transfers	2,439	3,500	1,506	61	-	(7,764)	258	-
Disposals	(778)	(818)	(1,122)	(918)	-	(462)	(409)	(4,507)
Foreign exchange differences	(1)	-	(57)	(230)	-	(202)	49	(441)
Disposal of OAO "Yakutskgeofizika"	(51)	(38)	(43)	(220)	-	(43)	(16)	(411)
Change in estimate of provision for restoration liability	112	41	8	1	-	-	-	162
Reversal of provision for restoration liability	(2,586)	(977)	(199)	(28)	-	-	(5)	(3,795)
Change in estimate of provision for land recultivation (see note 14)	-	(25)	-	-	-	-	-	(25)
Cost at 31 December 2007	**53,001**	**49,848**	**39,443**	**16,374**	**11,175**	**53,547**	**1,751**	**225,139**
Additions through consolidation of OAO "NNGK Sakhaneftegaz" (note 5)	230	609	309	54	-	125	24	1,351
Additions	339	1,912	2,982	918	5,430	19,277	734	31,592
Transfers	3,192	6,407	2,406	64	-	(12,400)	331	-
Disposals	(419)	(1,423)	(967)	(511)	-	(160)	(529)	(4,009)
Foreign exchange differences	36	795	5	516	-	665	(3)	2,014
Change in estimate of provision for land recultivation (see note 14)	-	(18)	-	-	-	-	-	(18)
Cost at 31 December 2008	**56,379**	**58,130**	**44,178**	**17,415**	**16,605**	**61,054**	**2,308**	**256,069**
Accumulated depreciation and impairment losses at 31.12.2006	**(16,114)**	**(16,018)**	**(20,364)**	**(10,016)**	**(345)**	**(429)**	**(525)**	**(63,811)**
Charge for the year ended 31 December 2007	(1,613)	(2,676)	(3,588)	(1,190)	(272)	-	(208)	(9,547)
Disposals	273	664	1,056	860	-	-	32	2,885
Reversal of provision for restoration liability	399	183	49	4	1	-	2	638
Foreign exchange differences	-	-	33	144	-	-	(19)	158
Reversal of impairment of property, plant and equipment	-	-	-	-	-	158	-	158
Disposal of OAO "Yakutskgeofizika"	4	10	13	42	-	-	7	76
Accumulated depreciation and impairment losses at 31.12.2007	**(17,051)**	**(17,837)**	**(22,801)**	**(10,156)**	**(616)**	**(271)**	**(711)**	**(69,443)**
Charge for the year ended 31 December 2008	(1,609)	(2,913)	(3,815)	(1,270)	(284)	-	(252)	(10,143)
Disposals	98	1,157	919	479	-	-	64	2,717
Foreign exchange differences	(12)	(264)	(3)	(331)	-	3	1	(606)
Impairment of property, plant and equipment	(178)	-	-	-	-	(342)	-	(520)
Accumulated depreciation and impairment losses at 31.12.2008	**(18,752)**	**(19,857)**	**(25,700)**	**(11,278)**	**(900)**	**(610)**	**(898)**	**(77,995)**
Net book value at 31 December 2007	**35,950**	**32,011**	**16,642**	**6,218**	**10,559**	**53,276**	**1,040**	**155,696**
Net book value at 31 December 2008	**37,627**	**38,273**	**18,478**	**6,137**	**15,705**	**60,444**	**1,410**	**178,074**

Additions to property, plant and equipment include licenses for exploration and production activities at four iron ore fields located in the Republic of Sakha (Yakutia) acquired by the Group in April 2008 for consideration of RR'mln 5,403.

Property, plant and equipment for the year ended 31 December 2008 includes an aircraft which the Group received under a finance lease agreement (see note 12). As at 31 December 2008 the carrying value of this aircraft is RR'mln 905 (31 December 2007: RR'mln 940). Property, plant and equipment for the year ended 31 December 2008 includes the mining equipment which OAO "Almazy Anabara", a subsidiary of the Group, received under finance lease agreements (see note 12). As at 31 December 2008 the carrying value of this equipment is RR'mln 343 (31 December 2007: RR'mln 407).

The Group conducted an impairment test of its property plant and equipment when there were indicators that these assets may be impaired. The recoverable amount used in the impairment tests has been determined on the basis of the projected cash flows and the value in use of such asset or cash-generating units. The Group conducted an impairment test of its cash-generating units, for which the values in use have been calculated as the present values of projected future cash flows discounted by the Group's weighted average cost of capital, as adjusted, where applicable, to take into account any specific risks of business operations related to the cash-generating units. The Group used discount rate of 20.1 percent, which



presents the weighted average cost of capital for the Group as at 31 December 2008. The cash flow projections cover periods commensurate with the production cycles and expected lives of the respective assets. The Group used steady growth rates of 3.5 percent to extrapolate cash flows beyond the period of 2009-2015, for which the Group prepared its budget.

The Group's assessment of value in use of its property, plant and equipment as at 31 December 2008 substantially exceeds its carrying value. The impairment test involves making judgment about several key future business indicators. Management believes that their judgements are reasonable and supportable in the current economic environment. However, as compared to the estimates used in the impairment test, if diamond prices fall by 12 percent or US$ depreciates against Russian Rouble by 11 percent or discount rate increases by 9 percent, there would be no excess of value in use over carrying amount of respective assets for cash-generating units.

Apart from an impairment test results, the Group recognised an impairment loss of RR'mln 520 for certain frozen assets under construction and lie idle buildings, which, in accordance with recent management's plans, will not be used in production activity of the Group.

9. INVENTORIES

	31 December 2008	**31 December 2007**
Diamonds	11,105	7,815
Ores and concentrates	5,273	3,730
Mining and construction materials	13,518	9,490
Diamonds for resale	1,399	535
Consumable supplies	1,012	638
	32,307	22,208

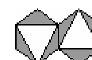
Diamonds for resale represent the diamonds purchased by the Group from Angolan diamond producers for the purpose of the subsequent resale on the open market.

10. TRADE AND OTHER RECEIVABLES

Long-term accounts receivable	**31 December 2008**	**31 December 2007**
Receivables from associates (see notes 5 and 27)	2,990	2,734
Loans issued	1,616	1,303
Long-term VAT recoverable	683	1,187
Notes receivable	636	654
Other long-term receivables	8	24
	5,933	5,902

Current accounts receivable	**31 December 2008**	**31 December 2007**
Trade receivables for supplied diamonds	12,787	65
Loans issued	4,508	4,063
VAT recoverable	1,564	930
Receivables from associates (see note 27)	1,108	486
Prepaid taxes, other than income tax	945	1,846
Advances to suppliers	823	1,157
Notes receivable	168	922
Receivables for sale of treasury shares	251	251
Receivables for sale of gold mining operations	-	555
Other receivables	3,355	2,289
	25,509	12,564

As at 31 December 2008 trade receivables for supplied diamonds include accounts receivable from OOO "Interdiam", a third party wholesale diamonds customer, totalling RR'mln 12,513. The original maturity date for these receivables was 26 March 2009. The nominal value of these accounts receivable is RR'mln 13,231; it was adjusted to the fair value of RR'mln 12,513 using the discount rate of 25 percent per annum, which is applicable to the RR denominated loans issued by the Group to third parties with the similar credit quality, with a corresponding debit recorded as a reduction of the respective revenue figure. The Group supplied diamonds for this company in December 2008 anticipating that it will subsequently resell them in the open market. OOO "Interdiam" failed to resell these diamonds; accordingly it failed to settle its debt to the Group within the contractual term. Management of the Group does not consider these receivables as impaired as it expects to recover them substantially by means of repurchasing of the initially supplied diamonds back from this customer during the second half of 2009 at prices not exceeding net realisable value of these diamonds.



The average effective interest rates at the balance sheet dates were as follows:

Long-term accounts receivable	31 December 2008	31 December 2007
Receivables from associates	5%	7%
Loans issued	17%	14%
Notes receivable	10%	10%
Other long-term receivables	10%	10%

The carrying amounts and fair values of long-term accounts receivable are as follows:

	31 December 2008		31 December 2007	
	Carrying value	Fair value	Carrying value	Fair value
Receivables from associates	2,990	2,575	2,734	2,896
Loans issued	1,616	1,402	1,303	1,251
Notes receivable	636	507	654	641
Other long-term receivables	8	5	24	22

The fair value of long-term accounts receivable is estimated by discounting the future contractual cash inflows at the market interest rates available to the Group at the balance sheet dates. These market interest rates for each class of long-term accounts receivable at the balance sheet dates were as follows:

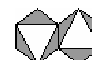
	31 December 2008	31 December 2007
Receivables from associates	15.0%	6.5%
Loans issued	19.2%	12.2%
Notes receivable	20.0%	11.5%
Other long-term receivables	20.0%	11.9%

The fair value of each class of short-term trade and other accounts receivable at 31 December 2008 and 31 December 2007 approximates their carrying value.

The impairment provision offset against individual receivable balances is as follows:

Long-term accounts receivable	31 December 2008	Bad debt write-off	Bad debt expense	31 December 2007
Loans issued	26	-	-	26
	26	-	-	26
Current accounts receivable				
Receivables from associates (see note 27)	188	-	-	188
Notes receivable	80	-	-	80
Loans issued	184	-	55	129
Other receivables	1,334	(114)	30	1,418
	1,786	(114)	85	1,815

Long-term accounts receivable	31 December 2007	Bad debt write-off	Bad debt expense (reversal)	31 December 2006
Loans issued	26	-	-	26
	26	-	-	26
Current accounts receivable				
Receivables from associates (see note 27)	188	(78)	-	266
Notes receivable	80	(143)	-	223
Loans issued	129	-	(8)	137
Receivables for sale of gold mining operations	-	(378)	378	-
Other receivables	1,418	(108)	219	1,307
	1,815	(707)	589	1,933



The individually impaired receivables mainly relate to the customers, which are in difficult economic situations or under bankruptcy procedures. Management assesses a portion of the receivables will be recovered. The ageing analysis of these receivables is as follows:

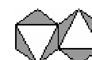
	31 December 2008				31 December 2007			
	Up to 1 year	1 to 3 years	Over 3 years	Total	Up to 1 year	1 to 3 years	Over 3 years	Total
Long-term accounts receivable								
Loans issued	-	-	26	26	-	-	26	26
	-	-	26	26	-	-	26	26
Current accounts receivable								
Receivables from associates	-	-	188	188	-	99	89	188
Notes receivable	-	-	80	80	-	-	80	80
Loans issued	55	68	61	184	25	43	61	129
Other receivables	-	252	1,082	1,334	86	261	1,071	1,418
	55	320	1,411	1,786	111	403	1,301	1,815

As at 31 December 2008 and 31 December 2007, trade and other receivables totalling RR'mln 31,035 and RR'mln 18,134, respectively, were neither past due nor impaired and have no history of overdue payments. Most of these debtors have no individual external credit rating.

For the purpose of analysis of credit quality of debtors management classified accounts receivable of the Group as follows:

31 December 2008	Large customers	Medium and small customers	Entities controlled by the Government	Individuals	Total
Long-term accounts receivable					
Receivables from associates	2,990	-	-	-	2,990
Loans issued	530	780	-	306	1,616
Notes receivable	636	-	-	-	636
Other long-term receivables	-	-	8	-	8
	4,156	780	8	306	5,250
Current accounts receivable					
Trade receivables for supplied diamonds	233	12,554	-	-	12,787
Loans issued	1,121	2,086	843	458	4,508
Receivables from associates	1,067	41	-	-	1,108
Receivables for sale of treasury shares	-	251	-	-	251
Notes receivable	88	80	-	-	168
Other receivables	182	2,494	383	296	3,355
	2,691	17,506	1,226	754	22,177

31 December 2007	Large customers	Medium and small customers	Entities controlled by the Government	Individuals	Total
Long-term accounts receivable					
Receivables from associates	2,734	-	-	-	2,734
Loans issued	530	482	-	291	1,303
Notes receivable	654	-	-	-	654
Other long-term receivables	18	-	6	-	24
	3,936	482	6	291	4,715
Current accounts receivable					
Loans issued	917	1,579	1,121	446	4,063
Notes receivable	70	852	-	-	922
Receivables for sale of gold mining operations	555	-	-	-	555
Receivables from associates	417	69	-	-	486
Receivables for sale of treasury shares	-	251	-	-	251
Trade receivables for supplied diamonds	17	48	-	-	65
Other receivables	248	1,406	433	202	2,289
	2,224	4,205	1,554	648	8,631



For the purposes of the above analysis customers are considered large if their total assets exceed RR'mln 5,000 and their revenue exceeds RR'mln 1,000. Management believes that balances of accounts receivable with large customers have higher credit quality than medium and small customers or individuals.

As at 31 December 2008 accounts receivable in the amount of RR'mln 407 (as at 31 December 2007: RR'mln 332) were past due but were not considered impaired. They include only other receivables and relate to a number of independent medium and small customers for whom there is no recent history of default.

The ageing analysis of receivables that are past due but not impaired is as follows:

	31 December 2008	31 December 2007
Up to 3 months	37	134
3 to 6 months	46	17
6 to 12 months	82	112
More than 1 year	242	69
	407	332

As at 31 December 2008 7 individual debtors of the Group (31 December 2007: 17 individual debtors) had the outstanding balance with the Group exceeding RR'mln 100. As at 31 December 2008 total amount of such accounts receivable was RR'mln 13,712 (31 December 2007: RR'mln 7,704).

11. SHAREHOLDERS' EQUITY

Share capital

Share capital authorised, issued and paid in totals RR'mln 12,473 as at 31 December 2008 (as at 31 December 2007: RR'mln 11,491) and consists of 272,726 ordinary shares (as at 31 December 2007: 200,000 ordinary shares), including treasury shares, at RR 13,502.5 par value per share. In addition as at 31 December 2008 and 31 December 2007 share capital includes hyperinflation adjustment totalling RR'mln 8,790, which was calculated in accordance with requirements of IAS 29 "Financial Reporting in Hyperinflationary Economies" and relates to the reporting periods prior to 1 January 2003.

Mineral Lease Agreement and an additional issue of shares

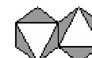
On 19 January 1993, the Company entered into a Mineral Lease Agreement (the "Lease Agreement") with the Republic of Sakha (Yakutia) for the "transfer of rights to use and exploit land, diamond deposits, main production and non-production facilities". This agreement had a term of 25 years and provided the Company with the right to use certain production and non-production assets for exploring, mining and operating diamond deposits. The agreement required the Company to return the assets in 2017 and reimburse the Government of Republic of Sakha (Yakutia) for depreciation of the assets. Production assets received from the Republic of Sakha (Yakutia) under the terms of the Lease agreement are recorded in accordance with IAS 20 "Accounting for Government Grants and Disclosure of Government Assistance", at historical cost adjusted for the effects of inflation, with, prior to 10 November 2007, a corresponding credit reflected as a Grant in the Group's balance sheet. The Grant was amortised in line with the reduction in the carrying value of the underlying assets, with the amortised portion recorded as an increase in other operating income. Management estimated the restoration liability based upon their interpretation of the Lease Agreement. The provision for restoration liability represented the net present value of the estimated future obligation, upon termination of the Lease Agreement, to return certain property, plant and equipment to the Republic of Sakha (Yakutia) under the terms of the Lease Agreement.

On 19 December 2006 the Governments of the Russian Federation and the Republic of Sakha (Yakutia) signed an Amicable Agreement in respect of the property, plant and equipment subject to the Lease Agreement. The parties agreed to do the following:

- the parties should establish the mutual property right of the Russian Federation and the Republic of Sakha (Yakutia) for the property, plant and equipment, which were subject to the Lease Agreement;
- the Company should issue new shares and the Russian Federation and the Republic of Sakha (Yakutia) should contribute this property, plant and equipment to the share capital of the Company in agreed proportions as payment for these new shares.

Following the Amicable Agreement on 29 December 2006 the Company signed an agreement with the Republic of Sakha (Yakutia) in accordance with which:

- the parties agreed to terminate the Lease Agreement early;
- the Republic of Sakha (Yakutia) agreed to transfer the property, plant and equipment, which were subject to the Lease Agreement, to the Company under a new medium-term lease until the new shares are issued.



On 10 November 2007 the extraordinary shareholders’ meeting of the Company approved the issue of 72,726 new shares and their placement among the Governments of the Russian Federation and the Republic of Sakha (Yakutia) and its districts. The Governments of the Russian Federation and the Republic of Sakha (Yakutia) and its districts should contribute the property, plant and equipment, which were subject to the Lease Agreement, to the share capital of the Company as payment for these shares.

Management believes that since the date of official approval of the new share issue and the conditions of this transaction, the assets received from the Republic of Sakha (Yakutia) in 1993 under the terms of the Lease Agreement no longer meet the criteria for granted assets and the issue of shares in favour of governments of the Russian Federation and the Republic of Sakha (Yakutia) and its districts in the exchange of these assets should be treated as a repayment of the previously recognised Grant. Accordingly, the unamortised amount of the Grant as at 10 November 2007 totalling RR’mln 7,537 was reclassified to equity as a deferred capital contribution. Management also believes that the additional issue of shares has no effect on recognised amounts of property, plant and equipment, which were subject to the Lease Agreement, as cash flows attributable to these assets as well as their operational and physical conditions will not change as a result of the transaction.

Management also believes that since the date of official approval of the new shares issue the Company has no longer an obligation to return the property, plant and equipment, which were subject to the Lease Agreement, to the Republic of Sakha (Yakutia) and, accordingly the amount of provision for restoration liability was reversed in the consolidated financial statements for the year 2007. Management considers this reversal as an inflow of economic benefits to the Company resulting from the contribution of shareholders, so the amount of provision for restoration liability as at 10 November 2007 (RR’mln 7,659) net of unamortised amount of the related asset (RR’mln 3,157) and the corresponding amount of deferred tax benefit (RR’mln 976) was recognised as at 31 December 2007 in equity as a deferred capital contribution.

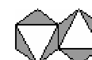
On 18 June 2008 the Company agreed to transfer 43,635 newly issued shares to the Government of the Russian Federation and 29,091 newly issued shares to the Government of the Republic of Sakha (Yakutia) and its districts. The Governments of the Russian Federation and the Republic of Sakha (Yakutia) and its districts, in their turn, contributed the property, plant and equipment, which were subject to the Lease Agreement, to the share capital of the Company as payment for these shares. These property, plant and equipment included plots of land, which were not previously recognised on the balance sheet of the Company. These plots of land were initially recognised within property plant and equipment as at the date of transaction at fair value totalling RR’mln 520, with a corresponding credit reflected in equity within a deferred capital contribution.

On 30 October 2008 the Federal Service on Financial Markets of the Russian Federation registered the results of additional issue of shares and the increase of share capital of the Company. At the same time the number of authorised shares of the Company increased to 272,726 shares. Accordingly, on 30 October 2008 the Company reclassified the deferred capital contribution totalling RR’mln 11,583 between the share capital and share premium. Transaction costs totalling RR’mln 170 relating to additional issue of shares were deducted from share premium.

In June 2008, prior to above described transaction, OAO “Bank VTB”, which owned 10.6 percent of shares of the Company, transferred these shares to the Government of Russian Federation in the exchange for part of property, plant and equipment, which were subject to the Lease Agreement. On 20 June 2008 OAO “Bank VTB” sold these property, plant and equipment to the Company for a total cash consideration of RR’mln 8,233. Management believes that, as in case of transactions with the Governments of Russian Federation and the Republic of Sakha (Yakutia) and its districts, the transaction with OAO “Bank VTB” has no effect on recognised amounts of property, plant and equipment, which were subject to the Lease Agreement, as cash flows attributable to these assets as well as their operational and physical conditions will not change as a result of the transaction. Management believes that by its substance the transaction with OAO “Bank VTB” should be treated as a distribution of retained earnings in favour of the Government of Russian Federation. Accordingly payment made to OAO “Bank VTB” totalling RR’mln 8,233 was recorded as a reduction of retained earnings of the Company.

Distributable profits

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 the years ended 31 December 2008 and 31 December 2007, the statutory profit of the Company as reported in the published statutory reporting forms was RR’mln 1,574 and RR’mln 14,133 respectively. However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation, and accordingly, management believes that at present it would not be appropriate to disclose an amount for the distributable reserves in these consolidated financial statements.



Other reserves

	Available-for-sale investments	Currency translation	Purchase of non-controlling interest	Total
Balance at 31 December 2006	**185**	**94**	**-**	**279**
Net gains arising from change in fair value of available-for-sale investments, net of income tax	329	-	-	329
Gain on disposal of available-for-sale investments recognised in statement of income, net of income tax	(514)	-	-	(514)
Currency translation differences	-	(287)	-	(287)
Balance at 31 December 2007	**-**	**(193)**	**-**	**(193)**
Currency translation differences	-	440	-	440
Purchase of non-controlling interest in OAO "Viluyskaya GES-3"	-	-	(309)	(309)
Balance at 31 December 2008	**-**	**247**	**(309)**	**(62)**

Treasury shares

At 31 December 2008 and 31 December 2007 OOO "MAK Bank", a subsidiary of the Group, held 420 and 280 ordinary shares of the Company, respectively. The Group management controls the voting rights of these shares.

Dividends

On 23 June 2007 the Company's shareholders approved dividends for the year ended 31 December 2006 totalling RR'mln 2,240. Dividends per share amounted to RR 11,200.

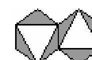
On 21 June 2008 the Company's shareholders approved dividends for the year ended 31 December 2007 totalling RR'mln 2,240. Dividends per share amounted to RR 11,200.

Non-controlling interest in subsidiaries

	Year ended 31 December 2008	Year ended 31 December 2007
Non-controlling interest at the beginning of the year	1,190	4,610
Non-controlling interest share of net (loss) / profit of subsidiaries	(169)	203
Non-controlling interest in acquired net assets of OAO "NNGK Sakhaneftegaz" and OAO "Lenaneftegaz" (note 5)	(1,068)	-
Purchase of non-controlling interest	(135)	(3,237)
Disposal of non-controlling interest through disposal of subsidiary	-	(50)
Dividends paid by subsidiaries to minority shareholders	(249)	(336)
Non-controlling interest at the end of the year	(431)	1,190

During the year ended 31 December 2008 non-controlling interest decreased by RR'mln 135 as a result of the acquisition of an additional 4.83 percent interest OAO "Viluyskaya GES-3". The difference between the carrying amount of the non-controlling interest and the amount paid to acquire it totalling RR'mln 309 was recorded in equity within other reserves.

During the year ended 31 December 2007 non-controlling interest decreased as a result of the acquisition of an additional 49 percent interest in OAO "Almazy Anabara" (for RR'mln 864), an additional 49.99 percent interest in OAO "Investment Group ALROSA" (for RR'mln 2,217), an additional 8 percent interest in OAO "Viluyskaya GES-3" (for RR'mln 150) and an additional 1 percent interest in OAO "ALROSA-Nyurba" (for RR'mln 6).



12. LONG-TERM DEBT

	31 December 2008	31 December 2007
Banks:		
US$ denominated floating rate	4,800	468
US$ denominated fixed rate	25,092	21,372
RR denominated floating rate	3,193	-
RR denominated fixed rate	44,484	305
	77,569	**22,145**
Eurobonds	14,681	19,631
Finance lease obligation	948	945
Commercial paper	466	545
Other US$ denominated fixed rate loans	213	227
Other RR denominated fixed rate loans	943	1,036
	94,820	**44,529**
Less: current portion of long-term debt (see note 13)	(14,489)	(12,233)
	80,331	**32,296**

At 31 December 2008 the Group breached covenants relating to certain financial ratios of the long-term loan of RR'mln 3,966. As a result, at the balance sheet date, the lender had the option to call this loan. The loan was classified as current at 31 December 2008 because the lender waived its right to request immediate redemption only after the balance sheet date.

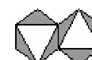
The long-term commercial paper is denominated in RR, has defined maturity dates ranging between one and ten years, and is carried at amortised cost.

The average effective interest rates at the balance sheet dates were as follows:

	31 December 2008	31 December 2007
Banks:		
US$ denominated floating rate	3.5%	6.8%
US$ denominated fixed rate	8.4%	7.7%
RR denominated floating rate	28.3%	-
RR denominated fixed rate	15.3%	12.6%
Eurobonds	8.7%	8.7%
Finance lease obligation	7.6%	7.6%
Commercial paper	26.3%	24.9%
Other US$ denominated fixed rate	9.0%	9.0%
Other RR denominated fixed rate loans	13.6%	10.6%

At 31 December 2008 long-term loans had the following maturity profile (based on the discounted contractual cash flows):

	Within 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 years and thereafter	Total
Banks:						
US$ denominated floating rate	3,993	384	27	396	-	4,800
US$ denominated fixed rate	8,575	564	3,574	12,237	142	25,092
RR denominated floating rate	1,637	-	1,556	-	-	3,193
RR denominated fixed rate	-	44,173	290	9	12	44,484
Eurobonds	-	-	-	-	14,681	14,681
Finance lease obligation	169	57	26	27	669	948
Commercial paper	-	170	296	-	-	466
Other US$ denominated fixed rate loans	115	98	-	-	-	213
Other RR denominated fixed rate loans	-	802	141	-	-	943
	14,489	46,248	5,910	12,669	15,504	94,820



At 31 December 2007 long-term loans had the following maturity profile (based on the discounted contractual cash flows):

	Within 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 years and thereafter	Total
Banks:						
US$ denominated floating rate	-	-	-	135	333	468
US$ denominated fixed rate	4,335	10,580	471	524	5,462	21,372
RR denominated fixed rate	2	2	2	2	297	305
Eurobonds	7,365	-	-	-	12,266	19,631
Finance lease obligation	133	151	58	21	582	945
Commercial paper	-	160	125	260	-	545
Other US$ denominated fixed rate loans	-	179	48	-	-	227
Other RR denominated fixed rate loans	398	498	-	-	140	1,036
	12,233	11,570	704	942	19,080	44,529

The carrying amounts and fair values of long-term debt are as follows:

	31 December 2008		31 December 2007	
	Carrying value	Fair value	Carrying value	Fair value
Banks				
US$ denominated floating rate	4,800	771	468	459
US$ denominated fixed rate	25,092	24,274	21,372	19,592
RR denominated floating rate	3,193	3,748	-	-
RR denominated fixed rate	44,484	43,495	305	361
Eurobonds	14,681	8,556	19,631	21,029
Finance lease obligation	948	825	945	851
Commercial paper	466	707	545	1,190
Other US$ denominated fixed rate loans	213	213	227	227
Other RR denominated fixed rate loans	943	643	1,036	1,028

The fair value of long-term debt is estimated by discounting the future contractual cash outflows at the market interest rate available to the Group at the balance sheet date. These market interest rates for each class of long-term debt at the balance sheet dates were as follows:

	31 December 2008	31 December 2007
Banks		
US$ denominated floating rate	9.1%	6.9%
US$ denominated fixed rate	10.7%	11.0%
RR denominated floating rate	28.7%	-
RR denominated fixed rate	15.5%	10.7%
Eurobonds	21.9%	5.4%
Commercial paper	19.3%	7.8%
Finance lease obligation	9.9%	9.8%
Other US$ denominated fixed rate loans	10.7%	11.0%
Other RR denominated fixed rate loans	15.5%	10.7%

As at 31 December 2008 and at 31 December 2007 there were no long-term loans secured with the assets of the Group.

Eurobonds

	Year ended 31 December 2008	Year ended 31 December 2007
Balance at the beginning of the year	19,631	21,005
Amortisation of discount	23	34
Repayment	(7,094)	-
Exchange loss / (gain)	2,121	(1,408)
Balance at the end of the year	14,681	19,631

Finance lease obligation

	Minimum lease payments 31 December 2008	Discounted value of minimum lease payments 31 December 2008	Minimum lease payments 31 December 2007	Discounted value of minimum lease payments 31 December 2007
Within 1 year	339	169	203	133
Between 2 and 4 years	293	110	402	231
5 years and thereafter	747	669	658	581
	1,379	948	1,263	945

13. SHORT-TERM LOANS AND CURRENT PORTION OF LONG-TERM DEBT

	31 December 2008	31 December 2007
Banks:		
US$ denominated floating rate	2,644	3,682
US$ denominated fixed rate	14,231	23,012
RR denominated floating rate	2,605	543
RR denominated fixed rate	15,528	3,509
	35,008	**30,746**
European commercial paper	1,366	3,510
Commercial paper	1,138	791
Other US$ denominated fixed rate loans	9	6
Other RR denominated fixed rate loans	2,058	2,166
	39,579	**37,219**
Add: current portion of long-term debt (see note 12)	14,489	12,233
	54,068	**49,452**

Commercial paper

Commercial paper comprises unsecured notes, denominated in RR, issued by the Group to provide short-term working capital facilities. The short-term commercial paper is typically a non-interest bearing instrument issued at a discount, with defined maturity dates ranging from 1 month to 1 year and is carried at amortised cost.

European commercial paper

In March 2005 "ALROSA Finance S.A.", a subsidiary of the Group, established a program for issuing European commercial paper (ECP). The program allows for the issue of US$ denominated short-term fixed rate commercial paper with maturity dates within 364 days.

	Year ended 31 December 2008	Year ended 31 December 2007
Balance at the beginning of the year	3,510	-
Issued	13,428	10,979
Repayment	(17,736)	(7,027)
Exchange loss / (gain)	2,164	(442)
Balance at the end of the year	1,366	3,510

As at 31 December 2008, short-term debt totalling RR'mln 226 (31 December 2007: RR'mln 1,028) was secured with the assets of the Group. As separate loan agreements stipulate that the respective debt "is secured with the assets of the Group" and do not specify individual pledged assets, the carrying amount of pledged assets is not disclosed.

The average effective interest rates at the balance sheet dates were as follows:

	31 December 2008	31 December 2007
Banks:		
US$ denominated floating rate	4.0%	5.6%
US$ denominated fixed rate	10.0%	9.1%
RR denominated floating rate	27.8%	11.7%
RR denominated fixed rate	15.9%	11.0%
European commercial paper	7.4%	9.6%
Commercial paper	21.4%	22.3%
Other US$ denominated fixed rate loans	3.7%	3.7%
Other RR denominated fixed rate loans	4.1%	2.4%

The carrying amounts and fair values of short-term debt are as follows:

	31 December 2008		31 December 2007	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Banks:				
US$ denominated floating rate	2,644	2,542	3,682	3,780
US$ denominated fixed rate	14,231	14,100	23,012	22,884
RR denominated floating rate	2,605	2,605	543	544
RR denominated fixed rate	15,528	15,564	3,509	3,511
European commercial paper	1,366	1,326	3,510	3,803
Commercial paper	1,138	1,155	791	864
Other US$ denominated fixed rate loans	9	11	6	5
Other RR denominated fixed rate loans	2,058	2,027	2,166	2,150

The fair value of short-term debt is estimated by discounting the future contractual cash outflows at the market interest rate available to the Group at the balance sheet date. These market interest rates for each class of short-term debt at the balance sheet dates were as follows:

	31 December 2008	**31 December 2007**
Banks:		
US$ denominated floating rate	10.0%	5.0%
US$ denominated fixed rate	13.5%	9.0%
RR denominated floating rate	27.8%	10.5%
RR denominated fixed rate	15.0%	10.9%
European commercial paper	14.4%	8.0%
Commercial paper	20.0%	19.1%
Other US$ denominated fixed rate loans	9.0%	4.3%
Other RR denominated fixed rate loans	12.0%	4.0%

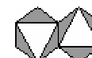
14. OTHER PROVISIONS

	Year ended 31 December 2008	**Year ended 31 December 2007**
Provision for land recultivation	369	444
Legal claim provision	-	99
	369	543

Provision for land recultivation

	Year ended 31 December 2008	**Year ended 31 December 2007**
At the beginning of the year	444	484
Change in estimate of provision for land recultivation	(18)	(25)
Unwinding of discount	14	62
Utilised	(71)	(77)
At the end of the year	369	444

In October 2006 Management Committee of the Company approved the "Program for improvement of environmental situation in the area of operating activity of the Company". In accordance with this Program the Company assumed an obligation to perform recultivation of certain disturbed lands and tailing pits in the areas of its operating activity during 2007-2010. The Company recognised a provision for these future expenses in its consolidated financial statements for the years ended 31 December 2008 and 31 December 2007 with a corresponding asset recognised within property, plant and equipment (see note 8). The discount rate used to calculate the net present value of the future cash outflows relating to land recultivation at 31 December 2008 was 20.1 percent (31 December 2007: 12.4 percent), which represents the weighted average cost of capital for the Group and is considered appropriate to the Group in the economic environment in the Russian Federation at the balance sheet date.



Legal claim provision

	Year ended 31 December 2008	Year ended 31 December 2007
At the beginning of the year	99	229
Utilised	(90)	(104)
Foreign exchange gain	(9)	(26)
At the end of the year	-	99

15. PROVISION FOR PENSION OBLIGATIONS

The amounts recognised in the consolidated balance sheet in respect of pension obligations associated with the defined benefit plan operated by the Group are as follows:

	31 December 2008	31 December 2007
Present value of obligations	9,581	11,375
Fair value of plan assets	(3,819)	(3,555)
Unrecognised actuarial losses	(2,775)	(5,857)
Unrecognised past service cost	(85)	-
Net liability	2,902	1,963

The amounts recognised in the consolidated statement of income in respect of the operation of the defined benefit plan are as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Current service cost	263	301
Interest cost	757	762
Expected return on plan assets	(254)	(228)
Net actuarial losses	437	468
Immediate recognition of vested prior service cost	471	-
Net expense recognised in the statement of income	1,674	1,303

Total expenses associated with pension obligations are included within wages, salaries and other staff costs within cost of sales in the consolidated statement of income.

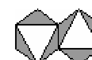
Movements in the pension liability and plan assets recognised in the consolidated balance sheet in respect of the defined benefit plan are as follows:

	31 December 2008	31 December 2007
Benefit obligation at the beginning of the year	11,375	11,388
Current service cost	263	301
Interest cost	757	762
Actuarial gain	(2,894)	(653)
Benefits paid	(475)	(423)
Past service cost	555	-
Benefit obligation at the end of the year	9,581	11,375

	31 December 2008	31 December 2007
Fair value of plan assets at the beginning of the year	3,555	3,120
Expected return on plan assets	254	228
Contributions made	735	682
Benefits paid	(475)	(423)
Actuarial loss	(250)	(52)
Fair value of plan asset at the end of the year	3,819	3,555

The expected return on plan assets is determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields as at the balance sheet date. Expected returns on equity investments reflect long-term real rates of return experienced in the respective markets.

In the year ended 31 December 2008 the actual return on plan assets was RR'mln 4 (year ended 31 December 2007: RR'mln 176).



The Group expects to contribute RR’mln 945 to the defined benefit plans during the year beginning 1 January 2009.

Principal actuarial assumptions used:

	31 December 2008	31 December 2007
Discount rate (nominal)	8.9%	6.8%
Future salary and pension increases (nominal)	5.8%	8.2%
Expected return on plan assets	7.1%	6.8%
Employees average remaining working life (years)	16	13
Estimated total service (years)	12	15
Average period of vesting pensions (years)	6	6

Life expectancies are as follows:

	31 December 2008	31 December 2007
Male aged 57 (years)	15	14
Female aged 55 (years)	22	23

Five-year defined benefit plan disclosure:

	31 December				
	2008	2007	2006	2005	2004
Present value of obligations	9,581	11,375	11,388	8,590	7,513
Fair value of plan assets	(3,819)	(3,555)	(3,120)	(2,648)	(1,544)
Deficit (surplus) in plan	5,762	7,820	8,268	5,942	5,969

	Year ended 31 December				
	2008	2007	2006	2005	2004
Experience adjustments on plan liabilities	(278)	(653)	587	443	1,332
Experience adjustments on plan assets	(250)	(52)	(67)	115	223

The major categories of plan assets as a percentage of total plan assets are as follows:

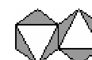
	31 December 2008, %	31 December 2007, %
Russian corporate bonds	31.8	54.5
Bank deposits	21.9	18.9
Current bank accounts	14.6	1.1
Promissory notes of Russian issuers	14.1	5.5
Equity securities of Russian issuers	13.3	12.4
Russian Government and municipal bonds	4.3	7.6
	100.0	100.0

16. TRADE AND OTHER PAYABLES

	31 December 2008	31 December 2007
Trade payables	6,749	3,728
Accrual for employee flights and holidays	4,697	4,393
Accounts payable of OAO “NNGK Sakhaneftegaz” to the companies of former “YUKOS” Group (see note 5)	3,688	-
Wages and salaries	1,374	1,657
Current accounts of third parties in OOO “MAK-Bank”	1,090	658
Advances from customers	893	278
Interest payable	790	565
Payables to associates	91	89
Other payables and accruals	570	508
	19,942	11,876

In accordance with Russian legislation, the Group entities are required to pay for the holiday entitlement and the cost of travel for employees and their family members to an agreed-upon destination and back, or a pre-determined allowance.

The fair value of each class of short-term trade and other payables at 31 December 2008 and 31 December 2007 approximates their carrying value.



17. INCOME AND OTHER TAX ASSETS AND LIABILITIES

Taxes payable, other than income tax, comprise the following:

	31 December 2008	31 December 2007
Value added tax	1,748	289
Property tax	934	88
Unified social tax	841	829
Extraction tax	610	713
Personal income tax (employees)	363	232
Tax penalties	179	178
Other taxes and accruals	257	145
	4,932	2,474

Taxes other than income tax, extraction tax and unified social tax included into other operating expenses comprise the following:

	Year ended 31 December 2008	Year ended 31 December 2007
Property tax	2,271	1,544
Other taxes and accruals	398	288
	2,669	1,832

In accordance with Resolution № 795 of the Government of the Russian Federation dated 23 December 2006, in addition to the taxes noted above, the Group is obliged to pay 6.5 percent on the value of diamonds sold for export in the form of an export duty (see note 18).

In accordance with the amendment to the license agreement registered in May 2007, OAO "ALROSA-Nyurba", a subsidiary of the Group, is obliged to make annual fixed royalty payments to the Republic of Sakha (Yakutia) starting from 1 January 2007 in the amount of RR'mln 3,509 per annum. In addition, in accordance with the agreement dated 29 December 2006 and its subsequent amendments, the Company made fixed royalty payments to the Republic of Sakha (Yakutia) in the amounts of RR'mln 481 in 2008 and RR'mln 1,307 in 2007.

During 2008, the Company accrued profit tax at the rate of 24 percent (year ended 31 December 2007: 24 percent). On 26 November 2008, the Russian Federation reduced the standard corporate income tax rate from 24 to 20 percent with effect from 1 January 2009. This tax rate was applied to determine the deferred tax balances as at 31 December 2008.

Income tax (benefit) / expense comprise the following:

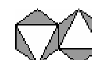
	Year ended 31 December 2008	Year ended 31 December 2007
Current tax expense	3,119	6,422
Deferred tax (benefit) / expense	(6,373)	1,383
Effect of reduction in tax rate	18	-
	(3,236)	7,805

Loss / profit before taxation for financial reporting purposes is reconciled to tax (benefit) / expense as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
(Loss) / profit before income tax	(36,003)	23,989
Theoretical tax (benefit) / charge at statutory rate of 24 percent thereon	(8,641)	5,757
Effect of reduction in tax rate to 20 percent	18	-
Income not assessable for income tax purposes	(65)	(633)
Unrecognised potential deferred tax assets relating to unused tax losses carry forwards (expiry date – 2019)	1,660	-
Expenses and losses not deductible for income tax purposes	3,792	2,681
	(3,236)	7,805

Expenses and losses not deductible for income tax purposes include mostly social expenses, impairment of goodwill arising from acquisition of OAO "NNGK Sakhaneftegaz" (see note 22) and non-deductible wages, salaries and other staff costs.

Differences between IFRS and Russian statutory tax accounting give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes. The tax effect of the movement in these temporary differences is recorded at the rate of 20 percent (2007: 24 percent).



	31 December 2008	Tax effect of movement in temporary differences		31 December 2007	Tax effect of movement in temporary differences			31 December 2006
		Charged to statement of income			Disposal of subsidiary	Charged to statement of changes in equity	Charged to statement of income	
		Effect from tax rate change	At 24 percent					
Deferred tax liabilities								
Property, plant and equipment	5,217	(1,044)	124	6,137	(27)	976	624	4,564
Inventories	2,238	(448)	598	2,088	-	-	55	2,033
Long-term investments	277	(55)	9	323	-	(58)	189	192
Deferred tax assets								
Derivative financial instruments	(4,490)	898	(6,613)	1,225	-	-	1,008	217
Accrual for employee benefits	(1,032)	207	59	(1,298)	-	-	(97)	(1,201)
Exploration costs written off	(353)	71	(20)	(404)	-	-	(97)	(307)
Provision for pension obligations	(580)	116	(225)	(471)	-	-	(106)	(365)
Write-down of inventories	(1,005)	201	(158)	(1,048)	-	-	(78)	(970)
Impairment of accounts receivable	(295)	59	(204)	(150)	-	-	(24)	(126)
Other deductible temporary differences	(67)	13	57	(137)	-	-	(91)	(46)
Net deferred tax (asset) / liability	**(90)**	**18**	**(6,373)**	**6,265**	**(27)**	**918**	**1,383**	**3,991**

At 31 December 2008 and 2007, the Group had not recorded a deferred tax liability in respect to taxable temporary differences of RR'mln 2,510 and RR'mln 2,450, respectively, associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

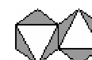
18. SALES

	Year ended 31 December 2008	Year ended 31 December 2007
Revenue from diamond sales:		
Export	38,880	47,477
Domestic	35,292	27,716
Revenue from diamonds for resale	4,072	4,578
	78,244	79,771
Other revenue:		
Transport	4,404	3,878
Social infrastructure	1,842	1,790
Construction	1,096	803
Trading	757	513
Gas and gas condensate	701	1,148
Other	4,038	2,831
	91,082	90,734

Export duties totalling RR'mln 2,243 for the year ended 31 December 2008 (year ended 31 December 2007: RR'mln 3,014) were netted against revenues from export of diamonds.

19. COST OF SALES

	Year ended 31 December 2008	Year ended 31 December 2007
Wages, salaries and other staff costs	18,737	16,135
Fuel and energy	9,075	8,402
Depreciation	8,897	8,611
Extraction tax	5,924	6,509
Materials	5,766	4,882
Services	3,720	2,764
Cost of diamonds for resale	3,415	3,904
Transport	1,696	1,397
Other	158	140
Movement in inventory of diamonds, ores and concentrates	(4,833)	(1,303)
	52,555	51,441



Wages, salaries and other staff costs include unified social tax in the amount of RR’mln 2,844 (year ended 31 December 2007: RR’mln 2,482).

Depreciation totalling RR’mln 1,246 (year ended 31 December 2007: RR’mln 937) and staff costs totalling RR’mln 2,979 (year ended 31 December 2007: RR’mln 2,649) were incurred by the Group’s construction divisions and were capitalised in the year.

20. GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December 2008	Year ended 31 December 2007
Services and other administrative expenses	3,580	2,936
Wages, salaries and other staff costs	2,714	1,741
Bad debt expense (see note 10)	85	589
	6,379	5,266

Wages, salaries and other staff costs include unified social tax in the amount of RR’mln 163 (year ended 31 December 2007: RR’mln 139).

21. OTHER OPERATING INCOME

	Year ended 31 December 2008	Year ended 31 December 2007
Negative goodwill on acquisition of non-controlling interest in subsidiaries	-	2,132
Gain on disposal of available-for-sale investments	-	676
Amortisation of Grant	-	507
Gain on disposal of OAO “Yakutskgeofizika” (see note 5)	-	104
Other	573	493
	573	3,912

22. OTHER OPERATING EXPENSES

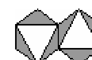
	Year ended 31 December 2008	Year ended 31 December 2007
Exploration expenses	4,520	4,150
Social costs	3,306	3,672
Taxes other than income tax, extraction tax and unified social tax (note 17)	2,669	1,832
Impairment of goodwill arising from the acquisition of OAO “NNGK Sakhaneftegaz” (see note 5)	1,531	-
Net loss from cross currency interest rate swap contracts (see note 6)	1,040	-
Loss on disposal of property, plant and equipment	890	1,061
Impairment (reversal of impairment) of property, plant and equipment	520	(158)
Other	1,516	1,563
	15,992	12,120

Social costs consist of:

	Year ended 31 December 2008	Year ended 31 December 2007
Maintenance of local infrastructure	1,620	1,804
Charity	774	746
Hospital expenses	227	391
Education	165	179
Other	520	552
	3,306	3,672

23. FINANCE INCOME

	Year ended 31 December 2008	Year ended 31 December 2007
Interest income	1,696	1,406
Exchange gains	3,360	4,687
	5,056	6,093



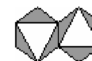
24. FINANCE COSTS

	Year ended 31 December 2008	Year ended 31 December 2007
Interest expense:		
Bank loans	7,397	3,999
Eurobonds	1,316	1,795
Commercial paper	272	261
European commercial paper	749	347
Other	78	182
Unwinding of discount of provision for restoration liability	-	283
Unwinding of discount of provision for land recultivation (see note 14)	14	62
Exchange loss	17,812	541
	27,638	7,470

25. CASH GENERATED FROM OPERATIONS

Reconciliation of profit before tax to cash generated from operations:

	Year ended 31 December 2008	Year ended 31 December 2007
(Loss) / profit before income tax	(36,003)	23,989
Adjustments for:		
Share of net profit of associates (note 5)	(676)	(936)
Interest income (note 23)	(1,696)	(1,406)
Interest expense (note 24)	9,826	6,929
Loss on disposal of property, plant and equipment (note 22)	890	1,061
Impairment (reversal of impairment) of property, plant and equipment (note 22)	520	(158)
Net loss from cross currency interest rate swap contracts (note 22)	1,040	-
Impairment of goodwill arising from the acquisition of OAO "NNGK Sakhaneftegaz" (note 22)	1,531	-
Negative goodwill on acquisition of non-controlling interest in subsidiaries (note 21)	-	(2,132)
Gain on disposal of OAO "Yakutskgeofizika" (note 21)	-	(104)
Gain on disposal of available-for-sale investments (note 21)	-	(676)
Amortisation of Grant (note 21)	-	(507)
Net loss / (gain) from foreign exchange forward contracts	25,077	(5,149)
Depreciation (note 19)	8,897	8,611
Adjustment for inventory used in construction	(2,031)	(1,995)
Adjustments for non-cash financing activity (note 28)	(141)	7
Net proceeds from exercising of foreign exchange forward contracts	1,377	945
Net proceeds from exercising of cross currency interest rate swap contracts	56	-
Receipts from restricted cash account (note 7)	102	10
Unrealised foreign exchange effect on non-operating items	15,958	(4,521)
Net operating cash flow before changes in working capital	24,727	23,968
Net increase in inventories	(6,222)	(2,825)
Net (increase) / decrease in trade and other receivables, excluding dividends receivable, receivables for sale of gold mining operations and treasury shares	(12,746)	10,404
Net increase in provisions, trade and other payables, excluding interest payable and payables for acquired property, plant and equipment	3,376	1,688
Net increase / (decrease) in taxes payable other than income tax	2,459	(20)
Cash generated from operations	**8,418**	**33,215**
Income tax paid	(3,291)	(7,944)
Net cash inflows from operating activities	**5,127**	**25,271**



26. CONTINGENCIES, COMMITMENTS AND OTHER RISKS

(a) Operating environment of the Russian Federation and impact of the ongoing global financial and economic crisis

The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation. Despite strong economic growth in recent years, the financial situation in the Russian market significantly deteriorated during 2008, particularly in the fourth quarter. The ongoing global financial and economic crisis that emerged out of the severe reduction in global liquidity which commenced in the middle of 2007 has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector and wider economy, and, at times, higher interbank lending rates and very high volatility in stock and currency markets. As a result of global volatility in financial and commodity markets, among other factors, there has been a significant decline in the Russian stock market since mid-2008. Since September 2008, there has been increased volatility in currency markets and the Russian Rouble (RR) has depreciated significantly against some major currencies. The official US$ exchange rate of the Central Bank of the Russian Federation increased from RR 25.37 at 1 October 2008 to RR 29.38 at 31 December 2008 and RR 32.04 at 10 July 2009. International reserves of the Russian Federation decreased from US$’mln 556,813 at 30 September 2008 to US$’mln 427,080 at 31 December 2008 and to US$’mln 412,591 at 30 June 2009. The commodities market was also impacted by the latest events on the financial markets. The spot Free On Board price per barrel of Urals oil decreased from US$ 91.15 at 29 September 2008 to US$ 41.83 at 31 December 2008 and then partially recovered to US$ 58.47 at 10 July 2009.

The uncertainties in the global financial markets have also led to failures of banks and to bank rescues in the United States of America, Western Europe, Russia and elsewhere. In this context the Group acquired a share in OAO “KIT Finance Investment bank” in order to support the process of normalisation of its financial position (see note 5). The full extent of the impact of the ongoing financial crisis is proving to be difficult to anticipate or completely guard against.

The availability of external funding in financial markets has significantly reduced since August 2007. Such circumstances may affect the ability of the Group to obtain new borrowings and re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions.

Debtors and borrowers of the Group may be adversely affected by the financial and economic environment, which could in turn impact their ability to repay the amounts owed. Deteriorating economic conditions for customers and borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has properly reflected revised estimates of expected future cash flows in its impairment assessments.

The Group is exposed to deteriorating economic conditions resulting from general economic downturn, decline in demand for certain commodities, including diamonds, and decline in prices for diamonds. These new market conditions have an impact on medium term cash flow forecast and assessment of potential impairment of property, plant and equipment. As at 31 December 2008 management has updated the Group’s medium and long-term cash-flow forecasts and impairment assessment (see note 8).

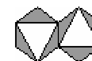
The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes, and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the 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.

Management is unable to reliably determine the effects on the Group’s future financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and development of the Group’s business in the current circumstances.

(b) Taxes

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 Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the 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. 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.

At 31 December 2008 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group’s tax, currency and customs positions will be sustained. Where management believes it is probable that the financial position cannot be sustained, an appropriate amount has been accrued for in the consolidated financial statements.



(c) Legal proceedings

The Group is a party to certain legal proceedings arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material adverse effect on the results of operations or financial position of the Group as at 31 December 2008.

(d) Insurance

The Group is assessing its policies for insuring assets and operations. At present, apart from the full insurance of movements of diamond inventory from the production location to the customers, very few assets and operations of the Group are insured and, in the instances where assets are insured, the amounts generally are not sufficient to cover all costs associated with replacing the assets.

(e) Capital commitments

At 31 December 2008, the Group has contractual commitments for capital expenditures of approximately RR’mln 10,622 (31 December 2007: RR’mln 2,014).

(f) Restoration, rehabilitation and environmental costs

Under its license agreements, the Group is not responsible for any significant restoration, rehabilitation and environmental expenditures that may be incurred subsequent to the cessation of production at each mine, apart from the obligation to perform recultivation of certain disturbed lands and tailing pits in the areas of its operating activity during 2007-2010 in accordance with the “Program for improvement of environmental situation in the area of operating activity of the Company”. The Company recognised a provision for these future expenses in its consolidated financial statements as at 31 December 2008 and 31 December 2007. Also the Group is obliged to restore riverbeds and the surrounding areas. These expenses are not expected to be material to the Group and are expensed in the period when incurred.

27. RELATED PARTY TRANSACTIONS

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 over the other party in making financial or operational decisions as defined by IAS 24 “Related Party Disclosures”. 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.

Governments of the Russian Federation and the Republic of Sakha (Yakutia)

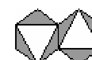
Governments of the Russian Federation and the Republic of Sakha (Yakutia) are the ultimate controlling parties of AK “ALROSA”. As at 31 December 2008 83 percent of AK “ALROSA” issued shares were directly owned by the Governments of the Russian Federation and the Republic of Sakha (Yakutia). Also as at 31 December 2008 8 percent of the Company’s shares were owned by administrations or 8 districts of the Republic of Sakha (Yakutia). Following the General Meeting of Shareholders in June 2008, the 15 seats on the Supervisory Council include 12 representatives of the Russian Federation and the Republic of Sakha (Yakutia), two management representatives and one representative of districts of the Republic of Sakha (Yakutia). Governmental, federal and local economic and social policies affect the Group’s financial position, results of operations and cash flows.

Tax balances are disclosed in the balance sheet and in notes 10 and 17. Tax transactions are disclosed in the income statement, cash flow statement and in notes 17, 18, 19, 22 and 25.

Parties under control of the Government

In the normal course of business the Group enters into transactions with other entities under Governmental control. The principal forms of such transactions are diamond sales, electricity purchases and borrowings. Prices of diamonds sales are set by price lists approved by the Ministry of Finance of the Russian Federation; electricity tariffs in Russia are regulated by the Federal Tariffs Service; other transactions with entities under Governmental control were performed under market terms; loans received from Government controlled entities and loans issued to Government controlled entities are provided on the basis of market rates.

As at 31 December 2008 the accounts payable to the parties under Governmental control totalled RR’mln 3,092 (31 December 2007: RR’mln 244). As at 31 December 2008 the accounts receivable from the parties under Governmental control totalled RR’mln 517 (31 December 2007: RR’mln 481). As at 31 December 2008 and 31 December 2007 the



accounts receivable from the parties under Governmental control and accounts payable to the parties under Governmental control were non-interest bearing, had a maturity within one year and were denominated in Russian Roubles.
During the years ended 31 December 2008 and 31 December 2007 the Group had the following significant transactions with parties under Governmental control:

	Year ended 31 December 2008	**Year ended 31 December 2007**
Sales of diamonds	13,244	10,864
Other sales	1,333	1,369
Electricity and heating purchases	4,330	4,131
Other purchases	1,301	855

As at 31 December 2008 and 31 December 2007 the amount of loans received by the Group from banks under Governmental control was as follows:

	31 December 2008	**31 December 2007**
Long-term bank loans		
US$ denominated fixed rate	5,364	2,342
RR denominated floating rate	3,193	-
RR denominated fixed rate	44,992	-
	53,549	2,342
Short-term bank loans		
US$ denominated fixed rate	14,141	6,883
RR denominated floating rate	2,605	-
RR denominated fixed rate	600	554
	17,346	7,437
	70,895	**9,779**

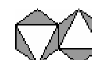
The average effective interest rates on the loans received by the Group from banks under Governmental control at the balance sheet dates were as follows:

	31 December 2008	**31 December 2007**
Long-term bank loans		
US$ denominated fixed rate	10.9%	8.8%
RR denominated floating rate	28.3%	-
RR denominated fixed rate	15.2%	-
Short-term bank loans		
US$ denominated fixed rate	10.0%	10.1%
RR denominated floating rate	27.1%	-
RR denominated fixed rate	18.5%	10.0%

In the year ended 31 December 2008 interest expense accrued in respect to the loans received by the Group from entities under Governmental control totalled RR'mln 3,077 (year ended 31 December 2007: RR'mln 701).

As at 31 December 2008 the amount of loans issued by the Group to the entities under Governmental control totalled RR'mln 843 (31 December 2007: RR'mln 1,121). These loans are short-term, denominated in Russian Roubles, the average effective interest rate on these loans is 15 percent (31 December 2007: 15 percent). In the year ended 31 December 2008 interest income earned by the Group in respect to the loans issued to the entities under Governmental control totalled RR'mln 141 (year ended 31 December 2007: RR'mln 144).

In December 2008 the Group acquired a 45 percent interest in share capital of OOO "KIT Finance Holding Company", which at the date of transaction owned 87 percent of shares of OAO "KIT Finance Investment bank" (see note 5). The rest 55 percent interest in share capital of OOO "KIT Finance Holding Company" was acquired by the companies of "Russian Railroads" group, which is controlled by the Government of the Russian Federation. As a result of these transactions OAO "KIT Finance Investment bank" became a related party of the Group. Cash balances held by the Group on current and long-term deposit accounts in OAO "KIT Finance Investment bank" as at 31 December 2008 are disclosed in note 7.



Key management compensation

The Supervisory Council of the Company consists of 15 members, including state and management representatives. Representatives of Governments of the Russian Federation and the Republic of Sakha (Yakutia) in the Supervisory Council of the Company are not entitled to compensation for serving as members of the Supervisory Council. Representatives of management in the Supervisory Council of the Company are entitled to compensation for serving as members of the Management Committee of the Company.

The Management Committee consists of 24 members, two of whom are also members of the Supervisory Council. Management Committee members are entitled to salary, bonuses, voluntary medical insurance and other short term employee benefits. Salary and bonus compensation paid to members of the Management Committee is determined by the terms of employment contracts. According to Russian legislation, the Group makes contributions to the Russian Federation State pension fund for all of its employees including key management personnel. Key management personnel also participate in certain post-retirement benefit programs. The programs include pension benefits provided by the non-governmental pension fund “Almaznaya Osen”, and a one-time payment from the Group at their retirement date.

Supervisory Council and Management committee members received benefits for the year ended 31 December 2008 totalling RR’mln 520 (year ended 31 December 2007: RR’mln 406).

Associates

Significant transactions with associates are summarised as follows:

Long-term accounts receivable	**31 December 2008**	**31 December 2007**
“Escom-ALROSA Ltd”, loan issued and interest receivable (see note 5)	2,990	2,734
	2,990	2,734

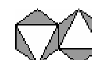
In the year ended 31 December 2008 the Group earned interest income in respect to the loan issued for “Escom-ALROSA Ltd” totalling RR’mln 188 (year ended 31 December 2007: RR’mln 219).

Current accounts receivable	**31 December 2008**	**31 December 2007**
“Escom-ALROSA Ltd”, current portion of the loan issued (see note 5)	592	75
“Catoca Mining Company Ltd.”, dividends receivable	402	234
ZAO “PIC Orel Almaz”, receivables for supplied diamonds	162	162
“LUO Camachia-Camagico”	73	108
Other	67	95
Less: provision for bad debt	(188)	(188)
	1,108	486

As at 31 December 2008 and 31 December 2007 the accounts receivable from associates were non-interest bearing, had a maturity within one year and were denominated mostly in US$.

28. SIGNIFICANT NON-CASH TRANSACTIONS

	Year ended 31 December 2008	**Year ended 31 December 2007**
Non-cash financing activities:		
Commercial paper issuance	401	500
Commercial paper and loans redemption	(542)	(493)
	(141)	7



29. SEGMENT INFORMATION

The Group has one reportable business segment, which is the production and sale of diamonds. The Group evaluates performance and makes investment and strategic decisions based upon review of profitability for the Group as a whole.

An analysis of revenue by type is disclosed in note 18. Revenue from sales by geographical location of the customer, and assets and capital expenditures by geographical location of the asset are as follows:

	Sales		Total assets		Capital Expenditures	
	Year ended 31 December 2008	Year ended 31 December 2007	31 December 2008	31 December 2007	Year ended 31 December 2008	Year ended 31 December 2007
Russian Federation	47,821	38,331	254,847	220,067	31,571	28,350
Western Europe	19,471	24,705	3,215	1,996	5	-
Other countries	23,790	27,698	4,597	3,670	16	537
	91,082	**90,734**	**262,659**	**225,733**	**31,592**	**28,887**
Associates	-	-	1,813	1,613	-	-
Unallocated assets	-	-	603	483	-	-
Total	**91,082**	**90,734**	**265,075**	**227,829**	**31,592**	**28,887**

30. POST BALANCE SHEET EVENTS

Borrowings

During January–June 2009 “ALROSA Finance S.A.”, a subsidiary of the Group, issued several series of European commercial paper (ECP) in the amount of RR’mln 12,083 (US$’mln 373) with maturity periods 6-12 months and fixed annual interest rates of 11.5-14.4 percent.

During January–June 2009 the Group received short-term and medium-term US$ denominated fixed rate loans from several Russian banks in the amount of RR’mln 52,465 (US$’mln 1,545). During the same period the Group repaid bank loans (including US$ denominated fixed rate and RR denominated fixed and floating rate loans) in the amount of RR’mln 28,828 in accordance with the repayment schedules established by the respective loan agreements.

Dividends

On 20 June 2009, the Company’s annual shareholders’ meeting decided not to pay dividends for the year ended 31 December 2008.